

# 1 Bangladesh

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## I. Introduction

Bangladesh, a small country of South East Asia emerged as an independent nation in the year 1971 after a bloody liberation war against Pakistan. Bangladesh is blessed with the largest unbroken sea shore, the largest mangrove forest, rich mountain ranges, vast green scenic serene, ample natural resources, and huge manpower; however despite huge potential, the country is still on her struggle to advance from a vulnerable economic state.

### Geography and Climate

The People's Republic of Bangladesh is a country in [South Asia](#). Bangladesh covers an area of 147,570 sq km. It situates from 20°34N to 26°38N latitude and from 88°01E to 92°41E longitude. The country is bordered by [India](#) on three sides and [Myanmar](#) to the southeast; the [Bay of Bengal](#) forms the southern coastline. The total length of the land border is about 4,246 km, of which 93.9% is shared with India and about 6.1% with Myanmar.

Bangladesh is located in the low-lying Ganges-Brahmaputra River Delta or Ganges Delta. This delta is formed by the confluence of the Ganges (local name Padma), Brahmaputra (Jamuna), and Meghna rivers and their respective tributaries. The alluvial soil deposited by these rivers has created some of the most highly fertile plains of the world. 254 rivers flowing through out the country make it a land of rivers.

Most parts of Bangladesh are within 10 meters above the sea level, and it is believed that about 10% of the land would be flooded if the sea level rises by 1 meter. The Chittagong Hill Tracts, the only significant hill area of the country, consists of hills, hillocks, valleys and forests, is quite different in characteristics and habitats from other parts of Bangladesh. Mostly, the hill ranges and river valleys are longitudinally aligned. The region lies in the southeastern part of the country bordering Myanmar in the southeast and the Indian states of Tripura in the north and Mizoram in the east. The coastal plain is partly sandy and partly composed of saline clay. Cox's Bazar, south of the city of Chittagong, has a beach that stretches uninterrupted over 120 kilometers; one of the longest unbroken natural sea beaches of the world. The country is bounded in the south by the Bay of Bengal. Although Bangladesh is a small country, the length of the coastline is more than 580 km. On the southwest the huge expanse of the largest mangrove forest of the world, known as Sundarbans fences the south west border of the country. This mangrove forest is the home to diverse flora and fauna, including the Royal Bengal Tiger.

Expanding along the Tropic of Cancer, Bangladeshi climate is characterized by tropical monsoon climate with a mild winter from November to February, a hot, humid summer from March to June. A warm and humid monsoon season lasts from June to October and supplies most of the country's rainfall. The pre-monsoon hot season comes with high temperature and occurrence of thunderstorms. April is the hottest month in the country when mean temperature ranges from 28°C in the east and south to 32°C in the west-central part of the country. After April, increasing cloud-cover dampens temperature. Wind direction is variable in this season, especially during its early part. Rainfall accounts for 10 to 25 percent of the annual total, which is caused by thunderstorms. Winter is very short goes at peak in early January. Average temperature in January varies from 17°C in the northwest and northeastern parts of the country to 20°C-21°C in the coastal areas. Minimum temperature in the extreme northwest in late December and early January reaches 5°C to 6°C. Natural calamities, such as floods, tropical cyclones, tornadoes, and tidal bores occur almost every year, combined with the effects of deforestation, soil degradation

and erosion. Droughts, cyclones, seasonal floods are common natural disasters which often devastate the country.

### **Natural Resources**

Because of a different geological environment, important mineral deposits of Bangladesh are natural gas, coal, limestone, hard rock, gravel, glass sand, white clay, brick clay, peat, and beach sand heavy minerals. Among the natural resources natural gas is the most important resource on which economy of Bangladesh largely depends. There are 22 discovered gas fields in Bangladesh of various sizes. The total reserve of 20 gas fields is about 20 to 25 Tcf (trillion cubic feet). Gas in most of the fields is dry; in a few fields it is wet, with considerable amounts of condensate. Bangladesh is basically a mono energy country, 70 percent of commercial energy comes from natural gas here. Power sector ranks the highest (44%); fertilizer sector ranks the second (28%); and industry, domestic, commercial and other sectors together rank third (22%) in gas consumption. Currently 12 gas fields under public and private sectors are in production with gas supply between 900 and 930 mmcfd per day.

### **History and Political Structure**

In the earliest period Bengal was known to be inhabited by different groups of people, whose names were associated with the area inhabited by them. The reconstruction of the history of Bengal in the pre-Muslim period is difficult due to paucity of sources. So far the earlier period so far for satisfactorily known to history is down to the 4th century AD, when Bengal came under the Imperial Guptas. The history of Bengal from the fall of the Mauryas (2nd century BC) to the rise of the Guptas (4th century AD) is obscure. After Guptas mainly two dynasties Pala and Sena ruled this region until The Muslim rule in Bengal had its beginning in the opening years of the thirteenth century (1204 AD). This period known as Sultanate period lasted until Mughal Dynasty took charge (1576 to 1757). Afterwards, British East India Company and British Empire ruled this region till 1947 when India and Pakistan emerged as two independent nations. Bengal got divided into two parts . East Bengal became the East Pakistan, a geographically separated province of Pakistan. Due to extreme economic, cultural, political oppressions and discrimination, people of East Pakistan choose to be separated from Pakistan. After a nine month long bloody war of independence, Bangladesh came to exist as an independent nation in the year 1971.

Bangladesh is a parliamentary democracy. The President is the head of state, a basically ceremonial post. The real power is held by the Prime Minister, who is the head of government. The Prime Minister, a member of parliament (MP), is ceremonially appointed by the president. The Prime Minister must command the confidence of the majority of the MPs. The cabinet is composed of ministers selected by the prime minister and appointed by the president. The unicameral parliament is the 300-members House of the Nation or Jatiyo Sangshad, elected by popular vote from single-member constituencies for five-year terms of office. There is universal suffrage for all citizens from the age of 18. Bangladesh has instituted a unique system of transferring of power; at the end of the tenure of a government. Power is handed over to a caretaker party neutral government which is composed by members of a civil society. For three months the care taker government rules and holds the general election, afterwards transfers the power to elected representatives.

### **Demographics**

Despite very vulnerable ecology, this delta basin of Bay of Bengal historically had been a densely populated region. In the year 2005, total population of Bangladesh went up to 141.8 million, the 7th most populated country of the world. A huge population in a comparatively small country makes it the most densely populated country of the world. Population and adverse ecology always had been a challenge for the economy. However, Bangladesh established a credible advancement in the basic human development sectors. At a comparatively low level of

development, it has also earned a major decline in population growth rate and advanced to the medium human development group of countries of UNDP's ranking. Child mortality was halved during the 1990s, life expectancy has increased to 65 years, and net primary enrolment went up significantly, while gender parity has been achieved in primary and secondary education.

**Table 1: Selected Demographic Indicators**

	Unit	2000	2001	2002	2003
Total population	Million	128.1	129.2	132	134.8
Sex ratio	Males per 100 females		104		105
Annual growth rate	Per 100	1.41	1.4	1.53	1.5
Crude birth rate	Per 1000	19	18.9	20.1	20.9
Crude death rate	Per 1000	4.9	4.8	5.1	5.9
Infant mortality rate	Per 100 live birth	58	56	53	54
Density	Population/square km	868	876	894	913
Life expectancy at birth	Years	63.6	64.2	65	64.9
Urban population	Percentage		23.4		23.2
Rural population	Percentage		76.6		76.8

Sources: 1. Bangladesh Bureau of Statistics, 2. Bangladesh Economic Review 2006

## II. Overview of Macroeconomic Activity

Though still a country with very low per capita income, economy of Bangladesh grew modestly in the last one decade. In the last three years overall macroeconomic activity got momentum with GDP growth rate over 6%. These growths are mainly attributed by high growths in industry, rapid growth in export and strong inward remittance. Banking sector reforms, developed infrastructure, sound monetary and fiscal policy brought about great positive impacts on the economic growth. Nevertheless, the present state of the economy is far behind to be considered as satisfactory. The economy must grow in faster pace to reduce level of poverty to a moderate level and, thereby achieve the set UN millennium development goals.

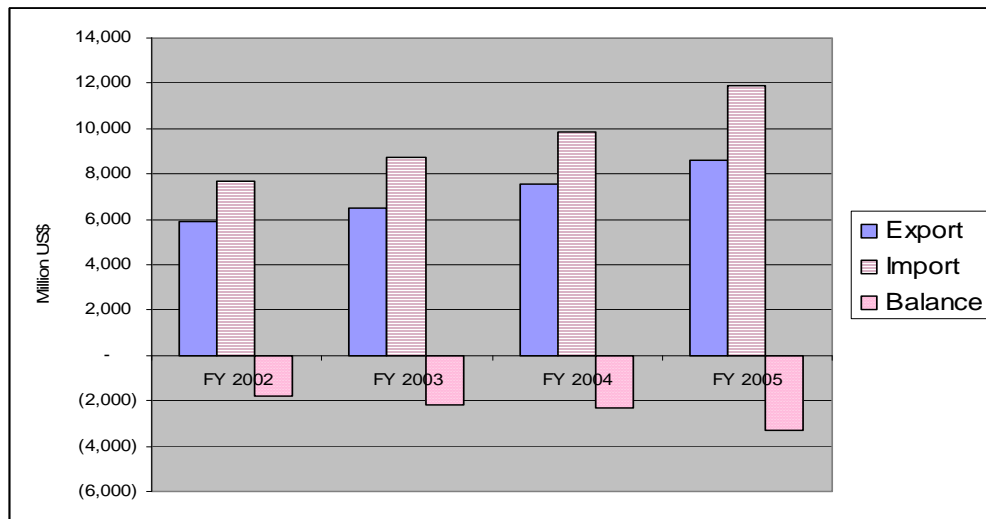
### A. International Environment

Soaring oil price, increased debt services, widened trade deficit, reduction of foreign loans posed enormous challenge for Bangladesh economy in the international arena. Yet rapid growth in exports and very strong remittance inflows aided the economy moving to positively.

### Trade Balance

Growing trade deficit has been a major concern for the economy. From FY 2002 to FY 2003 growth of trade deficit was only 4.7%, while from FY 2003 to FY 2004 trade deficit grew 42.42 %. In recent years exports earned modest growth which largely was offset by even higher growth in import. Only very recent data of FY 2006 shows that Bangladesh achieved impressive 21.63 % growth in export where import grew 12.17%. Ever increasing trade deficit is one of the biggest challenges the economy is facing in the recent years.

**Figure1: Trend in Growth of Trade Deficits**



Source: Bangladesh Bank, Major Economic Indicators: Monthly Update, August 2006

Bangladesh exports around 160 types of products. 10 of those constitute more than 92% of the total export. Lack of diversification of export items the economy is largely dependant on only few export items, which makes export sector much vulnerable. Woven and knitwear garments dominate exports of Bangladesh contributing altogether around 74% of the total export. Among the export items knitwear garments is showing strong prospect with a growth of 25%, 28% and 33% in the FY 2003, FY2004 and FY 2005 respectively.

**Table 2: Export by Major Product Categories**

	Total export (Million US\$)			% of total export		
	FY 2003	FY 2004	FY 2005	FY 2003	FY 2004	FY 2005
<b>Primary commodities</b>						
Frozen foods	321.8	390.3	420.7	4.91	5.13	4.86
Tea	15.5	15.8	15.8	0.24	0.21	0.18
Agricultural products	24.5	41.1	82.5	0.39	0.54	0.95
Raw jute	82.5	79.6	96.2	1.26	1.05	1.11
Others	17.4	26.5	33.1	0.26	0.35	0.39
<b>Sub Total</b>	<b>461.6</b>	<b>553.4</b>	<b>648.3</b>	<b>7.06</b>	<b>7.28</b>	<b>7.45</b>
<b>Industrial goods</b>						
Woven garments	3258.3	3538.1	3598.2	49.76	46.54	41.58
Knitwear	1653.8	2148.1	2819.5	25.26	28.25	32.58
Jute products	257.2	246.5	307.5	3.39	3.24	3.55
Leather	191.2	211.4	220.9	2.92	2.78	2.55
Fertilizer and chemical prod.	100.5	121.5	187.2	1.53	1.6	2.28
Footwear	46.6	68.3	87.5	0.71	0.9	1.01
Ceramic products	18.8	24.1	28.7	0.29	0.32	0.33
Petroleum by products	31.2	37.1	35.1	0.48	0.49	0.41
Others	528.17	654.5	721.6	8.60	8.60	8.22
<b>Sub Total</b>	<b>6085.8</b>	<b>7049.6</b>	<b>8006.2</b>	<b>92.94</b>	<b>92.72</b>	<b>92.51</b>
<b>Total</b>	<b>6548.4</b>	<b>7602.9</b>	<b>8654.5</b>	<b>100.00</b>	<b>100.00</b>	<b>100.00</b>

Source: Bangladesh Economic Review 2005, Ministry of Finance

The United States of America is the main destination of export items. In FY 2005, Bangladesh exported 27.87% of total exports to the United States of America. Woven garments, knitwear, shrimp are the main items exported to the country. Germany, UK, France, Belgium, Italy, Netherlands, Canada and Japan are the other major importing countries of Bangladeshi products. On the other end, petroleum products, food grains, cotton, yarn, capital machinery, textile items are main import products of the country. In FY 2005 import registered 20.6% growth. Abnormal increase of oil price in the international market caused a massive 63% increase in total petroleum import cost in FY2005. Import of capital goods show decline in FY 2005 due to change in classification of items in that one. A major portion of capital machinery is classified under the “Others” category.

**Table 3: Import by Major Product Categories**

	Million US \$			
	FY 2002	FY 2003	FY 2004	FY 2005
Rice and Wheat	186	409	431	574
Edible oil	251	364	471	440
Pulses (all sorts)	88	145	120	159
Clinker	150	144	139	170
Crude petroleum	242	267	252	350
Petroleum	481	620	770	1252
Chemicals	335	353	406	509
Fertilizer	107	109	150	332
Plastics and rubber articles	250	281	367	477
Raw cotton	312	393	583	666
Yarn	283	270	323	393
Textile articles	1063	1106	1295	1571
Iron, steel and other base metals	413	455	479	679
Capital goods	2617	2735	2875	1115
Others	1762	2007	2242	4460
<b>Total Imports</b>	<b>8540</b>	<b>9658</b>	<b>10903</b>	<b>13,147</b>

Source: Bangladesh Economic Review 2005, Ministry of Finance

China, India, Singapore, Japan, Hong Kong, Taiwan, South Korea, Malaysia are the major exporting countries to Bangladesh. In FY 2005, total import from India and China amounted 15.44 % and 12.49% respectively.

### **Current Account Balance**

In the FY 2005, current account balance turned to a negative figure with -557 million USD compared to positive 176 million USD in FY 2004. Huge surge in trade deficit (42.17%) mainly caused this negative current account balance. However, impressive growth of inward remittance (14.1%), and increased direct investment helped register a positive overall balance of 67 million USD in the FY 2005 compared to a negative overall balance of -171 million USD in the FY 2004.

**Table 4: Current Account Balance**

Million US\$

	FY 2002	FY2003	FY 2004	FY 2005
<b>Current Account Balance</b>	<b>157</b>	<b>176</b>	<b>176</b>	<b>(557)</b>
<b>Trade Balance</b>	<b>(1,768)</b>	<b>(2,215)</b>	<b>(2,319)</b>	<b>(3,297)</b>
Export f.o.b.	5,929	6,492	7,521	8,573
Import f.o.b.	7,697	8,707	9,840	11,870
<b>Services</b>	<b>(499)</b>	<b>(691)</b>	<b>(874)</b>	<b>(870)</b>
Receipts	865	887	924	1,177
Payments	1,364	1,578	1,798	2,047
<b>Income</b>	<b>(402)</b>	<b>(358)</b>	<b>(374)</b>	<b>(680)</b>
Receipts	50	64	63	116
Payments	452	422	437	(796)
<b>Current Transfers</b>	<b>2,826</b>	<b>3,144</b>	<b>3,433</b>	<b>4,290</b>
Official	69	82	61	37
Private	2,757	3,062	3,372	4,253
<b>Capital and financial Accounts</b>				
<b>Capital Account</b>	410	428	196	163
Capital Transfer	410	428	196	163
<b>Financial Account</b>	391	413	78	760
Foreign Direct Investment	391	376	385	776
Portfolio Investment	(6)	2	6	-
Other investment	6	35	313	(16)
<b>Net Errors and Omissions</b>	<b>(550)</b>	<b>(202)</b>	<b>(279)</b>	<b>(299)</b>
<b>Overall Balance</b>	<b>(408)</b>	<b>(815)</b>	<b>(171)</b>	<b>67</b>

Source: Bangladesh Bank, Major Economic Indicators: Monthly Update, August 2006

**Exchange Rate**

Bangladesh Taka entered into floating exchange rate quite recently, from May 31 2003. Before that government used to control the exchange rate through occasional adjustment of the value of Taka against US dollar. In that time the currency mostly kept overvalued, that eventually used to make exports of Bangladesh less competitive. Import got encouraged and domestic output and employment got impeded. Unlike in many other countries, while transit to floating exchange rate regime; the external sector did not face any volatility. The transition took place in a stable low inflation driven world economic environment and Bangladesh Bank took enough preparatory measures, which made the transition quite smooth.

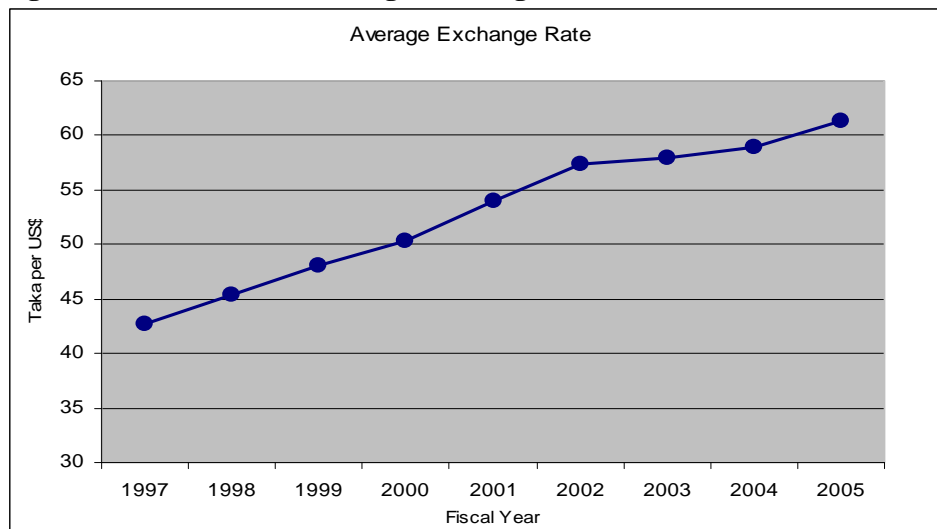
However, in recent years, exchange rate was always under heightened pressure due to pressure of different market forces and limited interventions of the central bank. Taka remained in the back foot due to large net outflows of trade credits and other long and short term net outflows. It seems continued depreciation of Taka will not stop until trade deficit narrow down and petroleum import bill gets some stability. On July 02, 2006 official exchange rate of buying 1 US\$ was 69.49 Taka.

**Table 5: Average Exchange Rate (Taka per US \$)**

Fiscal Year	1997	1998	1999	2000	2001	2002	2003	2004	2005
Average Exchange Rate	42.7	45.45	48.06	50.31	53.96	57.43	57.9	58.94	61.39

Source: Bangladesh Economic Review 2005, Ministry of Finance

**Figure 2: Movements of Average Exchange Rate**



Source: Bangladesh Economic Review 2005, Ministry of Finance

Moderate growth of export earning and impressive growth of remittance from expatriates helped rise foreign exchange reserve to US\$ 2705 million at the end of FY 2004 giving a growth of 9.51% than that of the previous year. At the end of FY 2005 foreign currency reserve went up to US\$ 3024 million with a strong 11.1% growth.

**Table 6: Foreign Exchange Reserve (million US\$)**

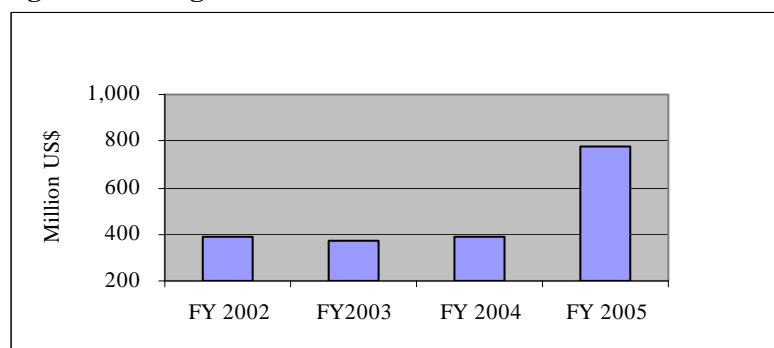
Fiscal Year	1997	1998	1999	2000	2001	2002	2003	2004	2005
Foreign Exchange Reserve	1719	1739	1523	1602	1307	1583	2470	2705	3004

Source: Bangladesh Economic Review 2005, Ministry of Finance

### Foreign Direct Investment

Bangladesh, a relatively under performer in attracting foreign direct investment shown some impressive improvements in the recent years. FDI inflow figures have jumped from 385 million US\$ in FY 2004 to 776 million US\$ in FY 2005, registering more than 100% growth in a single year. In FY 2006, total FDI inflow is estimated to be 800 million US\$.

**Figure 3: Foreign Direct Investment Inflow**



Source: Bangladesh Economic Review 2006

Service, textile and chemical are three dominant sectors where most of the FDI inflows are concentrated. According to the Board of Investment statistics, during 2003, Service, textile and chemical sectors attracted 34%, 27% and 28% of the total FDI inflows respectively. 41% of those investments came from European Union countries and 39% of the FDI came from south, east and south-east Asian countries.

### Borrowing from Abroad

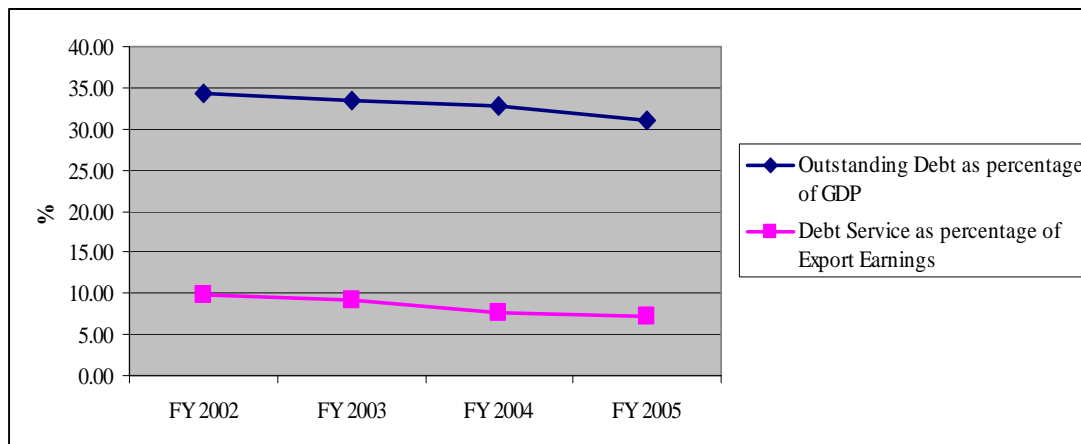
Official foreign loan and aid disbursement increased by 44.2% in FY 2005 than that of FY 2004. However, foreign aid disbursement decreased by significant 44.4 % in FY 2005 from FY 2004. External loan repayment increased slightly in FY 2005 than that of the previous year . Total outstanding official external debt stood at US\$ 18777 (31.1% of GDP) against US\$ 18511 in FY 2004 (32.77% of GDP). However, outstanding debt as a percentage of GDP is in a decreasing trend in the recent years.

**Table 7: External Aid and Loans**

	FY 2002	FY 2003	FY 2004	FY 2005
Loans (medium and long-term)	963	1,075	695	1,257
External aid	479	510	338	234
Total	1,442	1,585	1,033	1,491
Outstanding external debt balance	16,276	17,411	18,511	18777
Growth rate of outstanding external debt balance (%)	7.97	6.97	6.32	1.44
Outstanding Debt as percentage of GDP	34.21	33.54	32.77	31.09
Debt Service as percentage of Export Earnings	9.79	9.29	7.73	7.15

Source: Bangladesh Economic Review 2005, Ministry of Finance

**Figure 4: Trend of Debt Service and Outstanding Debt**



Sources: 1. Bangladesh Economic Review 2005, Ministry of Finance,  
2. Bangladesh Bank

The country repaid 619 million US\$ for external loans in FY 2005 compared to 619 million US\$ in FY 2004. However, external loan repayment as a percentage of export income is gradually decreasing in the recent fiscal years. In FY 2005 total debt services amounted 7.15% of the export income which was 7.73% in FY 2004.



**Table 8 : External Loan Repayment**

	Interest	Principal	Total	Export	Loan repayment as percentage of export income
FY 2002	151	435	586	5986	9.79
FY 2003	156	452	608	6548	9.29
FY 2004	165	423	588	7603	7.73
FY 2005	185	434	619	8655	7.15

Source: Bangladesh Bank

## B. Domestic Environment

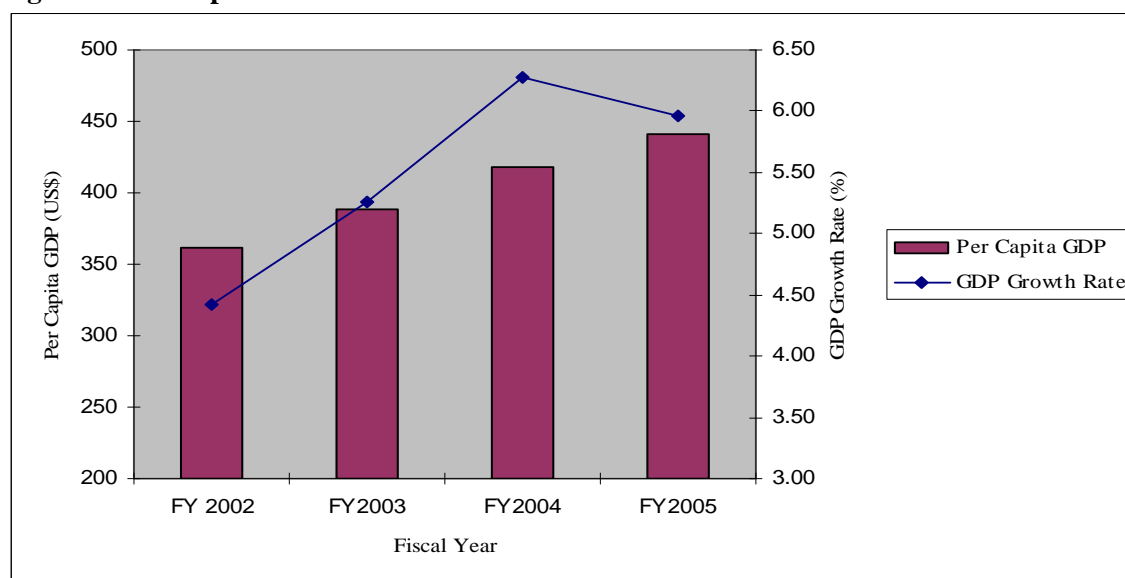
### Economic growth rate

Soaring oil price in the international market and phasing out of Multi Fiber Agreement (MFA) posed two major challenges for the economy. However, despite unfavorable international trade and economic environment, the economy grew steadily in the last few years. In FY 2005 GDP growth rate went up to 5.96 %, which was higher than the forecast. This moderately high growth rate is broadly contributed by steady growth in industrial and service sector. GDP per capita increased moderately up to US\$ 441 in FY 2005.

**Table 9: GDP at Current Market Price and Per Capita GDP**

	Unit	FY 2002	FY2003	FY2004	FY2005
GDP at current market price	billion Taka	2,732	3,006	3,330	3,707
GDP at current market price	billion US\$	47.57	51.91	56.49	60.39
Per Capita GDP	Taka	20754	22530	24628	27061
Per Capita GDP	US\$	361	389	418	441
Average Exchange rate	Taka /US\$	57.43	57.9	58.94	61.39

Sources: 1. Bangladesh Bureau of Statistics, 2. Bangladesh Bank

**Figure 5: Per Capita GDP and GDP Growth rate**

Source: Bangladesh Economic Review 2006, Ministry of Finance

In the recent years, robust growth in the industrial sector changed the basic characteristics of sector wise composition of GDP. In FY2005 industrial sector grew 8.28%, the highest growth achieved among all sectors. In FY 2002 agriculture sector used to contribute more in GDP than the industrial sector. After FY 2002, industrial sector left agricultural sector far behind in terms of share in GDP, and the gap is increasing steadily.

**Table 10 : GDP Growth Rate at Constant Price by Broad Sectors**

	FY 2002	FY2003	FY2004	FY2005
Agriculture	0.00	4.10	4.09	2.21
Industry	6.50	7.30	7.60	8.28
Service	5.40	5.40	5.66	6.36
Total GDP growth rate at constant market price	4.42	5.26	6.27	5.96

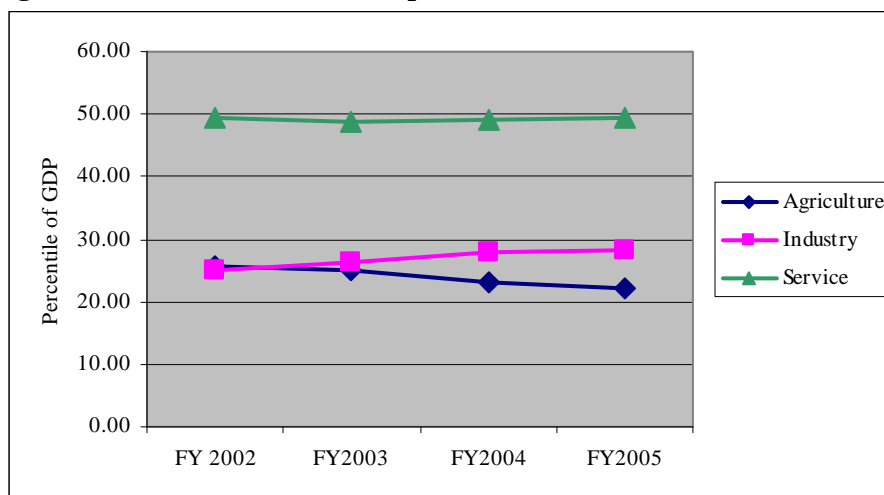
Source : Bangladesh Bureau of Statistics

**Table 11: Composition of Broad Sectors in GDP**

	FY 2002	FY2003	FY2004	FY2005
Agriculture	25.68	25.03	23.08	22.27
Industry	24.87	26.20	27.96	28.31
Service	49.45	48.77	49.22	49.42
Total	100.0	100.0	100	100

Source : Bangladesh Bureau of Statistics

**Figure 6: Growth Trends in Composition of Broad Sectors of GDP**

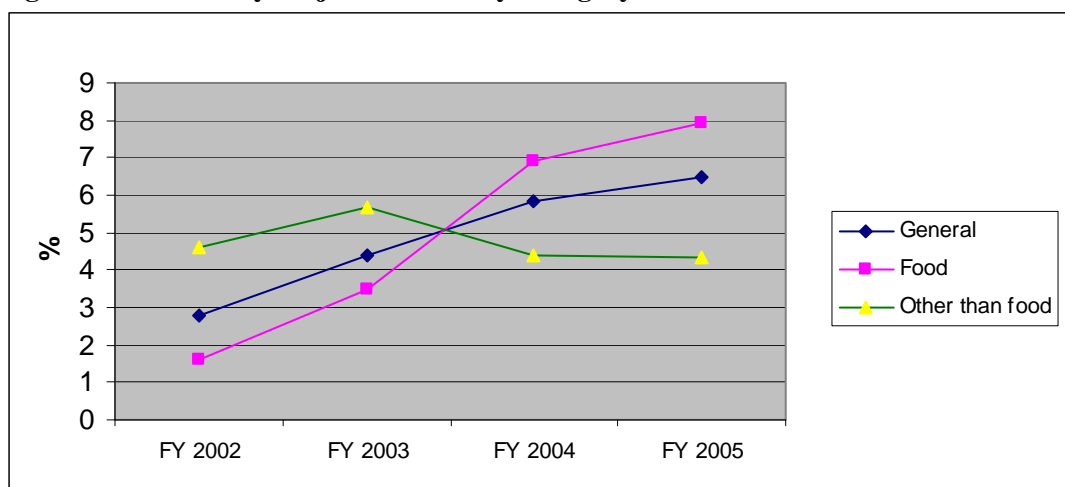


Source: Bangladesh Economic Review 2006, Ministry of Finance

## Inflation

Inflation on a slowly rising trend climbed further height of 6.65% in June 2005. Increase in the inflation mainly caused by increases in food prices. A rise in imported good prices stemming from taka/dollar depreciation also fed into price pressures. Increased global oil prices also mounted considerable pressure in overall prices. Central bank adopted accommodative monetary policy in support of increased private sector credit demands which eventually fueled inflationary pressures and depreciation.

**Figure 7: Inflation by Major Commodity Category**



Source: Bangladesh Bureau of Statistics

**Table 12: National Consumer Price Index and Inflation**

	FY 2002	FY 2003	FY 2004	FY 2005
General	130.26	135.97	143.9	153.23
<i>Percentile change</i>	2.79	4.38	5.83	6.48
Food	132.43	137.01	146.5	158.08
<i>Percentile change</i>	1.63	3.46	6.93	7.91
Other than food	127.89	135.13	141.03	147.14
<i>Percentile change</i>	4.61	5.66	4.37	4.33

Source: Bangladesh Bureau of Statistics

However, rising inflation is not a discrete incident in Bangladesh. Rather, in all other neighboring south East Asian countries inflation rose steady during the period. Average 12 month point to point inflation reflects the fact that overall price hikes in the world market of basic commodities and petroleum products created inflationary pressure in almost every country in this region.

**Table 13: Inflation in south Asian counties**

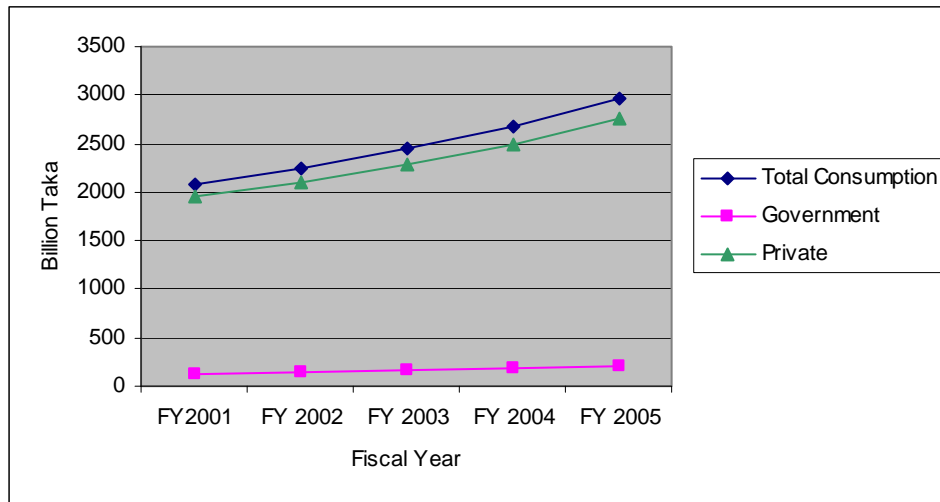
	FY 2002	FY 2003	FY 2004	FY 2005
Bangladesh	3.6	5	5.6	7.4
India	4.2	4.4	3.1	4.1
Pakistan	4.8	1.8	8.5	8.8
Sri Lanka	9.8	12.4	6.7	9.4

Source: Bangladesh Bank

### Consumption

Consumption grew steadily in a regular momentum over the last few years. Growth of consumption remained around 10% in last 3 consecutive years of FY 2005.

**Figure 8: Growth Trend of Public and Private Consumption**



Source: Bangladesh Economic Review 2006, Ministry of Finance

In FY2005 consumption amounted 80% of the GDP. Consumption of private sector shared 74.5% of GDP, while public sector consumption was around 5.5 % of GDP. However, consumption as the percentile of GDP is decreasing very slowly over the last five fiscal years.

**Table 14: Consumption as percentile of GDP**

	FY2001	FY 2002	FY 2003	FY 2004	FY 2005
Consumption	82.0	81.8	81.4	80.5	80.0
Government	4.5	5.0	5.4	5.5	5.5
Private	77.5	76.8	76.0	75.0	74.5

Source: Bangladesh Economic Review 2006, Ministry of Finance

### Investment and Savings

Domestic investment grew 13.6% in FY 2005 raising its share as percentage of GDP slightly more from 24.0 in FY 2004 to 24.5 in FY 2005. Considering investment as a share of GDP, share of private sector investments increased slowly, while public sector shares remained almost the same over the last few years. Private sector component of domestic savings moved up to 18.3 % of GDP in FY2005 from 17.8% in FY 2004. In recent years, it appears that private savings are higher than private investment, indicating that, induced by high interest rate of government bonds, some private investment channeled to public sector.

**Table 15: Public and Private Share of Investment and Saving****Investment**

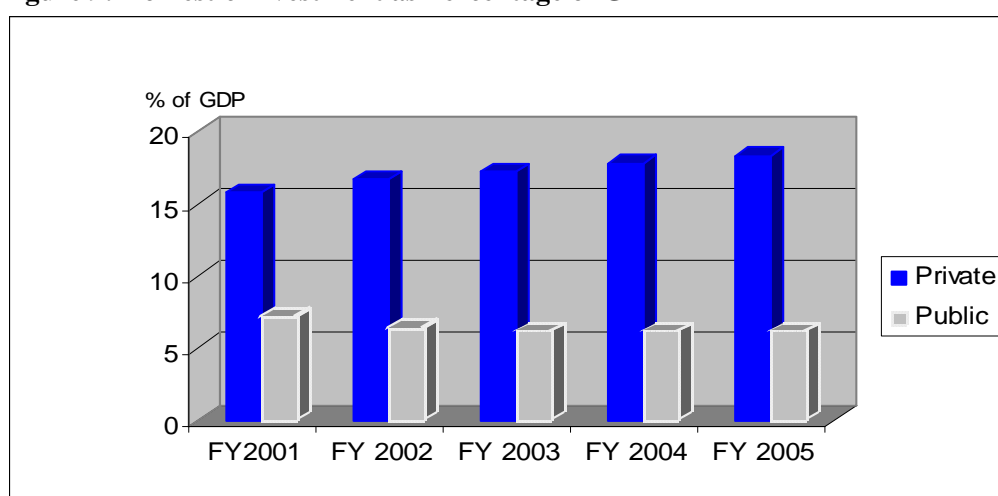
	Billion taka				
	FY2001	FY 2002	FY 2003	FY 2004	FY 2005
Total Investment	585	632	703	800	909
Private	401	458	517	594	679
Public	184	174	186	206	230

**Savings**

	Billion taka				
	FY2001	FY 2002	FY 2003	FY 2004	FY 2005
Gross Domestic Savings	456	496	560	651	742
Private	431	466	523	606	690
Public	25	30	37	45	52

Source :Bangladesh Bank

Privet sector investment grew 13.8% and 13.6% in FY 2004 and FY 2005 respectively indicating a strong private sector credit growth in the recent years.

**Figure 9: Domestic Investment as Percentage of GDP**

Source: Bangladesh bank

**Capital Stock**

Two stock markets Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE) are operating in two major cities in Bangladesh. In the year 1997 stock market suffered a major setback. Stock prices rocketed sky-high through some creating of artificial demand supply situation. General investors suffered a huge sock which took many years to recover. In recent years investors are again turning to stock markets. Steadily increasing stock exchange indexes are reflecting a growing confidence of the investors.

DSE is the major market place which virtually controls the overall stock market of the country. In year 2004 and 2005, DSE experienced strong momentum in every aspect of the market. In the year 2004, market capitalization grew a massive 130%. In year 2005 value of issued capital grew impressive 41.95. Yearly average and average daily transactions are also grew strongly in the year 2004 and 2005.

**Table 16: Investment Trends at Dhaka Stock Exchange**

	2001	2002	2003	2004	2005
<b>Listed Issues</b>					
No. of Securities	249	260	267	256	286
% of Annual Growth	3.32	4.42	2.69	4.12	11.72
<b>Issued Capital &amp; Debenture</b>					
Value million US\$	583.40	606.95	788.61	846.72	1,062.77
% of Annual Growth	6.61	5.86	30.83	7.55	41.95
<b>Market Capitalization</b>					
Value million US\$	1,118.75	1,228.65	1,668.53	3,831.78	3,522.90
% of Annual Growth	1.34	11.75	36.74	130.04	3.62
<b>Total Turnover:</b>					
Volume in million	1,107.20	1,309.14	612.74	681.38	883.30
Value million US\$	699.46	603.18	327.95	902.91	979.98
% of Annual Growth	(1.00)	(12.25)	(45.25)	177.68	21.91
<b>Daily Average Transaction :</b>					
Volume in million	4.15	4.56	2.14	2.55	3.42
Value million US\$	2.62	2.26	1.15	3.37	3.80
% of Annual Growth	2.70	(12.25)	(48.89)	196.33	26.64

Source: Dhaka Stock Exchange, Years are Calendar Year

### Money Supply

In FY 2005 the central bank continued with growth supportive accommodative monetary stance. Robust growth in private sector credits, targeted growth of GDP and growth in imports were broadly supported expansionary monetary policy. However, cautious and restrained monetary policy has been pursued from the middle of FY2005 to maintain price stability by restraining the robust growth rate of private sector credit. Various instruments like repo, reverse-repo, higher rate of treasury bills and higher rate of cash reserve requirement are used to keep credit supply within a reasonable limit.

In FY 2005 broad money (M2) was increased by Tk. 218.15 billion (16.8 %) from that of the previous year. In FY2004 Broad money (M2) was increased by Tk.157.80 billion (13.8 %). In FY 2005 currency in circulation increased by 17.1 % while demand deposit and time deposit showed an increase of 15.9% and 16.9 % respectively from that of the previous year. Increased usage of broad money in FY2005 indicates that credit to the public sector increased by Tk.36.84 billion (16.8 %) whereas credit to the private sector increased by Tk. 161.05 billion (17 %).

**Table 17: Money Supply**

Particulars	Billion Taka		
	FY 2005	FY 2004	FY 2003
1. Broad Money (M2) (a+b+c)	1515.9	1297.7	1139.945
a) Currency notes and coins with the public	185.2	158.1	139.018
b) Demand deposit	170.3	146.9	128.416
c) Time deposit	1160.4	992.7	872.511
2. Broad money (M2) (a+b)	1515.9	1297.7	1139.945
a) Net foreign assets of the banking system	186.7	163.3	140.94
b) Net domestic assets of the banking system ((1)+(2))	1329.2	1134.4	999.005
(1) Total domestic credit of the banking system (i+ii+iii)	1475.6	1255.5	1097.168
i) Government sector (net)	256.3	219.5	192.797
ii) Public sector (other)	111.9	89.7	75.435
iii) Private sector	1107.4	946.3	828.936
(2) Other assets (net)	-146.4	-121.1	-98.163

Source: Bangladesh Eco. Review 2005

## Employment

According to Labor force survey 2002-03 by Bangladesh Bureau of statistics, 51.69% of the total work force is engaged in agricultural sector. Through 1995-96 to 2002-03 share of labor force engaged in agriculture increased by 2.84%, while during the same period share of labor force engaged in industrial sector increased marginally 0.34%.

**Table 18: Share of Employed Labor Force (Above 15 years) by Sector**

	Percentile		
	1995-96	1999-00	2002-03
Agriculture, forestry and fishery	48.9	50.8	51.7
Mining & quarrying	-	0.5	0.2
Manufacturing	10.1	9.5	9.7
Power, gas & water	0.3	0.3	0.2
Construction	2.9	2.8	3.4
Trade, hotel & restaurant	17.2	15.6	15.3
Transport, maintenance & communication	6.3	6.4	6.8
Finance, business & services	0.6	1.0	0.7
Commodities & personal services	13.8	13.1	5.6
Public administration and defense	-	-	6.3
Total	100	100	100

Source: Labor Force Survey, 1995-96 , 1999-00 & 2002-03 BBS.

Male participation in labor force is much higher than female labor force participation. In year 2002-03, 22.1% of active labor force was female which is a bit higher since in the previous survey in year 1999-2000 showing 20.3 % of active labor force was female. Unemployment rate remained steady in the last few years.

**Table 19: Indicators of Labor and Manpower Sector**

	million		
	1995-96	1999-2000	2002-03
Total civilian labor force			
Both Sex	36.1	40.7	46.3
Male	30.7	32.2	36
Female	5.4	8.5	10.3
Active civilian labor force (Employed population)			
Both Sex	34.8	39	44.3
Male	29.8	31.1	34.5
Female	5	7.9	9.8
Unemployed Population			
Both Sex	1.3	1.8	2
Male	0.9	1.1	1.5
Female	0.4	0.7	0.5
Unemployment Rate (excluding underemployment)			(Percent)
Both Sex	3.5	4.3	4.3
Male	2.8	3.4	4.2
Female	7.8	7.8	4.9

Source: Labor Force Survey, Bangladesh Bureau of Statistics

A significant number of Bangladeshi workforce work outside of the country and contribute hugely to the foreign exchange income. In FY 2005, total 250,000 expatriates worked outside of the country and remitted 3848.3 million US\$ in the country. This figure equals 44.9% of the total national export income.

**Table 20: Inward Remittance Flow**

	No of expatriates	Remittance Income		Export Income	Remittance
	thousand	million US\$	million Taka	million US\$	as % of export income
FY 2005	213	3848.3	236,470	8573	44.89
FY2004	195	3372.0	198,698	7521	44.83
FY 2003	251	3062.0	177,288	6492	47.17
FY 2002	277	2501.1	143,770	5929	42.18
FY 2001	250	1882.1	101,700	6419	29.32

Source: Bangladesh Bank

## II.2 Fiscal Position

### Government Expenditure

As it is quite commonly adopted by other developing countries, Government of Bangladesh also chooses to adopt deficit financing for its annual budgets. In FY 2005, budget deficit and domestic borrowings were at sustainable level. Budget deficit was estimated at 4.5% of the GDP, which actually went down to 3.5 % of GDP due to lower than projected implementation of Annual Development Programs (ADP) under development budget.

**Table 21: Composition of Financing of Budget Deficits**

(As percentage of GDP)

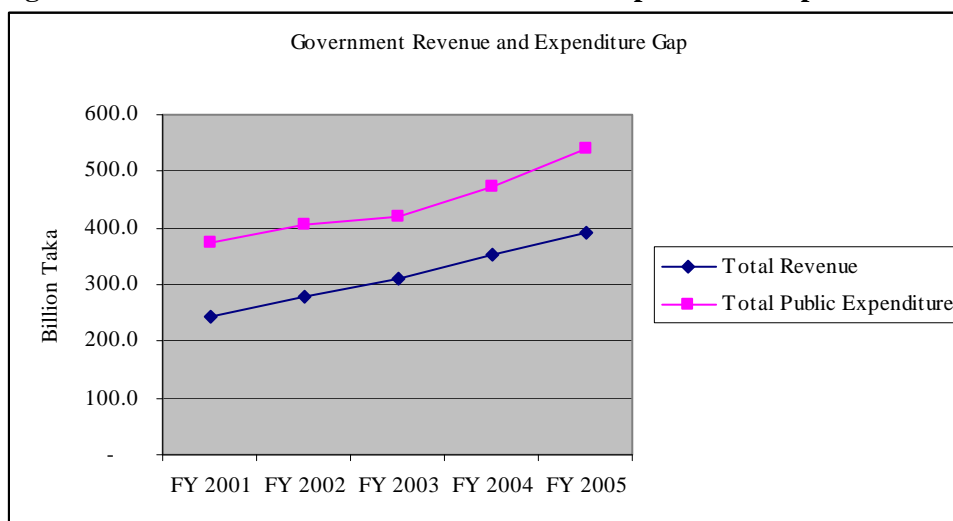
	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
Overall budget deficit (excluding foreign grants)	5.1	4.7	4.2	4.2	4.5
Foreign financing	2	2.1	2.3	2.4	2.4
Domestic Financing	2.8	2.6	1.9	1.8	1.8

Source: Bangladesh Economic Review 2006

Widening gaps in government revenue and public expenditures are triggering increasing budget deficits.



**Figure 10: Trends of Government Revenue and Expenditure Gap**



Source: Bangladesh Economic Review 2006

In Bangladesh government expenditure budget is allocated in two broad categories: Revenue Budget and Development Budget. A good portion of development budget is financed by foreign loans, foreign grants and local finances.

**Table 22: Composition of Government Development and Non Development Expenditure**

	Billion Taka				
	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
Non development expenditure	205.36	227	253.07	283.9	333.24
Development expenditure	159.01	150.5	152.71	168.17	187.71
other expenditure	9.62	30.08	14.97	19.77	18.08
<b>Total Public Expenditure</b>	<b>373.99</b>	<b>407.57</b>	<b>420.75</b>	<b>471.84</b>	<b>539.03</b>

Source: Bangladesh Economic Review 2006

The major head of revenue expenditure is government pay and allowances. In FY 2005, government had to spend 22.4% of its revenue income for pay and allowances. Interest repayment accounted for 14.8% of total government revenue in FY 2005.

**Table 23: Major Heads of Non Development Revenue Expenditure**

	Billion Taka			
	FY 2002	FY 2003	FY 2004	FY 2005
Pay and Allowances	68.01	72.82	79.13	87.62
Goods and services	34.52	42.65	48.8	57.94
Interest Payment	45.2	55.74	58.42	65.03
Subsidies and current transfer	59.15	70.84	81.86	104.37
Block allocations	12.31	5.66	4.41	6.34
Resource collection and public works	11.06	10.53	15.83	17.33
<b>Total</b>	<b>230.25</b>	<b>258.24</b>	<b>288.45</b>	<b>338.63</b>
Deduction	3.33	5.17	4.55	5.4
<b>Total</b>	<b>226.92</b>	<b>253.07</b>	<b>283.9</b>	<b>333.23</b>

Source: Bangladesh Economic Review

In Bangladesh still around 80% of the total population are rural inhabitants. Naturally, for annual development programs rural population gets the most priority. Rural development, electricity, transportation and education are the major areas where government allocates most resources for its development budget. For rapid urbanization and expansion in industrial sector demand for electricity and gas is increasing very quickly. The Government is already facing very difficult time to meet the surge in demand for electricity. To meet the future demand, allotment of resources in energy sector is increasing rapidly.

**Table 24: Major Heads of Development Expenditure**

	Percentile			
	FY 2002	FY 2003	FY 2004	FY 2005
Rural development	11.1	10.09	13.8	14.3
Water Resource	5.4	4.29	4.0	2.4
Industry	1.9	1.14	2.7	2.4
Electricity	12.1	13.7	17.3	20.7
Oil, gas and mineral resource	3.1	4	5.2	6.0
Transportation	19.9	16.15	18.0	12.3
Communication	6.1	3.63	2.2	2.9
Infrastructure, water supply and housing	6.6	5.61	5.9	6.0
Education	14.2	13.88	12.3	13.7
Health	7.9	6.72	8.3	8.2
Agriculture	4.4	3.74	4.0	3.6
others	7.4	17	6.2	7.4
Total	100	100	100	100

Source: Bangladesh Economic Review 2006

### Public Borrowings

Apart from foreign loans and grants; the government has to borrow money from internal source to finance the budget deficits. Government borrows money from Bangladesh Bank, commercial banks and through issuance of government bonds and savings certificates. In FY 2005 government borrowed total Taka 66.08 billion from domestic sources which was 9.1% lower than that of the previous year. Public borrowings as percentage of GDP decreased from 2.2 % in FY 2004 to 1.8% in FY 2005. Total domestic outstanding debt as percentage of GDP decreased slightly in FY 2005 than that of the previous year.

**Table 25: Public Debt from Internal Sources**

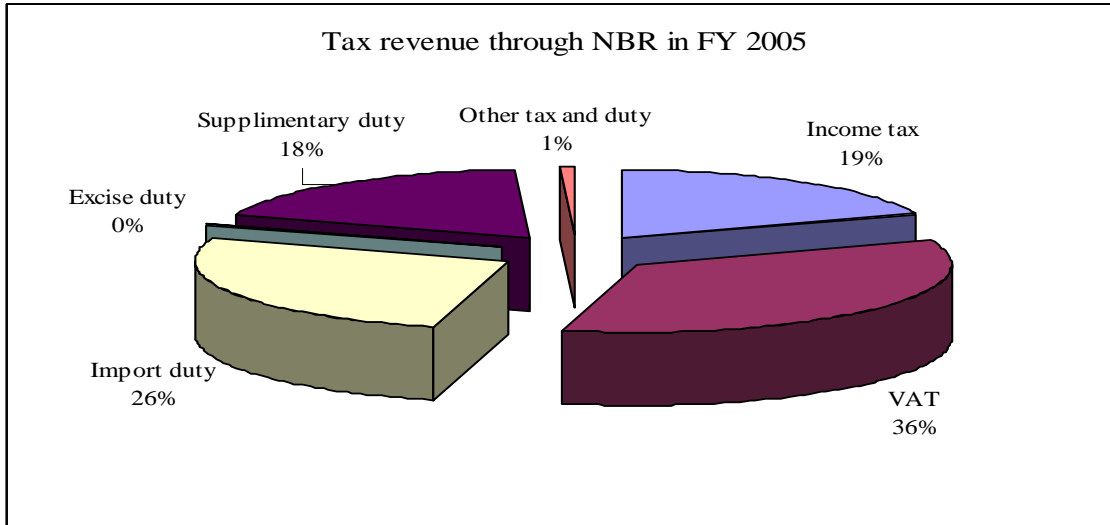
	Loans taken from banking sector			Loans taken from outside of Banking sector	Total internal public debt	Internal debt as % of GDP	Total domestic outstanding debt as % of GDP
	From Bangladesh Bank	From Commercial Banks	Total				
FY 2001	20.09	89.51	29.04	42.08	71.12	2.8	15.00
FY 2002	27.27	-1.58	25.68	47.11	72.80	2.7	16.54
FY 2003	-25.9	16.07	-9.82	47.95	38.13	1.3	16.26
FY 2004	16.53	10.16	26.69	45.99	72.68	2.2	16.43
FY 2005	38.27	-1.42	36.84	29.24	66.08	1.8	16.38

Source: Bangladesh Economic Review 2006

## Tax Revenue

National Board of Revenue (NBR), under Ministry of Finance is the apex authority of the government for collecting tax revenue. In FY 2005 government collected 77.8% of revenue through NBR sources. Import duty together with supplementary duty is still cater the largest share of tax revenue for the government. Value Added Tax (VAT) is second largest source followed by Income Tax. In FY 2005 VAT accounted for 36% of total NBR tax revenue where share of Income Tax was only 19%. These figures reveal the fact that government is largely dependant on indirect tax sources.

**Figure 11: Composition of Tax Revenue by Major Tax type**



Source: Bangladesh Economic Review 2006

Government also collects tax, duty and fees through different central government and local government organizations. Non judicial stamps, interest, dividends, profits, are few other major sources of government revenue.

**Table 26: Tax and Non Tax Revenue Collection by Major Heads**

Billion Taka

<b>NBR Tax Revenue</b>	FY2001	FY2002	FY2003	FY2004	FY2005
Income tax	36.0	41.0	47.9	52.7	58.5
VAT	61.3	69.6	80.7	85.8	106.1
Import duty	47.7	53.5	58.8	73.0	80.0
Excise duty	2.8	3.0	3.1	1.7	1.5
Supplementary tax	33.6	38.5	43.9	54.3	56.0
Other tax and duty	1.6	1.7	3.2	3.1	3.0
<b>Total NBR tax</b>	<b>183.0</b>	<b>207.3</b>	<b>237.5</b>	<b>270.5</b>	<b>305.0</b>
<b>Non NBR tax Revenue</b>					
Narcotics duty	0.40	0.30	0.35	0.40	0.45
Vehicle tax	1.44	1.45	2.25	2.41	2.67
Land revenue	2.14	2.14	2.06	2.59	3.26
Non judicial stamp	7.92	8.11	7.34	7.10	8.12
<b>Total Non NBR tax revenue</b>	<b>11.90</b>	<b>12.00</b>	<b>12.00</b>	<b>12.50</b>	<b>14.50</b>
<b>Non Tax Revenue</b>					
Dividend and Profits	7.74	11.62	8.32	10.54	11.65
Interest	5.50	4.49	7.25	7.50	6.36
Administrative fees	10.22	8.72	7.79	9.64	9.88
Service fees	2.56	2.74	4.72	4.82	4.33
Non commercial sales	2.13	2.52	2.96	3.10	2.64
Railroads	-1.34	3.90	4.15	4.53	4.79
Telegraph and Telephone board	12.60	16.03	16.00	17.02	16.50
Other non tax revenue	7.42	7.38	10.51	13.85	16.35
<b>Total non tax receipts</b>	<b>46.83</b>	<b>57.40</b>	<b>61.70</b>	<b>71.00</b>	<b>72.50</b>
<b>Total revenue receipt</b>	<b>241.73</b>	<b>276.70</b>	<b>311.19</b>	<b>354.00</b>	<b>392.00</b>

Source: Bangladesh Economic Review 2006

### III. Tax Structure: Institutions and the Reality

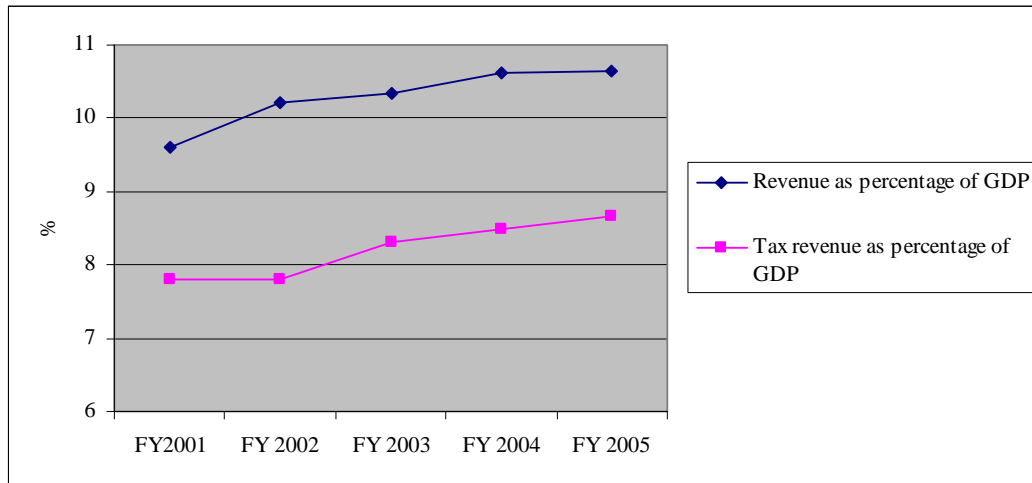
Internal resource is the key for sustenance and development for a nation. Revenue collection scenario in Bangladesh is not yet reached to any impressive stature. For very poor Tax-GDP ratio, government has to finance growing budget deficit through substantive amount of foreign loans and public debts. In FY 2005, Tax GDP ratio was 8.7, while Revenue GDP ratio stood at 10.64. These figures indicate the poorest performance even among the South East Asian subcontinent countries. However, for substantive growth in tax revenue collections, in the recent years, Tax-GDP ratio is increasing steadily.

**Table 27: Revenue-GDP Ratio**

	FY2001	FY 2002	FY 2003	FY 2004	FY 2005
Revenue as percentage of GDP	9.6	10.21	10.35	10.63	10.64
Tax revenue as percentage of GDP	7.8	7.8	8.3	8.5	8.7

Source: Bangladesh Economic Review 2006

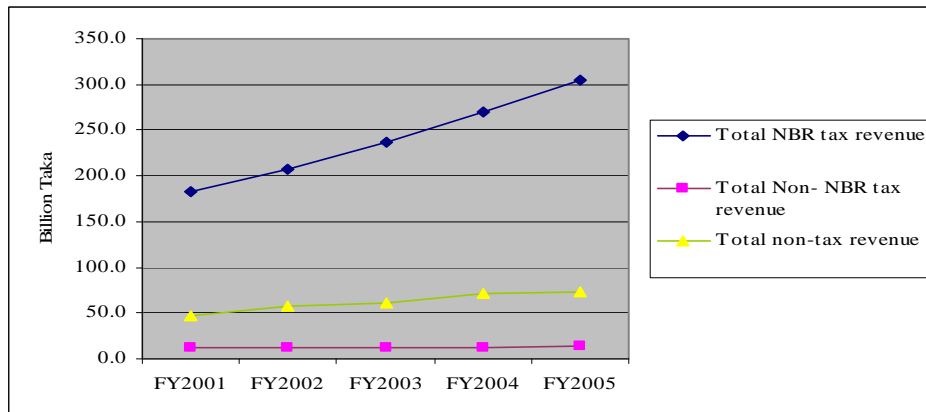
**Figure 12: Growth of Tax- GDP and Revenue- GDP Ratio**



Source: Bangladesh Economic Review 2006

Tax revenue constitutes more than 80% of government revenue receipts. National Board of Revenue (NBR), the authority for collecting tax revenues, registered impressive tax collection growth during the recent years. Over the last few years tax revenue from NBR grew steadily, while growth in non tax revenue sources remained stagnant.

**Figure 13: Tax and Non Tax Revenue Collections Trends**



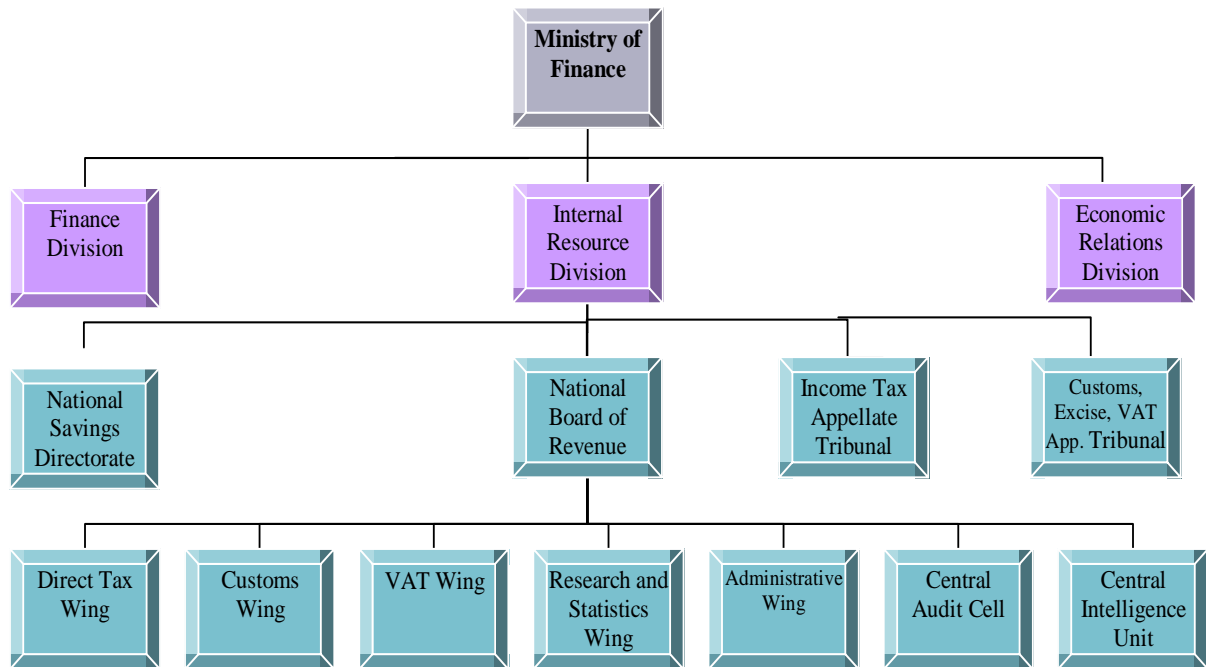
Source: Bangladesh Economic Review 2006

**National Board of Revenue (NBR): The Tax Central Collection Authority**

National Board of Revenue (NBR) is the apex authority of the government responsible for collecting tax revenue, administering taxation administration and framing taxation policies and laws for the government. The main responsibility of NBR is to mobilize domestic resources through collection of Import Duties, VAT, Excise and Income Tax for the Government. NBR through its different taxation sources collects more than 95% of the tax revenue for the government.

NBR was created by a Presidential Order in the year 1972 and placed under Internal Resource Division (IRD) of Ministry of Finance. Secretary of IRD acts as the Chairman of NBR. Four Members (top position of the hierarchy) of NBR from Direct Tax wing and four Members from Indirect taxation wing assist the chairman in executive, legislative and policy matters.

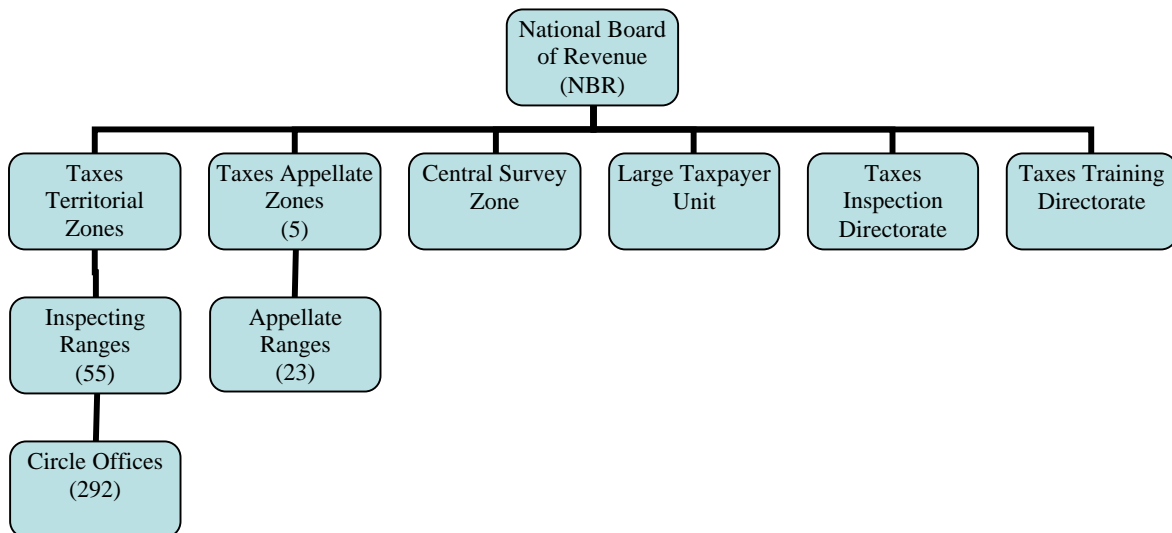
**Figure 14: Organizational Chart of Ministry of Finance and National Board of Revenue (NBR)**



**Direct Tax Administration**

Direct tax wing or generally known as Income Tax Department is responsible for collection of direct taxes like income tax, gift tax, and wealth tax.

**Figure 15: Organizational Structure of Income Tax Department**



**Table 28: Human Resource Position at Direct Tax Administration in FY2006**

Employee Class	Number working
First Class	397
Second Class	132
Third Class	2257
Fourth Class	1348
Total	4134

Source: National Board of Revenue

Income tax department is predominantly administered by old traditional single officer managed circle system. A circle is the administrative unit of tax administration which is generally headed by one class one officer. He is supported by one inspector and few clerks for his day to day operation. A circle is basically the building block of taxes system where the officer in charge is responsible for

- a) Receiving returns
- b) Assessment of returns
- c) Demand creation
- d) Collection of demands/enforcement
- e) Appeals management
- f) Reporting
- g) Administrative factions

There are four types of circles depending of jurisdictions and type of cases it handles. These four types are companies circle, salaries circle, contractors circle and normal circle. As it can be assumed from the names, a typical companies circle handles company cases and individual cases of its directors. Salary circle and contractor circle holds jurisdiction of personal income tax cases of salary holders and contractors respectively. A normal circle holds territorial jurisdiction of sole proprietorship and partnership businesses. However, it is not uncommon for a circle to hold mixed jurisdictions.

Circle office is monitored my inspecting range official. A range officer normally assigned to monitor all functions of 5 to 6 circle offices. Range officer reports to Commissioner of Taxes who is the administrative head of taxes zone.

A Commissioner holds all the administrative authority for overall management of a taxes zone. He monitors every legal and administrative aspect of taxes circles. Normally a taxes zone is consists of four range offices and around 20 circles. A typical circle office normally processes 3000 to 4000 income tax cases a year. Since all these work is done almost manually with no significant support of information technology, managing a circle becomes a daunting task for an officer. There are some circles which handle more than 10000 files, which is almost impossible to manage efficiently by a single officer.

### **Large Taxpayers Unit (LTU)**

After introduction of Large Taxpayers Unit (LTU), direct tax administration is now operating with a combination of old traditional type and functional type taxation administration. In November, 2003 LTU was established with intent to focus more on the largest taxpayers of the country who possesses the most concentration of tax revenue. LTU is responsible for collecting more than 30% of the total income tax revenue. LTU organization arranged around 4 core factions of a typical tax administration

1. Taxpayer Services Wing;
2. Revenue Accounting Wing;

3. Tax Collection Enforcement /Appeal Wing;
4. Audit Wing;

In the organizational design audit function has the most emphasis. Major portion of human resource is allocated for audit function of LTU. Basic activities of each functional wing are the followings

1. Taxpayers service wing
  - a. Providing taxpayers education
  - b. Receiving returns and payments
  - c. Apprising taxpayers of changes in tax laws
2. Revenue accounting wing:
  - a. Maintaining records of demand and payments
  - b. Making all correction, revision of demand
  - c. Maintaining all statistics audit report
3. Collection, enforcement/appeal wing
  - a. Monitoring of collection of advance tax, outstanding tax
  - b. Impose penalty on non-filers and defaulters
  - c. Filing appeal before Tribunal, High Court
  - d. Enforcement such as seizure, freezing, civil suit
4. Audit wing
  - a. Selecting audit cases
  - b. Determining audit points
  - c. Test and verification of audit points
  - d. Confront the audit findings with the taxpayer
  - e. Determine the tax payable as per audit

This reform attempt is still at its infancy; however, so far the results achieved are quite impressive.

### **Income Tax Mechanism**

A taxation cycle starts when a taxpayer submits his or her return. Taxpayers are required to submit income tax return by September 30 each year at their respective circle. A taxpayer can choose to submit her return basically either under Self Assessment System (SAS) or under Normal system. For LTU and Corporate taxpayers some other provisions apply. To qualify for SAS, a taxpayer must satisfy some certain conditions. A return submitted under SAS is treated as accepted and finalized unless it falls under risk based audit system.

In the second phase of the cycle, returns are scrutinized. The returns submitted under normal system and found suspicious or found not supported with enough evidence, receive notice for submitting required documents or appearing for personal hearings. After verifying additional records or after hearing and occasional audits the case is resolved. The officer then issue an assessment order together with a demand notice if additional demand is due from the taxpayer. Tax payer then can choose to go for appeal or can pay the demand. If she without doing an appeal fails to pay the tax within the specified period, tax office can impose penalty and take coercive actions to collect the demand. If a return submitted under SAS, and gets selected for audits, is treated as a return submitted under normal system and the same assessment procedure applicable for normal returns is followed.

### **Rights and Obligation of a Taxpayer**

Income Ordinance 1984 ensures certain rights of the taxpayers. At the same time it imposes some obligations.

### **General Rights**



1. Taxpayer is entitled to receive professional service and assistance from the Taxes office including supply of forms and brochures.
2. Taxpayer may either represent himself for any of his tax matters or, engage an authorized representative as provided in the law.
3. Taxpayer is entitled to have access to his own tax records held by the Taxes office.
4. The Tax Authorities are required to act impartially and use their powers in a fair and professional manner.
5. Burden of proof is shifted to the tax authority in figuring admissible disallowance or deduction.
6. The taxpayer has a right to be heard before a penalty is imposed.
7. Tax payer has the right to appeal against decision passed by the tax authority
8. The taxpayer is entitled to instant refund as soon as it becomes due
9. A taxpayer is entitled to 7.5% interest per annum on the unpaid refund if refund due is not paid within 2 months
10. Collection cannot be enforced on a taxpayer so long as his appeal is not disposed of
11. In certain situations, taxpayer may avail installment payment of arrears
12. Taxpayer enjoys a confidentiality privilege [protection of information]
13. A taxpayer applying for a Taxpayer Identification Number (TIN) in a prescribed manner becomes entitled to be registered with the tax authority
14. A taxpayer is protected from unilateral authoritarian action of the Revenue under a specific law enacted for the purpose
15. Taxpayers performing as withholding agents are indemnified for deduction or retention or payment of tax on behalf of other taxpayers

### **Obligations of a Taxpayer**

1. Taxpayer is required to file correct return by disclosing all his income, provide supporting documents and pay due tax within the time limit specified by law.
2. Taxpayer is required to pay advance tax on a four quarterly basis if his latest assessed income exceeded 200000 taka.
3. An individual taxpayer is obliged to provide details of his assets and liabilities as well as particulars of his lifestyle in the return.
4. A Taxpayer is required to comply with statutory notices issued by the tax authority.
5. A Taxpayer is required to furnish to the tax authority correct and accurate particulars of his income.
6. A Taxpayer having commercial transaction is required to maintain accounts in the prescribed manner.
7. A Taxpayer is obliged to furnish certificate, statement, accounts and information as required by the law
8. A Taxpayer having income from business or profession is obliged to display TIN certificate at a conspicuous location of his business premises.

9. A Taxpayer owning a property is obliged not to the transfer or otherwise deal with the said property following the receipt of notice of attachment issued by Tax Recovery Officer.

### Consequence of Default

	Nature of Default	Penalty applicable
1.	Failure to file return of income in due time.	(a) 10% of the tax imposed on last assessed income; (b) for continuing default Tk. 250 per day; (c) minimum penalty Tk. 2500
2.	Failure to furnish certificate, statement, accounts, information	(a) Tk. 500 (b) for continuing default, Tk. 250 per month.
3.	Failure to display TIN certificate	(a) Tk. 500 (b) for continuing default, Tk. 250 per month.
4.	Failure to maintain accounts of commercial transaction in the prescribed manner.	(a) An amount not exceeding 1.5 times of the tax payable. (b) For income below threshold limit, maximum penalty is Tk. 100
5.	Failure to pay minimum 80% of the admitted liability	Not exceeding 25% of the unpaid tax.
6.	Failure to pay advance tax	An amount not exceeding the short payment.
7.	Failure to comply with statutory notices	An amount not exceeding the tax changeable on total income.
8.	Concealment of income or furnishing inaccurate particulars thereof or understatement of the sale value of immovable property.	(a) Not exceeding 2.5 times of the evaded tax (b) Not exceeding 5 times of the evaded tax in self-asst. cases.

### Punishment for non-compliance of certain obligations

	Nature of noncompliance	Punishment
1.	a) failure to deduct or collect and pay tax as required under the relevant provisions except advance payment of tax b) failure to comply with third party obligation c) failure to produce, accounts, documents or statements; d) failure to furnish return of income; e) refusing to permit inspection or to allow copies to be taken in accordance with the provisions of f) failure to extend required co-operation to an income tax authority exercising powers g) refusing to permit or obstructing the exercise of powers by an income tax authority	maximum one year imprisonment or with fine or both
2.	a) making false statement in any verification in any return or document furnished b) aiding, abetting, assisting, inciting or inducing another person to make or deliver a false return account, statement, certificate or declaration. c) making or delivering himself knowingly and willfully any false return, account, statement, certificate or declaration on behalf of another person; d) signing and issuing any false certificate e) refusing to furnish required information	3 months to 3 years imprisonment or with fine or both.
3.	Concealment of income and furnishing inaccurate particulars thereof	3 months to 5 years imprisonment or with fine or both.
4.	Transferring property to pre-empt attachment by Tax Recover Officer	Maximum 5 years imprisonment or with fine or with both.

Note: No prosecution can be instituted except with the previous approval of the National Board of Revenue.

## Appeal

A taxpayer aggrieved with the assessment may choose to go for appeal and can choose among the following alternatives. In fact, taxpayers have a quite many and lengthy choices in their hand in this regard.

1. Can apply for commissioner's review. In this case, the Taxes Commissioner who controls the circle where the original assessment was made may review the assessment. In this case, the appellant must waive his further right to appeal. The decision passed by the commissioner is treated as final disposal of the case.
2. The appellant can choose to go to the appellate authority of the department.
3. If the appellant is still unsatisfied with the order passed by the appellant authority, she can choose to appeal the case in the Taxes Appellate Tribunal. This appellate authority is independent from the income tax department and is the highest appellate authority in the matter of factual grounds.
4. Still aggrieved with the decision of Taxes Appellate Tribunal, the taxpayer with enough legal ground can further make a reference to the High Court Division of the Supreme Court of the country. Finally, the aggrieved taxpayer may finally appeal against the verdict of High court Division to Appellate Division of the Supreme Court.

## Registration and Return submission

For income tax purpose, each taxpayer is assigned with a unique Taxpayer Identification Number (TIN). To become a taxpayer, every individual or company required to take a TIN. TIN is a computer generated 10 digit number which remains unchanged for a taxpayer for good. At the end of June 2006 total number of TIN stood at 1.78 million. For a country with a population over 140 million, this numbers seems very unimpressive. Moreover, many of these TIN holders are not active taxpayers.

## Income Tax Rates

Applicable individual and corporate income tax rates for FY 2004 and 2005 were:

**Table 29: Income Tax Rates for Individuals**

	Income slab	Rate
(i)	On first Tk. 1,00,000/- of total income	Nil
(ii)	On next Tk. 2,00,000/- of total income	10%
(iii)	On next Tk. 2,50,000/- of total income	15%
(iv)	On next Tk. 3,50,000/- of total income	20%
(v)	On the balance of total income	25%

Note: For non resident non Bangladeshi tax rate is flat 25%

**Table 30: Income Tax Rates for Corporations**

	Type of Company	Rate
(i)	Publicly traded companies (excepting Bank, Insurance, Leasing Companies & other financial Institution)	30%
(ii)	Non-publicly traded companies (excepting Bank, Insurance, Leasing Companies & other financial institution)	37.5%
(iii)	Bank, Insurance, Leasing Companies & other financial institution	45%

### Scope of Withholding Tax and Rates

Over the years, tax administration of Bangladesh is expanding areas of withholding tax net. Around 75% of income tax revenue comes from tax withheld at source. Withholding tax administration has been a major weakness for the tax administration of Bangladesh. In recent years, tax administration is putting much emphasis on this area. At present there are 32 heads on which deduction or collection of tax at source is applicable.

**Table 31: A Summary of the Deduction and Collection of Tax at Source (Withholding Tax)**

Sl. No.	Source on which tax to be deducted/collected Source on	Rate of deduction/collection
1.	Salary	Annual average rate of individual tax payers
2.	Discount on Bangladesh Bank Bill	Individual 25% Company - Rate applicable to company:
3.	Interest on security	10%
4.	Contract & Supply	According to prescribed rate schedule
5.	Indenting Commission	3.5%
6.	Shipping Agency Commission	5%
7.	(a) Services rendered by doctor in any hospital or diagnostic centre.	5% of the amount of fees for services rendered
	(b) Royalty or Technical - know how fees	10%
	(c) Professional or technical services fees	5%
8.	(a) Stevedoring Agency Commission	5%
	(b) Private security service	0.75%
9.	Clearing & Forwarding Agents Commission	5%
10.	Cigarette Manufacture	4% o the value of Banderol
11.	Compensation against acquisition of property	6%
12.	Interest on savings instruments	5%
13.	Brick Manufacture	(a) Tk. 7500/- for one section brickfield; (b) Tk. 10,000/- for one and half section brickfield; (c) Tk. 15,000/- for two section brickfield.
14.	L.C. Commission	5%
15.	Import	3% of the value of imported goods.
	House property income	Monthly rent Tk. 15,000: Nil; Up to Tk. 35,000/- : 3% above Tk. 35,000/- : 5%
17.	Shipping business	4% of total freight
18.	Manpower export	10% of service charge or fees
19.	Export of Garments (Knit & woven)	0.25% of export proceeds
20.	Value of Stocks/Shares	0.015% on the stock value
21.	Public Auction	3% of the Sale value
22.	Performance in film	5%
23.	Commission/discount or fees	5%
24.	Foreign buyers agency commission	2.5%
25.	Interest on Bank Deposits	10%
26.	Real Estate Business	Building or apartment: Tk. 175/- per square meter; Land: 2.5% of the value of land.
27.	Insurance Commission	5% of the commission above Tk 40,000
28.	Fees etc. of surveyors of general insurance company	5%
29.	Transfer of Property	5% of the deed value
30.	Dividend	(a) Resident individual 10%; (b) Non-resident individual 25%; (c) Company both resident & non resident 15%
31.	Lottery	20%
32.	Income of non-resident	Individual: 25%; Company: rate applicable to receiving company

### **Double Taxation Avoidance Treaty**

The Income Tax Policy section of the National Board of Revenue (NBR) is entrusted to negotiate the Double Taxation Avoidance Agreement (DTA) with foreign countries to eliminate double taxation and thus to promote foreign direct investment in Bangladesh.

The objectives of a Bangladesh Double Taxation Avoidance Agreement are as follows:

- To obtain a more effective relief from double taxation compared to relief gained under unilateral measures;
- To create a favorable climate for the inflow of foreign investment into the country;
- To make special tax incentives provided by Bangladesh fully effective for taxpayers of capital exporting countries; and
- To prevent evasion and avoidance of tax.

In the year 1980, Bangladesh concluded its first Bangladesh double taxation avoidance agreement ever with United Kingdom. So far, Bangladesh concluded signing double taxation avoidance treaty with 23 countries. Double taxation avoidance treaties with the following countries are in force.

**Table 32: List of Countries having Double Taxation Avoidance Agreement with Bangladesh**

No.	Country name	Conclusion year
1	United Kingdom	1980
2	Singapore	1982
3	Sweden	1983
4	Republic of Korea	1984
5	Canada	1985
6	Sri Lanka	1988
7	Pakistan	1988
8	Romania	1988
9	France	1989
10	Malaysia	1990
11	Japan	1991
12	India	1993
13	Germany	1994
14	Netherlands	1994
15	Denmark	1997
16	China	1997
17	Italy	1997
18	Belgium	1998
19	Thailand	1998
20	Poland	1999
21	Turkey	2004
22	Norway	2004
23	The United States of America	2006

Source: National Board of Revenue

The countries now in the advanced stage of entering into such deals on avoidance of double-taxation with Bangladesh are Indonesia, Mauritius, Qatar, Myanmar, Saudi Arabia, Switzerland, Russia, Nepal, Iran, Uzbekistan, South Africa and Morocco.

Though it is not explicitly mentioned, since Bangladesh is a capital importing country, it prefers to follow the UN Model Treaty. Similar to the UN Model Treaty, the Double Taxation Avoidance Agreements Bangladesh so far concluded with other countries generally has 29 articles.

### **Indirect Tax Administration**

Indirect tax administration basically divided into two broad wings, one is VAT wing and the other one is Customs wing. Personnel are appointed exclusively for indirect tax administration, and officials work in different wings of indirect tax administration in a regular rotation.

**Table 33: Human Resource Working for the Indirect Tax Administration during FY2006**

Employee Class	Number working
First Class	552
Second Class	1693
Third Class	2762
Fourth Class	381
Total	5388

Source: National Board of Revenue

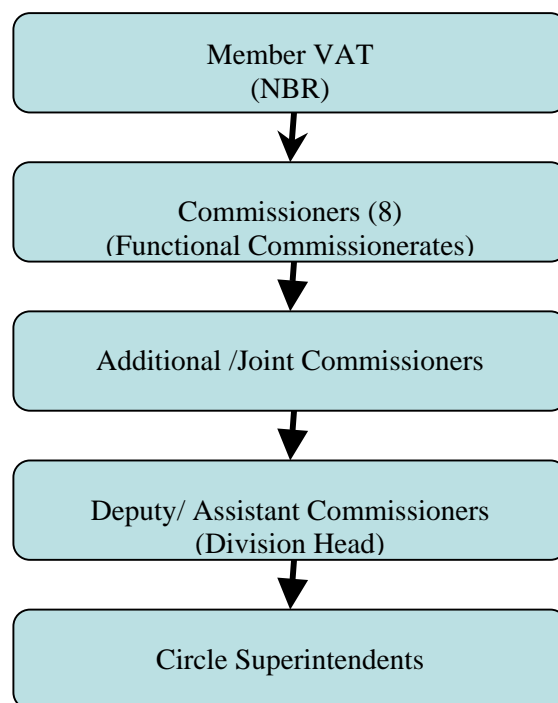
**Value Added Tax (VAT) Wing**

Value Added Tax (VAT) was first introduced in Bangladesh in the year 1991 by partially replacing the Excise Duty and wholly the sales tax at the import stage. In Bangladesh, only a single rate of VAT 15% is prevailing. However in some cases base value for VAT is truncated.

**VAT Administration**

VAT administration is one of the three wings of National Board of Revenue (NBR). Under the direct supervision and control of the Chairman NBR, Member (VAT) of NBR works as the head of operational and administrative activities of VAT administration. At present there are eight VAT Commissionerates all over Bangladesh each headed by a Commissioner of VAT. The Commissionerates are Dhaka (south), Dhaka (North), Rajshahi, Jessore, Khulna, Sylhet Chittagong, and VAT Large Taxpayers’ Unit (LTU). Each VAT Commissionerates has five to eight divisions which are headed by Divisional Officers who may be Deputy Commissioners or Assistant Commissioners. Under each VAT Division there are two to five circles which are headed by Superintendents. These circles are the basic building block of VAT administration. However, the head of each VAT division plays the most significant role for VAT collection and administration in the field level. Commissioners, Additional Commissioners, Joint Commissioners usually monitor and supervise the functions of VAT circles.

**Figure 16: VAT Organogram**



### VAT Mechanism

VAT system in Bangladesh operates under the legal framework of Value Added Tax Act 1991 and Value Added Tax Rules 1991 made under Value Added Tax Act 1991. As per VAT Act at a flat rate of 15% is chargeable on all goods and services imported in Bangladesh and on all goods and services produced in Bangladesh at every stage when the title of the goods and services of the concerned transaction is transferred. However there is exception for certain the goods and services listed in the first schedule and second schedule of VAT act 1991 respectively. The exempted items are basic agricultural products, live animals and animal products, education, books, magazines, newspapers, postal services and passengers and goods transportation services etc. Besides, according to the law, any person engaged in the business of goods and services subject to VAT having yearly sale of less than Taka two million has to pay Turn-over Tax (TT) instead of VAT, at the rate of 4% on the amount of the yearly sale. Any person doing the business in goods and services subject to VAT has to pay VAT under self clearance procedure. The person is required to comply with following procedures prior to clearing goods and services from taxpayer's premises:

- Get registered with VAT authority, collect Business Identification Number (BIN) which is referred in all matters relating to VAT.
- Submit value declaration – the basis for imposing VAT i.e. price per unit on which rate of VAT to be charged- and get it approved of VAT authority (basically Divisional Officer).
- Maintain prescribed books and record:

### VAT Collection Trends

VAT at this moment, is the most dominating revenue sources of the government. In FY2005, VAT revenues constituted 36% of the total tax revenue and 27% of the total revenue collection, making it to be the largest piece of the tax revenue pie. VAT collection is growing very rapidly over the last decade. In FY 2005 VAT achieved an impressive 23.7% growth.

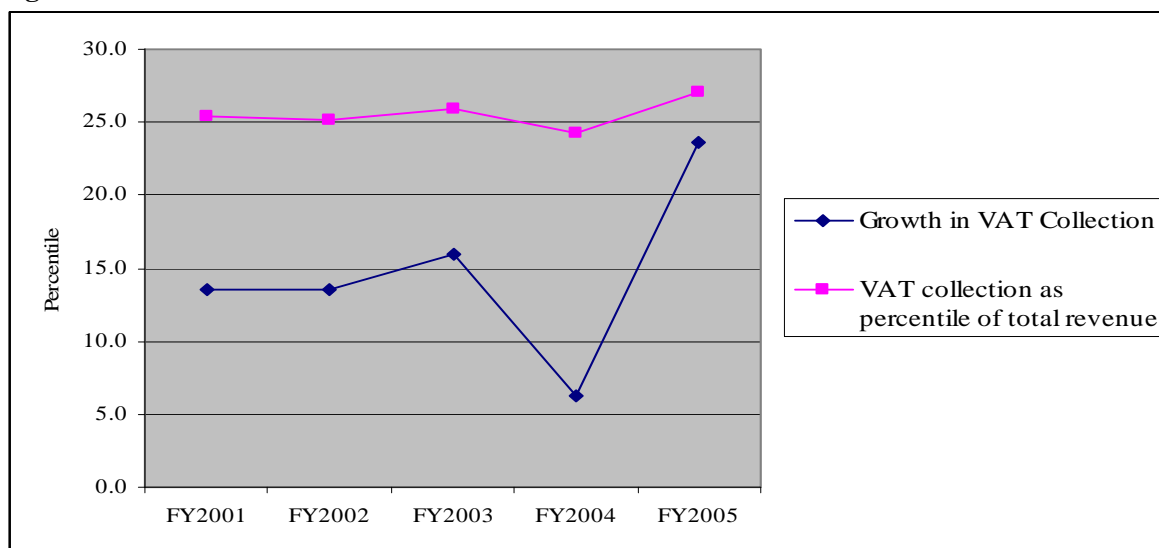
**Table 34: VAT Collection Scenario**

(Figures: Billion Taka and Percentile)

	FY2001	FY2002	FY2003	FY2004	FY2005
VAT Collection	61.32	69.6	80.71	85.75	106.05
Growth in VAT Collection	13.6	13.5	16.0	6.2	23.7
VAT collection as percentile of total revenue	25.4	25.2	25.9	24.2	27.1
Total revenue receipt	241.7	276.7	311.19	354	392

Source: Bangladesh Economic Review 2006

**Figure 17: Trends in VAT Collection**



Source: Bangladesh Economic Review 2006

### Customs and Excise Wing

Customs Wing is responsible for the collection of customs duties on all imported goods. Customs, Excise and VAT wing has 18 major offices including 4 customs houses, 7 Customs, Excise and VAT Commissionerates. At present International trade (Export-Import trade) is conducted through Dhaka, Chittagong, Benapole, and Mongla Custom Houses and through a few Land Customs Stations. There are total 101 declared duty stations round the country, among those 48 are active. Over the last decades consistent efforts have been made to rationalize the tariff structure in line with the world wide tariff liberalization trends. Now tariff structure has only three slabs. Tariff slabs have been reduced from 7.5%, 15%, and 25% in FY 2005 to 6%, 13% and 25% in FY 2006. However, present supplementary duty structure has six slabs 20%, 35%, 65%, 100%, 250% and 350%. Custom administration is quite similar to that of the VAT administration.

### Customs Duty Collection Trends

Still import duty shares around 26% of the government tax revenue. Together with supplementary duty, government earns around 44% of tax revenue from duties, which makes it the largest revenue contributing source of the government. However, total share of customs duty in total revenue collection is in a reducing trend. In FY 2005 customs duty shared 14.3% of total revenue collection, compared to 15.3 % in FY 2005.

**Table 35: Customs and Supplementary Duty Collections**

(Figures: Billion Taka and Percentile)

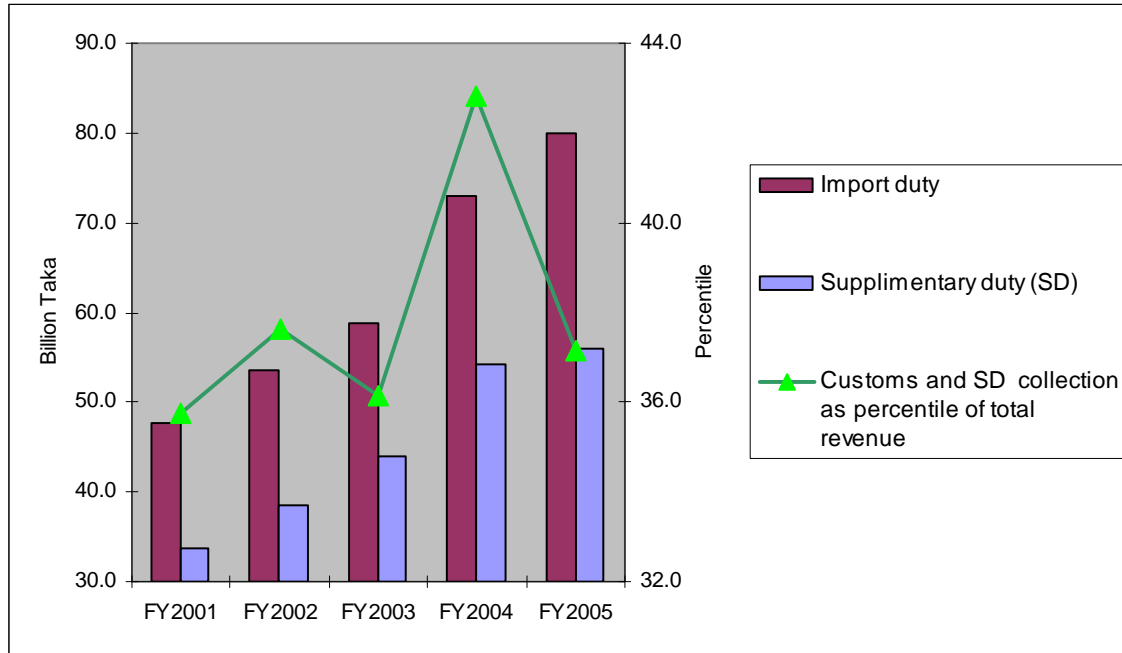
	FY2001	FY2002	FY2003	FY2004	FY2005
Import duty	47.7	53.5	58.8	73.0	80.0
Growth in import duty collection	5.1	12.2	9.8	24.3	9.6
Supplementary duty (SD)	33.6	38.5	43.9	54.3	56.0
Total Import and SD	86.4	104.2	112.5	151.6	145.6
Customs duty collection as percentile of total revenue	13.9	13.9	14.1	15.3	14.3
Customs and SD collection as percentile of total revenue	35.7	37.6	36.1	42.8	37.1
Total revenue receipt	241.7	276.7	311.2	354	392

Source: Bangladesh Economic Review 2006



Contribution of both Customs Duty and Supplementary Duty to total revenue is showing a decreasing trend. This missing gap of revenue is getting filled up by increasing VAT and Income Tax collections.

**Figure 18: Trends in Customs and Supplementary Duty Collections**



Source: Bangladesh Economic Review 2006

## IV. Country Specific Fiscal Issues

### A. Modernization of Revenue Management

Tax base of Bangladesh is extremely narrow in every sense. In a country with a population over 140 million, number of registered taxpayer is only 1.7 million. As a obvious result, in FY 2005 tax GDP ratio was only 8.7, while Revenue GDP ratio stood at 10.64. These figures are even the poorest in the South East Asian region. Bangladesh revenue administration is highly dependant on indirect sources of revenue. Income tax collection shares only around 17% of the total tax revenue collection. Revenue administration did not go through any comprehensive reform in the last few decades. As a result, the prevailing traditional revenue management system is not well integrated, and also not effectively information technology enabled. The tax administration is already facing extreme difficulties to handle the present tax base, when a rapid expansion of the tax base has become an extremely necessity. At the prevailing economic condition of the country, successive two digit GDP growth rate is highly expected to move the economy to a sustenance level. To achieve that target, government must accelerate tax GDP ratio to an acceptable level and thus generate adequate revenue from internal sources. Government must take major revenue administration modernization programs without any further delay.

## **B. Fragmented Revenue Administration**

At the present administrative setup direct and indirect tax administrations are working separately. Although these two types of taxes wings work under the same revenue authority, virtually they work very independently and almost in complete isolation from each other. This fragmentation and isolation leads to incapability of the revenue administration to understand and assess overall business activities of a taxpayer. As a result, it is relatively quite easy for an evader to conceal taxable activities from the tax administration. This two tax wings must work together to appear as a capable and effective revenue administration.

## **C. Export Diversification**

Export sector of Bangladesh is highly concentrated in one industry, the textile and garments industry. Around 77% of the total export income is generated from this industry. International trade is now passing through quite a turbulent and transitional period. In this period, extreme dependence on one sector can become very dreadful for a country. Implementation of WTO and phasing out of MFA posed serious challenge for this sector. There was a serious concern that garments sector of Bangladesh will be badly affected after phasing out of MFA. However, in spite of different impediments, this sector still doing quite well, but this sector as well as the whole economy is living with serious threats of facing very vulnerable situations. Not only export, local employment and banking sector are directly dependant on this sector. Definitely, this kind of high dependence on one particular sector is very dangerous for an economy. It severely reduces shock absorbing capacity of the economy. Beside private initiatives, government should promote entrepreneurs to diversify the exports. Government should create proper infrastructure and provide positive incentives to exporters to explore different and diversified export items.

## **D. Investment Environment**

Though FDI just doubled in FY 2005 than that of FY 2004, compared to other similar developing countries, Bangladesh can be termed as an underperformer in terms of attracting FDI inflows. Despite wide availability of extremely cheap skilled labor and very cheap energy supply, Bangladesh could not attract much significant FDI inflows. Lengthy bureaucratic procedures, inferior infrastructure, instable institutional and policy framework pushed many potential investors to invest in other regions of the world. In this era of globalization, FDI flows have increased in manifolds in the last decade all over the world. To register comprehensive macroeconomic growth, Bangladesh must display competitiveness in attracting FDI inflows.

## **E. Infrastructure Development**

In the recent years contribution of agriculture sector in GDP is sharply decreasing, while not the industry sector, the service sector is mostly filling out the vacuum. Although, industry sector is growing at the rate of around 8% per year, it seems it is not enough to achieve a meaningful economic development. One major impediment for rapid growth of industrial sector is power failures. Power sector of Bangladesh is passing through its worst condition. Many industries are suffering from disrupted power supply. In the recent years, industrial sector grew very fast. With this, electricity and gas coverage in the rural areas also increased a lot. As a consequence, demand for power increased very rapidly, however, government could not increase power production capacity in that pace. Businesses of all sorts are suffering very badly.

Chittagong port, the main sea port of Bangladesh is still in a measurable condition. While this port have every potential to become one of the leading sea ports of Asia. Telecom and information technology infrastructures are also very inadequate against prevailing market demand. To foster expected growth, creation of an investment friendly environment is a must. For that, we must ensure a fair, growth supportive infrastructure at the very first place.

## **V. Conclusion: Where We Stand and Where We Go**

Bangladesh, a country with a very low per capita GDP is suffering from mounted pressure of huge population and ever increasing budget deficits. Bangladesh is generally dependant on imports. Recent surge in oil prices and exceptional increases in prices of other essential commodities caused immense pressure on the balance of payment. Internal revenue collections have been very low; still a large portion of budget is financed by external borrowings. Rate of inflation also went beyond an acceptable limit. Though level of poverty is reduced considerably in the last few years; however, for achieving the millennium development poverty reduction goals, it seems lots of handworks still to do.

The present state of the economy looks very grim; however at the same time, few impressive indicators provide us with many reasons to be optimistic. The economy is now experiencing robust growth in exports; industrial sector is also growing rapidly. Inflow of expatriate worker remittance and FDI inflow also grew very impressively. To move from this state of low development to a moderate development level, Bangladesh must identify this economic situation as a crisis state and should formulate an action plan to confront the prevailing realities. Generation the general consensus of the opinion leaders of the society the country should move forward towards the successful implementation of the action plan.

As the first priority, a careful, well planned revenue and revenue related institutional reforms are extremely necessary at this point. Flourishing considerably in the last decade, the private sector is now making important contributions in every sector of the economy. Basic infrastructures improved steadily in last one decade. Bureaucratic procedures also got simplified gradually in the recent years. More orientation of information technology in the society and implementation of effective e-government can ensure existence of a growth supportive bureaucracy and government system. If the government can show policy consistency, stable law order situation and a bit more developed infrastructure, there is every reason for Bangladesh to achieve economic satiability in a very near future.

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