Fiscal policy to address growing inequality in Bangladesh

Selim Raihan

Economic growth with the reduction in poverty and inequality are important development objectives in the policy-making process in Bangladesh. However, over the past decade since 2010, despite high economic growth, the country has been witnessing a rise in the inequality index. According to the Household Income and Expenditure Survey (HIES) of the Bangladesh Bureau of Statistics (BBS), the Gini coefficient of income, which is a popular measure of income inequality, rose from 0.458 in 2010 to 0.482 in 2016. The actual inequality picture is thought to be worse than the BBS’s survey estimate, as these household-surveys mostly fail to capture the information from the ultra-rich households. However, despite the data limitation, the growing inequality index suggests that the richer segment of the society has been benefited more by economic growth during the aforementioned period, and the economic growth process has been far from inclusive.

The widening income inequality between the rich and poor in Bangladesh emphasizes the need to understand the causes of growing inequality and to undertake appropriate policies to narrow the income gap. A number of reasons can be mentioned as responsible for the rise in income inequality in Bangladesh. However, the fiscal policy during the aforementioned period can be considered as one of the major contributing factors to widen the income inequality in Bangladesh. Two major instruments of the government’s fiscal policy are very relevant for addressing challenges related to widening income inequality. These two instruments are revenue generation (especially tax and non-tax revenue), and public expenditure on social sectors (especially education, health and social protection).

It is important to mention that, tax revenue occupies more than 80% of government’s revenue in Bangladesh. However, over the past decade, tax revenue in proportion to the GDP declined and remained well below any international norm. In fact, the tax-GDP ratio now is around 8.6%, which is one of the lowest in the world. With such low tax-GDP ratio, the government has very limited ability to spend high on the social sectors. Furthermore, over the years, the government’s efforts to increase revenue from direct taxes (taxes on income and profit) haven’t seen much success. Less than a third of government revenue comes from direct taxes. In contrast, the reliance on indirect taxes (value-added tax, import duties, supplementary duties, and different other taxes) and non-tax revenue is huge as more than two-thirds of the government’s revenue comes from these sources. As far as the direct tax is concerned, a large number of potential taxpayers, which include many ultra-rich people, remain outside of the tax-net or pay a little amount of taxes. Also, a number of economic sectors, capable of paying taxes, are either fully exempted from paying taxes or enjoy the privileges of paying a substantially reduced amount of taxes.

It is also important to highlight here that, as far as the tax policy is concerned to achieve both horizontal and vertical equity, individuals in similar financial circumstances with similar fundamental ability to pay taxes should be taxed at the same rate (horizontal equity), and the individuals in different circumstances with different abilities to pay should not be taxed at the same rate (vertical equity). In Bangladesh, given the culture of tax avoidance, the objective of achieving horizontal equity is compromised. Also, due to the heavy reliance on indirect taxes, the objective of achieving vertical equity is seriously undermined. This has resulted in a tax system which is regressive and inequality enhancing where richer people become the larger beneficiaries of such weak tax system.

Now, if we look at the expenditure side of the fiscal policy, especially public expenditure related to education, health and social protection, there has been virtually no significant improvement in the allocation, in proportion to GDP, over the past decade. In 2010, the public expenditure on education and health in proportion to GDP were 2.1% and 0.5% respectively, which by 2016 came down to 1.5% and 0.4% respectively. In 2016, public expenditure on social protection was only around 1% of GDP. In all three social fronts (education, health and social protection) in Bangladesh, public expenditure in proportion to GDP is the lowest in the world. Despite that public expenditure on social sectors has been used in many countries to counter widening income inequality, this instrument has not been used judiciously in Bangladesh in the recent decade. Such low public education and health expenditure does not help improve the productivity of workers and is not consistent with the effort to reduce poverty and inequality. One obvious implication of the low public expenditure on education and health is the high degree of out-of-pocket private education and health expenditure in Bangladesh which is one of the major contributing factors behind the growing inequality. The inequality problem also involves regional disparity in development. While Dhaka and few metropolitan cities have been the major beneficiaries of the development so far, many regions in the country are seriously lagging behind. There are genuine concerns that large discrimination prevails when it comes to budgetary allocation for social sectors and physical infrastructure in Dhaka and few other metropolitan cities over many other regions in the country. With such a regional disparity in the allocation of development budget, the country’s inequality situation is deemed to get worse. Also, the government’s social protection programs are very inadequate in addressing pockets of poverty and regional disparity in poverty. Therefore, there is a need for enhanced budgetary allocation for these lagging regions.

One important aspect in the fiscal policy, both in the cases of revenue generation and public expenditure, is the corruption and leakage in the system. The high degree of rent-seeking activities in the public revenue and expenditure systems also contribute to enhanced inequality. Therefore, the need for institutional reforms in the areas of revenue generation and public expenditure is more than ever.

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Revenue Mobilisation in Bangladesh: Recent Trends

Bazlul Haque Khondker

Economic growth and poverty reduction performances have been very impressive in Bangladesh during the last few years. Real economic growth has been hovering above 7.5 percent rate and poverty reduction rate was 24.3 percent in 2016 according to the latest available household survey (i.e. HIES 2016). Given her ambitious growth targets propelled by investment to realize the upper middle-income status and zero extreme poverty by 2030 – mobilisation of revenue in the range of 15 to 16 percent of GDP is a pre-requisite. However, in one area performance has been disappointing, that is revenue mobilization. Revenue effort (i.e. Revenue to GDP ratio; less than 11 percent in FY 2018) has been the lowest in the World. This is however not a recent phenomenon – historically revenue mobilization has been poor in Bangladesh. This note tries to provide some way forward to realize revenue potential in Bangladesh.

Revenue Structure and Performance: there are two main revenue sources in Bangladesh: (i) tax revenue and (ii) non-tax revenue. Tax revenue is composed of two sources – taxes collected by National Board of Revenue (NBR – known as NBR taxes); and taxes collected outside National Board of Revenue (known as non-NBR taxes).

Share of non-tax revenue in total revenue collection has reduced by about half from 18 percent in FY 14 to 10 percent in FY 18. Share of non-NBR tax remained more or less stable at around 3 percent between FY 14 and FY 18. On the other hand, the share of NBR tax increased from 79 percent in FY 14 to over 87 percent in FY 18. NBR taxes have mobilised from four major sources such as income tax (i.e. 34% share); VAT (i.e. 37%); Supplementary duty (i.e. 16%); and Import duty (i.e. 12%). All together these four sources generate more than 98 percent of total NBR tax revenue.

In line with the ambitious growth projections as well as to cover ever increasing resource need for poverty reduction and SDG realization, Bangladesh has also been setting high revenue targets in budgets – relying mostly on NBR tax sources. In the last five budgets (i.e. from FY 14 to FY 18), Bangladesh has set revenue targets of around 12 to 13 percent of GDP – which implies raising additional 2 to 2.5 percentage points higher revenue. However, given the fast-expanding tax bases (especially the domestic tax bases for income tax and VAT due to sustained 13 nominal GDP growth) as well as the revenue efforts of countries with comparable per capita income, setting a target of around 12 to 13 percent appears on the lower side. Bangladesh should have set at least revenue targets of 15 to 17 percent of GDP.

But the unfortunate development is that Bangladesh has not been able to realize the revenue targets (which are on the lower side) set out in the last five budgets. Figure 1 below captures the cumulative revenue short falls in the last five budgets (i.e. from FY 15 to first six months of FY 19). Cumulative revenue short falls have been widening in each of the last five budgets. In FY 15, cumulative revenue short fall was BDT 124.8 billion. In FY 18, the cumulative revenue short fall increased by almost 3 times to BDT 342.8 billion. Cumulative revenue short fall in the first four months of FY 19 has been estimated at BDT 190.8 billion – more than double of the amount reported for FY 18 – BDT 87 billion.

Short fall in revenue from targets is not authorities as are not fully prepared to mobilise the additional revenue. NBR could not implement important reforms in the income and VAT fronts during the last decade. As a result, the gap between targets and actual mobilisation has been widening.

Value Added Tax: one of most important tax revenue sources in Bangladesh is VAT. It was introduced in 1991 with the enact of VAT law 1991. Thereafter, various ad hoc measures have been introduced into the VAT system – turning it an excise type system. Due to these ad hoc measures, revenue generation from this source has weakened – directly impacting the realization of revenue target. Considering the problems of this move may allow, application of VAT in its proper form to service sectors including wholesale, retail, and a broad range of services in order to gain more VAT productivity. Introduction of new law likely to boost revenue by about 1 to 2 percent percentage points of GDP.

Arguments for lowering VAT rate is that it would lead to lower prices and thus encourage higher consumption. VAT is a consumption tax and consumers bear the VAT burden. Consumers have been accustomed to pay 15 percent rate. Given that producers are a more organised group than consumers – there is no guarantee that reduction in VAT rate would be associated with commensurate fall in prices. Moreover, it has been estimated that 1 percent reduction in VAT rate would lead to revenue loss of BDT 8,000 crore (PRI Mimeo, 2018). Thus, it would be wise to keep the VAT rate unaffected.

Moreover, VAT should be applicable in its proper form to service sectors including wholesale, retail, and a broad range of services in order to gain more VAT productivity. Furthermore, the VAT administration needs to be efficient in providing taxpayers’ services through series of administrative and policy reforms.

Personal Income Tax: another important tax revenue source in Bangladesh is personal income tax. The individual income tax in Bangladesh, governed by the Income Tax Ordinance 1984 and Income Tax Rules 1984, is a major source of the government’s revenue from direct taxes. It is levied at graduated rates ranging between 10 and 30 percent on as many as seven sources of income, viz. wages and salaries, interest on securities, income from business or profession, capital gains, income from house property, agriculture income, and income from other sources.

The main problem with personal income tax is that only around 1.3 percent of the population is under the personal income tax net. The number of personal income tax-payers fares poorly against the rise of personal income and growth of ‘middle-class’ in Bangladesh. According to PPP $ 5.50 and higher per day measure, the number of economical secure and middle class has increased from 12.3 percent of the population in FY 2010 to 15.5 percent in FY 2016. Accordingly, numbers of income payers should have been between 12 to 15 percent of the population. Revenue potential of expansion of income tax net is huge. Using average income tax payment in FY 2017 and assuming 5 percent of the population is brought the tax net, would likely to generate 3 percentage points additional revenue.

Revenue mobilisation in Bangladesh can be improved significantly over the medium term by focusing reforms in the VAT and income tax fronts.

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Gender budgeting in Bangladesh: The challenges and way forward

Sayema Haque Bidisha

A national budget can be considered as a reflection of the commitment of the government in terms of allocation (redistribution of its resources based on certain objectives) and the priorities set to achieve them. Gender budgeting, in this context, can be defined as an exercise of preparing and analysing budgets from a gendered point of view. Broadly speaking, through gender budgeting, the mainstream budget is disaggregated based on its impacts on men and women (GoB, 2018a, 2018b).

Since early 90’s, different international agencies, particularly that of United Nations have started to consider about gender segregated analysis of national budgets and a number of countries have initiated gender budgeting. In recent years, most of the countries under the UN umbrella have incorporated gender budgeting within their national budget. While understanding gender budget, we should keep in mind that gender budgeting is not about having a separate budget for women or providing special allocation for women, rather this exercise, through proper allocation and distribution of resources aims at ensuring greater gender equity and empowerment of women. Given the patriarchal structure of our societies, on one hand women are often not being able to realize their potential in terms of education or occupation and on the other, in many instances are argued to be subject to violence and discrimination. In addition, the patriarchal society has also set number of gender-centric norms and socio-economic role of women which have historically constrained women’s advancement and empowerment. Against this backdrop of prevalent patriarchy and lagged position of women in terms of different socio-economic indicators, resource allocation as in national budget can help to narrow down the prevailing gender gap and in this context, gender sensitive budget can act as an important policy tool.

Since FY10, the Government of Bangladesh has started to analyze national budget through a gender lens and has been annually preparing a gender budget (GB) report. The process was initiated by 4 ministries, which later expanded to 43 ministries in FY19 (Table 1). According to Table 1, in these years, on an average around 25% of national budget has reported to be allotted for women where the figure has reached to more than 29% in FY19.

From a methodological view, gender budgeting in Bangladesh primarily involves a gender based disaggregation of allocation of resources where the Ministry of Finance (MoF) plays the leading role and follows certain common ‘rules’ for gender budget reporting. At the beginning of each financial year, the MoF sends a call circular (Budget Call Circular 1) to all of the ministries. The circular provides the key criterions and yardsticks for evaluating gender sensitivity of the development programs of the ministries. The criterions are the following (GoB, 2017a, 2017b): (1) Access to Health Service and Nutritional Development, (2) Access to Governmental Assets and Services, (3) Access to Education and Training, (4) Reduction of Working Hours for Women, (5) Participation of Women in Labor Force and Income-increasing Activities, (6) Increasing Social Security for Women and Reducing Probable Risk and Loss, (7) Women Empowerment, (8) Participation of Women in Different Forums, (9) Ensuring Safety and Safe Movement for Women, (10) Observation and Evaluation of Gender Equality, (11) Increasing Social Dignity for Women, (12) Access to Law and Order for Women, (13) ICT Training for Women, and (14) Reduction of Violence and Torture against Women. Based on these 14 criterion, gender sensitivity of the projects is evaluated on a 0 to 100 scale (0=no direct impact; 1-33=minimum/little direct impact; 34-66=medium direct impact; 67-99= significant and sustainable direct impact; 100= programs/projects having the specific goal of women’s development). For the development projects, based on these 14 standards, a percentage is assigned to each of the programs indicating the proportion of total expenditure that will directly benefit women. As for the operating budget, the proportion of women workforce is considered as the basis for women’s allocation. The MoF after receiving such an evaluation, analyzes the programs/projects of each of the ministries through a technical model, known as RCGP model (Recurrent, Capital, Gender and Poverty Model), which finally calculates the percentage of allocation of budget which benefits women. After combining information of all relevant ministries, the MoF generates the gender budgeting report (GoB, 2018a).

Although gender budgeting is considered as an important tool for attaining gender equity and women empowerment, there remains concern whether it has been able to fulfill the desired objectives. It is often argued that despite of gender budgeting exercise, the allocation of government expenditure has not been able to accomplish the desired objectives. A number of challenges remain while operationalizing gender budgeting in Bangladesh:

Methodological Challenges: As discussed before, the relevant ministries, in response to Budget Call Circular make an assessment of its development programs. The assessment is therefore primarily subjective and is argued to be subject to serious individual biases. Similarly, the MoF prepares the gender budget based on the assessment provided by the ministries and follows a standard RCGP model for this. The design of the model and specification of the parameters if not accurate, can lead to distorted results.

Institutional Challenges: There remains a number of institutional constraints for attaining gender equity through budgetary allocation. In this connection, it is crucial that development projects are selected on the basis of their own merits and are not influenced by any political or subjective bias. If the projects are not directly linked to the development priorities and are not selected through a gender lens, gender budgeting exercise is unlikely to meet its ultimate goal. In this connection, it should be kept in mind that, while assessing gender budget, we should not confine ourselves to mere qualitative aspects of the projects, rather the yard stick of assessment should be qualitative, e.g. those set under SDGs or other development priorities. Besides these, it should also be kept in mind that, as the goal of empowerment involves a number of relevant ministries, lack of coordination among projects and relevant ministries often hamper the process.

Operational Challenges: Given the patriarchal social structure, effective operationalization of gender demands a comprehensive analysis of the gender norm centric constraints that women face and relevant strategies and allocations in combating those obstacles. For example, a development project of establishing a training centre for women would not be effective if there are no supporting services related to gendered responsibilities of women (e.g. child care) as well as safe transportation and accommodation. In many cases, development projects are selected without considering related supporting arrangements and therefore may fail to attain desired outcomes.

There is no denying the fact that, for a patriarchal and conservative country like Bangladesh, gender budgeting can act as an important policy tool to attain gender parity in different aspects. However, given the methodological as well as institutional complexities associated with gender budgeting, we should not consider it as the sole instrument in accomplishing empowerment of women. With a view to realize the maximum potential of gender budgeting, it is crucial that the gender sensitivity assessment of both the line ministries as well as the MoF are conducted in a systematic and logical manner. In this connection, formation of a technical committee comprising of gender experts within the sphere of the MoF for the analysis of gender segregated information can be an important step forward. Secondly, instead of looking at the numerical value of gender sensitivity, while selecting development projects long term development objectives in terms of gender equity should be considered. In this connection, importance of regular monitoring and evaluation of projects of each of the ministries on the basis of certain set criterions and yardsticks related to the empowerment of women cannot be emphasized. Thirdly, while selecting development projects for attaining women empowerment, careful consideration is needed for designing and implementing gender friendly projects and policies. Finally, in order to reap the benefits of operating budget, the government can consider encouraging female officers as well as staffs by extending quota and other benefits—this type of positive discrimination can have long term benefit in closing the existing gender gap.

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Table 1: Trend of Gender Budgeting in Bangladesh

<table>
<thead>
<tr>
<th>Fiscal Year</th>
<th>Total Budget (crore taka)</th>
<th>Allocation for women dev. (crore taka)</th>
<th>Allocation for women in total budget (%)</th>
<th>Allocation for women in GDP (%)</th>
<th>No. of ministries and divisions</th>
</tr>
</thead>
<tbody>
<tr>
<td>2009-10</td>
<td>110523</td>
<td>27248</td>
<td>24.65</td>
<td>3.95</td>
<td>4</td>
</tr>
<tr>
<td>2010-11</td>
<td>130011</td>
<td>34221</td>
<td>26.32</td>
<td>4.36</td>
<td>10</td>
</tr>
<tr>
<td>2011-12</td>
<td>161213</td>
<td>42154</td>
<td>26.15</td>
<td>4.61</td>
<td>20</td>
</tr>
<tr>
<td>2012-13</td>
<td>185231</td>
<td>54302</td>
<td>28.68</td>
<td>5.23</td>
<td>25</td>
</tr>
<tr>
<td>2013-14</td>
<td>216222</td>
<td>59756</td>
<td>27.64</td>
<td>5.06</td>
<td>40</td>
</tr>
<tr>
<td>2014-15</td>
<td>239668</td>
<td>64087</td>
<td>27.74</td>
<td>4.23</td>
<td>40</td>
</tr>
<tr>
<td>2015-16</td>
<td>264565</td>
<td>71872</td>
<td>27.17</td>
<td>4.16</td>
<td>40</td>
</tr>
<tr>
<td>2016-17</td>
<td>340604</td>
<td>92765</td>
<td>27.25</td>
<td>4.73</td>
<td>40</td>
</tr>
<tr>
<td>2017-18</td>
<td>400266</td>
<td>112019</td>
<td>27.99</td>
<td>5.04</td>
<td>43</td>
</tr>
<tr>
<td>2018-19</td>
<td>464580</td>
<td>137742</td>
<td>29.65</td>
<td>5.43</td>
<td>43</td>
</tr>
</tbody>
</table>

Source: GoB (2018a).
SANEM, a non-profit research organization registered with the Registrar of Joint Stock Companies and Firms in Bangladesh, launched its first QRBE of the year 2019 to look back on the overall status of the economy of Bangladesh and critically analyze the problems and prospects. The programme was held on May 9 at BRAC Centre Inn. Dr. Selim Raihan, Executive Director, SANEM and Professor of Economics, University of Dhaka made the keynote presentation. In his presentation, Dr. Raihan said that better management of exchange rate, better handling of the mega projects and fast track implementation of the SEZs are needed for improving the quality of economic growth. He said that the main drivers of economic growth in Bangladesh are export, remittance, and foreign investment. He emphasized on the quality of growth as it is largely related to poverty, inequality, and employment. Dr. Raihan advocated a number of reform measures including banking sector reforms which is characterized by high non-performing loans, weak regulations, institutional weakness, and political patronization. He said that trade policy reform is also needed for export growth and diversification. He stressed on the importance of building strong capacity of mobilizing tax revenues and getting the priorities right when it comes to the allocation of public resources. Dr. Bazul Haque Khondker, Chairman, SANEM and Dr. Sayema Haque Bidisha, Research Director, SANEM were also present in the programme. Dr. Khondker emphasized on tax policy reformation for high revenue generation and Dr. Bidisha talked about female labour market stagnation in Bangladesh.

Top essay writers from “Youth’s thoughts on Economics – Part 2” were awarded

SANEM organized its monthly essay writing competition for the second consecutive month titled “Youth’s Thoughts on Economics – Part 2” on the topic “Poverty alleviation”. More than a hundred essays were submitted. From the submissions, five winners were declared. The winners are Md. Salay Mostofa, Shithee Ahmed, Anindya Adhikary, Md. Mehedi Hasan, and Nazia Tasnim. The winners were awarded with a token of money and certificates. Dr. Selim Raihan, Executive Director, SANEM and Professor of Economics, University of Dhaka handed over the certificates to the top 19 essay writers including the winners.

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