



## Managing the post-Covid economic recovery

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By *Dr. Sadiq Ahmed*

The onset of Covid-19 since early March 2020 has taken a huge toll on people's lives and livelihood. It is therefore a great relief that there are indications that the Covid incidence is waning and there are welcome signs of economic recovery. Nevertheless, considerable uncertainties prevail regarding the future course of Covid, and no country is letting its guard off on Covid management.

So, Bangladesh should be well-advised to continue to remain vigilant, pursue rigorously the vaccination course, and continue to encourage social distancing practices including enforcement of mask use as appropriate.

At the same time, Bangladesh should prepare to take advantage of the emerging signs of economic recovery and build on this to put the economy back to the growth path of the Perspective Plan 2041 (PP2041).

The signs of economic recovery, although still early, are nevertheless encouraging. Import demand has surged, exports are growing, manufacturing sector production has picked up speed. Agriculture continues to do well. Food prices surged in recent months but have now stabilised. There is adequate food stock and agricultural diversification is continuing, slowly

but steadily. The recovery of services is slow but will gain momentum as GDP growth picks up. Private investment is still sluggish. But interest rates are very low in both nominal and real terms, the exchange rate is stable, foreign exchange reserves are adequate, fiscal deficit is manageable, and inflation is below 6% per year. These provide a supportive macroeconomic environment for a recovery of private investment.

The government must cash in on this positive economic environment to regain the growth momentum and recoup the Covid losses that have been particularly harsh on the poor and the low-income group through loss of employment and income. While the unprecedented surge in remittances in FY2021 provided a huge social protection cushion for the rural and urban poor and the low-income group, remittances are now declining owing to loss of jobs in the Middle East and the Malaysian markets resulting from Covid impact. The recovery of economic growth and domestic employment is therefore of critical importance for sustained poverty reduction.

Apart from deft management of Covid, there are two major challenges facing policymakers. The first is to manage the post-Covid economic recovery by guarding against possible non-Covid related global economic uncertainties. The second is to resume the reform agenda that was halted due to Covid.

#### Short-term global economic uncertainties

The immediate concern is to guard the economy from the emerging global economic uncertainties due to disruption of supply chain and emergence of inflationary pressures. Commodity prices, especially oil, have been rising for a while that has adversely impacted the Bangladesh import bill. This is an important contributor to the sharp growth in the dollar value of imports.

In an open economy the pass-through effect of global inflation is hard to contain because price controls and subsidisation are unsustainable especially in an environment of a large fiscal constraint.

But there are several policy actions that can be taken to counter the adverse effects of these global developments.

First, the government could revisit the import duty policy and lower tariffs and supplementary duties to partially compensate for higher international prices. Trade policy reforms remain an unfinished policy agenda and now might be an opportune time to do some important reforms.

Secondly, the disruption of the supply chain that could hurt the buoyancy of the manufacturing sector can be managed better through advanced intelligence on alternative sources of supply, proper inventory management, improving the efficiency of the port clearance, and simplifying import documentation requirements. The trade facilitation reform is another unfinished agenda that needs to be tackled upfront. The return to this reform will be particularly large in the present environment of global supply disruptions.

Fundamentally, the most important policy task would be to preserve the prudent macroeconomic management stance that could be easily derailed by global inflationary pressure. Fiscal and monetary policy management will have to be ready to take countermeasures to lower domestic inflationary pressures by managing fiscal deficit at around the 5% of GDP benchmark and keeping the growth of broad money (M2) and domestic credit within prudent limits as presently.

The Bangladesh Bank (BB) will have to be especially watchful of the performance of the domestic banking system. The BB is aware of the vulnerabilities of the banking sector. High non-performing loans (NPLs) have been managed through cosmetic solutions like loan write-offs, loan restructuring, and redefinition of what constitutes an NPL. These are short-term accounting interventions that do not address the underlying risks of a contagious portfolio.

Against this background, it is little comfort that presently there is excess liquidity in the banking sector despite historically low nominal and real interest rates owing to Covid-induced depressed demand. Once economic recovery is well underway, there will be a sharp recovery of demand for private sector credit. With a government policy-imposed ceiling on deposit and lending rates, market clearance will require increased supply of credit.

The excess liquidity could disappear fast, and the availability of new liquidity could be constrained by the inadequacy of loan repayments and low growth of deposits owing to low deposit rates. In this environment, injection of fresh liquidity by the BB through monetary

policy instruments could easily create inflationary pressures. There is an additional risk that the size of NPLs inclusive of restructured loans could become overwhelming.

Resuming the long-term growth and poverty reduction agenda

In 2020, the government adopted the PP2041 that seeks to achieve Upper-Middle Income (UMIC) status and eliminate extreme poverty by FY2031. Among other strategies, the PP2041 adopted a growth path that envisaged the GDP growth to steadily increase to 9% per year by FY2031 and keep growing at that rate until FY2041.

The advent of Covid-19 has disrupted that growth path. GDP growth crashed to 3.5% in FY2020 and recovered modestly to 5.5% in FY2021. There are indications that growth might recover further to around 6.5% in FY2022.

While this recovery of growth should be celebrated in the present global context, the new growth path is nowhere close to the 8-8.5% path envisaged in PP2041 for these years. Most importantly, Covid-19 has badly disrupted the encouraging progress made by Bangladesh on the poverty front.

Unfortunately, the government has not updated the 2016 Household Income and Expenditure Survey (HIES) or the 2016-17 Labor Force Survey (LFS 2016-17). As a result, there is no reliable database to assess the impact of Covid on poverty and employment. Quick response telephone surveys done by national research institutes suggest that the immediate impact of Covid, especially during the months of March-June 2020, was harshly reflected in high unemployment and poverty estimates.

Economic recovery since July 2020 and the surge in remittances have provided much-needed relief and the year-round poverty impact is likely to have returned to the pre-Covid levels by the end of June 2021.

It is imperative for the government to quickly launch the new HIES and LFS to assess the poverty reduction and job creation tasks ahead. Yet, it is fair to assume that the Covid disrupted the poverty reduction progress and the task of eliminating extreme poverty by FY2031 has become much more challenging now than at the beginning of 2020.

While the switch back to the PP2041 growth path looks optimistic, there is ample scope for a stronger recovery than projected for FY2022. This is because first, Bangladesh has a record of doing well when supported by good economic policies, and second, there is a substantial unfinished reform agenda that could trigger a much stronger economic recovery. Similarly, while the task of eliminating extreme poverty by FY2031 looks daunting, substantial progress is possible by restoring the poverty reduction path and associated policies articulated in PP2041 and the 8FYP.

The PP2041 identified an array of macroeconomic and sectoral strategies and policies that under-pinned the growth and poverty reduction targets. These include the PP2041 Medium-Term Fiscal Policy Framework (MTFPF); PP2041 Poverty Reduction Strategy; PP2041 Agricultural Strategy; PP2041 Trade and Industrialisation Strategy; PP2041 Infrastructure Strategy; PP2041 Human Development Strategy; PP2041 Urbanisation Strategy; and PP2041 Environmental Strategy.

The first phase of implementation of these strategies for FY2021-FY2025 was intended under the 8FYP. Detailed policies, financing and institutional reforms underlying each area are available in the 8FYP. Since the 8FYP was approved by the Cabinet and Parliament, it is now an official medium term strategic document that needs to be fully implemented. Covid has disrupted the progress for the first year of the Plan (FY2021) but there is still ample time to catch up.

Implementation of the 8FYP requires concerted efforts by all line ministries and close monitoring and supervision by the Cabinet. The Cabinet may need to monitor progress of 8FYP implementation on a 6-month cycle based on the progress report prepared by the GED. The 6-month progress report could focus on some core intermediate indicators relating to growth, exports, and other macroeconomic indicators. There should be a full implementation review on an annual cycle using the Development Results Framework (DRF) of the 8FYP.

*Sadiq Ahmed is Vice Chairman of the Policy Research Institute (PRI) of Bangladesh. He can be reached at [sadiqahmed1952@gmail.com](mailto:sadiqahmed1952@gmail.com)*

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