

**Ex-Ante Evaluation (for Japanese ODA Loan)**

South Asia Division 4, South Asia Department

Japan International Cooperation Agency

**1. Name of the Program**

- (1) Country : The People's Republic of Bangladesh
  - (2) Program : Development Policy Loan for Strengthening Public Financial Management
  - (3) Project Site / Target Area : Throughout the country
- Loan Agreement : June 27, 2023

**2. Background and Necessity of the Program**

- (1) Current State and Issues of the Public Finance Sector and the Priority of the Program in Bangladesh

Concerning the real economy, the country's real GDP growth rate, which had been 7-8% per year before the COVID-19 pandemic, declined to 3.4% in FY2019/20 (July 2019-June 2020) due to the impact of the pandemic. After the pandemic, the GDP growth rate recovered to 7.1% in FY2021/22 but is expected to fall to 5.5% in FY2022/23, partly due to the Ukraine crisis and its impact of resource and food price spikes and other factors (International Monetary Fund (IMF), 2023). While the inflation rate (year-on-year) had been stable at around 5%, the target set by the Bangladesh Bank, since 2016, prices have been above the target due to rising prices for food, resources, and other items on the international market since 2022. According to IMF, the price increase rate for FY2022/23 is 8.6% (estimated).

Regarding the balance of payments, several factors, including the Ukraine crisis, caused import prices to soar and the trade deficit to widen. As a result, the current account deficit for FY2021/22 was 4.1% of GDP, a rapid increase from the previous year (1.1% of GDP). Foreign exchange reserves have been on a downward trend since their record high at the end of August 2021 (\$48 billion) and stood at \$31 billion at the end of April 2023. However, it still holds about 4 months of imports (Bangladesh Bank).

Regarding the national finance, the fiscal deficit is expected to widen to 5.6% of GDP in FY2022/23 (3.8% of GDP in FY2021/22) due to low tax revenues and an increase in expenditures including the increase of national subsidies. It is projected to remain at around 5% of GDP over the medium term (IMF), making it necessary to take measures to reduce the fiscal deficit.

Considering the economic situation described above, the government of Bangladesh is currently taking some measures such as limiting machinery and energy imports for government procurement (including the scheduled blackouts) and partly allowing exchange rate flexibility, in order to curb foreign currency payments and secure fiscal space. In addition, the government has requested budget support from Multilateral Development Banks (MDBs), including the IMF, the Asian Development Bank (ADB),

and the World Bank (WB), as well as from Japan, the largest bilateral partner. Although the current economic situation is not necessarily in need of urgent support (this view is consistent with IMF and MDBs), a further prolonged period of fiscal austerity, including a decline in foreign exchange reserves and government measures to curb foreign currency payments in response, could have a negative impact on the activities of the private sector, such as a decline in foreign currency procurement by the local private sector and a decrease of investment to the country by foreign firms, including Japanese firms.

To re-accelerate the economic growth and strengthen resilience against further external shocks that may occur in the future, it is necessary to secure foreign currency and fiscal space in the short term through budget support. In addition, the government needs to improve its macroeconomic management and a capacity of public financial management in the medium to long term. When it comes to public financial management, it is necessary to secure a sustainable and stable fiscal surplus through revenue expansion, improved expenditure management and to establish a foundation for strategic public investment for further growth. The IMF and MDBs will seek steady implementation of their reform programs by the government in providing budget support.

In terms of revenue expansion, the National Board of Revenue (NBR) is mainly responsible for the tax collection, and taxes collected by the NBR account for about 80% of the country's revenue (Ministry of Finance in Bangladesh (MOF)). Although the tax revenue from the NBR has increased from about 0.5 trillion taka (FY 2008/09) to about 3.1 trillion taka (FY 2021/22), due to the efforts to strengthen tax revenue and the expansion of tax collection targets with the national economic growth, the revenue of GDP is at about 9.6% (FY 2021/22), and this remains low compared to other countries (The average for the 30 emerging and developing Asian countries is 30.7%) (IMF). The main tax categories include income tax, value-added tax (VAT), customs duties, etc. The government is committed to reforms focusing on strengthening the collection of income tax and VAT, which account for more than half of total tax revenues. Both income tax and VAT collection rates are low despite the tax rates are comparable to those in other countries, and the reasons for this include weak tax base and insufficient tax collection capacity. To achieve a sustainable economic growth, in addition to the government's efforts to increase revenue, it is essential to improve the tax system to take into account vulnerable groups such as women, sexual minorities, and people with disabilities.

Regarding the improvement of expenditure management, the country's expenditure is largely divided into the development budget (about 37% of total expenditure), which is allocated to the government's public investment projects, and the non-development budget (about 58% of total expenditure), which is allocated to other current expenditures of the government (MOF). While the Ministry of Finance is responsible for overall budget management, the Ministry of Planning is responsible for budget management of the

development budget. It is important to improve the efficiency of public spending to maximize the use of limited public resources due to the low tax revenue rate. However, there are major challenges in expenditure management, such as inefficient budget allocation for the separation of development and non-development budgets, significant delays due to weak capacity of implementation management for the public investment projects, cost overruns, inefficient delivery of social benefits, and inefficient fiscal management by local governments.

Regarding the expenditure management, not only improving administrative systems and procedures but also establishing a mechanism for strategic public investment is important to achieve sustainable economic growth. In the Joint Statement released at the Japan-Bangladesh Summit in April 2023, it was announced that the bilateral relationship between Japan and Bangladesh has upgraded to a "Strategic Partnership," and the two leaders have agreed to 1) improve economic infrastructure, 2) improve the investment environment, and 3) enhance regional connectivity based on the "BIG-B Initiative" and the "An Industrial Value Chain connecting the Bay of Bengal and North Eastern Region of India", as well as to resume bilateral policy dialogue. The "Development Policy Loan for Strengthening Public Financial Management" (hereinafter referred to as "the Program") will support the agreed items and promote the strategic public investment.

This Program will help the government of Bangladesh to secure its short-term fiscal space. At the same time, the Program will support sustainable economic growth through the steady implementation of the public financial management reforms that the government is promoting to re-accelerate economic growth and improving resilience to external shocks that might happen in the future. Improving the tax revenue-to-GDP ratio and improving public investment management are considered key actions to promote recovery from the COVID-19 pandemic in the 8<sup>th</sup> Five-Year Plan (FY2020/21-FY2024/25) of Bangladesh (Ministry of Planning). The Program is also in line with the 8<sup>th</sup> Five-Year Plan and is, therefore, one of the top priority projects for the government of Bangladesh.

## (2) Japan and JICA's Policy Cooperation Policy and Operations in the Public Finance Sector

Japan's Country Assistance Policy for Bangladesh (February 2018) states that "To improve governance, which has been an issue in the past, we will ensure that government functions are strengthened, and administrative services are improved in all areas of assistance." In addition, the JICA Country Analysis Paper for the People's Republic of Bangladesh (March 2023) emphasizes "overcoming social vulnerabilities" by strengthening governance, etc. as a priority issue, and the Program's efforts to stabilize the balance of payments and secure fiscal capacity that will contribute to overcoming social vulnerabilities through the Program are consistent with these analyses and policies. The paper also states that the program is consistent with this

analysis, as it will work to strengthen the government's coordination function through enhancing public investment management, including the establishment of appropriate planning processes for the budget of development projects.

In addition, the "New Plan for a Free and Open Indo-Pacific (FOIP)" ("New FOIP Plan") announced by Prime Minister of Japan, Mr. KISHIDA Fumio in March 2023 specifically addresses strengthening the fundamental of national budget, including improving public investment projects and budget management in developing countries and improving the investment environment in Special Economic Zones. Furthermore, technical cooperation projects that are linked to the Program are specifically mentioned as examples.

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Furthermore, the Program is in line with the "Strengthening the Foundations of National Finances" cluster of the "Public Finance and Financial Systems" cooperation policy, which is one of the issue-specific project strategies in JICA's Global Agenda (June 2022).

### (3) Other Donors' Activity

The IMF will provide \$3.3 billion in financial support through the Extended Credit Facility (ECF) and Extended Fund Facility (EFF) and \$1.4 billion through the Resilience and Sustainability Facility (RSF). They were approved by the IMF Board of Directors in January 2023. Under the fiscal projection by IMF, budget supports from JICA is included as well as other MDBs.

ADB is considering a total of US\$1.05 billion in support through two development policy loans (one in the public finance area and the other in the climate change area). The development policy loan in the public finance area, named the Sustainable Economic Recovery Program (SERP), consists of two subprograms. US\$250 million was approved in October 2021 as the first subprogram, and US\$400 million was also approved in June 2023 as the second subprogram. For the development policy loan in the climate change sector, \$400 million is expected to be approved after June 2023. The Program is co-financed with ADB's development policy loans in the public finance sector.

The World Bank, is also considering providing a total of US\$750 million through two development policy loans (climate change and macroeconomic), with the climate change loan, named Green and Climate Resilient Development Credit (US\$500 million),

was already approved in May 2023, and the macroeconomic sector development policy loan, named Recovery and Resilience DPC, is expected to be approved in 2024.

The Asian Infrastructure Investment Bank (AIIB) has already approved a development policy loan (\$400 million) in June 2023 for economic and fiscal reforms in coordination with ADB's SERP (Subprogram 2).

### **3. Program Description**

#### **(1) Program Description**

##### **① Program Objective(s)**

The objective of the Program is to support economic recovery and strengthen public financial management capacity by providing budget support as precautionary measure and improving public financial management framework, thereby contributing to the economic recovery and development efforts of the country.

##### **② Program Component(s)**

The Program will provide concessional financing to the government of Bangladesh in public financial policy areas agreed upon with the government.

##### **③ Program Beneficiaries (Target Group)**

Citizens of Bangladesh (Population: Roughly 165 million (World Bank, 2022))

#### **(2) Estimated Program Cost (Loan Amount)**

30,000 million Yen

#### **(3) Schedule**

The Program will commence at the time of L/A signing. The target date for achievement of the policy actions is by June 2023, and all policy actions have been accomplished and the Program is considered complete upon completion of loan execution.

#### **(4) Program Implementation Structure**

- 1) Borrower : The Government of the People's Republic of Bangladesh
- 2) Guarantor : N/A
- 3) Executing Agency : Finance Division, Ministry of Finance (FD)

#### **(5) Collaboration and Sharing of Roles with Other Donors**

##### **1) Japan's Activity**

JICA is currently supporting capacity building for implementing agencies to improve the investment environment in Special Economic Zones (SEZs) such as Bangladesh Special Economic Zones (BSEZs) under the Technical Cooperation Projects, "Project for Promoting Investment and Enhancing Industrial Competitiveness" (FY 2017-2022) and the "The Project for Capacity Building of BEZA on EZ Management and Investment Promotion" (FY 2022-2027).

In addition, through the JICA Country-Focus Training Program, "Enhancement of Customs Administration" (FY2021-2025), the program is supporting transparency and efficiency of procedures based on international item classification standards

through capacity building of customs officer.

The Program has established policy actions in conjunction with these existing technical cooperation projects/programs, which are expected to promote investment by foreign firms, including Japanese firms, and increase related tax collection, thereby boosting the government's revenue.

In addition, JICA is supporting project managements related to public investment and efficient budget management through the creation and utilization of the public investment management reform tool on the "Strengthening Public Investment Management System Project" (Phase 1 in FY2013-2018 and Phase 2 in FY2019-2023). Furthermore, "Project for Strengthening Capacity for City Corporations" (FY2021-FY2024), the technical cooperation project is supporting for the efficient budget formulation in core cities such as North and South Dhaka City and Chattogram City. The Program also includes other policy actions in conjunction with these existing technical cooperation projects and is expected to support the improvement of the government's expenditure management capacity.

#### 2) Other Donor's Activity

The Program will be co-financed with the ADB's SERP. Some policy actions in the Program are the same as the policy actions of SERP.

#### (6) Environmental and Social Consideration

① Category: C

② Reason for Categorization: The Program is likely to have minimal adverse impact on the environment and society (January 2022).

#### (7) Cross-Cutting Issues:

The program will expand social services to vulnerable groups such as transgender people and people with disabilities through tax reform and promotion of public investment, thereby contributing to curbing the increase in the number of poor households.

#### (8) Gender Category: GI (S) (Integrated gender activity project)

The Program establishes policy actions from a gender perspective and calls for their achievement on the part of the partner government. Specifically, the policy action "②-11 The Ministry of Finance enforced gender equality and social inclusion (GESI) measures in income taxation", ②-12 Tax rebate for an employer employing transgender employees / handicapped individuals", and "②-13 Tax exemption for women-owned SMEs". Therefore, the program is categorized as the integrated gender activity project.

#### (9) Other Important Issues

N/A

### **4. Targeted Outcomes**

#### (1) Quantitative Effects

### Performance Indicators (Operation and Effect Indicator)

Indicator	Baseline (Actual Value in 2020)	Target (Dec. 2024)
Revenue of GDP Ratio (%)	9.7	10.4
Taxes to GDP Ratio (%)	8.1	8.8
Capital Expenditure to GDP Ratio (%)	5.6	6.3
Number of Electronic Fiscal Devices (EFDs) installed and in operation to issue electronic statements of taxable amounts (units)	0	20,000

#### (2) Qualitative Effects

Stable public financial management

#### (3) Internal Rate of Return

IRR is not calculated as this is a program loan.

### 5. External Factors and Risk Control

(1) Assumptions: N/A

(2) Externals Condition: N/A

### 6. Lessons Learned from Past Programs

The ex-post evaluation of the "Electricity Sector Reform Program" and "Electricity Sector Reform Program (II)" (evaluation year: FY2017), the loans to Pakistan, pointed out that JICA could support more effective policy improvement and policy reform by providing a combination of technical cooperation in parallel with the provision of development policy loans, specifically to support policy actions proposed in through the development policy loans.

The Program also seeks to ensure the effectiveness of policy improvement and reform by encouraging the progress of existing technical cooperation through the steady implementation of the policy actions proposed in the area of public investment.

### 7. Evaluation Results

This Program is consistent with the development issues and development policies of Bangladesh, as well as the assistance policies and analyses of the Government of Japan and JICA. The program will support sustainable economic growth of the country and the reforms in the field of public finance, thereby contributing to the achievement of SDG Goal 8 (Economic Growth), Goal 10 (Reduced Inequalities), Goal 16 (Develop effective, accountable and transparent institutions at all levels), and Goal 17 (Partnerships for the Goals). Since the government of Bangladesh expects Japan, as a major bilateral partner, to cooperate with international organizations as a precautionary measure against economic crises, there is a strong need to support the implementation

of the Program.

## **8. Plan for Future Evaluation**

(1) Indicators to be Used

As indicated in Sections 4.

(2) Future Evaluation Schedule

Ex-post evaluation: Two years after the program completion

END

Attachment:

Development Policy Loan for Strengthening Public Financial Management Policy Matrix



## Policy Matrix for “Development Policy Loan for Strengthening Public Financial Management”

Policy Area		Policy Objective	Policy Action	
			Policy Action 1 (Already achieved)* <sup>1</sup>	Policy Action 2 (*1) (Achieved by June 2023)
Re- acceler ating econo mic growth and strengt hening resilien ce to further extern al shocks that may occur in the	Expandi ng revenue through Tax Reform	Expanding tax revenues through policy/legal reforms and strengthening of tax administration authorities	(①-1) (Common Action with ADB’s SERP) The government secured parliamentary approval and has amended the Income Tax Ordinance, 1984 for all TIN holders (except those taxpayers who do not have a taxable income but have obtained a TIN for the purpose of sale of land or acquiring a credit card) to submit an annual income tax return for FY2021 and thereafter to expand the taxpayer base for income tax.	(②-1) (Dedicated action for the Program) The new Income Tax Bill was approved in principle by the cabinet and vetted by the Ministry of Law that (i) promotes digitization, (ii) simplifies returns, (iii) enhances enforcement by (a) mandating utility services disconnections on failure to pay undisputed tax arrears and (b) strengthening Income Tax Appellate Tribunal for tax disputes resolutions; (iv) broadens tax base and reduce loopholes by (a) treating written-off debts as taxable income, (b) treating capital gains from government securities as taxable income, and (c) enforcing income tax return filing by nonresident and digital providers not having permanent establishments in Bangladesh.
			(①-2) (Common Action with ADB’s SERP) The NBR mandated the exchange of information between the income tax and	(②-2) (Common Action with ADB’s SERP) The Ministry of Finance strengthened tax collection and compliance measures by (i) enforcing display of proof

future			VAT divisions for tax audits to enable improved tax compliance and minimize tax avoidance through identifying discrepancies in respect of tax liabilities and payments of firms and businesses.	of tax returns submission in business premises: (ii) penalty measures for (a) tax withholding noncompliance and (b) not disclosing any offshore assets in tax returns; (iii) empowering tax officials (a) to have full and free access to taxpayer's premises and accounts, and (b) to conduct spot assessments if a taxpayer is found to have not submitted their tax returns, and (iv) introducing withholding tax rate of 10% for (a) internet services and (b) service delivery agents for mobile financial services (MFS) which were previously tax exempt.
	Expanding tax collection through more efficient tax payers' service	(①-3) (Common Action with ADB's SERP) The NBR rolled out a simplified income tax return form for use by marginal taxpayers to file returns for FY2021 and thereafter to enhance efficiency and improve taxpayer services.	(②-3) (Common Action with ADB's SERP) The NBR implemented (i) online payment of VAT amounts exceeding TK5 million, (ii) online payment of income tax for amounts exceeding TK2 million, and (iii) pilot online personal income tax return filing for income exceeding TK7 million to improve tax collection efficiency and tax assessment.	
		(①-4) (Common Action with ADB's SERP) The NBR piloted the electronic deduction of income tax at source in 4 (of 29) tax zones for digitalization and improved management of withholding taxes.	(②-4) (Common Action with ADB's SERP) The NBR implemented electronic deduction of income tax at source for the entire country (all 29 zones) to promote digitalization and improve management of withholding taxes.	

				<p>(②-5) (Dedicated action for the Program) MoPA issued a letter which approves the necessary personnel assignment to the custom office which will be established in BSEZ.</p>
			<p>(①-5) (Common Action with ADB's SERP) The NBR commissioned at least 1,000 EFD for electronic tax invoices to address tax evasion, ensure due collection of VAT through digitalization, and thus facilitate improved VAT compliance.</p>	<p>(②-6) (Common Action with ADB's SERP) The NBR (i) implemented fully online VAT registration system with the target of receiving majority of the VAT returns through online system. (ii) imposed VAT on certain manufacturing products and services to raise VAT revenue collection and prevent leakage.</p>
		<p>Promoting investment by foreign companies and increasing related tax collections through the improvement of the investment environment and macroeconomic</p>		<p>(②-7) (Dedicated action for the Program) PMO approved the revision of the guideline concerning expatriate work permit policies.</p>
				<p>(②-8) (Dedicated action for the Program) PMO approved of the guideline concerning project office registration system.</p>

		stabilization.		
		Establishing a tax system that meets international standards and contemporary issues		(2-9) (Dedicated action for the Program) NBR formulated action plans for the improvement of HS Classification through training in Japan on the classification of items for customs procedures.
	(2-10) (Common Action with ADB's SERP) To address emerging issues in global taxation and to align the tax regime with international good practices, and Cabinet approved new Income Tax Bill incorporates provisions that enable (i) comprehensive treatment of capital gains taxation (by setting estimation rules and deductible allowances, and broadening the base); (ii) implementation of Thin Capitalization Rule by imposing deductible interest allowances up to Tk1.5 million in a given fiscal year; and (iii) implementation of Transfer Pricing, by constructing a range of acceptable "arm's length pricing" methods for international transactions.			
	(2-11) (Common Action with ADB's SERP)			

				<p>The Ministry of Finance enforced gender equality and social inclusion (GESI) measures in income taxation by</p> <p>(a) introducing tax-free annual income limit of TK350,000 for a third-gender assessee (vis-à-vis TK300,000 for a male assessee).</p>
				<p>(②-12)</p> <p>(Common Action with ADB’s SERP)</p> <p>(i) Tax rebate for an employer employing 10% of its workforce or at least 25 transgender employees</p> <p>(ii) Tax rebates for an employer employing 10% of its workforce or 25 handicapped individuals.</p>
				<p>(②-13)</p> <p>(Common Action with ADB’s SERP)</p> <p>Tax exemption for women-owned SMEs having an annual turnover of not more than TK7 million (vis-à-vis the limit of annual turnover of not more than TK5 million for SMEs in general) and (ii) introduced the provision of scheduler filling that removes bias against second earner income in the Cabinet approved new Income Tax Bill.</p>
	Improving Expenditure Management	Developing action plans for reform of public financial management		<p>(②-14)</p> <p>(Common Action with ADB’s SERP)</p> <p>The Finance Division, Ministry of Finance approved the PFM Reform Action Plan (2024-2028) with implementation effective from FY2024, based on the</p>

	ment			2022 PEFA Assessment and incorporated gender and climate-related actions to strengthen the PFM system.
		Improving the efficiency of public procurement procedures and project quality in development projects, etc.		<p>(2-15)  (Dedicated action for the Program)  The Planning Division, Ministry of Planning, issued a circular to all Sector Divisions, Planning Commission, to make mandatory apply Ministry Assessment Format and Sector Appraisal Format for all DPPs in 15 Sectors from FY2023-24.</p>
				<p>(2-16)  (Dedicated action for the Program)  The Programming Division, Planning Commission, approved the Public Investment Management Guidelines.</p>
				<p>(2-17)  (Common Action with ADB's SERP)  The Implementation Monitoring and Evaluation Division, Ministry of Planning rolled out the (i) e-CMS of e-GP nationwide, and (ii) digitalized the public procurement method to minimize cost escalations in public contracts, improve contract performance, and enhance the transparency and efficiency of public procurement payments.</p>

		<p>Developing efficient direct transfer of cash assistance to beneficiaries</p>	<p>(①-6) (Common Action with ADB's SERP) The government expanded the use of the G2P platform such that (i) benefits transfers for all new enrolments from 1 July 2021 will only be permitted through the G2P platform; and (ii) all remaining currently enrolled beneficiaries receiving payments outside the G2P platform will be progressively migrated to the platform by 30 June 2022 to promote transparency and ensure accurate efficient and timely transfer of cash assistance directly to beneficiaries.</p>	
		<p>Establishing more efficient fiscal management in local governments</p>	<p>(①-7) (Dedicated action for the Program) Prepared a draft of the new budget format based on the new system of accounts.</p>	<p>(②-18) (Dedicated action for the Program) LGD issued a letter to all City Corporations, instructing to use the new budget formats.</p>
				<p>(②-19) (Dedicated action for the Program) LGD issues a letter to all Upazila, ensuring the disclosure of budget information on the website.</p>
		<p>Concentrating investment based on a</p>		<p>(②-20) (Dedicated action for the Program) A high-level policy dialogue between the Government</p>

		strategic partnership between Japan and Bangladesh		of Bangladesh and the Government of Japan is agreed to be conducted.
				(②-21) (Dedicated action for the Program) PMO promotes legal and institutional arrangements for the establishment of the MIDI Authority.
				(②-22) (Dedicated action for the Program) Consent to cooperate in the survey (Data Collection Survey for Cross Border Logistics Promotion in South Asia) to strengthen the regional connectivity.

(\*1) Policy Actions set by ADB for Policy Action 2 have been confirmed to be achieved in the ADB Program by May 2023.