



Foreign Aid in Bangladesh: Its Contributions to Economic Growth and Development

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Master of Arts (International Development)*

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ABSTRACT

The literature on the aid-growth relationship is rife with debate. Most of the studies on aid effectiveness are based on cross-country panel analyses that create confusion in respect to understanding the real impact of aid utilization from an individual country context. Bangladesh, a developing country of South Asia, is considerably dependent on foreign aid to close the gaps in development financing. Aid effectiveness is crucial for the prosperity of Bangladesh but it is difficult to draw a firm conclusion on the impact of aid utilization in Bangladesh from the limited number of studies conducted thus far. This study assesses the actual contribution of aid to economic growth and development in Bangladesh. This thesis takes a more qualitative approach than the earlier studies on Bangladesh, drawing on the subjective findings of the donors, Government of Bangladesh, research organizations and scholars. It analyses the contribution of aid in terms of public investment to the economic, social, institution building and environmental sectors. I argue that the contributions of foreign aid to socioeconomic development, institutional capacity development and environmental management are significantly positive in Bangladesh. Nonetheless, due to the impediments to aid effectiveness and systematic deficiencies, Bangladesh has failed to maximise the benefits of aid utilization. This thesis discusses the aid effectiveness frameworks in Bangladesh along with the impediments operating against aid utilization in an effort to identify pathways that will ensure the maximum outcomes of aid utilisation. This study finds a conditional positive impact of foreign aid on growth and development in Bangladesh.

Keywords:

Foreign aid; public investment; economic growth; social development; institutional competence; aid effectiveness.

DECLARATION

I certify that this thesis does not incorporate without acknowledgment any material previously submitted for a degree or diploma in any university; and that to the best of my knowledge and belief it does not contain any material previously published or written by another person except where due reference is made in the text.

Signed 

Date 28 May 2018

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LIST OF ABBREVIATIONS

ADB	-	Asian Development Bank
ADP	-	Annual Development Program
AFT	-	Aid for Trade
AIIB	-	Asian Infrastructure Investment Bank
AIMS	-	Aid Information Management System
AP-DEF	-	Asia Pacific Development Effectiveness Facility
AusAid	-	Australian Aid
BDF	-	Bangladesh Development Forum
BNSDS	-	Bangladesh National Sustainable Development Strategy
BRIC	-	Brazil, Russia, India and China
CFC	-	Chlorofluorocarbon
CO ₂	-	Carbon Di-oxide
CPI	-	Consumer Price Index
CPI	-	Corruption Perception Index
DAC	-	Development Assistance Committee
DDM	-	Double Deficit Method
DFID	-	Department for International Development
DMA	-	Dhaka Metropolitan Area
EC	-	European Commission
EIA	-	Environmental Impact Assessment
ERD	-	Economic Relations Division
EU	-	European Union
FDI	-	Foreign Direct Investment
FFW	-	Food for Work
FY	-	Fiscal Year
GDP	-	Gross Domestic Product
GFC	-	Global Fund for Climate Change

GPEDC	-	Global Partnership for Effective Development Cooperation
HAP	-	Harmonised Action Plan
IATI	-	International Aid Transparency Initiative
IDA	-	International Development Association
IDB	-	Islamic Development Bank
IMF	-	International Monetary Fund
IPCC	-	Intergovernmental Panel on Climate Change
JCS	-	Joint Cooperation Strategy
LCG	-	Local Consultative Group
LDCs	-	Least Developed Countries
MDGs	-	Millennium Development Goals
MTBF	-	Medium-Term Budgetary Framework
NGO	-	Non-Government Organisation
NPDC	-	National Policy on Development Cooperation
ODI	-	The Overseas Development Institute
OECD	-	Organisation for Economic Co-operation and Development
PFM	-	Public Financial Management
PPP	-	Public-Private Partnership
SAPs	-	Structural Adjustment Programs
SWAp	-	Sector-wise Approach
UK	-	United Kingdom
UN	-	United Nations
UNDP	-	United Nations Development Programme
UNEP	-	United Nations Environment Programme
VAT	-	Value Added Tax
VGf	-	Vulnerable Group Feeding
WB	-	The World Bank

CHAPTER 1: THE FOREIGN AID REGIME IN BANGLADESH

1.1. Motivation

“Foreign aid very often and very accurately, I believe, is a condition of taking money from the poor people in a rich country and giving it to the rich people of a poor country.”¹

----- Ron Paul, an author and former American Congressman.²

“Aid has been, and continues to be, an unmitigated political, economic, and humanitarian disaster for most parts of the developing world.”³

----- Dambisa Moyo, an economist and author.⁴

‘Foreign aid’ or ‘development assistance’ or ‘development aid’ or ‘aid’ is a mechanism to support poor countries to achieve their long-standing economic, social and human development.⁵ Rich countries and multilateral aid agencies extend foreign aid in forms of financial and technical assistance. Foreign aid, basically comprising of loans and grants, intends to achieve sustainable development of poor countries through being invested in development initiatives.⁶ Nevertheless, the effectiveness of aid in achieving economic development for the recipient countries has always been open to challenge. Aid has been criticised as a wastage of resources, along with the charge that it does not aim to develop the poor countries, but continues the dependency of these countries on foreign aid donors.⁷ Institutional incompetence, corruption, political instability, macroeconomic policy issues and environmental hazards of the recipient countries along with aid conditionality from the donors are the most conspicuous reasons behind the ineffectiveness of aid.⁸ Bangladesh is a developing country (for more information on Bangladesh, see Appendix), and it experiences notable drawbacks in aid management like most other developing countries. A school of thought claims that aid has not contributed much to the economic growth of Bangladesh, rather it has benefited the non-democratic politicians and bureaucrats, and also increased unproductive public expenditure.⁹

¹ R. Paul, *Pillars of Prosperity: Free Markets, Honest Money, Private Property*, Ludwig von Mises Institute, Auburn, Alabama, 2008, p. 342.

² Ron Paul is an author and former American Congressman (Texas). He has written several books including *Pillars of Prosperity: Free Markets, Honest Money, Private Property*, and *A Foreign Policy of Freedom*.

³ D. Moyo, *Dead Aid: Why Aid Is Not Working and How There Is a Better Way for Africa*, Farrar, Straus and Giroux, New York, 2009, p. xix.

⁴ Dambisa Moyo is a well-known global economist and author born in Zambia. Her two bestselling books are *Dead Aid: Why Aid Is Not Working and How There Is a Better Way for Africa*, and *Winner Take All: China's Rush for Resources and What It Means for the Rest of the World*.

⁵ C. Lancaster, *Foreign Aid: Diplomacy, Development, Domestic Politics*, University of Chicago Press, Chicago and London, 2008, pp. 44-45.

⁶ T. Rady, ‘Foreign Aid and Development: What Can Developing Nations Learn’, *Journal of Economics and Economic Education Research*, vol. 13, no. 3, 2013, pp. 123-125.

⁷ F. Bourguignon and M. Sandburg, ‘Aid Effectiveness - Opening the Black Box’, *American Economic Review*, vol. 97, no. 2, 2007, pp. 316-318; P. Collier, ‘Aid ‘Dependency’: A Critique’, *Journal of African Economics*, vol. 8, no. 4, 1999, pp. 528-530.

⁸ M. In'airat, ‘Aid Allocation, Selectivity, and the Quality of Governance’, *Journal of Economics, Finance and Administrative Science*, vol. 19, no. 36, 2014, pp. 63-65.

⁹ B. Hossain, ‘The Effect of Foreign Aid on the Economic Growth of Bangladesh’, *Journal of Economics and Development Studies*, vol. 2, no. 2, 2014, pp. 103-104.

It is relatively easy to identify development projects in Bangladesh that failed to impact economic development due to these deficiencies. The evaluation report of one such failed project shows how aid can be ineffective in achieving its target outcomes. The 'Dhaka Urban Transport Project' aimed to improve urban transport system in the Dhaka Metropolitan Area (DMA), and to strengthen the institutional competence for long-term transport planning and coordination.¹⁰ With a US\$177 million allocation from the World Bank (WB), this project planned to build infrastructure, provide equipment to the relevant government authorities and procure consultancy services. Although the project was supposed to be completed in 2005, it was completed in 2006. The Evaluation Report (2007) appraises that the project could achieve some infrastructure development such as building roads, road signals and a flyover, but some of the major construction works were dropped due to poor progress in implementation. Only 53% of the planned infrastructure and services were implemented. Institutional strengthening and policy frameworks were not achieved due to low quality training and capacity-building programs.¹¹ A flyover was expected to alleviate the traffic congestion but ultimately it failed to achieve the outcomes. The WB itself rated the overall project outcomes as moderately unsatisfactory.¹² The performance of both the WB and the government entities has been unsatisfactory in that they ultimately had negligible impact on development of the concerned sector. The WB had substantial deficiencies in the project identification, preparation and appraisal phases. Institutional incompetence such as procedural delays, lack of commitment and accountability, administrative hurdles, indecisiveness and inadequate planning were the drawbacks from government authorities behind the project's failure.¹³

This particular case study suggests that foreign aid has very little or nothing to contribute to the economic growth of Bangladesh, implying that aid is a wastage of resources. But, there is more to the story of aid utilisation in Bangladesh. Despite some limitations in aid management, there is much evidence that aid is a blessing for Bangladesh and aid has been instrumental to achieve increased economic growth for the country.¹⁴ Donors' support has been very effective in achieving MDGs, improving Human Development criteria such as health and education, and meeting the financing shortfalls in implementing the development projects.¹⁵ Therefore, this paper argues that on balance foreign aid has positive impacts on economic growth and development of Bangladesh by contributing to capital accumulation and public investment in socioeconomic development approaches. This paper also claims that presently aid is more feasible than other alternatives for closing the financing

¹⁰ The World Bank (WB), *Project Performance Assessment Report Bangladesh: Dhaka Urban Transport Project*, The WB Report No. 39323, Dhaka, 2007, pp. 2-3, <<http://www.oecd.org/countries/bangladesh/39618742.pdf>>, consulted 09 March 2018.

¹¹ The World Bank, pp. 9-10.

¹² The World Bank, p. 13,

¹³ The World Bank, pp. 14-15.

¹⁴ M.Q. Rahim, 'Effects of Foreign Aid on GDP Growth and Fiscal Behavior: An Econometric Case Study of Bangladesh', *The Journal of Developing Areas*, vol. 38, no. 2, 2005, p. 95.

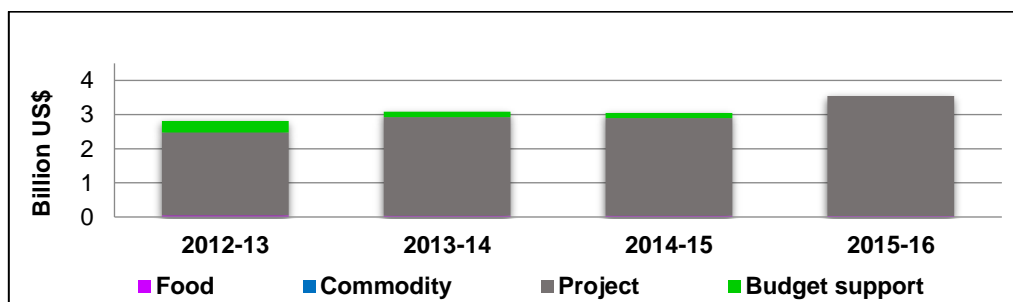
¹⁵ The Planning Commission of Bangladesh, *Millennium Development Goals: Bangladesh Progress Report 2015*, Government of Bangladesh, Dhaka, 2015, pp. 9-13, <http://www.plancomm.gov.bd/wp-content/uploads/2015/09/MDGs-Bangladesh-Progress-Report_-PDF_Final_September-2015.pdf>, consulted 12 March 2018.

gaps in Bangladesh, and aid returns can be maximised if aid effectiveness measures are implemented properly under sound macroeconomic framework.

1.2. Aim and Objective:

Bangladesh is considerably dependent on foreign aid to undertake various development activities as it has enormous constraint in domestic resources. Figure 1.1 shows that Bangladesh has mobilised around US\$3 billion in foreign aid annually to meet its fiscal deficit in recent years, which is 1% of the total GDP and 11% of the national budget in a year.¹⁶ Bangladesh already has an outstanding external debt totalling US\$29.19 billion. Yet still, both the short-term and long-term future plans of Bangladesh rely on investing high volumes of aid.¹⁷ Bangladesh is continuing its aid dependency to achieve economic growth while the effectiveness of aid has been controversial for the developing countries.¹⁸

Figure 1.1: Annual disbursement of foreign aid with aid categories (from FY 2012-13 to 2015-16).



(Source: ERD 2016)

Like most other developing countries, aid effectiveness is a debatable issue in Bangladesh because it raises some unsettling economic questions. For instance:

- i) What are the impacts of aid utilisation on growth and development?¹⁹
- ii) To what extent does aid effectiveness depend on the macro-economic policy framework?²⁰
- iii) To what extent do corruption, institutional incompetence, political instability and aid conditionality impede aid effectiveness?²¹

¹⁶ Economic Relations Division (ERD), *Flow of External Resources into Bangladesh (As of 30 June 2016)*, Ministry of Finance, Government of Bangladesh, Dhaka, 2016, pp. 1-8.

¹⁷ The Planning Commission of Bangladesh, *Seventh Five Year Plan: FY2016-FY2020*, Government of Bangladesh, Dhaka, 2015, <http://www.plancomm.gov.bd/wp-content/uploads/2015/11/7FYP_after-NEC_11_11_2015.pdf>, consulted 10 March 2018.

¹⁸ N. Gulrajani, 'Transcending the Great Foreign Aid Debate: Managerialism, Radicalism and the Search for Aid Effectiveness', *Third World Quarterly*, vol. 32, no. 2, 2011, pp. 199-200.

¹⁹ Hossain, pp. 103-104.

²⁰ K.M. Istiak, 'Foreign Aid to Bangladesh: Some Iconoclastic Issues', *The Journal of Developing Areas*, vol. 46, no. 1, 2012, p. 331.

²¹ M.M. Rahaman and N.A. Khan, 'The Realities of Aid Harmonisation and Aid Effectiveness: Views from Bangladesh', *Asia Pacific Journal of Public Administration*, vol. 32, no. 1, 2010, p. 109.

- iv) Is aid essential for Bangladesh or are alternative sources, such as internal revenue generation, more viable than aid?²²

This study intends to address these questions and, in doing so, resolves its foremost aim which is to assess how much foreign aid is contributing to the economic growth and development of Bangladesh. At the same time, the alternatives of aid, and the impediments for aid effectiveness along with the likely policy implications that can ensure the optimum benefit of aid utilisation, have also been explored in this study.

1.3. Justification and Significance

The contribution of foreign aid to economic growth and development as found in aid-growth literature is indecisive. Researchers like Easterly and Moyo strongly oppose the effectiveness of aid on development while Hansen and Tarp as well as Moreira intensely believe that aid can positively impact growth and development.²³ Most of the earlier studies focus on the developing countries overall by using cross-section panel data that created more confusion and thus often concluded with contradictory outcomes of aid on growth.²⁴ Bangladesh has been included as a sample in some of the cross-country studies, although it is not enough to investigate the effectiveness of aid in Bangladesh. Conversely, the limited studies that have been conducted exclusively on Bangladesh have some limitations such as covering aid data for short periods and overlooking external factors associated with aid flow.²⁵ Hence, there is enough scope for extensive research in this area to comprehend the importance and modalities of aid utilisation in Bangladesh. This study contributes to the existing literature in several areas. Firstly, this study considers the impact of aid consistently on economic, social, institution building and environmental sectors in Bangladesh. Secondly, this thesis critically analyses the feasibility of the alternatives of aid for development financing. Finally, it includes issues related to policy framework, governance, institutional competence and aid effectiveness that influence aid utilisation procedures in Bangladesh.

Weighing the contribution of aid to economic growth and development in Bangladesh will be influential to decide whether Bangladesh should prioritise effective foreign aid utilisation to meet the financing gaps in development activities, or to explore alternative sources of financing like domestic revenue generation and raising domestic savings. This study will assist policy makers, development partners and researchers to understand the real effects and importance of aid utilisation in Bangladesh for it to achieve economic growth and development.

²² Istiak, p. 341.

²³ Gulrajani, pp. 199-204.

²⁴ I.O. Fasanya and A.B. Onakoya, 'Does Foreign Aid Accelerate Economic Growth? An Empirical Analysis for Nigeria', *International Journal of Economics and Financial Issues*, vol. 2, no. 4, 2012, p. 424.

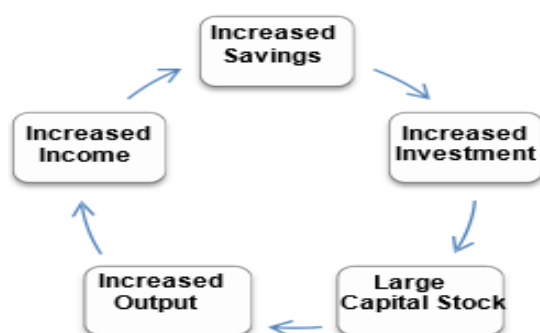
²⁵ M.W.R. Khan and H.A. Ahmed, 'Dynamics of Foreign Earnings, Assistance and Debt Servicing in Bangladesh', *International Journal of Development Issues*, vol. 11, no. 1, 2012, pp. 76-77.

1.4. Theoretical Framework

The modalities and effects of aid utilisation on growth has been highlighted from different points of views in various aid-growth studies.²⁶ Researchers use different theories and models to develop the conceptual framework to evaluate the impact of aid on development. The theoretical framework of aid-growth studies is ever evolving, aligning to the contemporary theories for growth and development of the day.²⁷

Early aid-growth studies broadly used the 'Harrod-Domar Model' of growth which aimed to evaluate the causal relationship between aid and growth through increases in savings and investment.²⁸ The basic fundamentals of this model are a) growth or income, b) savings or investments and c) capital-output ratio. Investment is considered as equal to savings. It is assumed that growth is driven by productive investment. Poor countries characterised with low savings have low investment and thus have low economic growth in turn.²⁹ Foreign aid can boost savings-investment nexus and increase economic growth. This model can be described by using the following diagram:

Figure 1.2: Impact of aid on growth through increases in savings, as per the 'Harrod-Domar Model'.



Previously, aid-growth studies have also used the 'Double Deficit Method (DDM)', prevalently known as the two-gap model. This model assumes that there might be gaps in savings-investment or export-import cycles. These gaps are considered as growth deficits which the poor countries mostly suffer from, mainly due to resource constraints.³⁰ When domestic savings are lower than investment requirements or the net receipts from exports is lower than the foreign exchange requirements for imports, the growth of a country is hampered. Foreign aid can close either or both of these gaps, assist in financing productive economic activity and thus contribute positively to economic growth.³¹

²⁶ C. Arndt, S. Jones and F. Tarp, 'Assessing Foreign Aid's Long-Run Contribution to Growth and Development', *World Development*, vol. 69, 2015, pp. 6-7.

²⁷ T.J. Mekasha and F. Tarp, 'Aid and Growth: What Meta-Analysis Reveals', *Journal of Development Studies*, vol. 49, no. 4, 2013, pp. 564-567.

²⁸ H. Hansen and F. Tarp, 'Aid and Growth Regressions', *Journal of Development Economics*, vol. 64, no. 2, 2001, p. 561.

²⁹ S. Kousar and S. Masood, 'Factors Promoting Foreign Aid Dependence in South Asian Countries', *South Asian Studies*, vol. 31, no. 1, 2017, pp. 182-184.

³⁰ M. Rahnama, F. Fawaz and K. Gittings, 'The Effects of Foreign Aid on Economic Growth in Developing Countries', *The Journal of Developing Areas*, vol. 51, no. 3, 2017, pp. 154-155.

³¹ Fasanya and Onakoya, p. 425.

The Modernisation Theory of development emphasises promoting education to produce modern individuals. It is also assumed that technological advancement can stimulate more economic activity to achieve increased economic growth.³² Modernisation Theory argues that development must be accompanied by assistance from developed countries in terms of financial and technical assistance and knowledge.³³

The Neoclassical Model of growth also has dominated aid-growth studies. This model concentrates on the fact that capital accumulation is the key to achieve economic growth. The basic motto of aid in this model is to accumulate capital in developing countries with a view to having an increased capital-labour ratio.³⁴ Aid can overcome the cost of capital depreciation and, hence, citizens can enjoy positive growth in per capita income. The improved version of the Neoclassic Model supports the belief that, besides capital accumulation, aid contributes to an acceleration toward technological evolution.³⁵ Moreover, some policy issues that can influence aid utilisation are been taken care of.

The contribution of foreign aid to growth is also acknowledged by the Human and Social Development Approaches. The Human Development Approach promotes human capital and capabilities like education, health, equality in income distribution, choice, and freedom and so on.³⁶ The Social Development Approach focuses on the overall well-being of people that makes them able to participate in economic activities equally and equitably, which eventually leads to increased economic growth for the country.³⁷ A significant portion of the aid in the form of technical assistance – utilised in human and social development such as health, education, skills development, social safety nets, governance, and justice and so on – is useful for development.³⁸

The Organisation for Economic Co-operation and Development (OECD) – through the Paris Declaration (2005), the Accra Agenda for Action (2008) and the Busan High Level Forum (2011) – recognises some guidelines that can ensure better aid utilisation and better impact of aid on growth and development.³⁹ The Paris Declaration focuses on Ownership, Alignment, Harmonisation, Results and Mutual Accountability. The Accra Agenda for Action draws attention to Ownership, Inclusive Partnership, Delivery Results and Capacity Development. Finally, the Busan High Level Forum adds some integral parts of aid management such as governance, institutional competence, macroeconomic policy frameworks and global partnership to the guidelines for aid effectiveness.⁴⁰

³² B. Bull and M. Bøås, 'Between Ruptures and Continuity: Modernisation, Dependency and the Evolution of Development Theory', *Forum for Development Studies*, vol. 39, no. 3, 2012, pp. 319-321.

³³ Bull and Bøås, pp. 319-321.

³⁴ S. Byron, 'Examining Foreign Aid Fungibility in Small Open Economies', *Open Economies Review*, vol. 23, no. 4, 2012, pp. 700-702.

³⁵ K. Willis, *Theories and Practices of Development*, Routledge, London and New York, 2005, pp. 45-48.

³⁶ A. Sen, *Development as Freedom*, Knopf, New York, 1999, pp. 40-42.

³⁷ J.N. Pieterse, *Development Theory: Deconstructions/Reconstructions*, 2nd edn, SAGE publication Ltd., London, 2010, pp. 130-132.

³⁸ S. Edwards, 'Economic Development and the Effectiveness of Foreign Aid: A Historical Perspective', *Kyklos*, vol. 68, no. 3, 2015, pp. 305-306.

³⁹ E. Mawdsley, L. Savage and S.M. Kim, 'A 'Post-Aid World'? Paradigm Shift in Foreign Aid and Development Cooperation at the 2011 Busan High Level Forum', *The Geographical Journal*, vol. 180, no. 1, 2014, pp. 28-32.

⁴⁰ Mawdsley, Savage and Kim, pp. 32-33.

Recent studies on the aid-growth relationship inevitably address these aid effectiveness issues. In addition, recent studies also focus on the impact of aid on environmental protection and management because environment is a crucial determining factor for sustainable socioeconomic development.⁴¹

Considering the evolution of conceptual frameworks of aid-growth studies, this paper measures the contribution of aid to growth by evaluating the investment of aid in productive economic sectors, the Human and Social Development Approaches, institutional competence, and environmental management. The policy frameworks for aid utilisation, progress on aid effectiveness guidelines as prescribed by the OECD, and the impediments that Bangladesh needs to overcome to optimise the benefit of aid have also been researched and evaluated.

1.5. Method

This thesis adopts a qualitative approach to investigate how aid contributes to economic growth and development through investment in the public sector in Bangladesh. This study examines the underlying relationship of foreign aid with growth and development by assessing the impact of public investment from aid in terms of socioeconomic development, institutional capacity building and environmental management. In addition, I have also appraised the progress of aid effectiveness measures and the weaknesses in aid management in Bangladesh. Furthermore, the probability of the alternatives to aid in achieving growth has also been critically evaluated. Different secondary data such as scholarly resources, government reports and donors' reports pertinent to the considerable variables and issues have been reviewed for this study. Aid data for the period of 1972-2016 has been analysed. The effect of aid on different criteria and variables, and the structural arrangement of aid utilisation as found in the aid-growth studies, have all been compared and analysed in the context of Bangladesh through reasoning and argumentation by using these secondary data sources and the results are presented accordingly. The secondary data sources have been utilised in this study due to time constraints. These secondary data sets are not complete because different organisations commissioning or collecting the data did so during different periods of time for the same variables. There might also be reporting inaccuracies and manipulation of accounts from the different reporting agents.

1.6. Outline of the Paper

This paper is structured as follows. **Chapter 2** follows the evolution of aid-growth literature over the decades in terms of theoretical perspectives and methodological techniques. This chapter also discusses the alternatives of aid along with their potential limitations in Bangladesh. It argues that the alternatives to aid are insufficient to meet the financing gaps required for development in Bangladesh. **Chapter 3** highlights the historical background and trends of foreign aid utilisation in

⁴¹ C. Chao *et al.*, 'Foreign Aid, Government Spending, and the Environment', *Review of Development Economics*, vol. 16, no. 1, 2012, pp. 62-63.

Bangladesh. This chapter also demonstrates the aid investment scenario in different economic and social sectors in Bangladesh. **Chapter 4** is dedicated to the impact analysis of aid on economic growth and development. This chapter explains the main argument of this paper that foreign aid has a positive impact on growth and development by contributing to investment and capital accumulation. **Chapter 5** deals with the problems and impediments that Bangladesh faces in aid utilisation. Particular focus has been given to corruption, institutional incompetence, political instability and aid conditionality. The likely solutions to the problems in aid utilisation are considered in **Chapter 6**. The aid effectiveness measures and the macroeconomic policy frameworks are also covered in this chapter. This chapter validates the argument that the impact of aid can be maximised if proper steps are taken to remove the impediments to aid utilisation and ensure aid effectiveness measures. **Chapter 7** concludes the thesis paper by succinctly synthesising the key findings, scope for future research and policy implications.

CHAPTER 2: THE AID-GROWTH DEBATE

2.1. Literature Review

2.1.1. Introduction

Foreign aid has been treated as one of the most important aspects of international relationship between developing and developed countries for many decades. In addition to supporting diplomacy, foreign aid started contributing to economic growth and promoting democracy in developing countries after the Cold War.⁴² The changes in patterns, modalities and objectives of aid utilisation have been closely monitored and reported in literature on the aid-growth relationship over the decades. Developing countries are largely dependent on aid, particularly to finance development initiatives. Nevertheless, aid effectiveness for economic growth and development has always been debated, even in aid-growth literature.⁴³ Though several quality studies have specifically aimed to evaluate the aid-growth relationship, the effectiveness of aid on growth and development in literature still remains indecisive.⁴⁴ Literature on aid effectiveness is ever developing in terms of hypothetical, methodological and conceptual perspectives.

2.1.2. Literature on the impact of aid on economic growth and development

The 'aid debate' is one of the most significant phenomenon in aid-growth literature. The debate ensues based on the disputed impact of foreign aid on macro-economic variables such as economic growth, poverty and inequality, and the subsequent impact of aid on the overall economic development of the recipient countries.⁴⁵ One school of thought claims that aid impacts positively on growth and development by contributing to capital accumulation and investment in economic activity and social development.⁴⁶ In addition, some of the research in this school of thought attribute the necessity of a policy-centric environment – including economic policies, matters of governance and institutional competence – as a precondition to ensuring aid effectiveness. Gulrajani ranks this school of thought as aid 'managerial reformers'.⁴⁷ In contrast, another school of thought argues that aid makes no contribution to investment or capital accumulation, in turn resulting in no contribution to growth and development either. They claim that aid is a waste of public money as it increases corruption and non-productive expenditure of the recipient governments.⁴⁸ They further claim that the flow of aid is harmful to the local economy of the recipient as it discourages domestic savings and investment, while increasing dependency on external powers. Interestingly, most of the aid

⁴² Lancaster, p. 44.

⁴³ R. Sobhan, 'Challenging the Injustice of Poverty: Rethinking Aid Strategies' in S. Folke and H. Nielsen (eds.), *Aid Impact and Poverty Reduction*, Palgrave Macmillan, New York, 2006, pp. 31-32.

⁴⁴ Fasanya and Onakoya, p. 424.

⁴⁵ Gulrajani, pp. 199-200.

⁴⁶ C. Arndt, S. Jones and F. Tarp, 'What Is the Aggregate Economic Rate of Return to Foreign Aid?', *The World Bank Economic Review*, vol. 30, no. 3, 2016, pp. 469-472.

⁴⁷ Gulrajani, pp. 199-200.

⁴⁸ S. Djankov, J. Garcia-Montalvo and M. Reynal-Querol, 'Does Foreign Aid Help?', *The Cato Journal*, vol. 26, no. 1, 2006, p. 2.

critics are from neoliberal and neo-Marxist schools who uncharacteristically come to consensus against aid.⁴⁹ To Gulrajani, these scholars are aid ‘radicals’. The aid debate persists in all generations of aid-growth literature although it peaks in more recent studies.

2.1.2.1. Generations of aid-growth literature

Hansen and Tarp group the studies on the aid-growth relationship into three different generations. The ‘First-Generation’ studies during the 1960s considered foreign aid as an “exogenous net increment of the capital stock of the recipient country”.⁵⁰ Pro-aid economists counted each dollar increase in aid as one dollar increase in savings and investments. The researchers mostly used the ‘Harrod-Domar Model’ of growth which expresses the casual correlation of aid with growth through increases in savings and investment, because capital accumulation is assumed to be the key to growth.⁵¹ The ‘Double Deficit Method’ was also frequently used where the impact of aid is evaluated from its contribution to export-import gaps or saving-investment gaps. Conversely, despite recognising the positive impacts of aid in the savings-investment-growth cycle, the First-Generation study admits that excessive foreign capital inflow may affect the domestic saving tendency of recipient countries. Since aid is easily available, it reduces the incentives and opportunities for domestic investors, and this can affect growth in the long run.⁵²

The ‘Second-Generation’ studies during the early 1970s to the early 1990s directly focused on estimations surrounding the aid-growth relationship instead of the aid-savings relationship, and the outputs of the aid-growth analyses advocated that aid can impact positively on growth.⁵³ Still, the focus remained on the role of aid only in capital accumulation to achieve increased economic growth and the studies of this generation are consistent with the ‘Harrod-Domar Model’ of growth’.⁵⁴

Table 2.1: Summary of the cross-country regression analyses based on the first and second-generation studies.

Impact of Aid	Savings regression	Investment regression	Growth regression
Positive	1	17	40
Negative	25	0	1
No relation	15	1	31
Total (131)	41	18	72

Source: Moreira (2005, p.29)

Moreira notes that by using periodical cross-section data, the first and second generation studies considered aid as an external factor to the economy and the impact of aid on savings, investment

⁴⁹ Gulrajani, pp. 199-200.

⁵⁰ H. Hansen and F. Tarp, ‘Aid Effectiveness Disputed’, *Journal of International Development*, vol. 12, no. 3, 2000, p. 377.

⁵¹ Hansen and Tarp, ‘Aid Effectiveness Disputed’, p. 378.

⁵² K.B. Griffin and J.L. Enos, ‘Foreign Assistance: Objectives and Consequences’, *Economic Development and Cultural Change*, vol. 18, no. 3, 1970, pp. 323-325.

⁵³ Hansen and Tarp, ‘Aid Effectiveness Disputed’, p. 385.

⁵⁴ Hansen and Tarp, ‘Aid Effectiveness Disputed’, p. 383.

and growth was calculated and analysed separately.⁵⁵ Moreira also states that the studies of these generations believed in the long-standing positive impact of aid on growth (Table 2.1).

The Third-Generation studies have developed both conceptual and methodological modifications in aid-growth literature. According to Roodman, the 'Third-Generation' studies started with Boone's work in 1994, are still continuing today.⁵⁶ Hansen and Tarp differentiated 'Third-Generation' studies from the earlier two generations as considering large panel data from many developing countries and economic sectors, policy variables (i.e. institutional competence, economic policies), 'endogeneity of aid'⁵⁷, separation of aid from foreign capital inflow, and non-linear aid-growth relationships.⁵⁸ These more recent Third-Generation studies on the aid-growth relationship use different stipulations, samples and methods to reach different contested opinions. Even the studies that use the same data and methods often come to different conclusions!⁵⁹ These aid-growth studies broadly conclude that the aid-growth relationship is either positive, or that aid does not impact on growth, or that aid negatively impacts on growth.⁶⁰

2.1.2.2. Literature on the positive aid-growth relationship

The recent studies which find a positive aid-growth correlation can generally be clustered as having 'unconditional' and 'conditional' impact of aid.⁶¹ Using various methods and samples, several studies find a positive aid-growth relationship regardless of the policy environment in the recipient countries. Moreira goes against the earlier perception of there being a 'non-existing aid-growth relationship' and the 'micro-macro paradox'⁶², arguing that aid has a straightforward positive effect on growth.⁶³ Hansen and Tarp also find an unconditional, positive and coherent outcome of aid utilisation, claiming that the aid-growth relationship is not hampered even in a country with an unfavourable policy environment.⁶⁴ Showing evidence from Albania, Reci argues that aid is very effective for delivering public services such as health, education, water and power in poor countries and, thus, aid is successful from a social development perspective.⁶⁵ Aided initiatives in Social Development Approaches and technical assistance in terms of capacity building enhance economic activities,

⁵⁵ S.B. Moreira, 'Evaluating the Impact of Foreign Aid on Economic Growth: A Cross-Country Study', *The Journal of Economic Review*, vol. 30, no. 2, 2005, pp. 28-29.

⁵⁶ D. Roodman, 'The Anarchy of Numbers: Aid, Development, and Cross-Country Empirics', *The World Bank Economic Review*, vol. 21, no. 2, 2007, p. 257.

⁵⁷ Endogeneity is a change which arises from within a system or model. For instance, a change in donor-recipient relationship may result in an endogenous change in aid allocation. Due to the changed contexts, the aid flow may increase or decrease that ultimately may hamper aid-consumption nexus.

⁵⁸ Hansen and Tarp, 'Aid Effectiveness Disputed', pp. 385-386.

⁵⁹ H. Doucouliagos and M. Paldam, 'Aid Effectiveness on Growth: A Meta Study', *European Journal of Political Economy*, vol. 24, no. 1, 2008, pp. 1-5.

⁶⁰ K. Gyimah-Brempong, J.S. Racine and A. Gyapong, 'Aid and Economic Growth: Sensitivity Analysis', *Journal of International Development*, vol. 24, no. 1, 2012, p. 19.

⁶¹ Gyimah-Brempong, Racine and Gyapong, p. 19.

⁶² The perception that aid impacts at micro level only, not at macro level is commonly known as the 'micro-macro paradox'

⁶³ Moreira, p. 34.

⁶⁴ Hansen and Tarp, 'Aid Effectiveness Disputed', p. 384.

⁶⁵ A. Reci, 'Advantages and Disadvantages of Foreign Assistance in Albania', *Forum Scientiae Oeconomia*, vol. 2, no. 3, 2014, pp. 123-125.

ensure the public wellbeing and can eventually encourage both social and economic development of the beneficiary country.⁶⁶

Nevertheless, Clemens *et al.* state that, depending on the policy environment in the recipient country, aid positively impacts on growth via an increase in investment.⁶⁷ Burnside and Dollar claim that when aid is combined with good fiscal, monetary, and trade policies, it can positively contribute to growth, but aid has an insignificant effect in a poor policy environment.⁶⁸ By increasing domestic investment, aid has had a strong positive effect on growth in Nigeria and other developing countries but political instability in the recipient countries is a great concern for both the recipients and the donors.⁶⁹ Aid generates the greatest positive impact on growth when it remains between the thresholds of 6.6% to 14.4% of the Gross National Income of a recipient country.⁷⁰ Sachs claims that aid accelerates capital accumulation, economic growth and household income. He argues that aid is effective for humanitarian emergencies, financing public sector investments and budgets, and financing private businesses through micro-finance. This last benefit helps breaking the poverty trap by lifting households above a subsistence level of existence by increasing their capital stock.⁷¹ Sahoo and Sethi report notable economic growth in India and other developing countries due to aid utilisation, although growth is not equally translated to economic development because of institutional incompetence, the unequal distribution of wealth, and corruption.⁷²

2.1.2.3. Literature on the negative or no aid-growth relationship

In contrast to literature on the positive impact of aid, some researchers conclude that aid marks either zero or negative outcome for economic growth. Conducting different 'economic analyses' with the data of 88 developing countries, Easterly finds no correlation between aid and investment in 87 countries except Zambia and thus concludes growth is not impacted by aid.⁷³ Revisiting the cross-section of evidence, Rajan and Subramanian also do not find any association between aid and growth, regardless of the categories of aid and policy environments.⁷⁴ Conversely, Moyo, one of the most well-known critics of aid, claims that existing aid mechanism has not had any positive impact on growth, rather it brings negative growth in most of the recipient nations including African countries.⁷⁵ Analysing the African aid data during 1970-2000, she claims that the higher the aid flow, the lower the economic growth. Djankov, Garcia-Montalvo and Reynal-Querol claim that economic

⁶⁶ T. Addison, M. Niño-Zarazúa and F. Tarp, 'Aid, Social Policy and Development', *Journal of International Development*, vol. 27, no. 8, 2015, pp. 1351-1355.

⁶⁷ M.A. Clemens *et al.*, 'Counting Chickens When They Hatch: Timing and the Effects of Aid on Growth', *The Economic Journal*, vol. 122, no. 561, 2012, pp. 613-614.

⁶⁸ C. Burnside and D. Dollar, 'Aid, Policies, and Growth', *The American Economic Review*, vol. 90, no. 4, 2000, p. 864.

⁶⁹ Fasanya and Onakoya, pp. 424-425.

⁷⁰ Gyimah-Brempong, Racine and Gyapong, p. 18.

⁷¹ J.D. Sachs, *The End of Poverty: Economic Possibilities for Our Time*, The Penguin Press, New York, 2005, pp. 245-246.

⁷² K. Sahoo and N. Sethi, 'Effect of Foreign Aid on Economic Growth and Development in India: An Empirical Analysis', *South Asian Journal of Management*, vol. 20, no. 1, 2013, p. 132.

⁷³ W. Easterly, 'Can Foreign Aid Buy Growth?', *The Journal of Economic Perspectives*, vol. 17, no. 3, 2003, pp. 32-33.

⁷⁴ R.G. Rajan, and A. Subramanian, 'Aid and Growth: What Does the Cross-Country Evidence Really Show?', *The Review of Economics and Statistics*, vol. 90, no. 4, 2008, pp. 659-660.

⁷⁵ Moyo, pp. 6-8.

growth is negatively impacted by foreign aid because aid increases non-productive government consumption and reduces investment.⁷⁶

2.1.2.4. Gaps in aid-growth literature

We can find literature supporting the positive aid-growth relationship but then we can find other literature challenging it. Glennie and Sumner note that most of the studies over the last decade show the positive effects of aid utilisation and thus suggest aid critics to rethink their negative findings.⁷⁷ They claim that debate on aid effectiveness in literature needs to be coherent and evidence-based as the studies often lack both definitional and methodological perfection.⁷⁸ Referring to the 'Paris Declaration'⁷⁹, they argue that aid effectiveness issues should not only be prioritised by the recipients and donors but also be reflected in literature on aid-growth relationship.⁸⁰ Sometimes literature on the aid-growth relationship has methodological and econometric weaknesses that may represent unreliable outcomes of regression studies.⁸¹ Tarp states that modern studies generally find positive impacts of aid on growth although researchers like Easterly often ignore these studies and criticise aid by using only cross-country works.⁸² He also notes that cross-country works may not be free of meaningless data and inappropriate variables which ultimately produce a zero result in the analysis.⁸³ Proclaiming the positive correlation among aid, growth and poverty reduction, Tarp calls for extensive and specific country based research to decide on the overall impact of aid on development.⁸⁴

2.1.3. Literature on the impact of aid on economic growth of Bangladesh

Turning to Bangladesh, there have been a limited number of studies which have evaluated the contribution of foreign aid to economic growth. Like other aid-growth literature, the studies on Bangladesh also find contradictory impacts of aid on economic growth and development. Hossain claims that foreign aid can be effective for economic growth in Bangladesh, though due to the institutional incompetence of Bangladesh in effective aid utilisation, aid generates nominal returns in Bangladesh.⁸⁵ In the context of savings-investment and export-import gaps, foreign aid generally raises the investment and savings of a country, but aid impacts inversely on domestic savings in Bangladesh.⁸⁶ Islam claims that foreign aid in terms of loans rather than grants, has some positive impact on growth but domestic resources are actually more instrumental for growth than foreign

⁷⁶ Djankov, Garcia-Montalvo and Reynal-Querol, p. 2.

⁷⁷ J. Glennie and A. Sumner, *Aid, Growth and Poverty*, Palgrave Macmillan, London, 2016, p. 75.

⁷⁸ Glennie and Sumner, p. 75.

⁷⁹ The Paris Declaration (2005) adopted by the Organisation for Economic Co-operation and Development (OECD), frames a guideline both for the donors and recipients to collectively work on aid effectiveness.

⁸⁰ Glennie and Sumner, pp. 75-77.

⁸¹ Moreira, p. 27.

⁸² F. Tarp, 'Aid and Development', *Swedish Economic Policy Review*, vol. 13, no. 2, 2006, pp. 46-47.

⁸³ Tarp, pp. 46-47.

⁸⁴ F. Tarp, 'Aid, Growth, and Development' in G. Mavrotas (ed.), *Foreign Aid for Development: Issues, Challenges, and the New Agenda*, Oxford University Press, New York, 2010, p. 47.

⁸⁵ Hossain, pp. 103-104.

⁸⁶ Istiak, p. 331.

aid.⁸⁷ Rahim argues that loans provided for public investment have a positive impact on growth but grants are mostly expended in non-productive civil expenditures.⁸⁸ Bangladesh is making some slow progress on aid effectiveness but aid cannot promote economic growth unless the aid effectiveness is ensured as per the 'Paris Declaration'.⁸⁹

These studies on the aid-growth relationship in Bangladesh are mostly dependent on data over a limited period of time and across a limited number of sectors.⁹⁰ These studies partially consider the impact of policy variables while measuring the effects of aid utilisation on growth.⁹¹ This literature on Bangladesh mostly focuses on the aid-growth relationship through investment in the economic sectors only, while aid can contribute to growth through Human and Social Development Approaches as well.

2.1.4. Conclusion

Studies on the aid-growth relationship mostly denote that aid positively impacts on growth, although specific and extensive research is required to weigh the real impact of aid on growth and development in Bangladesh. The study on the aid-growth relationship in Bangladesh needs to necessitate definitional and methodological perfection which is supported by large and correct panel data, coherent evidence and appropriate representation of the findings. Furthermore, considering the impact of aid on economic sectors only is insufficient to analyse the real impact of aid overall and, thus, the contribution of aid to social development activities is also to be negotiated in aid-growth literature. In addition, macro-economic policy variables, institutional competence, feasibility of the alternatives to aid, impediments for aid utilisation and the progress of aid effectiveness measures in Bangladesh should also be reflected in aid-growth studies on Bangladesh.

2.2. Alternatives to Aid in Bangladesh

2.2.1. Introduction

Bangladesh needs to undertake massive development in the economic and social sectors to attain increased economic growth but it has a notable constraint in capital formation and infrastructure.⁹² If Bangladesh aims to increase its economic growth from 6% to 8%, it needs to invest around 32%-34% of its GDP each year.⁹³ Bangladesh needs to depend on several external and internal sources including foreign aid to meet the investment gap.⁹⁴ Bangladesh mobilises capital for investment

⁸⁷ A.M. Islam, 'Foreign Assistance and Development in Bangladesh' in K.L. Gupta (ed.), *Foreign Aid: New Perspectives*, Springer Science + Business Media, LLC, New York, 1999, pp. 228-229.

⁸⁸ Rahim, p. 95.

⁸⁹ Rahaman and Khan, p. 109.

⁹⁰ Khan and Ahmed, pp. 76-77.

⁹¹ Khan and Ahmed, pp. 76-77.

⁹² E.A. Rana and A.N.M. Wahid, 'Fiscal Deficit and Economic Growth in Bangladesh: A Time-Series Analysis', *The American Economist*, vol. 62, no. 1, 2017, pp. 31-32.

⁹³ Bangladesh could invest 28.9% of its GDP in 2015; The Planning Commission of Bangladesh, *Seventh Five Year Plan*, p. 30.

⁹⁴ Asrafuzzaman, A. Roy and S.D. Gupta, 'An Empirical Investigation of Budget and Trade Deficits: The Case of Bangladesh', *International Journal of Economics and Financial Issues*, vol. 3, no. 3, 2013, p. 570.

mostly from internal revenue, exports and trade, Foreign Direct Investment (FDI), foreign aid, and domestic debts from the local banks. Recently, the possibility of public investment from the capital inflow of 'remittance'⁹⁵ has also been discussed.⁹⁶ Considering the disputed impact of aid on growth, it is often suggested that developing countries should focus on alternative options for public investment to reduce their dependency on aid.⁹⁷ This means Bangladesh needs to analyse whether it will continue its dependency on aid or consider other funding options for necessary public investment. This discussion intends to evaluate how far the alternatives to aid are viable to meet the public sector investment gaps in Bangladesh.

2.2.2. Alternative financing options in Bangladesh other than aid

2.2.2.1. Internal Revenue (Taxation)

Internal revenue generation, particularly taxation, is the key source of fiscal resource mobilisation and management in low-income countries, and Bangladesh is no exception to this.⁹⁸ Bangladesh still has a large annual budget deficit, however, which is financed with foreign aid and internal debt. Bangladesh is repeatedly advised to increase its revenue generation capacity to reduce its dependency on the debt. Unfortunately, however, the reality is far from expectations.⁹⁹ Bangladesh aims to generate a Tax-GDP ratio of 16.1% by 2020. It could only achieve a ratio of 9.3% tax revenue to GDP in 2015.¹⁰⁰ This is far behind of the world average Tax-GDP ratio in 2015 which was 15.06%.¹⁰¹ Only 1% of the population pays income tax and so the Tax-GDP ratio in Bangladesh is much lower than this of the South Asian countries and other developing nations.¹⁰² A poor taxation system, a weak enforcement of tax law, double taxation through Value Added Tax (VAT) and then also widespread corruption form the four major causes for this low revenue generation. Bangladesh needs to launch massive reform initiatives to increase its revenue.¹⁰³ Since Bangladesh is presently unable to increase its internal revenue generation, it cannot, therefore, reduce its dependence on foreign aid.

2.2.2.2. Export and Trade

Export earnings are one of the most crucial components of international trade for a country.¹⁰⁴ Exports contribute to economic growth by maintaining the trade balance and increasing the national

⁹⁵ Remittance is the inflow of credit to a country from the wages and salaries of its citizens who reside abroad.

⁹⁶ A.K.M.N. Hossain and S. Hasanuzzaman, 'Remittances and Investment Nexus in Bangladesh: An ARDL Bounds Testing Approach', *International Review of Economics*, vol. 60, no. 4, 2013, pp. 387-390.

⁹⁷ P. Aghion *et al.*, 'When Does Domestic Savings Matter for Economic Growth?', *IMF Economic Review*, vol. 64, no. 3, 2016, pp. 393-394.

⁹⁸ A. Sindzingre, 'Financing the Developmental State: Tax and Revenue Issues', *Development Policy Review*, vol. 25, no. 5, 2007, pp. 619-620; Rana and Wahid, pp. 31-32.

⁹⁹ M. Hassan and W. Prichard, 'The Political Economy of Domestic Tax Reform in Bangladesh: Political Settlements, Informal Institutions and the Negotiation of Reform', *The Journal of Development Studies*, vol. 52, no. 12, 2016, p. 1708.

¹⁰⁰ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, p. 122.

¹⁰¹ The World Bank (WB), 'Tax Revenue (% of GDP)', The WB's website, Washington, D.C., 2018, <<https://data.worldbank.org/indicator/GC.TAX.TOTL.GD.ZS>>, consulted 18 March 2018.

¹⁰² Rana and Wahid, p. 41.

¹⁰³ Rana and Wahid, p. 41.

¹⁰⁴ S.S. Makki and A. Somwaru, 'Impact of Foreign Direct Investment and Trade on Economic Growth: Evidence from Developing Countries', *American Journal of Agricultural Economics*, vol. 86, no. 3, 2004, p. 795.

income in Bangladesh.¹⁰⁵ To maximise export earnings, trade liberalisation has been a great policy focus for all countries. Bangladesh started its trade liberalisation in 1992 with a view to achieving efficient resource allocation, the removal of trade barriers, competitive import substitutions, greater growth in exports and eventually greater economic growth.¹⁰⁶ However, this liberalisation – comprising technology transfer as capital stock, reducing export duties or policy support – has not impacted export performance as significantly as hoped.¹⁰⁷ Bangladesh still has one of the biggest trade imbalances in the world as export earnings were only US\$31.73 billion in 2017, which was much lower than import payments of US\$48.06 billion in the same year.¹⁰⁸ Exchange rate appreciation, excessive dependency on garment production,¹⁰⁹ domestic inflation, lower price competitiveness and slow progress in removing trade barriers are all problems that slow trade performance.¹¹⁰ Therefore, it is difficult for Bangladesh to depend on export earnings for deficit financing without solving these problems first.

2.2.2.3. Foreign Direct Investment (FDI)

FDI is a significant contributor to economic growth in developing countries. It is one of the key instruments to transfer technologies and knowledge, both of which are necessary to stimulate domestic savings, investment, human development and institutional competence.¹¹¹ FDI is helpful for capital accumulation, human capital development and employment generation, thereby reducing poverty and encouraging growth.¹¹² Bangladesh aims to receive US\$9.6 billion – 3% of GDP – in the form of FDI by 2020 to ease the financing gap.¹¹³ There has been an increasing trend in FDI from US\$383.22 million in fiscal year (FY) 1999-2000 to US\$2.55 billion in FY 2016-17, though it is still much lower than expected.¹¹⁴ The government has initiated several one-stop service schemes and other policy support for foreign investors but attracting FDI has always been challenging for Bangladesh. Poor infrastructure, energy scarcity, incompetent bureaucracy, corruption and prolonged business procedures are the foremost impediments to Bangladesh in attracting FDI compared to its neighbouring countries.¹¹⁵ Bangladesh cannot expect higher FDI until it ensures political stability, better working conditions for labourers, improved safety measures, smoother

¹⁰⁵ M.M. Hoque and Z. Yusop, 'Impacts of Trade Liberalization on Export Performance in Bangladesh: An Empirical Investigation', *South Asia Economic Journal*, vol. 13, no. 2, 2012, pp. 208-209.

¹⁰⁶ Hoque and Yusop, pp. 208-209.

¹⁰⁷ Hoque and Yusop, pp. 208-209.

¹⁰⁸ World Integrated Trade Solution, 'Bangladesh Trade Statistics', The World Bank's website, Washington, D.C., 2018, <<https://wits.worldbank.org/CountryProfile/en/BGD>>, consulted 16 March 2018.

¹⁰⁹ Bangladesh's export earnings are predominantly dependent on the garments production including readymade garments and knitwear. Other export products except jute have little contribution to export earnings. Detailed statistics on Bangladesh's export earnings has been presented in Appendix 4.

¹¹⁰ M.M. Rahman, 'The Factors Affecting Bangladesh's Exports: Evidence from the Gravity Model Analysis', *The Journal of Developing Areas*, vol.44, no. 1, 2010, pp. 240-241.

¹¹¹ Makki and Somwaru, p. 796.

¹¹² S.H. Manzoor and M.E. Chowdhury, 'Foreign Direct Investments in Bangladesh: Some Recent Trends and Implications', *Journal of Business and Economics Research*, vol. 15, no. 1, 2017, p. 21.

¹¹³ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, p. 115.

¹¹⁴ Bangladesh Bank, *Foreign Direct Investment (FDI) in Bangladesh*, Government of Bangladesh, Dhaka, 2017, p. 23, <<https://www.bb.org.bd/pub/halfyearly/fdisurvey/fdisurveyjanjun2016.pdf>>, consulted 15 March 2018.

¹¹⁵ K.M.A. Islam, 'Foreign Direct Investment (FDI) in Bangladesh: Prospects and Challenges and Its Impact on Economy', *Asian Business Review*, vol. 4, no. 1, 2014, p. 30.

business processes, the necessary infrastructure and preparedness for environmental catastrophes. FDI has not significantly impacted economic growth in Bangladesh and the government still needs to do a lot to make FDI an appropriate alternative for development financing.¹¹⁶

2.2.2.4. Domestic Public Debt

Bangladesh is largely dependent on both external and domestic public debt to finance its development projects as it has a huge budget deficit every year.¹¹⁷ Bangladesh depends on domestic public debt also to offset its low internal revenue generation to meet other public expenditure. As a result, domestic public debt reached 23.1% of GDP and 192% of government revenue in FY 2016-2017.¹¹⁸ The domestic public debt is mainly sourced from the commercial banks' holdings of treasury instruments, national savings certificates, and net credit with the central bank known as 'Bangladesh Bank'.¹¹⁹ The interest rates for borrowing from commercial banks and national saving schemes are higher than that tied to foreign aid. Even the interest rate for savings certificates is higher than commercial bank loans.¹²⁰ Public borrowing from domestic sources is good for economic growth and it is welcomed provided that sufficient liquidity prevails in the banking system.¹²¹ If there is a liquidity crisis and domestic public debt is an increasing trend, it will squeeze the opportunity of private investment and the economy will suffer in the long run.¹²² Bangladesh should confine its domestic public debt to an acceptable level that can maintain financial discipline.¹²³ Therefore, it is unwise to meet the entire financing gaps using domestic public debt only, by ignoring foreign aid.

2.2.2.5. Remittance

Remittance is the inflow of credit to a country from the wages and salaries of its citizens who reside abroad. Some developing countries are largely dependent on remittance to meet foreign exchange requirements.¹²⁴ Bangladesh is also heavily dependent on remittance. In 2009, it was the 8th leading remittance-receiving country in the world in terms of total amount, and with remittance comprising around 11% of annual GDP, it was listed among the top thirty countries measured by percentage of the GDP.¹²⁵ Bangladesh received US\$12.77 as remittance from its non-resident nationals in FY

¹¹⁶ A. Rahman, 'Impact of Foreign Direct Investment on Economic Growth: Empirical Evidence from Bangladesh', *International Journal of Economics and Finance*, vol. 7, no. 2, 2015, pp. 182-183.

¹¹⁷ M. Saifuddin, 'Public Debt and Economic Growth: Evidence from Bangladesh', *Global Journal of Management and Business Research*, vol. 16, no. 5, 2016, p. 72.

¹¹⁸ International Monetary Fund (IMF), *Bangladesh: Staff Report for the 2017 Article IV Consultation-Debt Sustainability Analysis*, IMF, Dhaka, 2017, p. 2, <<https://www.imf.org/external/pubs/ft/dsa/pdf/2017/dsacr17147.pdf>>, consulted 18 March 2018.

¹¹⁹ International Monetary Fund, p. 2.

¹²⁰ International Monetary Fund, p. 3.

¹²¹ M.A. Majumder, *Does Public Borrowing Crowd-out Private Investment? The Bangladesh Evidence*, Working Paper Series: WP 0708, Bangladesh Bank, Government of Bangladesh, Dhaka, 2007, pp. 1-2, <<http://siteresources.worldbank.org/PSGLP/Resources/WP0708Final.pdf>>, consulted 18 March 2018.

¹²² G. Bua, J. Pradelli and A.F. Presbitero, 'Domestic Public Debt in Low-Income Countries: Trends and Structure', *Review of Development Finance*, vol. 4, no. 1, 2014, pp. 1-5.

¹²³ Majumder, pp. 4-5.

¹²⁴ D. Hossain, 'Differential Impacts of Foreign Capital and Remittance Inflows on Domestic Savings in Developing Countries: A Dynamic Heterogeneous Panel Analysis', *Economic Record*, vol. 90, 2014, pp. 102-104.

¹²⁵ Hossain and Hasanuzzaman, pp. 387-388.

2016-17.¹²⁶ It has been discussed whether this sizeable amount of remittance can be invested in public sectors, although no significant initiative or even a government-commissioned study has yet been instigated. Emigrant nationals are not wholly aware of the business and investment scenario in Bangladesh and are also ever-confused about the political environment, and thus they are reluctant to invest in a common fund for these reasons.¹²⁷ Remittance is one of the key instruments to maintain the balance of payments for the government and strengthen the foreign exchange reserve.¹²⁸ Remittance has the potential to be invested in the public sector in the future by building confidence among emigrant earners and providing adequate investment mechanisms. Nevertheless, being private capital, it is claimed that remittance cannot replace foreign aid presently in development financing.¹²⁹

2.2.3. Conclusion on the alternatives to aid

It is evident that Bangladesh has considerable resource gaps in its fiscal management. There are external and internal options for Bangladesh to mobilise capital to meet its fiscal deficit. From the above discussion it is apparent that, despite having significant potential, the financing options available such as internal revenue, exports and trade, FDI and remittance are not sufficiently feasible to cover the financing shortfalls and reduce dependency on debt. Therefore, the government of Bangladesh must borrow resources from internal and external sources.¹³⁰ Internal borrowings can be effective for filling the resource gaps to a certain level and, hence, Bangladesh must borrow from overseas governments and multilateral aid organisations to plug the remaining gap. Bangladesh may face some challenges in aid utilisation but it can overcome these hurdles by taking the necessary steps.¹³¹ The next chapters of this paper will explain how foreign aid is an essential funding option for Bangladesh by positively impacting on growth and development, while also exploring how Bangladesh can maximise the benefits of aid by overcoming its challenges in aid utilisation.

¹²⁶ Bangladesh Bank, 'Wage Earners Remittance Inflows', Bangladesh Bank's website, Government of Bangladesh, Dhaka, 2018, <<https://www.bb.org.bd/econdata/wagermidtl.php>>, consulted 18 March 2018.

¹²⁷ H. Zaman and M.I. Akbar, 'Exploring Non-Traditional Sources of Development Finance: The Case of Remittance in Bangladesh', *Progress in Development Studies*, vol. 13, no. 2, 2013, p. 113.

¹²⁸ Zaman and Akbar, p. 107

¹²⁹ Hossain and Hasanuzzaman, pp. 403-404.

¹³⁰ M.M. Rahman, M.A. Bashar and S. Dey, 'External Debt and Gross Domestic Product in Bangladesh: A Co-Integration Analysis', *Management Research and Practice*, vol. 4, no. 4, 2012, pp. 35-36.

¹³¹ Rahman, Bashar and Dey, pp. 35-36.

CHAPTER 3: OVERVIEW OF FOREIGN AID IN BANGLADESH

3.1. Introduction

Bangladesh has been dependent on foreign aid to meet the shortfalls in the financing of the public sector since it achieved independence from Pakistan through the Liberation War of 1971. Initially it was largely dependent on grants for humanitarian assistance such as food and commodities, and reconstruction of war-devastated infrastructure for the survival of this newly born nation.¹³² Gradually the economy of Bangladesh has stabilised and it has undertaken a series of development initiatives to achieve economic and social development for the country. Still, Bangladesh has not yet been able to overcome its financial shortfalls and remains dependent on aid, although the categories and modalities of aid utilisation have been considerably modified over time.¹³³ Bangladesh is still receiving foreign aid generally in terms of loans, which are invested in development projects. Aid is expended in different economic and social sectors to ensure sustained economic growth, human capital development, good governance, justice, resistance to environmental disasters, and so on with a view to achieving sustainable socioeconomic development.¹³⁴ At the beginning of its independence, only a few friendly countries and the United Nations (UN) offered aid but currently Bangladesh receives aid from many bilateral and multilateral countries and organisations.¹³⁵ Bangladesh mobilises around US\$3 billion in aid annually although aid effectiveness in Bangladesh is still debateable. With this backdrop, this chapter aims to provide a synopsis of aid investment modalities in Bangladesh.

3.2. Historical Background of Aid Utilisation

Bangladesh's dependency on aid is closely related to its emergence as a sovereign state from being a colonised region of Pakistan named East Pakistan. Due to resource constraints and in part due to international relationships, Pakistan started receiving substantial foreign aid in the late 1950s.¹³⁶ Initially, both the USA and the socialist bloc were the primary donors for Pakistan, although it received aid from other OECD countries too. Under the Pakistani rule, East Pakistan (Bangladesh) suffered economic and political discrimination, and ordinary East Pakistani people suffered discrimination in employment. West Pakistan drained resources from East Pakistan whose economy was already vulnerable.¹³⁷ The discrimination could also be seen in the foreign aid allocation between these two regions. East Pakistan received insufficient benefit of the aid flow and faced

¹³² Hossain, 'The Effect of Foreign Aid on the Economic Growth of Bangladesh', p. 94.

¹³³ B. Hossain, 'Nexus between Foreign Aid and Economic Growth: Evidences from Bangladesh', *Global Journal of Management and Business Research*, vol. 14, no. 6, 2014, p. 64.

¹³⁴ M.G. Quibria, 'Aid Effectiveness: Research, Policy and Unresolved Issues', *Development Studies Research*, vol. 1, no. 1, 2014, pp. 79-80.

¹³⁵ Economic Relations Division, pp. 5-7.

¹³⁶ M.A. Obaydullah, 'Impact of Foreign Aid on Development in Bangladesh', PhD thesis, RMIT University, Melbourne, Australia, 2007, pp. 38-39.

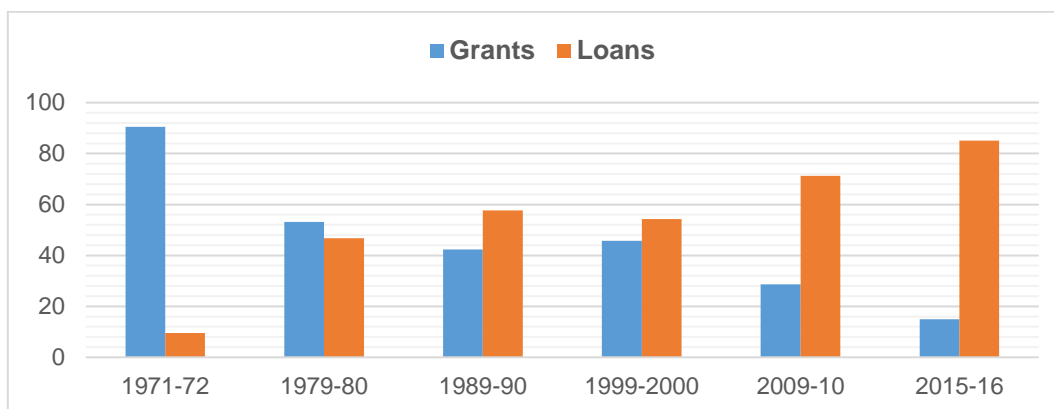
¹³⁷ R. Sobhan, *From Aid Dependence to Self-Reliance: Development Options for Bangladesh*, University Press Ltd., Dhaka, 1990, pp. 7-12.

challenges in capital formation. Consequentially, there were huge resource gaps in East Pakistan which continued even after Bangladesh's independence. As a further setback, Bangladesh had to concede a hereditary outstanding debt of US\$483 million against the projects which were completed in its territory before independence.¹³⁸

After its independence, Bangladesh inherited a dependence on aid from external sources. This was necessary because Bangladesh had huge resource gaps coupled with a need to meet imminent requirements such as emergency humanitarian assistance to the newly born nation. The initial flow of aid was utilised for food, shelter, emergency medicine, rehabilitation of misplaced people and the reconstruction of necessary infrastructure that was damaged in the war.¹³⁹ This aid was mostly bilateral in nature where India and The Soviet Union played the key role. The UN coordinated the aid received from other sources. The incurred losses of the war were notably recovered by 1973 and Bangladesh needed to launch some development activities to get its economy growing.¹⁴⁰ As the resource gaps were still there, aid flow continued and eventually aid became the necessary part of development planning of Bangladesh. Under the First Five-Year Plan (1973-1977), Bangladesh sourced 100% of the development budget (ADP) from aid, which was around 10% of GDP in those years. Bangladesh continued financing the ADP totally with aid until the 1980s.¹⁴¹ In due course, Bangladesh's aid dependency has continued to finance the development budget under different plans and aid utilisation has remains incorporated into the institutional framework. There have, however, been several modifications in categories, patterns and modalities of foreign aid in Bangladesh.

3.3. Categories of Foreign Aid in Bangladesh

Figure 3.1: The ratio of loans to grants in aid disbursement (from FY 1971-72 to 2015-16)



(Source: ERD 2016)

¹³⁸ Sobhan, *From Aid Dependence to Self-Reliance*, pp. 7-12.

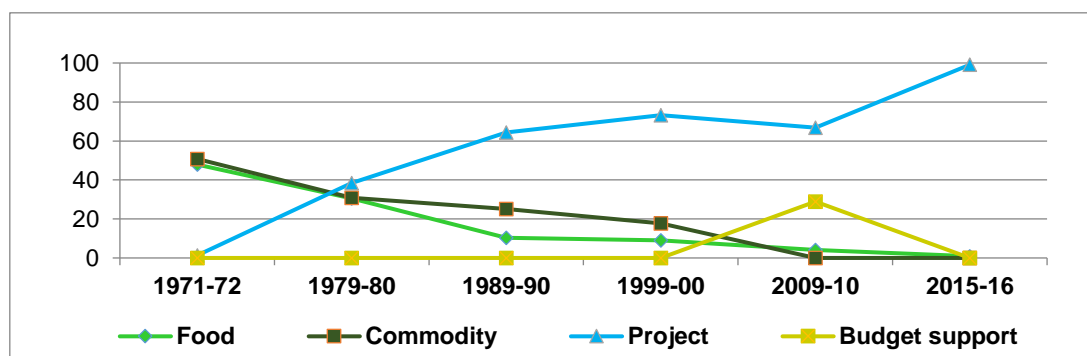
¹³⁹ Hossain, 'Nexus between Foreign Aid and Economic Growth', p. 59.

¹⁴⁰ Sobhan, *From Aid Dependence to Self-Reliance*, pp. 7-12.

¹⁴¹ Obaydullah, p. 39.

Over the years, there have been several changes in categories of foreign aid in Bangladesh. So far, Bangladesh has received foreign aid basically as Food Aid, Commodity Aid, Project Aid and Budget Support. Bangladesh has received this aid in the forms of both grants and loans. It is noticeable from Figure 3.1 that the portion of grants in aid flow is declining while loans are increasing steadily.¹⁴² The grant-loan ratio in FY 1971-72 was 90.5% to 9.5% respectively but this changed to 15% to 85% respectively in FY 2015-16. Figure 3.2 indicates that Food Aid and Commodity Aid comprised the major shares of aid in FY 1971-72 at 47.9% and 50% respectively. By contrast, by FY 2015-16, Food Aid decreased to 0.9% while Commodity Aid decreased to 0% of the total aid. The utilisation of aid as Project Aid has become the most crucial aid contributor for Bangladesh over the same period comprising 99.1% of the total aid volume in FY 2015-16, compared to comprising only 1.3% of total aid volume back in FY 1971-72.¹⁴³ Bangladesh has occasionally received Budget Support from the International Monetary Fund (IMF) during FY 1989-90 to 2014-15 and has not received any Budget Support in FY 2015-16.

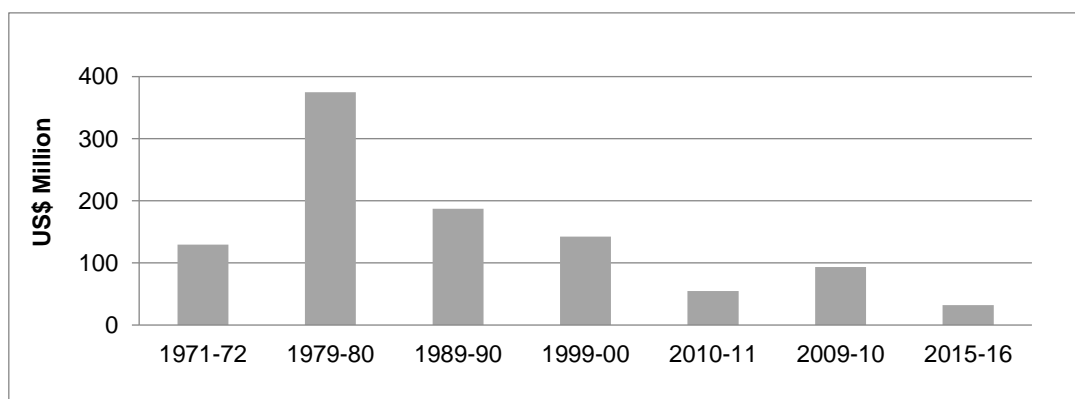
Figure 3.2: Percentage of aid categories in aid disbursement (from FY 1971-72 to 2015-16).



(Source: ERD 2016)

3.3.1. Food Aid

Figure 3.3: Disbursement of Food Aid (from FY 1971-72 to 2015-16).



(Source: ERD 2016)

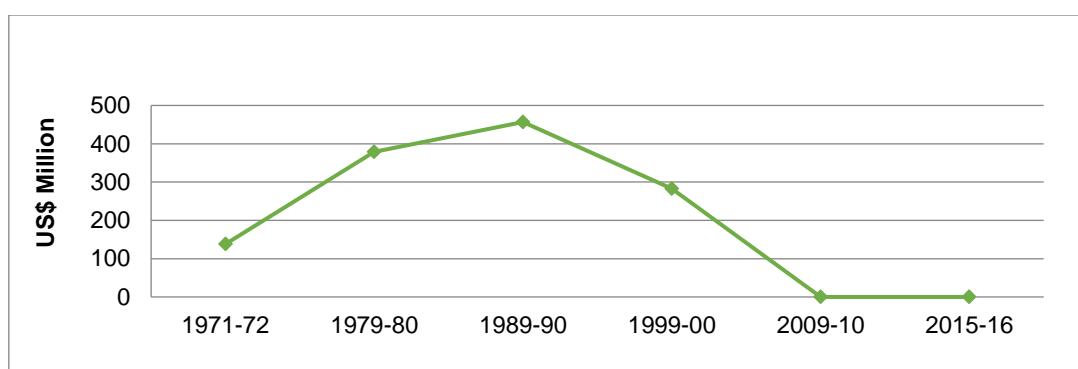
¹⁴² Hossain, 'Nexus between Foreign Aid and Economic Growth', p. 60.

¹⁴³ Economic Relations Division, p. 6.

Since gaining independence, Bangladesh has depended on Food Aid to address its deficiency in food supply resulting in part from its war for independence and several natural calamities including floods, cyclones and famine.¹⁴⁴ Figure 3.3 shows that dependency on Food Aid significantly continued into the 1990s. Bangladesh is almost close to achieving self-sufficiency in food by increasing its production.¹⁴⁵ Therefore, Food Aid is now generally sourced in small volumes and occasionally on a larger scale to cover the losses incurred from natural disasters. In addition, a certain level of Food Aid is utilised by different safety-net programs such as Vulnerable Group Feeding (VGF), Test Relief (TR) and Food for Work (FFW) to provide food support to the people living in extreme poverty.

3.3.2. Commodity Aid

Figure 3.4: Disbursement of Commodity Aid (from FY 1971-72 to 2015-16).



(Source: ERD 2016)

In general, Commodity Aid is received to source raw materials and intermediate input for production and manufacturing from donor countries.¹⁴⁶ The basic motto is to reduce stress on the Balance of Payments. Bangladesh has been able to increase both its export earnings and internal revenue in recent years. Furthermore, the flow of remittance from Bangladesh's expatriates living abroad has assisted Bangladesh to have an attractive foreign exchange reserve. Therefore, Bangladesh has gradually moved into a position of being able to self-manage its Balance of Payments using its own resources and has thus been able to reduce its dependency on Commodity Aid from 1990, as noted in figure 3.4, and ultimately it reached to zero in FY 2015-16 accordingly.¹⁴⁷

3.3.3. Project Aid

Figure 3.5 shows how currently the prime share of foreign aid in Bangladesh is Project Aid. This type of aid is received from the donors to finance projects that are being implemented under the ADP. These projects are categorised as Development Projects and Technical Assistance Projects. The

¹⁴⁴ N.T. Dristy, *The Macroeconomic Impact of Foreign Aid in Bangladesh Before and After the Paris Declaration*, Bangladesh Development Research Working Paper Series (BDRWPS)-32, Bangladesh Development Research Center (BDRC), Dhaka, 2016, p. 7, <http://www.bangladeshstudies.org/files/WPS_no32.pdf>, consulted 20 March 2018.

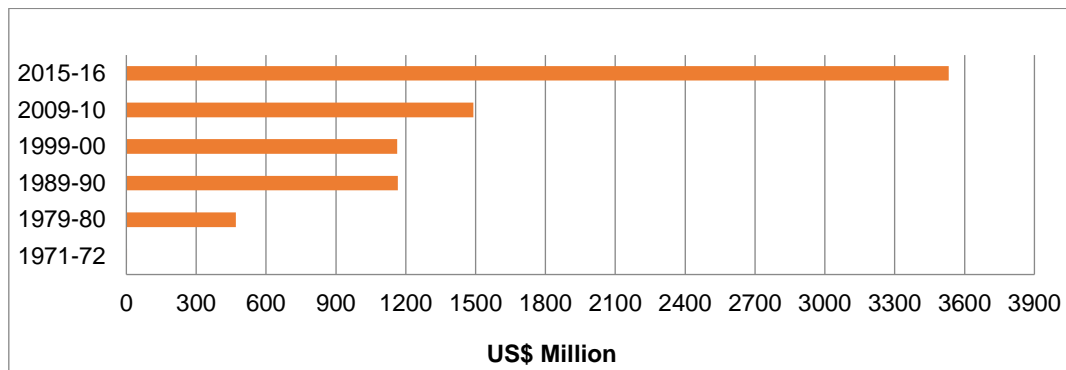
¹⁴⁵ S. Sala and S. Bocchi, 'Green Revolution Impacts in Bangladesh: Exploring Adaptation Pathways For Enhancing National Food Security', *Climate and Development*, vol. 6, no. 3, 2014, pp. 238-239.

¹⁴⁶ Obaydullah, p. 53.

¹⁴⁷ Economic Relations Division, p. 8.

development projects cover different economic and social sectors to stimulate numerous activities for economic and social development.¹⁴⁸ Technical assistance projects are implemented with a view to ensuring the institutional competence of government entities from different sectors and effectiveness of structural reforms in the macroeconomic policy framework.¹⁴⁹

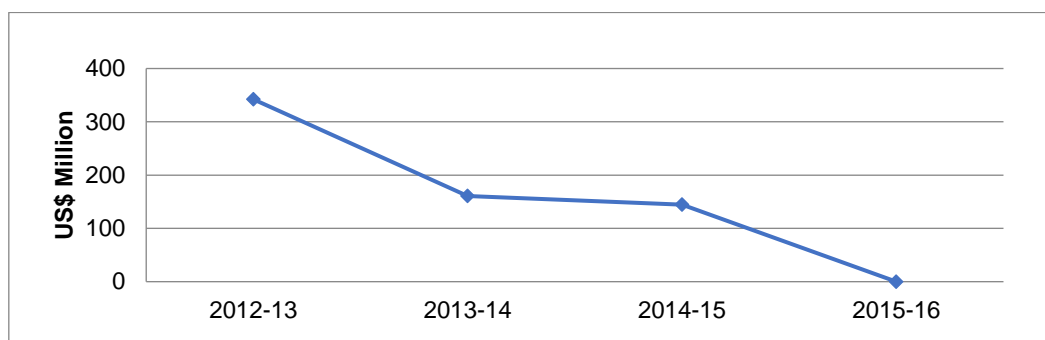
Figure 3.5: Disbursement of Project Aid (from FY 1971-72 to 2015-16)



(Source: ERD 2016)

3.3.4. Budget Support

Figure 3.6: Disbursement of Budget Support (from FY 1971-72 to 2015-16)



(Source: ERD 2016)

Budget support is offered occasionally by multilateral donors in single or multiple instalments to finance the priority programs of the recipient country.¹⁵⁰ The transaction is subject to the accomplishment of agreed policy requirements and benchmarks between the donor and recipient.¹⁵¹ Budget Support is a popular form of aid as it offers more flexibility for the recipient to spend the money in the prioritised sectors of its national interest. Bangladesh intermittently received this type of aid to adopt structural reforms in the 2000s under the Poverty Reduction Strategy Papers (PRSPs).¹⁵² Figure 3.6 notes that Budget Support fell to zero in FY 2015-16.

¹⁴⁸ M.S. Rahman, M.N. Sadath and L. Giessen, 'Foreign Donors Driving Policy Change in Recipient Countries: Three Decades of Development Aid Towards Community-Based Forest Policy in Bangladesh', *Forest Policy and Economics*, vol. 68, 2016, pp. 39-40.

¹⁴⁹ S.N. Parnini, 'Public Sector Reform and Good Governance: The Impact of Foreign Aid on Bangladesh', *Journal of Asian and African Studies*, vol. 44, no. 5, 2009, pp. 567-569.

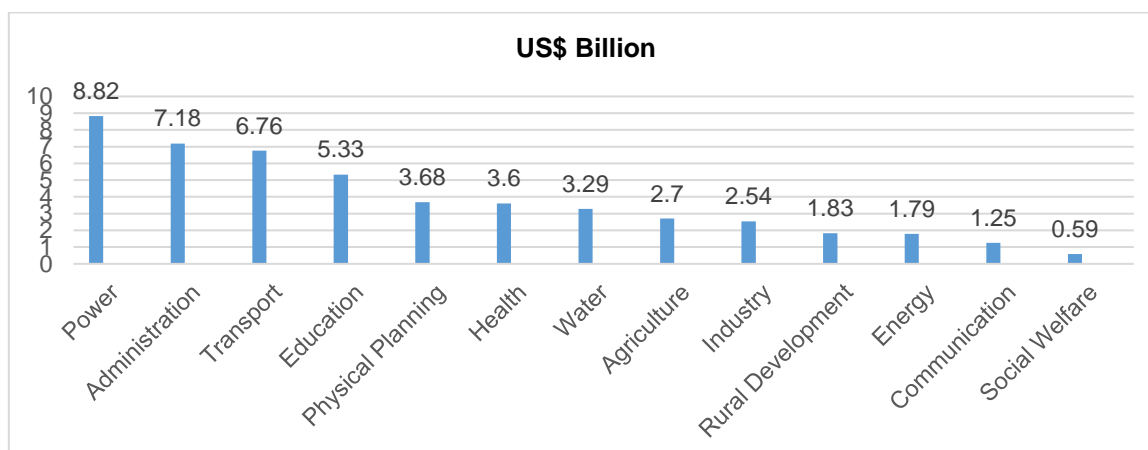
¹⁵⁰ N. Molenaers, 'The Great Divide? Donor Perceptions of Budget Support, Eligibility and Policy Dialogue', *Third World Quarterly*, vol. 33, no. 5, 2012, pp. 791-793.

¹⁵¹ R. Hayman, 'Budget Support and Democracy: A Twist in the Conditionality Tale', *Third World Quarterly*, vol. 32, no. 4, 2011, pp. 679-680.

¹⁵² Obaydullah, p. 53.

3.4. Aid Investment Scenario by Sector

Figure 3.7: Disbursement of foreign aid in major sectors (from FY 1971-72 to 2015-16).



(Source: ERD 2016)

Bangladesh has 17 sectors (and several sub-sectors under each of these sectors) under the ADP. Almost all the public investment in the form of development projects are allocated to these sectors. The aid investment pattern and scenario as indicated in figure 3.7 reflects that Bangladesh utilises most of its aid in productive socioeconomic sectors. The economic sectors such as Power, Transport, Communication, Water Resource, Industry and Physical Planning consume the lion share of foreign aid. The economic sector projects are expected to stimulate economic activities to achieve energy sufficiency, smooth communication networks, industrial progress, improved infrastructure, increased export earnings and employment generation.¹⁵³ The social sectors like health and education also receive significant amount of aid for social and human capital development initiatives such as promoting health, education, social justice and gender equality.¹⁵⁴ External resources are also invested in Rural Development and Agriculture to ensure food security for the nation and better living conditions for rural people. Several social welfare services are also carried out with foreign aid to improve the living standards of poor people across the country.¹⁵⁵ Apart from this, some small amount of aid supports the government to meet foreign exchange requirements in terms of payment for crude oil to address the energy deficiency. In addition, a sizable portion of development aid goes to the public administration sector to bring about reforms in public management with a view to achieving functional macroeconomic frameworks including different national policies, institutional competence, better governance and justice.¹⁵⁶

Bangladesh invests aid mostly in the productive sectors that cover economic activities, human development, social services, social justice, poverty reduction and the institutional capacity building of the government system. It is often questioned whether Bangladesh gets a satisfactory return on

¹⁵³ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 26-29.

¹⁵⁴ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 26-29.

¹⁵⁵ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 26-29.

¹⁵⁶ Parnini, pp. 569-572.

this aid investment or whether this investment is a waste of public money and serves only to increase the debt burden on the nation.¹⁵⁷ Chapter 4 of this paper explores the contribution of aid investment in these economic and social sectors towards the growth and development of Bangladesh.

3.5. Disbursement of Aid and Debt Servicing Liability

3.5.1. Commitment and disbursement

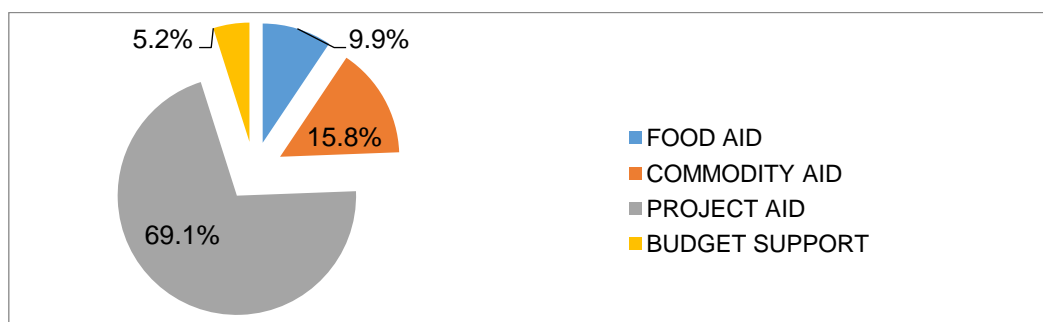
Table 3.1: Total commitment and disbursement in each category of aid (from FY 1971-72 to 2015-16).

<i>Aid Category</i>	<i>Commitment (US\$ billion)</i>	<i>Disbursement (US\$ billion)</i>	<i>% of Disbursement against Commitment</i>
<i>Food Aid</i>	6.88	6.87	99.85
<i>Commodity Aid</i>	11.07	10.91	98.55
<i>Project Aid</i>	77.67	47.81	61.56
<i>Budget Support</i>	3.58	3.57	99.72
Total	99.20	69.15	69.71

(Source: ERD 2016)

We can see from Table 3.1 that from independence to June 2016, the donors committed to lending Bangladesh approximately US\$99.20 billion in foreign aid comprising all the categories. Bangladesh received an aggregated amount of US\$69.15 billion out of the committed aid in this period. Bangladesh received US\$26.50 billion as grants and US\$42.65 billion as loans of the total disbursed amount. The disbursement in FY 1971-72 was US\$270.8 million before rising dramatically to US\$3.56 billion in FY 2015-16.¹⁵⁸

Figure 3.8: The ratio of aid categories in total aid disbursement (From FY 1971-72 to 2015-16).



(Source: ERD 2016)

It is indicative from Table 3.1 that the amounts committed as Food Aid, Commodity Aid and Budget Support were disbursed almost completely. In contrast, the disbursement rate of Project Aid is comparatively lower than the other categories of aid, although Figure 3.8 shows that Project Aid occupies the largest share (69.1%) of the public debt from external sources. It is the most crucial part of aid to Bangladesh not only for being the largest volume but also its contribution to the economic and social development of the country, which is discussed in Chapter 4 of this paper.

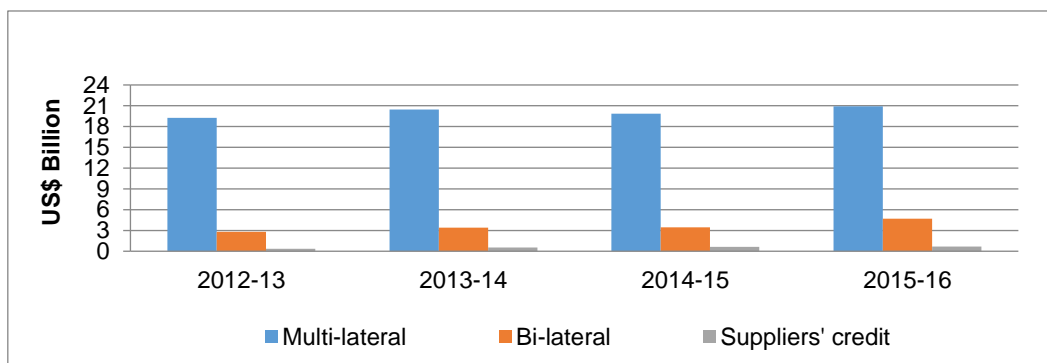
¹⁵⁷ Hossain, 'The Effect of Foreign Aid on the Economic Growth of Bangladesh', pp. 103-104.

¹⁵⁸ Economic Relations Division, pp. 10-12.

Nevertheless, Bangladesh struggles to receive the committed Project Aid due to some procedural hurdles, institutional incompetence and aid conditions.¹⁵⁹ The problems associated with the utilisation of Project Aid are discussed at length in Chapter 5.

3.5.2. Debt service liability

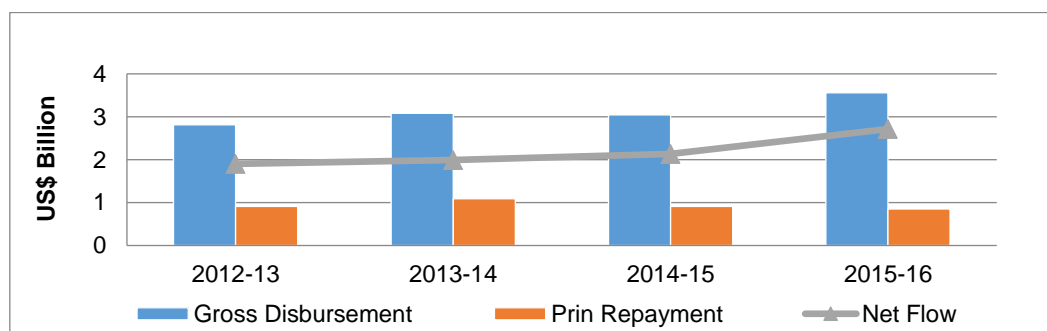
Figure 3.9: Outstanding debt by source of aid (from FY 2012-13 to 2015-16).



(Source: ERD 2016)

Total public debt from external sources was US\$973.80 million in FY 1974-75 while figure 3.9 shows that it reached US\$29.19 billion in FY 2015-16. This debt liability was 13.2% of GDP in FY 2015-16. The debt per capita of the country also rose from US\$6.59 in FY 1973-74 to US\$182.58 in FY 2015-16. The total expense of servicing external debt for the government was US\$1.05 billion in FY 2015-16 while the repayment of the principal and interest were US\$848.5 million and US\$202.1 million respectively. The net flow, which is the difference between the disbursement and repayment of the principal, showed a positive value of US\$2.715 billion in FY 2015-16 (figure 3.10). This was 27.3% higher than the previous year. This net flow has always reported a positive value in Bangladesh since independence.¹⁶⁰ In addition, the net transfer, which is the remaining value after paying the interest on the net flow, has also always recorded a positive value. These positive net flow and net transfer amounts since 1971 have contributed to capital accumulation in Bangladesh.¹⁶¹

Figure 3.10: Disbursement, repayment of principal and net flow of aid (from FY 2012-13 to 2015-16).



(Source: ERD 2016)

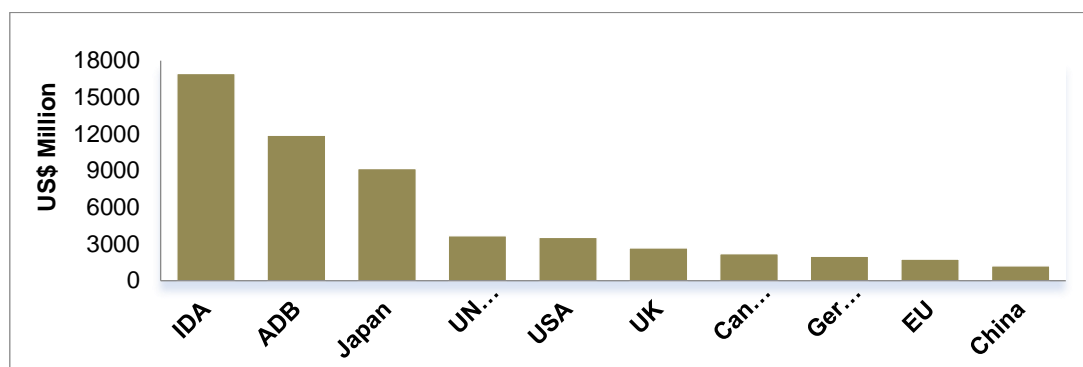
¹⁵⁹ Parnini, p. 559.

¹⁶⁰ Economic Relations Division, pp. 12-13.

¹⁶¹ Dristy, pp. 7-8.

3.6. Major Donors and Aid Conditionality

Figure 3.11. Top ten donors as per accumulated disbursement (from FY 1971-72 to 2015-16).



(Source: ERD 2016)

Immediately after independence, Bangladesh was supported by few bilateral and multilateral donors; these were namely the USA, the Soviet Union, India and the UN. Eventually, more donors put their assistance forward to many of the sectors in Bangladesh; figure 3.11 shows how aid from multilateral sources has increased significantly since independence. In FY 1971-72, bilateral and multilateral aid were 85.7% and 14.3% respectively. Inversely, multilateral aid contributed 65.2% of total aid composition in FY 2015-16 while bilateral aid stood at 34.8%. Nevertheless, there is an increasing trend in bilateral aid again from FY 2010-11.¹⁶² Considering the accumulated contribution, The World Bank (IDA) is the leading multilateral donor while Japan has been the largest bilateral donor. ADB, EC, IMF, IDB and the UN are all other important multilateral donors for Bangladesh while the USA, the UK, Canada, China, Germany, India, South Korea and AusAid are the major bilateral donors.¹⁶³ The contribution of China and India increased dramatically after 2010 due to geopolitical affairs.¹⁶⁴ AIIB is the latest edition of the multilateral donors. This aid has different conditions – in general and through to specific.

3.6.1. Financial conditions of aid

The accumulated General Government Debt is US\$26.31 billion,¹⁶⁵ and this debt is utilised in different development projects within the ADP. These loans are commonly Medium and Long Term (MLT) in nature. MLT debt is mostly termed as concessional (soft) aid/loans with weighted averages of 9.4 years as a 'grace period'¹⁶⁶, 38 years as a 'maturity period'¹⁶⁷ and 28.6 years as a 'repayment period'¹⁶⁸.¹⁶⁹ The weighted average of interest for these loans is 0.92%. These financial conditions

¹⁶² Economic Relations Division, pp. 5-8.

¹⁶³ Economic Relations Division, pp. 4-8.

¹⁶⁴ C. Wagner, 'The Role of India and China in South Asia', *Strategic Analysis*, vol. 40, no. 4, 2016, pp. 312-313.

¹⁶⁵ Total external outstanding debt of Bangladesh up to FY 2015-16 is US\$29.19 billion. Out of this, government utilised US\$26.31 billion as General Government Debt for investment in development projects. The rest amount has expended to repay crude oil prices and state guarantees for different loans taken by the autonomous entities.

¹⁶⁶ 'Grace period' is counted from the date when the loan becomes effective, to the repayment date of the 1st instalment of the principal.

¹⁶⁷ 'Maturity period' runs between the date when the loan becomes effective and the last repayment date.

¹⁶⁸ 'Repayment period' is the difference between maturity period and grace period, when the repayments are made.

¹⁶⁹ Economic Relations Division, pp. 12-14.

of aid are generally much softer than those attached to commercial loans extended by domestic and international financial institutions.¹⁷⁰ It should also be noted that the multilateral loans are more concessional (softer) than bilateral loans. In addition to these financial conditions, Bangladesh needs to comply with other conditions to receive aid both from the bilateral and multilateral donors.

3.6.2. Conditions on aid utilisation modalities

Aid conditionality from the donors may be at project, sectoral or macroeconomic policy levels. Some of the conditions serve donors' purposes and some aim to improve the performance of Bangladesh in aid utilisation. At the project level, the donors want to ensure that the relevant government entity has appraised, formulated and produced the project documents as per the guidelines prescribed by the respective donor. They also call for quick approval of the project by the government. Financial expenses are to be done as per donors' guidelines. Monitoring and coordination of the implementation of the project need to be strengthened. Safeguard, sustainability and maintenance plans for the project are also requirements from the donor's side. The stakeholders' consultation and participation, people empowerment, and project accountability are additional concerns for the donors at the project level.¹⁷¹ At the sectoral level, the donors often impose the conditions of bringing sectoral reforms before committing any aid. For example, all the loans from the ADB in the railway sector are conditional upon the implementation of the railway sector reform projects. At the macroeconomic level, the donors advise the government to reform key policies like procurement guidelines, the health policy, the education policy, the monetary and fiscal policy, the exchange rate policy, the trade policy, the tax policy, and the structural adjustment policies and so on.¹⁷²

The government often cannot resist these pressures due to the vested interests of the domestic and international political elites.¹⁷³ Some of the donors impose the condition of appointing consultants and project managers from the donor's country for the project. Even, the construction and services are sometimes to be provided by the big companies of the donor countries. Since the Paris Declaration, Accra Agenda for Action and Busan High Level Forum, greater attention has been paid to institutional competence, country ownership, governance, democracy, transparency, human rights, the environment and gender related issues. The government has modified some of the aid utilisation modalities to align to donors' requirements.¹⁷⁴

3.7. Modifications in Aid Utilisation Modalities

Immediately after independence, Bangladesh received foreign aid essentially to meet emergency requirements. However, gradually aid utilisation has become institutionalised in Bangladesh as aid contributes to the productive socioeconomic sectors as well. The government of Bangladesh

¹⁷⁰ Obaydullah, p. 52.

¹⁷¹ Obaydullah, pp. 41-43.

¹⁷² Parnini, pp. 564-567.

¹⁷³ Obaydullah, p. 54.

¹⁷⁴ Dristy, pp. 13-15.

considered the challenges in aid utilisation and tried to implement various reforms by modifying some of the aid utilisation modalities. Recognising the importance of donors' contributions to the development of Bangladesh on the one hand while enjoying country ownership over the aided development initiatives on the other, Bangladesh regarded the 'Donors' as the 'Development Partners'. The conventional donor-recipient relationship has turned into a development partnership where aid is not only a financing tool but also a partnership-based approach for the overall development of the country.¹⁷⁵ The term 'aid' has also been officially replaced by 'development assistance'. In the new era of development partnership, the partners are coming up with financial and technical assistance whereas Bangladesh is prioritising its development requirements and implementing the projects and programs with mutually agreed guidelines. Still, Bangladesh needs to ensure some modalities like ownership, aid harmonisation, transparency, mutual accountability, results-based aid management, institutional capacity development and so on.¹⁷⁶

In response to these requirements, Bangladesh has started executing some of the aid effectiveness measures. Bangladesh is formulating its national plans and aid strategies through consultation with all the relevant stakeholders including development partners, the private sector, NGOs, civil society, the media, citizen representatives, local government institutions and other financial institutions.¹⁷⁷ It is working closely with development partners including the Bangladesh Development Forum (BDF), the Local Consultative Group (LCG) and the South-South cooperation. It has introduced an e-procurement system and strengthened the monitoring and evaluating procedures of project implementation. There have been several capacity development programs to improve institutional competence.¹⁷⁸ Detailed discussion on the aid effective measures adopted by Bangladesh and their progress is covered in Chapter 6 of this paper.

3.8. Conclusion

This chapter intended to provide an overview of the facts associated with aid utilisation in Bangladesh. It has found that, despite inheriting a dependency on aid mostly in the form of grants, Bangladesh is gradually moving forward to taking loans instead of grants to utilise aid as development financing for public sector development projects. Bangladesh has reduced its dependency on aid in terms of a decreased GDP-aid ratio but still, Bangladesh mobilises a large amount of aid to finance its development activities. Bangladesh has diversified its source of aid to several bilateral countries and multilateral organisations, and the financial conditions of these loans have been beneficial for Bangladesh. The necessity of technical know-how and development financing in the productive sectors has led to partnerships between Bangladesh and its donors. To optimise the outcomes of this partnership, Bangladesh has reformed many of its macroeconomic

¹⁷⁵ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 132-134.

¹⁷⁶ Rahaman and Khan, pp. 118-120.

¹⁷⁷ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 146-149.

¹⁷⁸ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 132-134.

policies and dedicated great commitment to various aid effectiveness measures. Still, the question remains unsolved whether aid contributes positively to Bangladesh or whether its impact is actually insignificant, even though so many constructive steps have been taken. The next chapter analyses the contribution of aid to growth and the development of the country.

CHAPTER 4: THE IMPACT OF AID ON ECONOMIC GROWTH AND DEVELOPMENT

4.1. Introduction

There are several determinants of economic growth and development, and these determinants may vary from country to country depending on the domestic resources, local political conditions, the strength of the local economy, and the international relationships of a country.¹⁷⁹ Petrakos and Arvanitidis prioritise Investment, Human Capital, Research and Development, Economic Policies and Macroeconomic Conditions, Trade Openness, FDI, the Institutional Framework, Political Factors and Geography as the key determinants of growth, irrespective of whether developed or developing countries are being examined.¹⁸⁰ Bhattacharjee and Haldar highlight Physical and Human Capital, Openness, Institutional Frameworks and Political Stability as the key determinants for growth and development for the developing countries of South Asia.¹⁸¹ Turning back to Bangladesh, Income and Investment, External Trade, Macroeconomic Conditions, the Balance of Payments and Political stability are the fundamental determining factors of economic growth according to Rao and Hassan.¹⁸² Environmental Management is also a crucial factor for the sustainable development of Bangladesh.¹⁸³ Therefore, public investment should focus on these determinants for achieving growth and development. Chapter 3 demonstrated how foreign aid is an essential part of public investment, being invested in public sector development projects. To evaluate the impact of aid on growth and development in Bangladesh, one must analyse what the impact is of these aid investments on the determining factors for development. For better synchronisation, this chapter clusters the impact of aid into four categories – Macroeconomic Variables, Human and Social Development, Institutional Capacity Building and Environmental Management. This chapter argues that foreign aid contributes positively to economic growth and development in Bangladesh.

4.2. The Impact of Aid on Macroeconomic Variables

In this section, I present an overview of the issues surrounding the impact of aid on macroeconomic variables in Bangladesh. I analyse the relationship of aid with the core macroeconomic determinants for growth being Public Investment, Macroeconomic Conditions, Trade, FDI, Domestic Savings and Internal Revenue Generation in order to assess the impact of aid on macroeconomic variables in Bangladesh.

¹⁷⁹ G. Petrakos and P. Arvanitidis, 'Determinants of Economic Growth', *Economic Alternatives*, vol. 1, no. 1, 2008, pp. 11-13.

¹⁸⁰ Petrakos and Arvanitidis, pp. 14-17.

¹⁸¹ J. Bhattacharjee and S.K. Haldar, 'Economic Growth in South Asia: Binding Constraints for the Future', *Journal of South Asian Development*, vol. 10, no. 2, 2015, p. 231.

¹⁸² B.B. Rao and G.M. Hassan, 'An Analysis of the Determinants of the Long-Run Growth Rate of Bangladesh', *Applied Economics*, vol. 44, no. 5, 2012, pp. 572-573.

¹⁸³ J.M. Ayers *et al.*, 'Mainstreaming Climate Change Adaptation into Development: A Case Study of Bangladesh', *Wiley Interdisciplinary Reviews: Climate Change*, vol. 5, no. 1, 2014, pp. 37-39.

4.2.1. Aid and Public Investment

Investment in the public sector is one of the most essential determining factors to achieve economic growth of a country. Due to domestic resource constraints, like most other developing countries, Bangladesh depends on foreign aid to fill its gaps in public investment. All forms of foreign aid raise capital accumulation and investment; it is thus, an efficient method to achieve economic growth and development for developing countries.¹⁸⁴ Traditionally, Bangladesh has a dependency on aid to run public sector investment projects under the ADP. Bangladesh financed the ADP in 1973-74 completely with aid. Although Bangladesh has gradually reduced its financing of the ADP from the aid it receives, it is still investing large amounts of aid into the public sector.¹⁸⁵ In FY 2015-16 Bangladesh spent US\$11.12 billion on the ADP, with investment from domestic resources versus foreign aid being US\$8.22 billion and US\$2.9 billion respectively.¹⁸⁶

Most of the project aid, along with technical assistance, has been utilised in the productive economic sector. Public investment in transport and communications, power and energy, industry, infrastructure and water resources have stimulated economic activity in Bangladesh. As a result, Bangladesh is satisfactorily achieving an economic transformation from a rural-based agricultural economy to an urban-based manufacturing and service-oriented economy with technological progress and employment generation.¹⁸⁷ While the agriculture sector is substantially subsidised with public investment, Bangladesh is about to achieve food self-sufficiency¹⁸⁸ – an area where aid has played a considerable role.¹⁸⁹ This investment has been functional in achieving and sustaining steady economic growth of above 6% for the country over the last decade. Moreover, after the repayment of the principal plus interest, the net flow of aid to Bangladesh has always been positive.¹⁹⁰ Therefore, aid is helpful for physical and financial capital accumulation, and public investment in Bangladesh. Nonetheless, Bangladesh could only utilise 67.1% of the committed project aid (refer to figure 3.8) and failed to maximise the benefits of aid utilisation. This indicates that, despite Bangladesh benefitting from the positive impact of aid, it still struggles to use the committed project aid completely because of some issues associated with aid utilisation. Chapter 5 of this paper widely discusses the challenges for aid effectiveness in Bangladesh.

¹⁸⁴ Moreira, p. 34; Sachs, pp. 245-246.

¹⁸⁵ Hossain, 'Nexus between Foreign Aid and Economic Growth', p. 59.

¹⁸⁶ Economic Relations Division, pp. 5-7.

¹⁸⁷ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 2-20; It can be seen in Appendix 3 that the share of Agriculture to GDP in Bangladesh is continuously reducing and has reached at 11.70% in FY 2015-16. In contrast, Manufacturing and Service have occupied the major portion of the rest of the shares of GDP. This indicates that Bangladesh is transforming to be a manufacturing and service-based economy.

¹⁸⁸ Sala and Bocchi, pp. 238-239.

¹⁸⁹ Rahman, Sadath and Giessen, pp. 40-41.

¹⁹⁰ Economic Relations Division, pp. 11-13.

4.2.2. Aid and Macroeconomic Conditions

Table 4.1: Trends in aid flow and the inflation rate (from FY 2008-09 to 2015-16).

Variables	2008/09	2009/10	2010/11	2011/12	2012/13	2013/14	2014/15	2015/16
Aid Disbursement (in US\$ million)	1847.31	2227.77	1776.74	2126.48	2811.00	3084.39	3043.07	3542.51
Rate of Inflation	6.66	7.31	8.80	10.62	7.70	7.35	6.40	6.16

(Source: ERD 2016)

Rao and Hassan focus on issues related to the inflation rate, public consumption, ‘the real exchange rate’¹⁹¹, the balance of payments, and the level of external debt as the key components of the macroeconomic conditions of Bangladesh.¹⁹² The inflation rate is the measure of change in the percentage of the Consumer Price Index (CPI) in each year. A lower inflation rate is beneficial to achieve economic growth.¹⁹³ It is a standard criticism that foreign aid impacts negatively on the inflation rate if it remains unutilised; however, it has a positive impact when it is utilised in productive sectors.¹⁹⁴ When foreign aid is invested in productive sectors, it results in having a positive impact on the inflation rate in Bangladesh. Table 4.1 shows that there is a non-linear relationship between aid and the inflation rate, although in most of the cases it is positive. The congenial Monetary Policy has contributed to the declining of the inflation rate in Bangladesh.

If the recurrent expenditure of aid is directed at public sector investment and, more specifically, into productive sectors such as capital projects and infrastructure, the impact of aid will be positive on public consumption.¹⁹⁵ To maximise the impact of aid, public consumption should be focused on traded goods rather than non-traded products.¹⁹⁶ In Bangladesh, aid is mostly utilised in the productive sectors for procuring materials for the construction of infrastructure including roads, bridges, power plants, railways, and infrastructure for industry, buildings and other public facilities. So, the public usage of aid investment should be positive for Bangladesh.¹⁹⁷ However, it needs to be acknowledged that there may also be some suspicious public usage of aid due to corruption, which is discussed in the upcoming chapter of this paper.

¹⁹¹ The nominal exchange rate is the price of a currency against another currency. For instance, US\$1=AUD1.3. In contrast, real exchange rate is the relative price of goods between two countries. For example, with this rate, the Australian can trade their own goods for those of the United States.

¹⁹² Rao and Hassan, pp. 572-573.

¹⁹³ M.U. Ahmed, M.M. Muzib and M.M. Hasan, ‘Inflation, Inflation Uncertainty and Relative Price Variability in Bangladesh’, *Eurasian Economic Review*, vol. 6, no. 3, 2016, pp. 390-391.

¹⁹⁴ A.A. Hossain, ‘Inflation Volatility, Economic Growth and Monetary Policy in Bangladesh’, *Applied Economics*, vol. 47, no. 52, 2015, p. 5683.

¹⁹⁵ S. Feeny and T.R.L. Fry, ‘How Sustainable is the Macroeconomic Impact of Foreign Aid?’, *Journal of Policy Modeling*, vol. 36, no. 6, 2014, p. 1075.

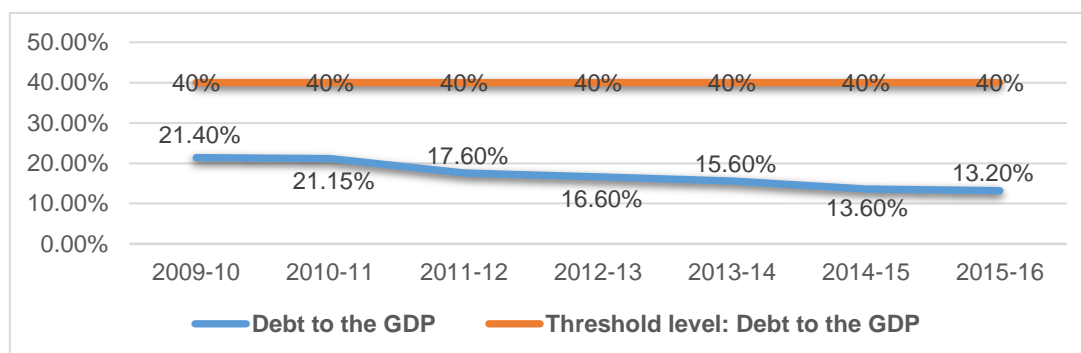
¹⁹⁶ S.B. Amin and M. Murshed, ‘An Empirical Investigation of Foreign Aid and Dutch Disease in Bangladesh’, *The Journal of Developing Areas*, vol. 52, no. 2, 2018, p. 180.

¹⁹⁷ Obaydullah, pp. 139-140.

It is often claimed that external resources in terms of aid may cause currency appreciation of the recipient country and negatively impact the real exchange rate and export earnings of the country.¹⁹⁸ On the one hand, Amin and Murshed claim that foreign aid does not hamper the real exchange rate in Bangladesh and hence has no harmful impact on export earnings and economic growth.¹⁹⁹ On the other hand, foreign aid has historically been effective to maintain the Balance of Payments for developing countries and to stimulate export earnings by fulfilling the foreign exchange requirements of the recipient country.²⁰⁰ Referring to government reports, Dristy notes that foreign aid has been effective for maintaining the Balance of Payments in Bangladesh by mitigating the foreign exchange and import-export gaps.²⁰¹

There has been a long-standing controversy regarding the limit of external debt for a country. Figure 4.1 shows that the external debt limit can go up to a maximum of 40% of the GDP,²⁰² and the total external outstanding debt of Bangladesh has always been below this threshold.²⁰³ In addition, according to Gyimah-Brempong, Racine and Gyapong, aid returns the most positive impact for a country when it persists within the range of 6.6% to 14.4% of the GDP or the National Income of a country.²⁰⁴ Figure 4.1 notes that it was 13.6% and 13.2% of the GDP respectively in FY 2014-15 and 2015-16. As aid remains within the expected threshold of the aid-GDP ratio, it has a positive impact on growth in Bangladesh.

Figure 4.1: The ratio of outstanding external debt to GDP (from FY 2009-10 to 2015-16).



(Source: ERD 2016)

4.2.3. Aid and Trade

Aid can be instrumental to promote international trade for developing countries. The export earnings of the least developed countries are hampered due to weak infrastructure, low quality products, inadequate loan schemes and an incompetent business environment.²⁰⁵ Aid for Trade (AFT)

¹⁹⁸ Z. Askarov and H. Doucouliagos, 'Spatial Aid Spillovers during Transition', *European Journal of Political Economy*, vol. 40, 2015, p. 81.

¹⁹⁹ Amin and Murshed, p. 180.

²⁰⁰ Tarp, 'Aid and Development', pp. 21-22.

²⁰¹ Dristy, p. 7.

²⁰² IMF has determined in 2010 that the maximum limit of the aid ratio to the GDP for developing and emerging nations can be 40%.

²⁰³ Economic Relations Division, pp. 15-19.

²⁰⁴ Gyimah-Brempong, Racine and Gyapong, p. 18.

²⁰⁵ M. Busse, R. Hoekstra and J. Königer, 'The Impact of Aid for Trade Facilitation on the Costs of Trading', *Kyklos*, vol. 65, no. 2, 2012, pp. 143-145.

approaches – aimed at reforming relevant policies – are effective at removing these limitations to trade and, hence, aid encourages global trade for poor countries to achieve increased economic growth.²⁰⁶ AFT has been effective for Bangladesh to overcome infrastructural constraints and to reform different policies such as the National Land Transport Policy, the National Telecommunications Policy, and the International Long Distance Telecommunication Services Policy so as to enjoy increased export earnings.²⁰⁷ Bangladesh, under a ‘Comprehensive Trade Policy’, focuses on increasing its export diversification and ensuring its trade openness by using AFT, which is projected to impact positively on the export earnings and economic growth of the country.²⁰⁸

4.2.4. Aid and FDI

Table 4.2: Bangladesh’s aid, 1995-2012, broken down by purpose and expressed as percentages.

Infrastructure Aid	
<i>Aid for Social infrastructure</i>	37.73
<i>Aid for Economic infrastructure</i>	28.06
<i>Aid for Production and services</i>	7.67
<i>Aid for Multi-sector/cross-cutting</i>	9.03
Non-infrastructure Aid	
<i>Aid for Commodity aid and general programme assistance</i>	4.94
<i>Aid for Action relating to dept.</i>	7.77
<i>Humanitarian aid</i>	4.80
Total	100

(Source: Bhavan 2014, p. 1782)

FDI promotes the economic growth of a country by contributing to employment generation, meeting the saving-investment gaps, and via the sharing of knowledge and managerial skills for forward and backward linkages in the production sectors.²⁰⁹ It is helpful for creating new market facilities, cheap production amenities, technological affluence and additional financing in Bangladesh.²¹⁰ As in most other developing countries, foreign aid in Bangladesh can facilitate effective FDI inflows by being invested in the relevant social and economic infrastructure.²¹¹ Analysing the FDI data of Bangladesh for the period of 1995 to 2012, Bhavan claims that aid which is invested in social infrastructure such as education, health and skills development, and economic infrastructure like transport, energy and

²⁰⁶ M. Vijil and L. Wagner, ‘Does Aid for Trade Enhance Export Performance? Investigating the Infrastructure Channel’, *The World Economy*, vol. 35, no. 7, 2012, pp. 838-841.

²⁰⁷ Hasanuzzaman, ‘Assessing the Aid for Trade (AFT) Agenda: Bangladesh Case Study’, *Asia-Pacific Business Review*, vol. 6, no. 2, 2010, pp. 13-14.

²⁰⁸ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 216-218.

²⁰⁹ M. Dion and J. Parlinggoman, ‘The Role of High-Tech Exports and of Foreign Direct Investments (FDI) on Economic Growth’, *European Research Studies*, vol. 20, no. 4A, 2017, pp. 197-198.

²¹⁰ S.M. Reza *et al.*, ‘The Impact of Foreign Direct Investment Inflows on Economic Growth: Evidence from Bangladesh’, *Journal of Business and Retail Management Research*, vol. 12, no. 2, 2018, pp. 212-214.

²¹¹ T. Bhavan, ‘Effectiveness of Foreign Aid in Facilitating Foreign Direct Investment: Evidence from Four South Asian Countries’, *Asian Economic and Financial Review*, vol. 4, no. 12, 2014, pp. 1770-1772.

financial services, has a significant impact on promoting the flow of FDI.²¹² Table 4.2 shows that 82.49% of the aid in Bangladesh is utilised as economic and social infrastructure aid. Therefore, aid contributes positively to the economic growth and development of Bangladesh by improving the necessary infrastructure for attracting an inflow of FDI.

4.2.5. Aid and Domestic Savings

The key determinant of economic growth is investment. Investment schemes are expected to be financed from the domestic resources and savings accrued from national income such as export, revenue and private capital.²¹³ Developing countries have resource constraints in almost all of the categories and suffer from low domestic savings.²¹⁴ To meet the savings-investment gap, particularly with regard to development expenditure, developing countries depend on external resources such as foreign aid which is effective to reduce investment deficits. Kousar and Masood claim that foreign aid has a positive impact on investment but negative impacts on domestic savings in developing countries because it is often invested in unproductive sectors such as government consumption.²¹⁵ Analysing the aid data of Bangladesh from 1971-2008, Istiak concludes that foreign aid is required in Bangladesh to meet investment gaps but foreign aid itself does not raise domestic savings. Therefore, there is a positive relationship between aid and investment, but aid and domestic savings are independent variables and they cannot influence each other.²¹⁶

4.2.6. Aid and Domestic Revenue Generation

The flow of aid to developing countries is often criticised with the charge that aid reduces tax initiatives and, hence, this reduces domestic savings, which ultimately inspires recipient countries to be more dependent on donor countries. Conversely, it is claimed that aid in terms of grants increases the flow of public money and discourages improvements to the taxation system. By contrast, it is claimed loans are substantially effective for reforming the taxation system because technical assistance and additional investment are helpful for reforming tax infrastructure and ensuring an efficient taxation structure.²¹⁷ In Bangladesh, the donors always try to instigate the government to undertake reform programs to maximise revenue generation. The pressure from donors, especially from the IMF and the WB, has been continuously mounting since 2009. As a result, Bangladesh has started implementing several reform measures. Although the reforms have not been accomplished yet and Bangladesh is still to get optimum benefits from these reforms, there are some successful

²¹² Bhavan, pp. 1777-1780.

²¹³ P. Sahoo and R. Dash, 'Financial Sector Development and Domestic Savings in South Asia', *Economic Modelling*, vol. 33, 2013, pp. 388-390.

²¹⁴ I. Gocer, T. Akin and S. Alatas, 'The Effects of Saving-Investment Gap on Economic Growth in Developing Countries: A Clustering and Panel Data Analysis', *Theoretical and Applied Economics*, vol. 23, no. 2, 2016, pp. 169-170.

²¹⁵ Kousar and Masood, pp. 182-184.

²¹⁶ Istiak, p. 341.

²¹⁷ J. Thornton, 'Does Foreign Aid Reduce Tax Revenue? Further Evidence', *Applied Economics*, vol. 46, no. 4, 2014, pp. 359-361; P. Clist, 'Foreign Aid and Domestic Taxation: Multiple Sources, One Conclusion', *Development Policy Review*, vol. 34, no. 3, 2016, pp. 379-380.

implications of these aided programs on the taxation system.²¹⁸ Appendix 2 shows that Bangladesh has been able to increase its Tax Revenue up to US\$19.4 billion in FY 2015-16 which was only US\$7 billion in FY 2007-08. Apart from this, as Bangladesh mostly receives aid as loans and not as grants, it has some positive impacts on domestic taxation and revenue.

4.3. The Impact of Aid on Human and Social Development

Human Development Approaches aim to develop human capital with a view to making an individual capable of taking part in the development process via his or her own capability. Human capital such as education, health and skills development are the most necessary requirements for Human Development.²¹⁹ If the human development schemes are successfully implemented, a nation can achieve faster economic growth and development. The social development and social welfare initiatives mostly focus on reducing income poverty and inequality.²²⁰ Therefore, these days, developing countries aim to expend a significant portion of the national budget on social development and human development initiatives. The Government of Bangladesh also undertakes several schemes for human and social development, and similar to the economic sector projects, Bangladesh is largely dependent on aid to implement these social development initiatives.²²¹

Bhavan names the human development approaches as an 'investment in social infrastructure'. He also shows that Bangladesh invested 37.73% of the total aid flow into social infrastructure during 1995-2012 (see table 4.2). As a result, economic activities increased and human development approaches returned a better FDI inflow, remittance and self-employment; which all contributed positively to economic growth.²²² Health aid, which is invested in Bangladesh as sector-wide approaches (SWAp), created treatment facilities, awareness building on health and nutrition among people, and eventually contributed to an increase of the average life expectancy.²²³ Most importantly, it is a government-owned comprehensive health program where all the donors provide health aid within the sector program that ensure aid harmonisation in terms of effective budget support.²²⁴ Foreign aid also plays a significant role in promoting education and skills development in Bangladesh. There are several technical assistance projects that are aimed at curriculum development, teachers' professional development, and the skills development of both the students and the labour force via both formal and non-formal education including general education, technical education and madrasa (Islamic) education.²²⁵ These human development approaches contributed

²¹⁸ Hassan and Prichard, pp. 1708-1710.

²¹⁹ G. Koehler, 'Some Preliminary Reflections on Development, Public Policy and Welfare States' in G. Koehler and D. Chopra (eds.), *Development and Welfare Policy in South Asia*, Routledge, New York, 2014, p. 16.

²²⁰ Quibria, pp. 79-80.

²²¹ Dristy, pp. 7-8.

²²² Bhavan, pp. 1770-1772.

²²³ H. White, 'The Bangladesh Health SWAp: Experience of a New Aid Instrument in Practice', *Development Policy Review*, vol. 25, no. 4, 2007, pp. 451-454; Some of the health indicators including life expectancy can be seen in Appendix 1.

²²⁴ White, pp. 451-454.

²²⁵ G.M. Alam, 'The Role of Technical and Vocational Education in the National Development of Bangladesh', *Asia-Pacific Journal of Cooperative Education*, vol. 9, no. 1, 2008, pp. 25-26; The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 602-608.

to achieving a better Human Development Index (HDI),²²⁶ and 6 (out of 8) socioeconomic MDG targets achieved, including poverty reduction, the net enrolment in primary education and reducing child mortality.²²⁷ It is expected that these human development approaches will be effective to achieve the SDGs by 2030 as well.²²⁸

Apart from these human capital approaches, people awareness programs regarding population growth, gender, inequality and self-employment also play significant roles for the social development in Bangladesh.²²⁹ Mahmud claims that the South Asian countries including Bangladesh spend very little on human development and social development initiatives from their own revenue generation. Foreign aid plays a commendable role to mitigate investment gaps in such approaches.²³⁰ Aside from being given to the government, a sizable portion of foreign aid is also directed to the NGOs in Bangladesh, particularly for social development programs. Using foreign aid, several NGOs operate social services such as health, education, skills development, microfinance, employment generation, legal aid, gender equality, social justice and poverty reduction for marginalised Bangladeshis.²³¹ Another important feature of social development strategies in Bangladesh is several social welfare programs in the form of social safety nets, which aim to improve the living standards, equality and social justice for people living in extreme poverty. There are several cash and food transfer programs for the elderly people, freedom fighters, primary school children, poor people, the unemployed poor, widows and so on.²³² Some examples are the VGF, TR and FFW programs, which are all financed by aid for the distribution of food aid in particular.²³³ The human and social development approaches supported with foreign aid are collectively contributing to economic growth and social transition in Bangladesh.

4.4. The Impact of Aid on Institutional Capacity Building

Petrakos and Arvanitidis note that institutional framework is important for shaping the economic performance and development of a country. The institutional framework generally includes institutions that are responsible for regulatory activities, governance, macroeconomic stabilisation,

²²⁶ Bangladesh is noting a consistent improvement in its HDI value since 1990. Detailed statistics on Bangladesh's HDI can be seen in Appendix 1.

²²⁷ United Nations Development Programme (UNDP), 'Bangladesh's Progress on the MDGs', UNDP's website, New York, 2018, <<http://www.bd.undp.org/content/bangladesh/en/home/post-2015/millennium-development-goals.html>>, consulted 06 April 2018; United Nations Development Programme (UNDP), 'Bangladesh Improves in Human Development Index', UNDP's website, New York, 2017, <<http://www.bd.undp.org/content/bangladesh/en/home/ourwork/news/bangladesh-improves-in-human-development-index/>>, consulted 03 April 2018

²²⁸ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 24-25.

²²⁹ M. Mahmud *et al.*, 'Development Transformation in Bangladesh: An Overview' in Y. Sawada, M. Mahmud and N. Kitano (eds.), *Economic and Social Development of Bangladesh: Miracle and Challenges*, Palgrave Macmillan, Cham, 2018, p. 15.

²³⁰ W. Mahmud, 'Social Development in Bangladesh: Pathways, Surprises and Challenges', *Indian Journal of Human Development*, vol. 2, no. 1, 2008, pp. 85-86.

²³¹ Mahmud *et al.*, pp. 15-20.

²³² M.M. Rahman, 'Estimating the Average Treatment Effect of Social Safety Net Programmes in Bangladesh', *The Journal of Development Studies*, vol. 50, no. 11, 2014, pp. 1550-1554.

²³³ Economic Relations Division, pp. 7-10.

social insurance and the management of political conflict.²³⁴ These institutions not only pursue economic growth but also influence growth in other areas such as physical and human capital, public investment and technological progress. Instability in politics, the legal system, the level of corruption and the bureaucratic process may affect economic growth and development adversely.²³⁵ Therefore, strengthening the institutional capability is crucial to achieve sustained economic growth and development.

One of the worrying issues for most developing countries is that they themselves do not initiate sufficient reform programs for the building of institutional capacity. It is the donors who often influence them to undertake several reform programs related to policy, governance, democracy, efficient bureaucracy and effective macroeconomic and fiscal management.²³⁶ Addison and Tarp claim that aid-assisted initiatives have been successful – not only in promoting supply-side economics covering investment, human capital, physical capital and exports – but also in supporting institution building in terms of quality financial management and the taxation system.²³⁷

Development partners started propelling the Government of Bangladesh to reform some of the macroeconomic policies including the fiscal policy, monetary policy, trade policy and procurement policies specifically from the 1990s. Donors have also imposed conditions on aid to ensure transparency and accountability, efficient public administration, human rights, democracy and public sector reforms.²³⁸ In addition, participatory governance, and the inclusion of local citizens and gender mainstreaming in project management have attracted donors' concern.²³⁹ In response to the donors' requirements, Bangladesh has been trying to implement several aid-assisted reform projects for the last three decades.²⁴⁰ So far, Bangladesh has spent the second largest portion of total aid (7.18%) on the public administration sector (see figure 3.7). These initiatives have been aimed at the strengthening of the judiciary, law enforcement agencies, financial institutions, democratic institutions, and decentralisation and public administration reforms; and while there has notable progress, these initiatives have been faced with huge challenges.²⁴¹ The government adopted the National Integrity Strategy (NIS) in 2012 along with e-governance, all with a view to promoting the reforms but corruption and political instability has remained the major impediments to ensure institutional competence.²⁴² Despite efforts with foreign aid, the Government of Bangladesh is not fully in harmony with donors' views of speedy reform of public administration following neoliberal

²³⁴ Petrakos and Arvanitidis, pp. 15-16.

²³⁵ Bhattacharjee and Haldar, pp. 230-231.

²³⁶ M.S. Winters and G. Martinez, 'The Role of Governance in Determining Foreign Aid Flow Composition', *World Development*, vol. 66, 2015, pp. 516-520.

²³⁷ T. Addison and F. Tarp, 'Aid Policy and the Macroeconomic Management of Aid', *World Development*, vol. 69, 2015, pp. 1-5.

²³⁸ Parnini, pp. 553-554.

²³⁹ W. Waheduzzaman, 'Politics and Policy in Achieving Participatory Governance in a Developing Country Context', *Politics and Policy*, vol. 43, no. 4, 2015, pp. 474-476.

²⁴⁰ Waheduzzaman, pp. 474-476.

²⁴¹ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 22-23.

²⁴² The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 22-23.

concepts. The absence of good governance, corruption, a lack of political commitment and political instability are all hindrances to the reforms and building of institutional capacity.²⁴³ So far, foreign aid has had some positive but slow impacts on institution building in Bangladesh due to a range of home-grown challenges and aid conditions imposed by the donors. As the core problems lie with the local system of the recipient country, aid itself is not responsible for its failure to make a sizeable impact on institution building in Bangladesh.²⁴⁴ The next chapter discusses how these institutional weaknesses deprive Bangladesh of enjoying the maximum benefits not only from the huge development paradigm but also foreign aid utilisation in Bangladesh.

4.5. The Impact of Aid on Environmental Management

The impact of climate change on development is of great concern to the world, especially to developing countries. The impact of climate change is generally experienced through natural disasters, which affect the development paradigms and cause intolerable suffering for poor people.²⁴⁵ Since environmental management, climate change adaption and disaster management are now considered as crucial determinants for sustained economic growth and sustainable development, donors now commit to much work for the sake of environmental protection.²⁴⁶ There has been a shift in aid management to focus on mitigating the global challenges of climate change and achieving global environmental goals, along with improving the livelihoods of the poor in developing countries. Development assistance itself cannot ensure environmental objectives are met, rather it is the responsibility of both the aid agencies and development institutions to work together toward environmental protection.²⁴⁷

As a consequence of global warming and the impact of climate change, Bangladesh now suffers from drought, unwarranted rainfall, frequent cyclones, immense landslides, destructive floods, rising salinity, siltation, water-logging, deforestation and tidal overflows.²⁴⁸ Bangladesh is one of the most at-risk or prone countries to the impact of climate change in the world according to the IPCC. Global warming is projected to raise the sea level and submerge two-thirds of the country by 2100.²⁴⁹ Therefore, Bangladesh needs to mitigate the impact of climate change to ensure sustainable growth and development for future generations.

Bangladesh has already started working with the global community for climate change mitigation and has undertaken noticeable initiatives. With support from United Nations Environment Programme (UNEP), the 'Bangladesh National Sustainable Development Strategy-NSDS (2013)'

²⁴³ Parnini, pp. 571-572.

²⁴⁴ Addison and Tarp, pp. 1-5; Parnini, pp. 571-572.

²⁴⁵ Ayers *et al.*, pp. 37-39.

²⁴⁶ Chao *et al.*, pp. 62-63.

²⁴⁷ C. Arndt and F. Tarp, 'Aid, Environment and Climate Change', *Review of Development Economics*, vol. 21, no. 2, 2017, pp. 285-288.

²⁴⁸ A.K.M.A. Sabur, 'Disaster Management System in Bangladesh', *India Quarterly*, vol. 68, no. 1, 2012, pp. 30-35.

²⁴⁹ Intergovernmental Panel on Climate Change (IPCC), 'Working Group II: Impacts, Adaptation and Vulnerability', IPCC's website, Geneva, 2016, <<http://www.ipcc.ch/ipccreports/tar/wg2/index.php?idp=41>>, consulted 2 April 2018.

has been adopted in respect to environmental management and disaster management through mitigation of the climate change challenges.²⁵⁰ The development partners along with several international NGOs have been supporting the government to reduce the emission of greenhouse gases like CO₂ and CFC as well as other causal factors of climate change.²⁵¹ Collaborative efforts among the government and development partners had raised a total of US\$390 million as Global Funds for Climate Change (GFC) by 2015. Several aid agencies are financing the environmental protection and disaster management approaches which have made Bangladesh capable of facing its natural disasters with fewer casualties and economic losses than previously. In 1991, a single cyclone with a wind speed of 225 km/h, a Cyclone Severity Index of 6,²⁵² and covering the eastern coastal area of Bangladesh killed 138,958 people. By contrast, the last of the devastating cyclones named Sidr (2007), which had a wind speed of 250 km/h, a Cyclone Severity Index of 7, and covering the south-western coastal area of Bangladesh killed 4234 people only.²⁵³ The aided approaches such as the construction of cyclone-centres, improved policy support, disaster readiness training, public awareness building and the building of institutional capacity have all successfully contributed to the preparedness of Bangladesh to mitigate the risks and casualties associated with climate change.²⁵⁴ In addition, the government is trying to ensure Environmental Impact Assessments (EIA) for its capital investment projects, which is seen as a key part of mainstreaming environmental management.²⁵⁵ Despite all these efforts and the potential of the GFC to protect its ecosystem, Bangladesh is still to ensure effective utilisation of all the GFC due to the barriers of corruption, institutional incompetence and some aid conditions.²⁵⁶

4.6. Findings and Conclusion

Bangladesh mobilises a sizable portion of its development financing from aid which is mostly invested in public sector development projects. This chapter intended to evaluate how much these investments are contributing to the economic growth and development of the country. The determinants of economic growth and development were broadly categorised into four segments (that is, macroeconomic determinants, social and human development, institution building and environmental management) and the impact of aid on each of the segments were analysed separately. The relationship of aid to macroeconomic determinants such as Public Investment, Macroeconomic Conditions, Trade, FDI and Internal Revenue Generation were found positive,

²⁵⁰ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 445-446.

²⁵¹ Sabur, p. 43.

²⁵² Cyclone Severity Index is prepared based on the size of the cyclone considering the wind speed and areas covered. The index starts from 1. The destructiveness of cyclones goes up as long as the index moves high.

²⁵³ U. Haque *et al.*, 'Reduced Death Rates from Cyclones in Bangladesh: What More Needs to Be Done?', *Bulletin of the World Health Organization*, vol. 90, no. 2, 2012, pp. 150-151.

²⁵⁴ Sabur, pp. 38-39.

²⁵⁵ S.H. Shakil and T.H. Ananya, 'Effectiveness of Environmental Impact Assessment (EIA): Bangladesh Perspective', *Bangladesh E-journal of Sociology*, vol. 12, no. 1, 2015, pp. 115-116.

²⁵⁶ N. Tashmin, 'Can Climate Finance in Bangladesh Be Helpful in Making Transformational Change in Ecosystem Management?', *Environmental Systems Research*, vol. 5, no. 1, 2016, pp. 9-10.

whereas aid has no relationship with Domestic Savings. The macroeconomic conditions – for example, the inflation rate, public consumption, the balance of payments and the level of external debt – are positively influenced by the flow of aid but aid impacts very little on the real exchange rate. Nonetheless, effective aid utilisation is of great concern as this needs to be ensured to achieve the maximum benefits of aid in the macroeconomic sector. Development assistance was found to be successful in human and social development approaches that promote education, health, skills development, equality, poverty reduction, social protection and justice. In the case of institution building, aid noted some positive progress but this progress is very slow due to some challenges such as corruption, political instability, bureaucratic delays and some conditions imposed upon aid being given. The aided approaches in Bangladesh are effective for environmental management, the mitigation of the impact of climate change as well as disaster management. Even still, Bangladesh is struggling to utilise aid for climate change effectively due to corruption, institutional incompetence and aid conditions.

Foreign aid in Bangladesh makes a significant and positive contribution to economic growth and development, essentially through capital accumulation and public investment in macroeconomic sectors, human and social development approaches, institutional capacity building programs and environmental management. Despite noting positive impacts, foreign aid sometimes cannot return the expected outcomes due to aid utilisation challenges in Bangladesh. The next chapter elaborately discusses the most critical impediments that restrain Bangladesh from reaping the highest benefits of aid utilisation.

CHAPTER 5: IMPEDIMENTS TO AID EFFECTIVENESS

5.1. Introduction

Bangladesh mobilises foreign aid to meet deficit financing in the development budget. It utilises most of the aid in productive socioeconomic sectors. The previous chapter expresses that foreign aid has a notable positive impact on economic growth and development by virtue of these investments. At the same time, it is to be noted that Bangladesh failed to maximise the benefits of aid investment due to some impediments to aid utilisation. There are number of reasons that restrain the recipient countries from receiving full benefits of aid utilisation. Generally, transparency and accountability, governance, institutional capability and political stability of the recipient country are the preconditions for effective aid utilisation.²⁵⁷ Prioritising sectors for investment with aid is also very important. In addition, there must be smooth coordination in donor-recipient, institution-institution of the recipient, and donor-donor nexus to ensure effective aid management.²⁵⁸ The recipient countries often fail to meet these preconditions of foreign aid conjuncture that eventually bring aid into criticism.²⁵⁹ In Bangladesh, several home-grown deficiencies within the government system and political conditions have posed challenges for effective aid utilisation.²⁶⁰ Some aid conditionality from the donors as external factors are also responsible for slow and poor aid utilisation. In this context, this chapter aims to discuss the major impediments to aid utilisation in Bangladesh. Here I predominantly discuss how corruption, institutional incompetence, political instability and aid conditionality affect aid effectiveness in Bangladesh.

5.2. Institutional Incompetence

Government practices and institutional strengths in Bangladesh bear the testimony of an unforeseen competition among the interest groups who hold the key positions in the government. The main institutions of the government mechanism – being the political, economic, administrative, regulatory and legislative authorities – are mostly controlled by these vested groups in virtue of their position.²⁶¹ The frequent military dictatorships during 1975-1989 and dysfunctional democratic system afterwards are responsible for creating challenges in establishing a functional government system by strengthening the institutions.²⁶² As a result, the government system is greatly hampered and eventually not mature enough to establish and reform the key institutions or refine the operational processes and management strategies to push the country forward with a more competent

²⁵⁷ E. Kim and J. Lee, 'Busan and Beyond: South Korea and the Transition from Aid Effectiveness to Development Effectiveness', *Journal of International Development*, vol. 25, no. 6, 2013, pp. 791-794.

²⁵⁸ M. Owa, 'Revisiting the Paris Declaration Agenda—An Inclusive, Realistic Orientation for Aid Effectiveness', *Development in Practice*, vol. 21, no. 7, 2011, pp. 987-989.

²⁵⁹ Addison and Tarp, pp. 1-5.

²⁶⁰ Rahaman and Khan, pp. 118-120.

²⁶¹ Q. Alam and J. Teicher, 'The State of Governance in Bangladesh: The Capture of State Institutions', *South Asia: Journal of South Asian Studies*, vol. 35, no. 4, 2012, pp. 858-859.

²⁶² Alam and Teicher, pp. 858-859.

system.²⁶³ These systematic faults are challenging for all sorts of development and non-development expenditures and initiatives. The political willingness and bureaucratic adeptness are preconditions for an effective government system but Bangladesh has shortfalls in these areas. The political issues have been discussed in another section of this chapter. In this section, I focus on the bureaucratic incompetence as the systematic weakness of Bangladesh.

The structure and operational modalities of Bangladesh's bureaucracy originated from British colonial rule, and have been inflexible in nature to accept reforms and modernisation after independence. The politicisation of the governance and administrative system as well as civil-military exclusivities combined to decrease the accountability and transparency of the administration; this, in turn, nourished a bureaucracy generally characterised with dominance and corruption.²⁶⁴ The developing partners of Bangladesh ask the government to undertake reform measures to ensure good-governance with a transparent and functional public administration as a precondition of providing aid.²⁶⁵ The government is also interested in public sector reforms and has initiated several measures in terms of good-governance activities, capacity-building programs and strengthening of monitoring systems with the support of aid agencies to develop a government system of international standard.²⁶⁶ Still, Khan and Islam claim that an underdeveloped political system, the politicisation of public institutions, dominating bureaucrats, poorly trained and less skilled officials, a lack of long-term monitoring and feedback mechanisms, and low quality capacity-building programs are hindering leadership development in public sector management.²⁶⁷ They also note that the implementation of the aided reform programs are slow and their achievements are severely inadequate. As a result, Bangladesh is still struggling to ensure the institutional competence and this failure impedes the development activities as well as effective aid utilisation.

The deficiencies of the government system affect aid utilisation in several ways in Bangladesh. Firstly, the poorly functioning government mechanism fails to address the real development necessities of the country and, thus, the flow of aid can often be misdirected to unproductive sectors and the aid is, therefore, wasted.²⁶⁸ Secondly, the weak monitoring system cannot ensure the quality implementation of the aided projects. The lack of coordination among relevant government entities may cause an overlapping of aid utilisation which is also a waste of public money.²⁶⁹ Thirdly, systematic weaknesses encourage more corruption as well as unproductive and suspicious public consumption, resulting aid becoming derailed and not returning its expected outcomes. Fourthly, institutional incompetence reduces the bargaining capacity of the government bodies, which

²⁶³ Alam and Teicher, pp. 858-859.

²⁶⁴ M.A.H. Mollah, 'Growth and Development of Civil Service and Bureaucracy in Bangladesh: An Overview', *South Asian Survey*, vol. 18, no. 1, 2011, p. 137.

²⁶⁵ Parnini, pp. 553-554.

²⁶⁶ H. Zafarullah and R. Rahman, 'The Impaired State: Assessing State Capacity and Governance in Bangladesh', *International Journal of Public Sector Management*, vol. 21, no. 7, 2008, pp. 748-749.

²⁶⁷ M.M. Khan and M.S. Islam, 'Public Sector Leadership Development in Bangladesh: Present State and Future Prospect', *The International Journal of Leadership in Public Services*, vol. 10, no. 1, 2014, pp. 17-22.

²⁶⁸ Rahaman and Khan, pp. 111-112.

²⁶⁹ Rahaman and Khan, pp. 111-112.

restrains them from enjoying the same status as the donors in the negotiation process.²⁷⁰ Hence, they need to accept whatever conditions are imposed by the donors. Finally, the systematic deficiencies cannot fulfil the donors' requirements for governance and institutional strengths, and thus the donors are often discouraged to disburse the committed aid.²⁷¹ The institutional incompetence in Bangladesh affects aid utilisation and, hence, Bangladesh should continue its reform programs to develop an effective government system in order to ensure aid effectiveness and maximise the benefits of aid.

5.3. Corruption

Foreign aid has noteworthy positive impacts on achieving economic growth for developing countries but economic growth is not equally transformed to economic development due to corruption alongside institutional deficiency and uneven resource distribution.²⁷² Corruption is a major development problem in South Asian countries. Transparency International's 'Corruption Perception Index (CPI)' shows that the SAARC member countries generally receive low scores with Bangladesh generally remaining at the bottom of the index. Regrettably, Bangladesh achieved among the lowest scores in the index from 2001 through to 2005.²⁷³ Bangladesh was positioned 143rd of 180 nations in 2017 on the CPI. The position of Bangladesh only improved as the position of other corrupt countries deteriorated. Corruption in Bangladesh has become an art form among the interest groups of the political and bureaucratic hierarchy.²⁷⁴ The inclination towards corruption in Bangladesh is rooted in the absence of good-governance. Having acquired a pervasive character, corruption is an impending threat for the development of the country as a whole, which may cause unending suffering and socioeconomic crises for the country in the future.²⁷⁵

Corruption has had a long-running negative impact on the economic development of Bangladesh. Pulok and Ahmed, in their study for the period of 1984-2013, show that corruption negatively impacted on real GDP per capita in Bangladesh.²⁷⁶ They also claim that government expenditure – in terms of public investment sourced both from domestic and external resources – had a positive impact on economic development but corruption reduced the volume of public investment because the resources were utilised for unproductive and suspicious consumption.²⁷⁷ They further show that corruption caused about a 28% reduction in public investment in the investment-growth nexus and, hence, had a demolishing impact on public investment, growth and development. Corruption reduces

²⁷⁰ R. Berlinschi, 'Reputation Concerns in Aid Conditionality', *The Review of International Organization*, vol. 5, no. 4, 2010, pp. 446-447.

²⁷¹ Obaydullah, pp. 174-175.

²⁷² Sahoo and Sethi, p. 132.

²⁷³ Transparency International, 'Corruption Perception Index: Overview', Transparency International's website, Berlin, 2018, <<https://www.transparency.org/research/cpi/overview>>, consulted 08 April 2018.

²⁷⁴ S.H. Bhuiyan, 'Modernizing Bangladesh Public Administration through E-governance: Benefits and Challenges', *Government Information Quarterly*, vol. 28, no. 1, 2011, pp. 54-57.

²⁷⁵ M.S. Mashreque, 'Politics of Rural Development in Bangladesh: Manipulation, Criminalization and Corruption', *Himalayan and Central Asian Studies*, vol. 19, no. 1/2, 2015, p. 11.

²⁷⁶ M.H. Pulok and M.U. Ahmed, 'Does Corruption Matter for Economic Development? Long Run Evidence from Bangladesh', *International Journal of Social Economics*, vol. 44, no. 3, 2017, pp. 358-359.

²⁷⁷ Pulok and Ahmed, pp. 358-359.

the economic performance of Bangladesh and hinders the public service delivery system, seriously affecting poverty reduction and social justice approaches.²⁷⁸ The foreign aided initiatives related to public investment and service delivery in Bangladesh are also challenged by the pervasiveness of corruption.

Foreign aid is extended by donors to Bangladesh to implement specific programs on the basis of national requirements, as included in the long-term and annual plans of Bangladesh.²⁷⁹ The corrupt system, however, often results in showy projects that are the result of political influence, nepotism or corruption.²⁸⁰ Aid flows are often directed based on the ministries' communication, presentation skills and maintaining of relationships with the donors rather than the actual necessities in that particular sector.²⁸¹ As a result, the productive sectors struggle to receive necessary aid allocation. In the procurement process, corrupt systems intentionally award contracts to the companies allied to corrupt politicians or bureaucrats so that they can get personal benefits. Again, the selection of clients for service delivery is also hampered by this corruption. The food aid and financial incentives earmarked for poverty reduction programs often do not reach the targeted poor.²⁸² In addition, a significant portion of aid money is paid as salary to government officials and the staff of the aid agencies.²⁸³ This tendency towards corruption by vested interest groups obstructs institution building, which in turn, results in the failure of quality implementation of development projects. As a result, there could be a mistrustful donor-recipient relationship. Hence, corruption is one of the major impediments for all development approaches and it needs to be reduced to maximise the benefits of aid utilisation as well.

Bhuiyan urges the promotion of an e-governance system covering all government business, thereby ensuring greater transparency and reducing corruption levels to establish an efficient and cost-effective service delivery process for the people of the country.²⁸⁴ Institutional reforms, public awareness building and obliterating the drawbacks of policies and programs are also important for reducing corruption.²⁸⁵ If the level of corruption can be reduced, Bangladesh can maximise its economic growth by achieving the expected benefits of aid utilisation.

5.4. Political Instability

Political stability is a necessary determinant for the growth and development of a country. Political instability adversely affects development, particularly of the low-income countries, by hampering the evolution of efficient economic and political institutions. In addition, political instability negatively

²⁷⁸ Bhuiyan, pp. 59-60.

²⁷⁹ Economic Relations Division, pp. 1-3.

²⁸⁰ Obaydullah, pp. 57-58.

²⁸¹ M.G. Quibria and S. Ahmad, *Aid Effectiveness in Bangladesh*, Munich Personal RePEc Archive Paper 10299, Munich, 2007, pp. 30-31. <https://mpra.ub.uni-muenchen.de/10299/1/MPra_paper_10299.pdf>, consulted, 13 April 2018.

²⁸² Mashreque, pp. 20-22.

²⁸³ Mashreque, pp. 20-22.

²⁸⁴ Bhuiyan, pp. 59-60.

²⁸⁵ Pulok and Ahmed, pp. 358-359.

impacts on growth and development as it affects the public investment process and accumulation of both physical and human capital.²⁸⁶ Foreign aid is expected to alleviate the socioeconomic conditions of the recipient country but political stability is a requirement to make aid operationalised. Although weakness in both the donors' operational modalities and the recipients' management system negatively impact on aid effectiveness, the recipients' institutional arrangement and political condition are mostly responsible for the disappointing outcomes of aid utilisation.²⁸⁷ Therefore, modern studies on aid are mainly focused on both the external and internal issues and modalities that can ensure the effective utilisation of aid. Bearce notes that aid effectiveness is conditional on the economic and political conditions of the recipient countries, and that political regime type or democratic behaviour of the political system are even more important than the economic condition.²⁸⁸

Political instability or undemocratic behaviour of the political system have been challenging for the sustainable socioeconomic development of Bangladesh. The political performance of Bangladesh is non-functional because all three fundamental organs of the state (that is, Legislative, Judiciary and Executive) remain almost ineffective in performing their designated functions.²⁸⁹ There is a lack of coordination among the three organs and there has been an ever-evolving conflict between the presidency and parliament since independence. In addition, the country endured 15 years of military rule after 1971 and the resulting power imbalance in the civil-military relationship greatly hampers the democratisation of the major political institutions.²⁹⁰ Moreover, politicisation of the civil bureaucracy, local government institutions and law enforcement agencies has further worsened the democratic characteristics of the state. Nonetheless, the main reason for political instability is the result of internal power struggles and accumulated mistrust among the political parties; mainly between the two major parties namely the Bangladesh Awami League and the Bangladesh Nationalist Party.²⁹¹ Modalities of general elections, handing over the power, increasing mistrust, ideological differences, disregarding each other's development policies and excessive power inclination are the causes for the clashes between the two parties.²⁹² Most of the people of the country support these two parties and hence are politically divided. Both the parties do not practice democracy within themselves, often engage in political violence and steer the nation toward political turbulence and uncertainty.²⁹³

²⁸⁶ M.A. Uddin, M.H. Ali, and M. Masih, 'Political Stability and Growth: An Application of Dynamic GMM and Quantile Regression', *Economic Modelling*, vol. 64, 2017, pp. 610-611.

²⁸⁷ N. Dutta, D. Mukherjee and S. Roy, 'Re-examining the Relationship between Domestic Investment and Foreign Aid: Does Political Stability Matter?', *International Review of Applied Economics*, vol. 29, no. 3, 2015, pp. 259-261.

²⁸⁸ D.H. Bearce, 'Reconsidering the Effect of Political Regime Type on Foreign Aid Effectiveness', *International Interactions*, vol. 39, no. 3, 2013, pp. 416-417.

²⁸⁹ Q. Fatima and K. Imran, 'Political Development and Modernisation in Bangladesh', *South Asian Studies*, vol. 32, no. 1, 2017, pp. 123-124.

²⁹⁰ Fatima and Imran, pp. 111-112.

²⁹¹ M.M. Karim, 'Socio-economic and Political Development of South Asian Countries: In Bangladesh Perspective', *International Journal of Humanities and Social Science Invention*, vol. 2, no. 2, 2013, pp. 29-30.

²⁹² M. Hassan and S. Nazneen, 'Violence and the Breakdown of the Political Settlement: An Uncertain Future for Bangladesh?', *Conflict, Security and Development*, vol. 17, no. 3, 2017, pp. 205-207.

²⁹³ A. Ahmad, 'Bangladesh in 2012: Economic Growth, Political Under-development', *Asian Survey*, vol. 53, no. 1, 2013, pp. 78-80.

Table 5.1: Percentages of ADP utilization and disbursement of aid in FY 2014-15 and 2015-16.

ADP Utilization			Foreign Aid Disbursement		
Variables	2014-15 (BDT billion)	2015-16 (BDT billion)	Variables	2014-15 (US\$ million)	2015-16 (US\$ million)
Allocation	860.00	970.00	Commitment	5252.60	7048.08
Utilization	712.14	867.45	Disbursement	3005.54	3531.72
%	82.82	89.42	%	57.22	50.11

(Source: ERD 2016)

Political instability is harmful for economic growth in Bangladesh because it discourages both local and foreign investments, which obstructs capital accumulation. The undemocratic behaviour of the political institutions is responsible for reducing the credibility of the government because it enhances both the level of corruption and institutional incompetence.²⁹⁴ Political uncertainty is a concern for the government and development partners because political violence, corruption and conflict interrupt development initiatives.²⁹⁵ Whenever the political turbulence is at a peak, Bangladesh experiences a low implementation of the ADP and a relatively low disbursement of aid. For example, there were severe political clashes after the Bangladesh Awami League won the 2014 general election. These clashes seriously affected all the development activities across the country in that period as there were several strikes from the opposition Bangladesh Nationalist Party.²⁹⁶ Moreover, some of the infrastructure was greatly damaged by these activities. As a result, only 82.82% and 89.42% of ADP allocation was utilised in FY 2014-15 and 2015-16 respectively (Table 5.1). It is also to be noted from Table 5.1 that only 57.22% and 50.11% of the committed aid was disbursed respectively in FY 2014-15 and 2015-16, which were two of the lowest disbursements by percentage since the independence.²⁹⁷ Changes in power often entail changes in the national priorities and the country frequently experiences discontinuation of development approaches by a new government.²⁹⁸ This also affects foreign aid project implementation and the disbursement of aid. Project implementation is also hampered due to interference of the political parties as they often receive different undue facilities including bribes from project personnel and the contractors.²⁹⁹ The politicised administration and law enforcement agencies cannot prevent these undemocratic practices. Therefore, less functional political institutions, political violence, political interference and frequent shifting in national priorities affect effective aid utilisation in Bangladesh.

²⁹⁴ S.N. Parnini, and M.R. Othman, 'Democratic Consolidation and Credibility of Governance Institutions in Bangladesh', *Journal of Asian and African Studies*, vol. 49, no. 1, 2014, pp. 34-35.

²⁹⁵ M.U. Ahmed and M.H. Pulok, 'The Role of Political Stability on Economic Performance: The Case of Bangladesh', *Journal of Economic Cooperation and Development*, vol. 34, no. 3, 2013, pp. 81-82.

²⁹⁶ Hassan and Nazneen, pp. 216-218.

²⁹⁷ Economic Relations Division, p. 275.

²⁹⁸ F.A. Osman, 'Bangladesh Politics: Confrontation, Monopoly and Crisis in Governance', *Asian Journal of Political Science*, vol. 18, no. 3, 2010, pp. 324-325.

²⁹⁹ Osman, pp. 324-325.

5.5. Aid Conditionality

The donor-recipient relationship determines the implementation modalities of foreign aid development projects as well as the level of aid flow and, hence, is very important for aid effectiveness. The typical donor-recipient relationship is generally characterised by a resource flow from developed countries to developing countries along with sets of conditions. This aid conditionality has two aspects. Firstly, donors set prerequisites to reform the institutional frameworks of recipient countries. The reform includes macroeconomic and financial policies, institutional capacity building, governance and democracy, justice, gender equality, human rights and monitoring systems for project implementation.³⁰⁰ Secondly, donors sometimes impose strict conditions upon the recipients so as to serve their own interests related to geopolitical, diplomatic and economic affairs.³⁰¹ For example, donors ask for support from the recipient in respect to their own position on global issues or to promote their materials, technical know-how, personnel and companies in the recipient countries.³⁰² The conditions related to the institutional development of the recipient country are desirable because these can assist the recipient to grow as a politically and economically resilient state.³⁰³ However, the recipients neither initiate the reforms themselves nor willingly comply with the donor initiated approaches. Rather they develop an attitude of dependency among themselves and expect the reforms to be executed by the donors themselves.³⁰⁴ This tendency affects administrative reforms and institution building that impedes the recipient countries to adopt necessary policies and transformations to ensure aid effectiveness.³⁰⁵ On the one hand, conditions that serve donors' interests have long-term negative impacts on the recipient's economy by limiting the opportunities of local enterprises while, on the other hand, affect the aid flow if the recipient fails to meet the demands of the donors.³⁰⁶ Therefore, the imbalance of the donor-recipient relationship is considered one of the reasons why aid returns diminishing outcomes.³⁰⁷ In addition, donors have some lack of coordination among themselves in managing the flow of aid in the same sector. As a result, there is some overlapping in aid utilisation and hence, aid harmonisation is affected.

Bangladesh needs to comply with some conditions for borrowing aid from the bilateral and multilateral development partners. Immediately after independence, Bangladesh mostly received unconditional grants from the donors which was helpful to meet the immediate humanitarian

³⁰⁰ N. Molenaers, S. Dellepiane and J. Faust, 'Political Conditionality and Foreign Aid', *World Development*, vol. 75, 2015, pp. 8-9.

³⁰¹ O. Stokke, 'Aid and Political Conditionality: Core Issues and the State of the Art' in O. Stokke (ed.), *Aid and Political Conditionality*, Frank Cass, London, 1995, pp. 1-5.

³⁰² L. Tajoli, 'The Impact of Tied Aid on Trade Flows between Donor and Recipient Countries', *Journal of International Trade and Economic Development*, vol. 8, no. 4, 1999, pp. 374-375.

³⁰³ A. Scholl, 'Aid Effectiveness and Limited Enforceable Conditionality', *Review of Economic Dynamics*, vol. 12, no. 2, 2009, pp. 377-378.

³⁰⁴ Berlinschi, pp. 446-447.

³⁰⁵ S. Dietrich, 'Donor Political Economies and the Pursuit of Aid Effectiveness', *International Organization*, vol. 70, no. 1, 2016, pp. 69-70.

³⁰⁶ Tajoli, pp. 374-375.

³⁰⁷ J.S. Davies, 'Against Partnership: Toward a Local Challenge to Global Neoliberalism' in R. Hambleton and J.S. Gross (eds.), *Governing Cities in a Global Era*, Palgrave Macmillan, New York, 2007, pp. 199-202.

requirements. When Bangladesh focused on implementing development projects with aid, it faced several challenges in terms of mis-governance and institutional incompetence, and its fiscal management was also questionable. Democracy in Bangladesh is relatively new and fragile. Also, the institutions have not been developed to a fully functional level. Since the 1990s, the donors started imposing conditions of reforming the political and economic environment of the country.³⁰⁸ By the end of the 1990s, the implementation of SAPs, governance, democracy and public-sector reforms for poverty reduction measures became the major conditions for receiving development aid in Bangladesh.³⁰⁹ Despite taking some donor-driven initiatives, the expected reforms were still not achieved. Later, aid conditionality was incorporated into the PRSPs (adopted in 2001), MDGs and Sector-wide Approaches (SWAPs). Nonetheless, Bangladesh did implement several reforms in its policy environment in terms of its trade policy, procurement guidelines, and monetary policy and so on but these reforms returned very little due to lack of country ownership of the reform programs.³¹⁰ These reforms partially failed due to an unequal power relationship between the government and donors where the donors dominated and imposed governance conditions on Bangladesh and did not allow Bangladesh to determine its own development discourses.³¹¹ Therefore, the noncompliance with the conditions required for aid continuation affected both the flow of aid and the effectiveness of the disbursed aid. Recently, the OECD, through the Paris Declaration and The Accra Agenda for Action, has adopted a new agenda for improved aid effectiveness measures and it is expected that the new tools will increase partnerships and mutual cooperation between the government and its development partners. The next chapter discusses what Bangladesh has done so far against the new agenda for aid effectiveness and what it has achieved so far.

5.6. Conclusion

Foreign aid has made a significant contribution to economic growth in Bangladesh through investment and capital accumulation but there are many shortfalls in Bangladesh that reduce the effectiveness of aid utilisation. Both the internal deficiencies within the Bangladesh institutional system and external issues associated with donors' operational procedures collectively challenge aid effectiveness in Bangladesh. The political, economic, administrative, regulatory and legislative authorities in Bangladesh are not capable enough to design, implement and monitor their obligations as per expectation. The immature democracy, corruption, politicisation of civil bureaucracy, political clashes and political uncertainty have obstructed the country to produce an efficient system of governance. Therefore, it is difficult for Bangladesh to benefit from the impact of the massive development initiatives it has been implementing over the years. Foreign aid efforts are expected to contribute to both investment and reforms of the macroeconomic frameworks. Aid is contributing to

³⁰⁸ M. Nuruzzaman, 'Neoliberal Economic Reforms, the Rich and the Poor in Bangladesh', *Journal of Contemporary Asia*, vol. 34, no. 1, 2004, pp. 33-35.

³⁰⁹ Parnini, pp. 557-558.

³¹⁰ Obaydullah, pp. 60-61.

³¹¹ Parnini, pp. 557-560.

investment but the deficiency within the Bangladesh institutional system function like a vicious cycle that hinders the effective aid utilisation for making the necessary and planned changes. Simultaneously, donor-guided reform programs and their aid conditions rarely align with the needs of the country for Bangladesh to take ownership of the proposed aid reforms and conditions attached. As aid is essential for meeting the investment gaps, Bangladesh must work on how aid effectiveness can be ensured. The recent endeavours of the OECD aim to achieve aid effectiveness through mutual donor-recipient collaboration by removing internal deficiencies and aligning the aid conditionality with that of the country for the country to take ownership of the aid's goals and conditions. The next chapter discusses what Bangladesh has done so far to address the new agenda for aid effectiveness, what progress it has achieved and what it can further do to ensure aid effectiveness.

CHAPTER 6: AID EFFECTIVENESS – MEASURES AND ANALYSIS

6.1. Introduction

Most of the recent studies on the aid-growth relationship find a positive impact of aid on the growth and development of the recipient countries. Simultaneously, these studies consider the impact of aid on the structural and systematic reforms of the recipient countries. The reform initiatives are implemented to promote a well-organised management system for the recipient government so that it can ensure sustainable socioeconomic development through efficient resource allocation and utilisation thereof.³¹² A significant portion of aid is utilised in the reform programs alongside the productive economic and social sectors but aid is frequently criticised for not making a substantial impact on the reform arrangements.³¹³ Hence, effectiveness in achieving the expected outcomes of aid utilisation covering growth and reforms is a considerable issue for the donors, recipients, policy makers, development professionals and academics.³¹⁴ Until now, I have discussed how, despite some wastage, aid has made a significant contribution to socioeconomic development in Bangladesh through capital accumulation and investment. Aid has some positive effects in promoting systematic reforms of the Government of Bangladesh but the progress is slow due to corruption, institutional inefficiency, political uncertainty, aid conditionality and a lack of country ownership over the reform programs. The impediments for aid effectiveness are persistent in almost all the recipient countries. As donors are also responsible for ensuring aid effectiveness, the OECD has adopted a new set of guiding principles for aid management and coordination by addressing the roles of both sides.³¹⁵ This chapter discusses the measures that Bangladesh has taken so far to ensure aid effectiveness along with their progress. This chapter also includes some policy implications for Bangladesh to ensure aid effectiveness in the years ahead.

6.2. Progress of Aid Effectiveness Measures

Bangladesh has implemented some of the reform programs related to the macroeconomic framework, governance, public management and aid management – which have mostly been prescribed by the donors. However, there are considerable differences in the reform scenario before and after the Paris Declaration in 2005. The earlier reforms were strictly donor driven where only the internal factors and the role of the Government of Bangladesh were taken into consideration.³¹⁶ Conversely, the modalities of aid effectiveness since the Paris Declaration have strategically focused

³¹² D.K. Christopoulos, G. Siourounis and I. Vlachaki, 'Democratic Reforms, Foreign Aid and Production Inefficiency', *The Manchester School*, vol. 84, no. 3, 2016, pp. 366-367.

³¹³ N. Gulrajani, 'Dilemmas in Donor Design: Organisational Reform and the Future of Foreign Aid Agencies', *Public Administration and Development*, vol. 35, no. 2, 2015, pp. 152-154.

³¹⁴ Mawdsley, Savage and Kim, pp. 27-28.

³¹⁵ J.W. Choi and J. Bak, 'Governance and Management for Better Aid Effectiveness: A Donor Country's Perspective', *International Review of Public Administration*, vol. 22, no. 1, 2017, pp. 47-48.

³¹⁶ Dristy, pp. 12-14.

on mutual cooperation and accountability of the donors and the Government of Bangladesh. Therefore, I have discussed the aid effectiveness measures in Bangladesh in two parts; that is, before and after the Paris Declaration.

6.2.1. Aid effectiveness measures and progress before the Paris Declaration

Bangladesh started receiving aid immediately after independence to deliver humanitarian assistance. Gradually, Bangladesh began to invest aid in development activities and the development budget (ADP) became completely dependent on foreign aid from 1974 to the late 1980s. By the end of the 1980s, the flow of aid was around 10% of the GDP and almost 100% of the ADP.³¹⁷ At that time, no budget was possible without pledging for aid utilisation at the 'Paris Consortium Meetings'³¹⁸ in April of each year. This aid dependency of Bangladesh had given the opportunity to the donor to practise unparalleled influence in the reform and formulation of the country's policies. Hence, the WB and the IMF imposed the Structural Adjustment Programs (SAPs) on Bangladesh. SAPs were designed to be implemented by the aid recipient to promote a free market economy in light of the neoliberal economic theories associated with the Washington Consensus.³¹⁹ The main features of the consensus were broadly related to financial liberalisation, privatisation, tax reforms, trade openness and removing trade barriers, reduction in public expenditure, decreasing state interventions in the market and ensuring property rights in the aid recipient countries.³²⁰

Bangladesh accepted these reform programs under the SAPs but due to several drawbacks in the Bangladesh institutional system and the operational modalities of the donors discussed in the previous chapter, Bangladesh could not implement the programs satisfactorily. The WB and the IMF overlooked their own drawbacks in the reform agenda and focused only on the weakness of the Bangladesh institutional system in dealing with the economic policies as the causes behind the failure of the reform programs.³²¹ They described the numerous operational failures collectively as the failure of governance. To the WB, the failure of governance in the macroeconomic management of Bangladesh is related to weaknesses in fiscal management, quality public expenditure, financial sector reforms, the promotion of the private sector, and the pricing of tradable goods.³²² The policy makers, officials and professionals of Bangladesh identified hard conditions of the reform proposals and internal political constrictions as well as institutional incompetence as the causal factors behind the weak outcomes, compared to the actual commitments of the reform programs.³²³

³¹⁷ Sobhan, *From Aid Dependence to Self-Reliance*, pp. 7-12.

³¹⁸ 'Paris Consortium Meetings' is referred to the Aid Group's meeting. It is a consortium of donor countries who met in Paris till 2001 to pledge resources for the recipient countries for a given period. After 2001, for Bangladesh, this group was converted into Bangladesh Development Forum (BDF) with similar agenda.

³¹⁹ Willis, pp. 52-53.

³²⁰ J. Williamson, 'The Strange History of the Washington Consensus', *Journal of Post Keynesian Economics*, vol. 27, no. 2, 2004, pp. 195-196.

³²¹ Obaydullah, pp. 46-47.

³²² The World Bank (WB) and The Asian Development Bank (ADB), *Bangladesh: Economic Trends and the Policy Agenda*, The WB and The ADB, Dhaka, 2008, pp. 10-15,

<<http://documents.worldbank.org/curated/en/691201468768008848/pdf/30617.pdf>>, consulted 12 April 2018.

³²³ Obaydullah, pp. 46-47.

The implementation of the SAPs had an inverse impact on the political economy of Bangladesh. The vested interest groups used their political power and bureaucratic influence to empower and enrich themselves whereas the masses were deprived of the benefits of the reforms and the financial incentives from the flow of aid as well.³²⁴ The failure of the SAPs was not sufficient for the donors to rethink their reform agenda; rather they continued imposing further reform programs, assuming that the core problems lied with the governance. Poverty reduction alongside achieving growth was prioritised by the donors where the new issues like good governance, judicial reforms and democracy were attributed with the SAPs.³²⁵ Eventually, Bangladesh needed to prepare and finalise a Poverty Reduction Strategy Paper (PRSP) covering the new agenda and related issues by 2005. Apart from this, donors have also emphasised improving institutional competence and effective project management by duly incorporating accountability, transparency and stakeholders' participation and empowerment.³²⁶

Still, these reforms could not impact very much on the building of structural capacity in Bangladesh for aid management. On the one hand, the home-grown impediments and the donor-driven reform programs, combined with a lack of country ownership on the other, collectively contributed to the failure of the reform programs. As a result, aid effectiveness was not achieved as per expectations. These failures in Bangladesh were not unique. As a consequence, the OECD-DAC moved to then rethink the entire gamut of the aid utilisation modalities and finally came up with a set of aid effectiveness guidelines for recipient countries through the Paris Declaration in 2005; and these were reinforced by the Accra Agenda for Action in 2008 and finally again the Busan High Level Forum in 2011.

6.2.2. Aid effectiveness measures and progress after the Paris Declaration

6.2.2.1. *The aid effectiveness principles*

The international community of more than 150 donor countries/agencies and recipient countries have endorsed 'The Paris Declaration' to mutually launch practical and results-based roadmaps to utilise aid successfully and assess aid effectiveness progress in the recipient countries.³²⁷ The declaration encompasses five core principles together with 56 partnership commitments among the donors and recipient countries with a view to enhancing aid effectiveness. The core principles are:³²⁸

³²⁴ Nuruzzaman, p. 52.

³²⁵ Dristy, pp. 12-14.

³²⁶ Waheduzzaman, pp. 474-476.

³²⁷ N. Dabelstein and M.Q. Patton, 'The Paris Declaration on Aid Effectiveness: History and Significance', *Canadian Journal of Program Evaluation*, vol. 27, no. 3, 2013, pp. 19-21.

³²⁸ Organisation for Economic Co-operation and Development (OECD), 'Paris Declaration and Accra Agenda for Action', OECD's website, Paris, 2018, <<http://www.oecd.org/dac/effectiveness/parisdeclarationandaccraagendaforaction.htm>>, consulted 12 April 2018.

Ownership: The partnered developing countries shall prioritise their development requirements, prepare their own policies and strategies for development, and coordinate the development actions.

Alignment: The donor countries/agencies shall extend development assistance as per the partner country's development strategies, institutions and procedures.

Harmonisation: The procedures of the development partners are harmonised, simplified, transparent and mutually effective to avoid duplication in aid utilisation.

Managing for Results: The donors and recipients shall collectively manage the allocated resources and the decision makings shall be focused on achieving development results.

Mutual Accountability: The donors and the recipients are mutually accountable for their actions in achieving development outcomes.

The Accra Agenda for Action was organised in Ghana in 2008 to facilitate in-depth discussion and negotiation among the Least Developed Countries (LDCs) and their donors to fully implement the principles of the Paris Declaration. A schedule was fixed to achieve the commitments of the Paris Declaration by 2010.³²⁹ Considering the progress of the Paris commitments, the Accra Agenda for Action emphasises on promoting Country Ownership, Inclusive Partnership, Delivery of Results and Capacity Enhancing for Development of the recipient countries.³³⁰ The Paris and Accra events were helpful to reshape the conventional donor-driven aid mechanism as a partnership-based approach for development. The fourth high-level forum on aid effectiveness, held in Busan in 2011, added new dimensions to the era of development cooperation. Reiterating the Paris and Accra principles, the forum acknowledged that aid is only an alternative source of development financing and the external supports alone cannot eradicate poverty and ensure development.³³¹ Rather, a multi-stakeholder development partnership is crucial for the development of the recipient country where the financial support and technical know-how of the development partners can be instrumental.³³² Hence, the Global Partnership for Effective Development Cooperation (GPEDC) was created. The GPEDC emphasises accountability and transparency of the aided efforts through a strong monitoring system including institutional capacity development, enhancing multi-stakeholder development cooperation among all the local and global stakeholders, ensuring governance and accountability, and promoting gender equality. This notion of development cooperation was agreed by the conventional donors, partners of the South-south Cooperation, BRICs,³³³ and private investors and so on.

³²⁹ Dristy, pp. 12-14.

³³⁰ Organisation for Economic Co-operation and Development.

³³¹ A. Bigsten and S. Tengstam, 'International Coordination and the Effectiveness of Aid', *World Development*, vol. 69, 2015, pp. 75-78.

³³² Mawdsley, Savage and Kim, pp. 28-30.

³³³ The four developing countries i.e. Brazil, Russia, India and China are collectively known as BRICs. All the countries are from Higher Middle Income Country group and lead several regional cooperation and thus influential to the Least Developed and other developing countries.

6.2.2.2. Progress of aid effectiveness measures after the Paris Declaration

The Government of Bangladesh signed the Paris Declaration in 2005 to improve its efficiency in managing and coordinating the development assistance offered by the multilateral and bilateral development partners. Bangladesh received almost all its aid in light of the guiding principles of the Paris Declaration in that period.³³⁴ In compliance with the principles, Bangladesh formulated national strategies and undertook several reform initiatives to perform its part in enhancing country ownership, alignment with the donors and results-based monitoring and evaluation plans for the aided projects. These initiatives were helpful in achieving aid effectiveness to some extent in terms of aid disbursement as per national plans and MDGs, better coordination among the donors and strengthening of the aid management system in Bangladesh.³³⁵

Bangladesh participated in the Accra Agenda for Action in 2008 and declared to form a Joint Cooperation Strategy (JCS) between the government and the donors. The JCS was made effective in 2010 as a way to make the Paris Declaration a reality in Bangladesh. It included action plans to improve the aid transfer mechanism, strengthen the aid management capacity of the government, improve fiscal management in the public sector, and ensure mutual responsibility for poverty reduction and the creation of opportunities for the wider community. The JCS is the avenue where the donors and the government are accountable to each other in respect to the actions taken by both sides to ensure aid effectiveness.³³⁶ One key instrument of the JCS is the BDF which unites the development institutions of the government, development partners, the Local Consultative Group (LCG), civil society, NGOs, the media and the private sector together to take part in dialogue and discussion on the country's development framework.³³⁷ The BDF intends to consult on the country's development policies and priorities with a view to adopting the best conceivable approaches to work collectively. Another component of the JCS is the LCG which aims to coordinate the government-led and donor-supported development programs with a view to ensuring aid harmonisation.³³⁸ Bangladesh also introduced the Harmonised Action Plan (HAP) in 2006 to ensure better coordination with its partners.

The last OECD evaluation report of 2011 on the progress of the Paris Declaration shows that Bangladesh only succeeded to achieve three (3, 4 and 8 of table 6.1) out of the 12 indicators under the five core principles. There was some progress in Ownership, Alignment and Harmonisation up to 2010 although there were still a lot of challenges for Bangladesh.³³⁹ On the contrary, nothing was achieved in case of results-based frameworks and dimensions of mutual accountability, meaning Bangladesh needed to face severe challenges as a consequence. Donors' prolonged disbursement

³³⁴ Rahaman and Khan, pp. 112-114.

³³⁵ Dristy, pp. 12-14.

³³⁶ International Aid Transparency Initiative (IATI), 'Joint Cooperation Strategy of Bangladesh', IATI's website, New York, 2010, <<https://www.aidtransparency.net/news/joint-cooperation-strategy-of-bangladesh>>, consulted 12 April 2018.

³³⁷ Dristy, pp. 12-14.

³³⁸ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 132-134.

³³⁹ Organisation for Economic Co-operation and Development (OECD), *Bangladesh*, OECD, Paris, 2011, pp. 1-5, <<https://www.oecd.org/dac/effectiveness/Bangladesh%203.pdf>>, consulted 13 April 2018.

procedures while aid volatility, politicised aid management of the development ministries, political instability and the absence of all-inclusive capacity improvement procedures were the causes for slow progress in negotiating the Paris Declaration.³⁴⁰ Despite the slow progress, Bangladesh did not stop working and continued several approaches to ensure aid effectiveness as per the principles acknowledged in 2011 in the Busan High Level Forum.

Table 6.1: The progress of aid effectiveness measures in Bangladesh up to 2010.

INDICATORS		2005 REFERENCE	2007	2010 ACTUAL	2010 TARGET
1	Operational development strategies	C	C	C	B or A
2a	Reliable public financial management (PFM) systems	3.0	3.0	3.0	3.5
2b	Reliable procurement systems	Not available	Not available	Not available	No Target
3	Aid flows are aligned on national priorities	88%	92%	100%	94%
4	Strengthen capacity by co-ordinated support	31%	69%	54%	50%
5a	Use of country PFM systems	53%	77%	65%	No Target
5b	Use of country procurement systems	48%	66%	29%	No Target
6	Strengthen capacity by avoiding parallel PIUs	38	24	18	13
7	Aid is more predictable	91%	100%	84%	96%
8	Aid is untied	89%	89%	93%	More than 89%
9	Use of common arrangements or procedures	41%	50%	34%	66%
10a	Joint missions	19%	20%	29%	40%
10b	Joint country analytic work	38%	42%	47%	66%
11	Results-oriented frameworks	D	C	C	B or A
12	Mutual accountability	N	N	N	Y

(Source: OECD 2011)

The JCS is still functioning in terms of LCG plenary and BDF meetings and efforts are being undertaken to work on aid effectiveness. As part of the commitment to the International Aid Transparency Initiative (IATI), Bangladesh has developed a web-based Aid Information Management System (AIMS) to promote transparency in aid management and information.³⁴¹ The Economic Relations Division (ERD) is the central organisation in Bangladesh for coordinating and managing development assistance. The ERD, with financial and technical support from the UNDP, is executing a capacity development project titled 'Strengthening Capacity for Aid Effectiveness in Bangladesh'. The core objective of this project is to promote transparency and accountability in the allocation, coordination, utilisation and management of development assistance.³⁴² The objectives plan to achieve the strengthening of the country's aid administration capabilities and systems while improving collective coordination mechanisms. The outcomes of the project are expected to entail

³⁴⁰ Organisation for Economic Co-operation and Development, *Bangladesh*, pp. 1-5; Dristy, pp. 12-14.

³⁴¹ United Nations Development Programme (UNDP), 'Strengthening Capacity for Aid Effectiveness in Bangladesh: What is the Project about?', UNDP's website, Dhaka, 2018, <http://www.bd.undp.org/content/bangladesh/en/home/operations/projects/democratic_governance/strengthening-capacity-for-aid-effectiveness-in-bangladesh.html>, consulted 15 April 2018.

³⁴² United Nations Development Programme, 'Strengthening Capacity for Aid Effectiveness in Bangladesh'.

enhanced development results. The project has been helpful for the government in institutionalising and instigating aid effectiveness issues both at the local and global level. Bangladesh is a member of the steering committee of the GPEDC, the Vice Chair of IATI and the Chair of the Asia Pacific Development Effectiveness Facility (AP-DEF).³⁴³ Bangladesh has already prepared and adopted a 'National Policy on Development Cooperation (NPDC)' with the core objectives of providing a coherent and integrated institutional and policy approach, ensuring the alignment of development assistance with national requirements and safeguarding the results of effective aid utilisation.³⁴⁴ In addition, through the Right to Information Act, the government is making arrangements to publicly share government documents, aid data and project documents so that the transparency and accountability of the aided efforts are ensured.³⁴⁵ As part of the functional Monitoring and Evaluation system for financial management, Bangladesh introduced the Medium-Term Budgetary Framework (MTBF). It is the key instrument for coordination among the administrative and regulatory institutions of the government in respect to national planning and fiscal management. The adoption of the world-accredited Public Procurement Guidelines and e-tendering as part of efficient public expenditure have added new dimensions to Bangladesh's efforts for ensuring aid effectiveness.

Still, the Public Financial Management (PFM) system in Bangladesh is not strong enough mainly due to the poor coordination of the central ministries with the local government offices at the sub-national levels.³⁴⁶ Whatever steps on aid effectiveness Bangladesh has taken so far have contributed to the knowledge and perception level of the ERD but it is not sufficient for ensuring comprehensive aid effectiveness in Bangladesh. Political interference, corruption, deception and malpractice discussed in Chapter 5 are all still threats for the public procurement system, which are collectively responsible for the slow delivery of aid.³⁴⁷ The limited capacity of the development ministries is an obstacle for designing and implementing quality development projects. Government agencies often appoint skilled and trained officials to such positions which, unfortunately, are positions not aligned to their expertise. Consequentially, the government misses the opportunity of developing specialisations in development management. Moreover, the development ministries are somehow incapable of managing programs in accordance with the national and sectoral development strategies.³⁴⁸ Not even consistent data regarding the impact evaluation of the aided projects are available within the development ministries. Therefore, despite all efforts, Bangladesh is still expected to achieve set outcomes regarding aid effectiveness. Nonetheless, the aid effectiveness

³⁴³ United Nations Development Programme, 'Strengthening Capacity for Aid Effectiveness in Bangladesh'.

³⁴⁴ Economic Relations Division (ERD), '*Bangladesh: National Policy on Development Cooperation*', Ministry of Finance, Government of Bangladesh, Dhaka, 2018, <[http://erd.portal.gov.bd/sites/default/files/files/erd.portal.gov.bd/page/9d1a9f30_664e_4ac0_93bf_07163494bdfe/FINAL%20DRAFT%20NPDC%20\(1\).pdf](http://erd.portal.gov.bd/sites/default/files/files/erd.portal.gov.bd/page/9d1a9f30_664e_4ac0_93bf_07163494bdfe/FINAL%20DRAFT%20NPDC%20(1).pdf)>, consulted 16 April 2018.

³⁴⁵ The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 132-134.

³⁴⁶ Waheduzzaman and C.H.B. Mphande, 'Gaps in Pursuing Participatory Good Governance', *Administration and Society*, vol. 46, no. 1, 2014, pp. 53-55.

³⁴⁷ M.H. Khan and R.M. Gisselquist, 'Aid and Governance in Vulnerable States: Bangladesh and Pakistan since 1971', *The Annals of the American Academy of Political and Social Science*, vol. 656, no. 1, 2014, pp. 74-76.

³⁴⁸ Dristy, pp. 24-26.

measures have been reinforced properly since 2008 in light with the Accra agenda and streamlined since the Busan Forum in 2011; so it appears more time is required to witness substantial progress in this area in a country like Bangladesh. Interestingly, there is a general perception in Bangladesh that the aided projects are more transparent and, hence, more successful.³⁴⁹ Bangladesh should adhere to its missions and carry on the measures with innovation to ensure aid effectiveness.

6.3. Identifying Weaknesses in the Aid Delivery System

Considering the impediments for aid utilisation, the efforts for aid effectiveness and the progress of effectiveness measures in Bangladesh, I have identified some weaknesses in the foreign aid management and coordination system. These weaknesses must be removed to ensure a results-based aid utilisation mechanism in Bangladesh.

Firstly, as argued in sections 3.7, 5.5 and 6.2 of this paper, Bangladesh has not been able to completely comply with the aid effectiveness measures as per OECD guidelines. Country ownership over development planning and programs as well as their alignment to the national requirements are yet to be established as the core principle of the aid effectiveness framework.³⁵⁰ The dependency attitude of the government and the dominating roles of the development partners impede the evolution of an effective development partnership in this regard.³⁵¹ Bangladesh is substantially dependent on overseas consultants and guidance for generating policies and reform measures that somehow fails to place the nation's requirements at its core.³⁵²

Secondly, section 6.2 discusses how strengthening of the ERD in terms of knowledge development is not in itself sufficient to modernise the aid management and coordination system in Bangladesh. The sectoral planning and the ministries' undertakings are not sufficiently synchronised with the national development plans. The ministries are not sufficiently competent in the areas of planning, execution or budgeting to deliver on the development programs.³⁵³ Ministries have a dearth of skilled and specialised workforces suited to efficient development management.³⁵⁴ The ERD has insufficient authoritative influence over the development ministries and agencies in monitoring all the phases of planning, implementation and evaluation of aided development projects.³⁵⁵ As the central coordinating agency, the ERD has limitations in performing its roles.

³⁴⁹ M.S. Winters, S. Dietrich and M. Mahmud, 'Perceptions of Foreign Aid Project Quality in Bangladesh', *Research and Politics*, vol. 4, no. 4, 2017, pp. 1-5.

³⁵⁰ Rahaman and Khan, pp. 118-120; Obaydullah, pp. 60-61; Dristy, pp. 24-26.

³⁵¹ C. Blampied, *Where Next for Development Effectiveness? Recommendations to the GPEDC for Nairobi and Beyond*, The Overseas Development Institute (ODI), London, 2016, pp. 4-7, <<https://www.odi.org/sites/odi.org.uk/files/resource-documents/11089.pdf>>, consulted 16 April 2018.

³⁵² M.M. Rahaman and N.A Khan, 'Making International Aid Effective: An Agenda for Aligning Aid to Social Business', *Development Policy Review*, vol. 35, 2017, pp. 104-105.

³⁵³ Winters and Martinez, pp. 520-522.

³⁵⁴ Dristy, pp. 24-26.

³⁵⁵ Rahaman and Khan, 'The Realities of Aid Harmonisation and Aid Effectiveness', pp. 118-120.

Thirdly, the current aid allocation system is distorted by the communication skills and relationship of the ministries with the donors (see sections 5.2, 5.3 and 6.2). Aid flow needs to be directed based on the nation's actual requirements, tangible and assessable results, and objective assessments but so far the shadowy requirements have been much influential in attracting aid allocation.³⁵⁶ The ERD has limitations in playing the role of mediator between the donors and government ministries in this concern. Again, sections 5.5 and 6.2 argue that the development partners are sometimes strict on their conditions and have been slow in the financing and disbursement of the committed assistance for development projects.³⁵⁷ In addition, aid is provided by the donors in a segregated way, where aid flow is sometimes not harmonised and aligned to the national priorities and development planning of Bangladesh.

Fourthly, sections 5.5 and 6.2 claim that public expenditure and financial management in Bangladesh are not transparent or results-oriented.³⁵⁸ Despite taking some initiatives such as e-tendering and the MTBF, the procurement system is still suffering from corruption and nepotism. In addition, only two-thirds of the aid flow is reported in the national budget and other reporting on aid utilisation.³⁵⁹ Although AIMS has been launched, there is some confusion on the impact of aid delivery because both the donors and the ministries are yet to provide the entire updated aid data to the system.

Fifthly, as discussed in section 6.2 above, the GPEDC is focusing on multi-stakeholder partnerships for development effectiveness. All the stakeholders are expected to appraise each other's role for effective aid delivery. However, the platforms at the national level such as the LCG or the BDF meet approximately once every two or three years. These are functional but irregular and not well-represented by all the stakeholders, and is not, therefore, adequate to ensure mutual accountability and a results-based partnership.³⁶⁰

Finally and most importantly, Bangladesh is struggling to ensure development effectiveness irrespective of domestically or externally financed initiatives, mainly due to lack of political commitments from the ruling parties (sections 4.4, 5.4, 6.1 and 6.2).³⁶¹ The politicisation of government institutions are the root cause for systematic incompetence, corruption, political interference on public expenditure and political uncertainty.³⁶² This is also responsible for fluctuations in the donor-recipient relationships in Bangladesh because changes in power entail changes in international relationships.

³⁵⁶ Rahaman and Khan, 'The Realities of Aid Harmonisation and Aid Effectiveness', pp. 111-112; Quibria and Ahmad, pp. 30-31; Obaydullah, pp. 57-58.

³⁵⁷ Blampied, pp. 2-5.

³⁵⁸ Waheduzzaman and Mphande, pp. 53-55; S. Younus, 'Monetary Transmission Channels in Bangladesh: Evidence from a Floating Exchange Rate Regime', *Journal of Developing Areas*, vol. 51, no. 2, 2017, pp. 255-258.

³⁵⁹ United Nations Development Program, 'Strengthening Capacity for Aid Effectiveness in Bangladesh'.

³⁶⁰ Rahaman and Khan, 'The Realities of Aid Harmonisation and Aid Effectiveness', pp. 113-115; Blampied, pp. 2-5.

³⁶¹ Osman, pp. 324-325.

³⁶² Ahmed and Pulok, pp. 81-82.

6.4. Conclusion

The above aid effectiveness issues have been highlighted since the 1990s in Bangladesh. I classify the aid effectiveness discussion in Bangladesh into two different eras from the 1990s to 2005 and from 2005 to present. The aid effectiveness measures before 2005 were essentially donor-driven reform programs where the WB and the IMF performed the key roles. With the spirit of the Washington Consensus, Bangladesh had to implement SAPs to reform some of the macroeconomic policy frameworks. Due to institutional incompetence, corruption, political volatility and lack of country ownership of the reform programs, Bangladesh could achieve very little from the aid effectiveness measures before 2005. Since 2005, the OECD through the Paris Declaration, the Accra Agenda for Action and the Busan High Level Forum have developed new principles of aid effectiveness. Bangladesh has already implemented and is still planning to implement several initiatives to ensure aid effectiveness as per OECD guidelines. These guidelines are based on mutual responsibility between the Government of Bangladesh and its development partners, and can be, therefore, instrumental for aid effectiveness. Bangladesh has reformed some mechanisms for better aid coordination and to promote country ownership, alignment, transparency and a results-based framework for effective aid utilisation as per the national interests. The OECD is working to develop a multi-stakeholder global partnership for development by ensuring mutual responsibilities and accountability of all the stakeholders. Bangladesh is still to achieve expected outcomes in aid effectiveness and must face several challenges in this regard which are mostly associated with conventional systematic weaknesses. Bangladesh needs to continue its aid effectiveness efforts to achieve desired success in this area. Nonetheless, some of the initiatives in Bangladesh are very new and it will take time to evaluate the outcomes of these new principles and measures on aid effectiveness.

CHAPTER 7: THE AID-GROWTH DEBATE IN BANGLADESH: A REFLECTION

The impact of foreign aid on economic growth and development has been an issue of much controversy.³⁶³ Most of the recent studies on the aid-growth relationship find a positive impact of aid on economic growth and development in the recipient countries, though the sound macroeconomic policy framework has been the precondition for aid effectiveness.³⁶⁴ Bangladesh has depended on foreign aid since its independence in 1971 to meet deficits in development financing. Even though Bangladesh has been becoming less aid-dependent in terms of the aid-to-GDP ratio, it still mobilises a substantial portion of its development budget from foreign aid.³⁶⁵ Over time, there have been several changes in the aid utilisation modalities in Bangladesh. Currently, it mobilises foreign aid mostly in forms of loan and as project aid, investing that aid in development projects in the productive public sector.³⁶⁶ Still, the impact of aid utilisation on development is debatable in Bangladesh both from socioeconomic and institutional perspectives.³⁶⁷ This study is an attempt to weigh the overall contribution of foreign aid to the socioeconomic and institutional development of Bangladesh. At the outset of this paper, I discussed the potential of the alternatives to foreign aid for development financing in Bangladesh. Then I examined the impact of aid in the form of public investment on the determinants of economic growth and development by classifying them into four categories, with these being macroeconomic variables, human and social development, institutional capacity building, and environmental and disaster management. I have compared the impact of aid on these determinants as found in aid-growth literature with the actual context in Bangladesh by using several secondary data sources. In addition, I have analysed the impediments for aid utilisation and the current macroeconomic framework along with its weaknesses for aid effectiveness in Bangladesh.

This study argues that the alternative options for development financing in Bangladesh such as internal revenue, exports and trade, FDI, domestic public debt, and remittance have significant potential for public investment. However, due to a lack of appropriate policy environment and efficient institutional frameworks, these alternatives are not sufficiently feasible to reduce dependency on foreign aid currently. Therefore, foreign aid is an essential part of development financing in Bangladesh.³⁶⁸ I have found that investment with aid positively impacts on the macroeconomic determinants such as macroeconomic conditions, trade, FDI and internal revenue generation, whereas aid has no considerable relationship with domestic savings. Aid positively influences the management of some macroeconomic conditions such as the inflation rate, public consumption, the balance of payments and the level of external debt but aid impacts little on the real exchange rate.

³⁶³ Gulrajani, 'Transcending the Great Foreign Aid Debate', pp. 199-200.

³⁶⁴ Gulrajani, 'Dilemmas in Donor Design', pp. 152-154.

³⁶⁵ Quibria and Ahmad, pp. 2-7.

³⁶⁶ Economic Relations Division, *Flow of External Resources into Bangladesh*, pp. 10-15.

³⁶⁷ Hossain, 'The Effect of Foreign Aid on the Economic Growth of Bangladesh', pp. 103-104.

³⁶⁸ Hossain, 'Nexus between Foreign Aid and Economic Growth', pp. 59-60.

Development aid is successful in human and social development approaches and MDG achievement by promoting education, health, skills development, gender equality, poverty reduction, social protection and social justice.³⁶⁹ Foreign aid has some positive but slow progress on the capacity building of the political and administrative institutions of the government. The aided approaches in Bangladesh are effective for environmental management, mitigation of climate change impacts and disaster management. Therefore, foreign aid in Bangladesh has a significant positive contribution to economic growth and development through capital accumulation and public investment in the macroeconomic sectors, human development and social development approaches, institutional capacity building programs, and environmental management. Despite noting the positive impact of aid, the quality implementation of the aided projects and maximising the benefits of aid utilisation in Bangladesh is hampered by traditional impediments in development discourse.

The internal deficiencies within the Bangladesh institutional system and the donors' rigid operational procedures are collectively challenging for aid effectiveness in Bangladesh.³⁷⁰ The political, economic, administrative, regulatory and legislative authorities in Bangladesh have less capacity to design, implement and monitor their responsibilities as per expectation. The immature democracy, corruption, politicisation of civil bureaucracy and political violence and uncertainties are responsible for the inefficient management system.³⁷¹ Foreign aid is projected to entail growth and development accompanied by institutional improvement but the deficiencies within the Bangladesh institutional system create a vicious cycle that hinders aid effectiveness in making constructive changes.³⁷² The notion that aid returns can be maximised by removing these impediments puts forward transformative actions to ensure aid effectiveness on occasion. Before 2005, the aid effectiveness measures were mostly donor-driven reform programs such as the implementation of SAPs and PRSPs. These donor-guided reform programs have not been very effective for Bangladesh because of inflexible aid conditionality, lack of country ownership and deficiencies within the Bangladesh institutional system.³⁷³ The OECD guiding principles commenced from 2005 for aid effectiveness are focused on a global multi-stakeholder partnership for development effectiveness. The donors are expected to ensure aid harmonisation and aid alignment to the national priority of Bangladesh, whereas Bangladesh needs to ensure country ownership over the development discourse. Bangladesh started executing the OECD aid effectiveness measures in 2005 but could not achieve notable progress between 2005 and 2010.³⁷⁴ Bangladesh is presently trying to alleviate the aid effectiveness framework through different policies and programs.

Bangladesh has been working both at the local and global levels to ensure aid effectiveness based on the global partnership for development effectiveness. At the global level, Bangladesh is actively

³⁶⁹ Mahmud *et al.*, pp. 15-20; The Planning Commission of Bangladesh, *Seventh Five Year Plan*, pp. 24-25.

³⁷⁰ Parnini, pp. 557-560.

³⁷¹ Ahmed and Pulok, pp. 81-82.

³⁷² Ahmed and Pulok, pp. 81-82.

³⁷³ Waheduzzaman, pp. 474-476.

³⁷⁴ Organisation for Economic Co-operation and Development (OECD), *Bangladesh*, pp. 1-5,

participating in the OECD platforms such as GPEDC, IATI and so on that are working on the aid effectiveness across the world. At the national level, it organises several consultation sessions like the LCG and the BDF to come up with appropriate procedures to ensure aid effectiveness. I argue that Bangladesh has benefited from aid utilisation and that the Government of Bangladesh has demonstrated its willingness to work on aid effectiveness to maximise the benefits of aid.³⁷⁵ It has launched some reform and capacity-building programs, and policies to reshape the aid coordination and management system. However, it is still struggling to make these efforts fully effective because it is difficult to remove the challenges and impediments of aid utilisation that have accumulated over the years in Bangladesh. From a self-reliant economy perspective, it would have been better for Bangladesh if it could increase its domestic revenue generation and export earnings to meet the deficit budget and gradually decrease its dependence on external debt such as foreign aid.³⁷⁶ However, considering the huge development requirements on the one hand and the limitations of the alternative sources for financing on the other, it is assumed that Bangladesh needs to mobilise foreign aid in the upcoming years too.³⁷⁷ Nonetheless, some more issues such as the changing modalities in aid utilisation in the Post-Aid world after the Busan High Level Forum for development effectiveness, the projected role of aid in achieving SDGs for Bangladesh and the potential of the South-South and Triangular cooperation can be explored through further research. The government and the development partners should jointly concentrate on how aid effectiveness can better be ensured and how the benefits of aid utilisation can be maximised.

The donors need to engage in a development partnership, align their aid flow with the national requirements of Bangladesh, promote aid harmonisation among themselves and ensure mutual accountability in the development partnership.³⁷⁸ Donors should consider aid as a financing alternative, allow the Government of Bangladesh to invest the aid money on its own and perform the roles of the development partners. The Government of Bangladesh must be given the driving seat to steer its own development paradigm.

Bangladesh needs to formulate all policies and programs based on its own procedural necessities and actual national requirements. It must have full ownership over the reform measures for aid management and coordination. Bangladesh should design its development projects considering its actual needs as well as the socioeconomic and political context, not based on the availability of aid flow.³⁷⁹ It needs to pursue and negotiate with the development partners to align and harmonise aid flow with the national interests. The institutional competence in terms of planning, implementation and monitoring of development projects needs to be strengthened at the development ministry level. As the central aid coordination and management agency, the ERD must be given appropriate

³⁷⁵ Hossain, 'Nexus between Foreign Aid and Economic Growth', pp. 59-60.

³⁷⁶ Sahoo and Dash, pp. 388-390; Islam, 'Foreign Assistance and Development in Bangladesh', pp. 228-229.

³⁷⁷ Hossain, 'Nexus between Foreign Aid and Economic Growth', pp. 59-60.

³⁷⁸ Blampied, pp. 2-5.

³⁷⁹ Quibria and Ahmad, pp. 30-31.

regulatory authority to oversee the pros and cons of the aided development projects.³⁸⁰ The ERD also should play a more proactive role in maintaining functional communication both at the global and local level to ensure mutual accountability. In addition, political commitments, a results-based framework, transparency and accountability, and stakeholders' empowerment are also the prerequisites for the government to ensure aid effectiveness. Though foreign aid has had a positive impact on the socioeconomic development of Bangladesh so far, it cannot enjoy the maximum benefits of aid unless it successfully meets the necessary requirements of aid effectiveness. Bangladesh has already started implementing several capacity-building programs to promote country ownership over the development discourse, transparency and mutual accountability, institutional improvement, public fiscal management and results-based framework.³⁸¹ These approaches have mostly been launched after the Busan High Level Forum and are, thus, relatively new. These measures must face the conventional systematic impediments and Bangladesh has far to go to make foreign aid fully effective and maximise its benefits from aid. Assessing the contribution of aid to economic growth and development in Bangladesh is an ongoing process. There is much more to investigate and to know about aid effectiveness in Bangladesh. This study can be useful in opening the doors for further research on the aid-growth debate in Bangladesh.

³⁸⁰ Rahaman and Khan, 'The Realities of Aid Harmonisation and Aid Effectiveness', pp. 118-120.

³⁸¹ Dristy, pp. 24-26.

APPENDIX

Appendix 1: Socioeconomic and Political Statistics of Bangladesh

General Geographical Location/Characteristics			
Official Name	: The People's Republic of Bangladesh		
Location	: 200 34' & 260 38' North Latitude 880 01' & 920 41' East Longitude		
Continent	: Asia		
Sub-continent	: South Asia		
Area (Sq. Km)	: 147,570		
Boundary	: North: India West: India South: Bay of Bengal East: India and Myanmar		
Standard Time	: GMT+6 Hours		
Major Religion	: Islam (88%), Hinduism, Buddhism, Christianity and Tribal Beliefs.		
State Language	: Bangla.		
Capital	: Dhaka		
Nationality	: Bangladeshi		
Currency	: Taka (TK/BDT)		
Government and Administration			
Government	: Republic, Parliamentary system, Unitary state, Parliamentary republic		
Formation	: 17 April 1971 (1st Government)		
Parliament	: Jatiya Sangsad		
General Elections	: 10 th (January 2014), 9 th (December 2008)		
Ruling Party	: Bangladesh Awami League (from 29 December 2008)		
Other major political parties	: Bangladesh Nationalist Party (BNP), Jatiya Party (JP).		
Administrative Units			
Central	: 58 Ministries,		
Local	: 8 Divisions, 64 Districts.		
Population Statistics			
Population (In Million)		Crude Birth Rate (Per 1000 Population), 2015	: 18.8
Population Census 2001	: 130.0	Crude Death Rate (Per 1000 Population), 2015	: 5.1
Population Census 2011	: 151.7	Infant Mortality Rate (Per Thousand Live Birth),	: 29
2015 (Estimated)	: 158.9	(Below 1 Year of Age), 2015	
Population Growth Rate (Percentage), 2015	: 1.37	Total Fertility Rate Per Women (15-49), 2015	: 2.10
Male-Female Ratio, 2015	: 100.3	Contraceptive Prevalence Rate (%), 2015	: 62.1
Population Density/Sq. Km., 2015	: 1077	Mean Age (yrs.) at First Marriage, 2015	
Life Expectancy (yrs.),	: 2015	Male	: 25.3
Both Sex	: 70.9	Female	: 18.4
Male	: 69.4		
Female	: 72.0		

Health, Social Services and Education

Persons Per Bed in Govt. Hospitals, 2013-14	: 1,652	Literacy Rate of Population 7 +yrs. (%), 2015	: 63.6
		Male	: 65.6
Persons Per Registered Physician, 2014	: 2,039	Female	: 61.6
Improved Drinking Water Coverage (%), 2015 (tube-well)	: 97.9		
Improved Sanitation facility (%), 2015	: 73.5		

Rate (%) of Poverty Based on Report on Household Income & Expenditure Survey (HIES)- 2016 [Based on Cost of Basic Needs (CBN) Method]

Using upper poverty line

National	: 24.3
Rural	: 26.4
Urban	: 18.9

Using lower Poverty line

National	: 12.9
Rural	: 14.9
Urban	: 7.6

Human Development Index of Bangladesh

Year	Life expectancy at birth	Expected years of schooling	Mean years of schooling	GNI per capita (2011 PPP\$)	HDI value	HDI Position (World)
1990	58.4	5.7	2.8	1286	0.386	122
1995	61.9	6.6	3.3	1435	0.423	120
2000	65.3	7.5	4.1	1679	0.468	126
2005	68.0	8.4	4.5	2036	0.506	133
2010	70.1	9.4	4.9	2652	0.545	143
2011	70.5	9.9	5.1	2784	0.557	141
2012	70.8	10.0	5.2	2943	0.565	143
2013	71.2	10.0	5.2	3071	0.570	142
2014	71.6	10.2	5.2	3179	0.575	142
2015	72.0	10.2	5.2	3341	0.579	139

Labour Force and Employment

Labour Force Survey, 2015-16

Total Labour Force (15 +yrs.), (million)	: 6.21	Percentage of Total Labour Force by Broad Sectors	
Male	: 4.31	Agriculture Sector	: 42.7
Female	: 1.91	Non Agriculture Sector	: 57.3
Unemployment, total (% of total labor force)	: 4.427 (The World Bank 2015)		

Statistics on Financial Institutions (June, 2017)

Financial Institutions

Total Number of Commercial Banks	: 57
State Owned Bank	: 6
Specialised Bank	: 2
Local Private Bank	: 40
Foreign Bank	: 9
Non-Bank Financial Institution	: 34

Capital Markets (Share Price Index)

Dhaka Stock Exchange (DSE) Broad Index (Base=100)	: 5656
Chittagong Stock Exchange (CSE) (Base=1000)	: 15580

Sources:

Bangladesh Bank (2018), Bangladesh Bureau of Statistics (2017), Finance Division (2017), The World Bank (2018) and United Nations Development Programme (2016).

Appendix 2: Selected Macroeconomic Indicators

(Amounts in US\$ billion)

Indicator	Figures/Amounts			% of GDP		
	2007-08	2011-12	2015-16	2007-08	2011-12	2015-16
Gross Domestic Product (GDP)				-	-	-
At current price	91.64	133.40	221.42	-	-	-
At constant price	79.80	87.04	112.89	-	-	-
Growth rate of GDP at constant price (%)	6.01	6.52	7.11	-	-	-
Per capita GDP(US\$) at current price	559	880	1385	-	-	-
Population (million)	142.4	151.6	159.9	-	-	-
Consumption						
Total	74.06	105.09	166.12	80.8	78.8	75.0
Public	4.74	6.723	13.05	5.2	5.0	5.9
Private	69.32	98.365	153.07	75.6	73.7	69.1
Savings						
Domestic	17.64	28.31	55.31	19.3	21.2	25.0
National	25.52	39.83	68.13	27.9	29.9	30.8
Investment						
Total	24.01	37.70	65.66	26.2	28.3	29.7
Public	4.12	7.69	15.76	4.5	5.8	6.7
Private	19.89	30.01	50.90	21.7	22.5	23.0
Total Revenue	8.83	14.4	21.9	9.6	10.9	10.2
Tax Revenue	7.00	12.04	19.40	7.6	9.1	9.0
Total Expenditure	13.65	19.07	29.13	14.9	15.3	15.3
Revenue Expenditure	10.37	14.11	20.41	11.3	11.4	10.0
Development Expenditure	3.28	4.96	8.72	3.6	3.9	5.3
Budget Balance	-4.82	-5.86	-11.13	-5.3	-4.4	-5.0
Financing	4.82	5.86	11.13	5.3	4.4	5.0
Net Foreign Finance	1.29	1.50	3.19	1.4	1.1	1.4
Domestic Financing	3.53	4.36	7.94	3.9	3.3	3.6
Aid Disbursement	2.06	2.12	3.54	2.2	1.6	1.6
Outstanding External Debt	21.29	23.54	29.19	23.2	17.7	13.2
Imports	21.63	35.52	42.92	23.6	26.6	19.4
Exports	14.11	24.30	34.26	15.4	18.2	15.5
Trade Balance	-7.52	-11.22	-8.66	-8.2	-8.4	-3.9
Current Account Balance	0.68	-0.44	47.35	0.7	-0.3	21.4
Foreign Exchange Reserve	6.15	10.36	30.18	6.7	7.8	13.6
Net Foreign assets	5.51	9.96	29.79	6.0	7.5	13.5
Broad Money Supply	36.27	65.37	117.1	39.6	49.0	52.9
Inflation (%)	12.3	8.69	5.9	-	-	-
Remittance	7.92	12.73	14.72	8.6	9.5	6.6
BDT Exchange Rate per US\$	68.60	79.10	78.26	-	-	-

Sources:

Bangladesh Bank (2018), Bangladesh Bureau of Statistics (2017), Economic Relations Division (2016) and Finance Division (2017).

Appendix 3: Sectoral Share of GDP (%) and Growth Rate at Constant Prices (Base Year: FY 2005-06)

Sector	Sectoral Share of GDP (%)			Growth Rate		
	2007-08	2011-12	2015-16	2007-08	2011-12	2015-16
Agriculture and Forestry	14.89	13.70	11.70	3.87	2.41	1.79
Fishing	3.79	3.68	3.65	7.00	5.32	6.11
Mining and Quarrying	1.54	1.61	1.77	7.67	6.93	12.84
Manufacturing	16.88	18.28	21.01	7.33	9.96	11.69
Electricity, Gas and Water Supply	1.21	1.41	1.50	7.75	10.58	13.33
Construction	6.50	6.78	7.26	5.99	8.42	8.56
Wholesale and Retail Trade	13.96	14.02	13.98	7.27	6.70	6.50
Hotel and Restaurants	0.74	0.74	0.75	5.69	6.39	6.98
Transport, Storage and Communication	10.61	11.49	11.31	8.26	9.15	6.08
Financial Intermediations	3.03	3.21	3.39	3.92	14.76	7.74
Real Estate, Renting and Business Activities	7.87	7.22	6.64	3.79	3.92	4.47
Public Administration and Defense	3.14	3.35	3.63	6.51	7.53	11.43
Education	2.24	2.23	2.39	7.14	7.75	11.71
Health and Social Works	1.99	1.90	1.84	5.87	3.81	7.54
Community, Social and Personal Services	11.61	10.38	9.18	3.19	3.25	3.30
GDP and Growth Rate	100.00	100.00	100.00	6.01	6.52	7.11

Sources:

Bangladesh Bureau of Statistics (2017) and Finance Division (2017).

Appendix 4: Value of Exports and Imports by Major Commodities

Exports:

(Amounts showed in US\$ million)

Commodity	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16
a) Primary Commodities									
1. Raw jute	165	148	196	357	266	230	126	112	173
2. Tea	15	12	6	3	3	2	4	3	2
3. Frozen food	534	455	445	625	598	544	638	568	536
4. Agricultural products	120	147	184	262	304	351	402	339	308
5. Other primary commodities	154	108	53	69	96	183	209	244	286
Total Primary Commodities (1-5)	988	870	884	1316	1267	1310	1379	1266	1305
b) Manufactured Goods									
6. Jute goods	318	269	540	758	701	801	699	757	747
7. Leather	284	177	226	298	330	400	506	398	278
8. Naphtha, furnace oil and bitumen	185	142	301	261	275	314	162	78	297
9. Readymade garments	5167	5919	6013	8432	9603	11040	12442	13065	14739
10. Knitwear	5533	6429	6483	9482	9486	10476	12050	12427	13355
11. Chemical products	216	280	103	105	103	93	93	112	124
12. Shoe	170	187	204	298	336	419	172	189	219
13. Handicrafts	5	6	4	4	5	6	8	9	10
14. Engineering products	220	189	311	310	376	368	367	447	510
15. Other mfg. products	1025	1096	1135	1664	1820	1800	2309	2461	2673
Total Manufactured Goods (6-15)	13123	14695	15321	21612	23035	25717	28808	29943	32952
Grand Total (a+b)	14111	15565	16205	22928	24302	27027	30187	31209	34257
Annual change (%)	15.87	10.31	4.11	41.49	5.99	11.21	11.69	3.39	9.77

Imports

(Amounts showed in US\$ million)

Commodity	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14	2014-15	2015-16
a) Major primary goods	3455	2916	2940	5626	4148	4075	5349	4477	4206
Rice	874	239	75	830	288	30	348	508	112
Wheat	537	643	761	1081	613	696	1126	983	945
Oilseeds	136	159	130	103	177	242	524	374	532
Crude petroleum	695	584	535	923	987	1102	929	316	384
Raw cotton	1213	1291	1439	2689	2083	2005	2422	2296	2233
b) Major intermediate goods	4844	5035	4957	7511	9263	8529	9475	7906	8506
Edible oil	1006	865	1050	1067	1644	1402	1766	924	1436
Petroleum products	2058	1997	2021	3186	3922	3642	4070	2076	2256
Fertilizer	632	955	717	1241	1381	1188	1026	1339	1112
Clinker	347	314	333	446	504	487	615	638	571
Staple fiber	110	112	118	180	428	454	492	1078	1172
Yarn	691	792	718	1391	1384	1356	1506	1851	1959
c) Capital machinery	1664	1420	1595	2325	2005	1835	2288	3321	3399
d) Other goods	11666	13136	14246	18196	20099	19645	23563	25000	26810
Total imports (a+b+c+d)	21629	22507	23738	33658	35516	34084	40675	40704	42921
Annual change (%)	26.1	4.1	5.5	41.8	5.5	-4.0	19.3	0.1	5.4

Source:

Bangladesh Bank (2018) and Finance Division (2017).

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