HIGH-LEVEL SUMMARY TECHNICAL ASSISTANCE REPORT

BANGLADESH

Disaster Risk Financing

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The *High-Level Summary Technical Assistance Report* series provides high-level summaries of the assistance provided to IMF capacity development recipients, describing the high-level objectives, findings, and recommendations.

ABSTRACT: Disasters have posed significant economic costs to Bangladesh, and financing needs associated with disaster response are estimated to be substantial. Bangladesh has put in place fiscal mechanisms, social protection programs, and financial instruments to respond to natural disasters. While the country has adequate resources for recurrent disasters, financing gap for moderate and severe disasters remains large. The government could strengthen fiscal policy mechanisms to help close the financing gap and make social programs more shock-responsive and scalable in times of disaster. Bangladesh could also better leverage financial sector instruments to enhance disaster resilience.

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Background

This technical assistance conducts an assessment associated with disaster risk financing needs and necessary policy and institutional changes and develops the main analytical building blocks of a national disaster risk financing strategy under preparation by the authorities. The policy assessment covers fiscal policy response to disaster risks, shock-responsive social protection, financial sector instruments, and institutional framework relevant for disaster risk financing.

Main Messages and Recommendations

Disasters have posed significant economic costs to Bangladesh. The country is highly exposed to disasters, particularly floods and tropical cyclones. Between 2000-2023, natural hazards affected 130 million people and caused US$13.6 billion in total damage. Disasters are impediments to Bangladesh's poverty reduction and development objectives, while climate change is expected to make extreme events more severe and frequent. Disasters in Bangladesh have profound economic impacts, affecting agriculture by destroying crops and fisheries, disrupting industries, damaging infrastructure like roads and buildings, and leading to loss of lives and displacement of people. The country's low-lying delta region makes it particularly vulnerable to these disasters, requiring significant resources for recovery and rebuilding efforts.

Bangladesh's financing needs for disaster response are substantial. The total funding need in response to a recurrent event that occurs once every 2 years is estimated at US$4.7 billion, about 1 percent of annual Gross Domestic Product (GDP). This comprises immediate response and early recovery efforts (including food, shelter, health, and income recovery support) for floods and cyclones of US$1.2 billion and medium-term costs for rehabilitation and reconstruction of US$3.5 billion. The total resource requirements are expected to increase significantly for more severe natural disasters such as those that occur once in 50 years—the needs would amount to US$20 billion (about 4 percent of annual GDP) and are comparable in magnitudes to the 2004 floods and the 2007 Cyclone Sidr in terms of the share of GDP. In this scenario, the short-term needs for relief and early recovery is estimated at US$5 billion and the needs for medium-term reconstruction at US$15 billion.

Bangladesh has put in place fiscal mechanisms, social protection programs, and financial instruments to respond to natural disasters. With the policy mechanisms that are already in place, a total of approximately US$1.5 billion can be mobilized for the immediate response and early recovery phase of disaster response. The government's fiscal instruments consist of the annual budget allocation to disaster relief efforts and the general budget contingency for unexpected events. With respect to social programs, the government has relief-focused social safety nets and a contingency fund to channel relief assistance to vulnerable households. In addition, financial sector's resources can be mobilized through a number of channels including social services financing from micro-finance institutions, the climate risk fund which banks in Bangladesh may establish as part of the central bank's Corporate Social Responsibility initiative, as well as the disaster recovery loans to affected households extended by the Palli Karma-Sahayak Foundation. For the mid-term rehabilitation and reconstruction, it is estimated that US$3.2 billion can be mobilized post disaster through the Annual Development Programme for capital investments.

While Bangladesh has adequate resources for recurrent natural hazards, the financing gap in response to moderate and severe disasters remains large. The government has initiated the process of developing a disaster risk layering approach consisting of multiple financial instruments to finance disaster response for small, to moderate, to large disasters, in alignment with international best practice. Under the status quo, the financial resources available to the government can fully finance response costs and the majority of reconstruction costs up to the disaster event which is expected to occur every other year. However, for moderate disasters such as those occurring every three to five years, the government faces a financing gap. For a one-in-five-year disaster event (with a 20 percent chance of occurrence in a year), the financing gap for immediate relief and early recovery is US$0.9 billion (0.2 percent of GDP), and the mid-term reconstruction financing gap is US$4 billion (nearly 1 percent of GDP). For catastrophic disaster events, the financing gap increases significantly—a one-in-fifty-year disaster event leads to a short-term financing gap of US$3.5 billion (0.8 percent of GDP), and the reconstruction financing gap of US$11.8 billion (2.6 percent of GDP).

Fiscal policy mechanisms can be strengthened to help close the financing gap. Bangladesh's current fiscal buffers—fiscal space available to cover unexpected expenditure increases—are at the level that is sufficient to meet the needs of the annual average cost of immediate disaster response and relief. Strengthening fiscal buffers will support closing the short-term financing gap for moderate disasters, while putting in place contingent lines of credit would help create fiscal space for more severe disasters. In addition, Bangladesh could consider insurance of public assets, including critical public infrastructure and large assets under public-private partnerships, to control fiscal risks associated with natural disasters. The government could also integrate disaster risk financing need considerations in its medium-term budget framework and conduct a public expenditure review of disaster related expenditures to reveal the true fiscal cost of natural disasters in Bangladesh.

Making social programs more shock-responsive and scalable is crucial in the times of disaster. Utilizing already established social protection systems can be a key element to protecting livelihoods, ensuring food security and improving resilience. The government has widely recognized the social protection systems' responsibility to deliver shock-responsive relief and mainstream adaptive social protection across strategies. In Financial Year 2022-23, Bangladesh spent about 2.7 percent of GDP on social assistance, with only around 3.4 percent of this being allocated to relief programs. The government has a dedicated budget line for dealing with economic and natural shocks that can provide support to victims of natural calamities. This budget item doubles the size of the social safety net budget that can be allocated for relief and provides flexible resources to scale up programs when disasters occur. Also, Bangladesh is a large recipient of humanitarian aid, which can play an important role in disaster response. However, humanitarian financing can be uncertain. Looking forward, the government should identify scalable programs for relief support and could establish a harmonized database that can be used to rapidly scale up and identify beneficiaries during times of disaster, based on multi-hazard vulnerability maps. Digitalization of cash transfer and consolidation of cash support programs could help improve the efficiency of relief delivery.

Bangladesh could better leverage the financial sector instruments to enhance disaster resilience. The financial sector, including private actors, has a major role to play in disaster risk financing. Bangladesh's efforts to strengthen financial inclusion offers opportunities to enhance private sector resilience, while the central bank emphasizes risk management of financial institutions and use of innovative products in under-served sectors. The central bank promotes the establishment of climate risk fund to support post-disaster response and recovery as part of corporate social responsibility, and operates nation-wide partial credit guarantee schemes for the cottage, micro, small and medium-size enterprises sector and other vulnerable groups. Bangladesh has an extensive network of micro-finance institutions, which foster financial resilience against disaster shocks. The non-life insurance market is fragmented with limited penetration, though efforts are ongoing to strengthen demand- and supply- side enablers including an introduction of compulsory insurance for public and private high-rise buildings and pilot testing of promising index-based agriculture insurance schemes. Looking ahead, the government should develop alternative channels to encourage disaster-related insurance, insurance linked loans and post-disaster credit access to different segments of population. To encourage greater financial sector engagement, the government should better-target needs-based support to the most vulnerable, while scaling down broad-based post-disaster support and strengthen the capacity of the domestic insurance sector.

Bangladesh has a robust foundation of legal and institutional framework to support disaster risk financing. Roles and responsibilities regarding disaster risk management are clearly defined in the country's 2019 Standing Order on Disasters. However, the country would benefit from mainstreaming the national disaster risk financing strategy into the National Plan for Disaster Management and the five-year national development plan. The government could also develop a comprehensive implementation plan and a monitoring and evaluation framework and establish a timeline for mid-term review and update of the national disaster risk financing strategy.