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HIID/ESEPP PROJECT

A HISTORICAL SURVEY OF SMALL INDUSTRIES IN BANGLADESH

WORKING PAPER NO. 1

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CHAPTER 1

A HISTORICAL SURVEY OF SMALL INDUSTRIES IN BANGLADESH

> "There are ideologies, interests and experience behind existing policies. If policy is to change, it is necessary not only to understand the impact of alternative policy sets but the forces behind each alternative. For that reason studies of the political economy of policy are an essential part of policy change. Such a study would be part of this project." (Project Document, Statement of Work, p.8.).

The small sector of Bangladesh has not received the attention of policy-makers to the same extent as its large sector or as the small sectors in some of the other countries of the Indian subcontinent and East Asian countries have. It was not until the June 1986 Industrial Policy was announced, that small and cottage indsutries were declared a "priority sector" in Bangladesh, even though the importance of this sector has been recognized since the First Five Year Plan of the Pakistan rule. Even the new emphasis on small enterprises has, however, not been accompanied by any coherent strategy or comprehensive small enterprise policy. Almost simultaneously with the announcement of the 1986 industrial policy, the contract for the present Employment/Small Enterprise Policy Analysis (EEPA) Project was signed. The objective of this project is to analyze the direct and indirect effects of national policies on the genesis and growth of small enterprises and derive policy implications for future. With a view to streamlining the setting in which the project research will be carried out, a brief survey of the relevant policies of recent decades as well as existing studies and on-going research projects will be presented.

Bangladesh's policy towards small establishments cannot be properly appraised without viewing it in conjunction with the wholesale nationalization in the wake of the National Independence in 1971 and a continual movement toward liberalization and privatization by successive governments since then. The progress in privatization has been implemented so speedily in the 1980s that Bangladesh has started being acclaimed among donors as a success case in this specific change.

Before taking up the surveys of policies and literature relating to small industries, in the next subsection we summarize general reasons for the recent popularity of small scale enterprises in Bangladesh. The rest of the chapter is divided into two parts. Part A presents a brief survey of changes in national policies bearing on small business. Existing Literature and on-going research studies are summarized in Part B. The discussion of this chapter provides the raw material for the development of the methodology of this project in Chapter 2.

Reasons for the Recent Heightened Interest in Small Sector in Bangladesh

The failure of a quarter century growth since World War II in many developing countries of the world in reducing income inequalities, poverty, and unemployment has had several repercussions. The results of a number of studies in different countries have suggested that the disappointing outcome has, in part, been due to capital intensive investment in large enterprises. An implication derived from these results is that small-size enterprises might be labor-intensive and poverty-reducing. If the productivity levels of small enterprises in the LDCs were not inordinately lower than their larger counterparts, they would naturally be seen as an appropriate sector to promote.

The size and past growth of small industries

Statistics on the size and growth of small and cottage industries in Bangladesh are scanty. The changes in the definitions of these industries over the decades have created additional problems in gauging this sector's progress. The coverages of whatever few surveys and censuses have been taken have been less than satisfactory. Whatever data have been collected are not considered all that trustworthy. With these caveats, the picture that emerges from the available evidence is summarized below.

According to ILO estimates, the manufacturing sector as a whole contributed about 9% to GDP in 1968, which has practically not changed since (ILO, 1986, p.8). The ILO estimates for the overall manufacturing sector reveal a dismal picture of a precipitous fall in labor productivity to about one-third of what it was in the late 1960s (ILO, 1986, p.9). In other sources of statistics, the fall is not that steep, but it has occurred all the same. It provides employment to approximately 7.3 percent of labor force. Of this, large-scale industries

add about 4.8 percent to GDP and provide direct employment to about 1.6 percent of labor force. Small-scale and cottage industries account for above 3.8 percent of GDP and direct employment to about 5 percent of labor force (BSCIC, Oct., 1986, p.3 and World Bank, 1987, p.156). The data from the 1986 economic census (BBS, 1987) indicate that among all nonagricutural permanent establishments, manufacturing establishments account for 28.3 percent of persons engaged, of which 11.5 percent are in establishments with fewer than 20 workers and 16.8 percent in those with 20 workers or more. Within the manufacturing sector, thus, the small sector (thus defined) accounts for only 41% of this sector's workers. The service sector, "wholesale and retail trade, hotels, and restaurants" accounts for 40 percent of total employment, 97 percent of which is in units with fewer than 20 workers and 96.5 percent in fewer than 10 workers. The less-than-20-worker small subsector of the entire nonagricultural permanent-establishment sector provides work to 65 percent of its labor force. Thus, the manufacturing sector probably enjoys significant scale economics, whereas the service sector doesn't. It may also be of interest to note that the female workers form 13% of labor force in manufacturing and only 2% in the service sector. In terms of its size, thus, small establishments remain a viable sector of Bangladesh.

The estimates of growth face serious measurement problems: The definition and the coverage of this sector have changed over time. The data are scanty. For less-than-10 worker establishments, statistics are hardly trustworthy, and only once since 1961 has this sector been surveyed, namely the surveys of small establishments in 1978 and cottage industries in 1980. With these qualifications, the available data indicate that small

and cottage industries proliferated from an index of 100 in 1949, to 168 in 1959, and to an estimated 213 in 1969 (World Bank Report, 1973). Other sources show an increase of combined small and cottage industry units of 38 percent from 1962 to 1978 (BSCIC, 1986). An annual rate of growth of 1.8 percent of enterprises and 2.2 percent of employment is estimated for cottage industries between 1961 and 1980. The annual rates of growth were 2.29 percent in enterprise units and 4.82 percent in employment in aggregate small indsutries and 5.35 percent in units and 7.41 percent in employment in major small industries (accounting for approximately 81 percent of total) during 1961 and 1978 (ILO, Tables 2.1 and 2.2). No such data on growth in output are available. From 1962 to 1980, employment in rural industries grew at an annual rate of 2.9 percent(ILO, 1985). In the 1980s, the small-scale sector continued its modest expansion. Small industries increased from 24005 units and 3,22,126 employees in 1978 to 28304 units (an increase of 18 percent in 7 years) and 379840 employees in 1985, while the corresponding figures for cottage industries are 3,21,743 units and 9,16,806 workers in 1980 and 3,68,064 units (an increase of 14 percent in 5 years) an[illegible] 1048982 workers in 1985 (BSCIC, October 1986, p.3).

According to the World Bank Report (March 10, 1987, Vol.II, Tab[illegible] 6.10), the real wage rate of unskilled labor (1973-74 prices) in the small-[illegible]ale rural industry rose from 100 in 1973-74 to 117 in 1982-83 and 170 in 1985[illegible] against a delcine from 100 in 1973-74 to 99 in 1985-86 for workers o[illegible] the large-scale cotton textile industries, and from 100 in 1973-74 to 72 [illegible] 1982-83 and 71 in 1985-86 in jute textile industries. Agricultural [illegible]age declined by 8 percent during 1974-1982. The real wages of construct[illegible]orkers declined by 7 percent between 1973-74 and 1982-83 and 11 percent be[illegible] 1973-74

and 1985-86. Bangladesh experts seem reluctant to believe that the observed facts reflect an increase in productivity of small rural industries or a wage catching-up process. The presence of over 300 NGOs during the reference period as well as such domestic low-income-family focused programs as the innovative Grameen Bank--whose half a million members have witnessed an estimated near-20 percent annual rate of increase in their real earnings in the 1980s--seem, however, to give some credence to real growth. Another possible reason could lie in the fact that rural industries are private, while the bulk of the other industries are in the public sector. Wages in public enterprises are partly influenced by public wage policy and are less sensitive to market force than are small, rural industry wages. Perennial losses incurred by public enterprises could be a reason for lower nominal wage increases of their workers. Finally, the choice of base year, 1973-74, may be imparting a statistical distortion to the wage indices of large industries, in particular the nationalized ones. Whatever the reasons for the observed spectacularly high improvement in the real wage rate in rural small industries in comparison to other sectors, there is a prima facie evidence for a poor subsector of small enterprises bypassing other sectors. These statistics favor investment in small industries.

Whatever evidence there is, thus, suggests that in non-rural traditional, small undustries, the proliferation in numbers has been accompanied by growth neither in productivity nor real wage rate. The reasons that will be investigated in this project can only be speculated at this introductory stage, namely, lack of access to resources, knowledge, markets, improved technology, and so forth. On the other hand, the small and medium nontraditional export sector--such as ready-made garments, frozen shrimp, and

specialized textile--for which the stated constraints were mitigated and new incentives were given, has grown at a very high rate (though from a low base). For instance, the latter sector's exports in constant US Dollars increased by 140 percent between 1982 and 1987 (projected) as against the corresponding rate of minus six percent for the export of the large industries (World Bank, ibid.). A silver lining has thus appeared in the clouds.

A. The Evolution of Small Business Policy since the Colonial Rule

1. Pre-Independence Period: the colonial status quo more or less continues

During the pre-Independence decades, the importance of small enterprises was recognized but not actively promoted, as will also be seen to be the case during the post-Independence years,
inherited nationalized railways, communications, broadcasting, telegraph and telephone, and defense establishments from the British colonial rule. The Pakistan Industrial Development Corporation (PIDC) was established in 1952, which promoted mainly large-scale industries. It was bifurcated in 1962, when the East Pakistan Industrial Development Corporation (EPIDC) took

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constrained by the implication of the nationalization policy to invest in in small industrial, transport, and some service enterprises, with investment not exceeding Taka 1.5 million (equivalent to US$ 193 thousand). They were specifically excluded from the three major industries of the country, jute, textile, and sugar as well as raw jute export trade and banking and insurance. More specifically, the 1972 Industrial Investment Policy permitted the following role to the private sector:

a) a private enterprise would be allowed to grow up to a size of Tk. 2.5m initially and Tk. 3.5m with reinvested profits
b) there would be a moratorium on nationalization for 10 years for existing units of Tk. 2.5m
c) sick enterprises would be nationalized
d) preference for new enterprises would be given in less developed areas
e) foreign collaboration would be allowed only in public enterprises, where government would retain 51% of the equity. Tea estates are excepted from this restriction. Maximum limit on remittances was £150 p.m. per individual.

It was soon realized that the bureaucratic control and management of industrial enterprises was not a solution to the lack of private entrepreneurs. Whatever entrepreneurial talent existed in the private sector was either strangled or it lost confidence in the security of their investment or seemed to be marking time. In hindsight, the nation was probably not ready for socialism. Those whose enterprises were nationalized resented the policy. Some observers tend to compare Sheikh Mujibur Rahman's Bangladesh

with Allende's Chile--an attempt to impose socialism on an otherwise capitalistic social structure by the erstwhile middle-of-the-road freedom-fighters, without the pre-requisite political content, ideological conviction, public and professional debate, and consensus-building, or the co-operation of the military. The difficulties with the new economic organization became apparent soon after nationalization. Capacity-utilization rate was inordinately low and industrial production remained stagnant. Labor productivity fell. Many of the public enterprises incurred heavy losses in consecutive years, without any prospects of surpluses in the near future. Government efforts to encourage private investment in small enterprises within the socialist framework did not succeed.

The policy of import-substitution, started in the Pakistan years, received further fillip. Nationalization enhanced the already existing monopoly power of firms behind high tariff walls. Modal import duties ranged between 50% to 100%. Although export-promotion policy, which started as the 1980s approached, led to some gradual downward adjustments in import duties, the import-substitution policy continued without significant change for several years. In the 1980s, however, import-substitution policy started a downward trend (see below).

3. The Industrial Investment Policy of 1973: Modest Attempt to woo small entrepreneurs

The industrial policy was revised twice during 1973. It gave somewhat greater scope to private investment. Investment ceiling by private investors was raised to Taka 3.5m. A small tax holiday to private investors was granted, provided 60% of tax-exempt profits were ploughed back. In 1974, the

ceiling on private investment was raised from Taka 3.5m to Taka 30m. Foreign investors were allowed to collaborate with local private entrepreneurs. A moratorium of 15 years on nationalization was announced. The previous ceiling of £150 p.m. on remittances of salary incomes by foreign nationals was raised to £200 p.m.

Unfortunately, the government policy towards private enterprise remained ambivalent. The new concessions could not woo private investors when most of modern industry remained in public sector. But small establishments were not threatened. Neither were they given any incentives. Non-industrial private property-ownership was hardly touched. The combined revenue of the three wealth-based taxes--estate duty, wealth tax, and gift tax--was zero till 1979-80. The trickle that started after that year rose to a pittance 0.0162% of total revenue in 1985-86. The combined income and wealth taxes in 1979-80 were only 8.6% of total revenue. Yet the business family of this project's consultant, Najmul Hossain, sold its second home in Dhanmondi, fearing requisition. Nationalization did not seem to deliver goods.

4. The Industrial Investment Policy of December 1975: Setting the Stage for Mixed Economy

The change was imminent when President Sheikh Mujibur Rahman was assassinated and the socialist government was overthrown by a coup d'etat on August 15, 1975. The new industrial policy introduced the following main changes.

(1) the ceiling on private fixed investment was raised from Taka 30m to Taka 100m (and even that ceiling was abandoned in 1978), implying that the private sector could now enter big business

(2) nationalization was abandoned; the Constitution was amended (in due course) to allow denationalization and divestiture of jute, textile and other enterprises[2]

(3) the number of industries reserved for the public sector was reduced to 8, and 10 sectors were put on the concurrent list

(4) industrial finance bodies were permitted to participate in and provide equity and loan capital to private enterprises

(5) the stock exchange (which was closed in 1972) was reactivated

(6) people were permitted to use concealed funds to purchase divested enterprises without being asked questions

(7) Foreign investors were to enjoy the same treatment as national investors

By June 1982, 375 of the 725 nationalized (mostly abandoned and relatively small) units were divested (sold to public). Thus, while upto 1973 private investors were constrained to invest only in small business, but without any incentives, during the 1975-82 years they were offered to buy hundreds of already established small enterprises with credit and other facilities. At the same time they could also invest in big business. The shift in policy was, however, not pushed vigorously.

5. The New Industrial Policy (NIP), 1982:

A Determined Push to Privatization

The year 1981 and 1982 saw another round of violent changes in Bangladesh Government, including the assassination of a second President, General Ziaur Rahman. The military government that came to power, lost no time in making a major break with the past by speeding up the process of privatization, liberalization, and dispersion of industry. The head of the new government, General H. M. Ershad, came into power in March 1982. The landmark NIP was issued in June, 1982. The policy reflected a rapid acceleration of the process of privatization: a change of strategy from

public-led growth to private-led growth; a slight tilt from import-substitution to export-promotion from restrictions on private investment to investment incentives; from positive to a negative list of imports, supplemented by a restricted list; and from the public ownership (of not only the "commanding heights" but also the surrounding terrains of the economy) to denationalization of public enterprises. As many as 57 enterprises of the premier duo of the Bangladesh manufacturing industry, namely jute and textile industries, were sold to public during 1982-83. Soon after that, a few of the banks were denationalized.

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More than the substantive changes, the shift in policy gave the needed signal to entrepreneurs of the government posture to promote and stabilize free enterprise.

Industries were classified into two lists: (1) the Reserve List, which included arms and defense equipment, atomic energy, air transport, telecommunications, generation and distribution of electricity, and mechanized forest extraction. (2) The Concurrent List, where both public and private investment could take place. All industries outside the Reserve List became open to the private sector. Some of the time-consuming administrative formalities were simplified. Investment process was shortened by initiating a "one-stop-service," relieving investors of the time-consuming task of visiting various offices for obtaining different sanctions, though policy intentions were not really translated into action.

The NIP was implemented speedily. Several experts believe that some of the problems[3] concerning the denationalized industries that have been encountered in the post-NIP period could perhaps have been avoided had its first phase--namely analysis, policy design, and information--been duly carried out. The overwhelming evidence of the inefficiency of Bangladesh's public enterprises and the swelling international environment favoring the change could not obviate the need for the requisite analysis and the data needed for such major policy shifts. At the same time, there is some trade-off between good analysis and speedy implementation. The change [illegible] not bogged down in the [illegible]

prolonged analysis. Military dictatorships usually have the advantage of speedy implementation without serious constraints of socio-political repercussions that democratic governments usually do not have.

The latest situation concerning the balance between the public (invariably large) sector and the private sector (which consists of both large and small enterprises), as of December 1986, has been brought out in the Economic Census 1986 (BBS, 1987, Table 5). According to it, Bangladesh's public sector (including government and semi-government owned enterprises) accounted for 13.7 percent of industrial employment and 8.1 percent of industrial units of all size classes of establishments.

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6. The Industrial Policy of 1986: Incentives galore, Small Industries Declared a Priority Sector

The process of private investment promotion that started in 1975, approached its peak in the Industrial Policy of 1986.[4] The main incentives under this policy are summarized below according to 3 classes: (a) industrial development in general, (b) export promotion, and (c) support to small and cottage industries.

(a) Industry in general

i) Fiscal incentives

(1) To promote industrial development in the country, tax holiday has been allowed to the newly established industries for 5 years for developed areas, 7 years for less developed areas, 9 years for least developed areas, and 12 years for special economic zones.

(2) An assessee is entitled to accelerated depreciation at the rate of 80% of the actual cost of machinery or plant from the year the unit starts commercial production and at 20% for the following year if the industry is set up in a developed area. If the unit is set up in a less developed area,

the depreciation shall be 100%. Depreciation allowance can be carried forward to the next year and so on for succeeding yea.s if the unit sustains losses.

(3) Normal depreciation on machinery and plant is allowed at 15%. In addition to this, an extra allowance up to a minimum of 50% of normal depreciation for double-shift-working and 100% of normal depreciation for triple-shift-working may be allowed in proportion to the number of days during which double or triple shifts are worked.

(4) An investment allowance is allowed at the rate of 20% of the actual cost of the plant and machinery of an industrial undertaking which is entitled to accelerated depreciation in respect of the year in which the industrial undertaking starts commercial production, if the industrial undertaking is set up in a developed area. The investment allowance is allowed at the rate of 25% in place of 20% of the cost of the machinery and plant if the undertaking is set up in a less developed area. Investment allowance is also admissible in respect of inland passenger vessels and fishing trawlers.

(5) The facilities available for setting off of losses and carry forward of losses are also liberal whenever a tax payer sustains any business loss, it is permissible to carry it forward to the following year and set it off against profit in that year.

(6) Exemption from tax on capital gain arising from sale of buildings or lands if such gains are invested in the acquisition of capital asset i.e. land, machinery, plant, furniture etc. of industrial undertaking within a period of 2 years from the date of transfer.

(7) Capital gain arising from transfer of land or building invested towards equity of a new industrial company is exempted from tax.

(8) Capital gain arising out of a process of transformation of a firm into a company is exempted from tax if all capital gains are invested in the equity of the said company.

(9) Dividend or income received by an assessee other than a company is exempted from tax upto Tk 15,000.00 in a year irrespective of whether it is distributed by a public or private company.

(10) Exemption from payment of a tax on royalty, technical know how and technical assistance fee is allowed.

(11) There is relief from double taxation in case of the foreign investors of the countries with whom Bangladesh has agreement to that effect.

(12) Exemption is allowed from taxes on interest accrued on foreign loans under certain conditions provided there is an agreement of avoidance of double taxation with concerned countries.

(13) Certain expenditures, namely, expenditure on foreign travel by the employees and their dependants once every two years, expenditure on the training of individual employee at home or abroad, expenditure on scientific research, etc., are allowed for deduction for the purpose of computation of income, profits, and gains from business liable to tax under the Income Tax Act.

(14) Concessional rates of import duty are allowed at 20% ad-valorem rate (no sales tax) for import of capital machinery for industries to be set up in developed area, 7-1/2% ad-valorem rate (no sales tax) in less developed area, and 2.5% ad-valorem rate (no sales tax) in the least developed areas. Payment of 2.5% import duty on capital machinery is also allowed for export oriented industries (minimum of 70% exports), selected industries using 70% or more indigenous raw materials, and industries set up in BSCIC Estates--irrespective of locations.

(15) For less and least developed areas, 50% of the effective customs duty is allowed for payment in 2 half yearly equal instalments.

(16) A rebate of 25% in excise duty is allowed on the additional production for essential and selective industries if such manufacturing units produce more than 100% of their sanctioned capacity.

(ii) Other Incentives:

(1) The period of repayment of both local and foreign currency loan is 12-15 years depending on the repaying capacity of projects.

(2) The repayment of foreign currency loan starts after 30 months of opening L/C or 18 months after the unit goes into commercial production, whichever is later.

(3) The repayment of local currency loan becomes due after 24 months from the final disbursement or 18 months after the unit goes into production, whichever is later.

(4) Employment of foreign nationals in the enterprises where their services are essentially required is allowed with the approval of the appropriate authority.

(5) Supplier's Credit is allowed on approved terms by the Hard Terms Loan Committee (HTLC) of the Ministry of Finance (Bangladesh Bank).

(6) Pay-As-You-Earn (PAYE) Schemes are approved on merit of the cases.

(7) Facilities of long term credit from DFIs are available.

(8) No limitation on percentage of Bangladesh capital in industry where foreign investment is approved.

(9) Tariff protection is provided to the deserving industries.

(10) Provision of liberal debt-equity ratio exists.

(b) Incentives to exports

(1) Credit facility may be available upto 90% of the value of irrevocable letter of credit from any nationalized commercial banks for export.

(2) Income tax rebate is allowed ranging from 20% to 60% of tax attributable to export sales of nontraditional items.

(3) Exemption is allowed from the tax payable on the income, profits and gains of any industry set up in any Export Processing Zone for a period of 5 years beginning with the month in which commercial production commenced.

(4) Certain exemptions are considered for income tax payable on the salaries of foreign technicians.

(5) State recognition may be available in the form of awards and trophies for successful exporters, particularly of non-traditional items.

(6) Facilities under Export Credit Guarantee Scheme are available.

(7) For export-oriented industries, the rate of interest to be charged by the financing institutions is one percent less than that charged for the other industries located in developed areas.

(8) In deserving cases of export-oriented industries the government allocates cash foreign exchange from time to time for the import of capital machineries.

(9) A system of notional payment of import duty and sales tax for export industries exists.

(10) Promotion of export of non-traditional items is given greater emphasis. Efforts are made not only to discover such new items but also to devise a package program of incentives for the existing ones with a view to expanding efforts.

(c) Incentives to small and cottage industries

As on previous occasions, small industry sector has been redefined to include any industrial undertaking engaged either in manufacturing process or service activity, within a total investment up to Tk 15 million and the investment in machinery and equipment not exceeding Tk 10 million excluding taxes and duties.

(1) The small sector will enjoy a tax holiday for the period of five years, seven years and nine years, if set up in developed areas, less developed areas, and least developed areas, respectively. The period of the holiday will be calculated from the month of the commencement of commercial production.

(2) The rate of import duty on machinery and equipments in less and least developed areas and also in BSCIC Industrial Estates will be 2.5 percent ad valorem and no sales tax will be imposed.

(3) For small and cottage industries, irrespective of debt equity ratio and areas, the rate of interest will be 10 percent.

(4) All income arising from export of handicrafts shall be exempted from income tax.

(5) For the development of small and cottage industries, BSCIC will: organize training for the artisans for skill development as well as for improvement of management technique; conduct continued research and disseminate knowledge for achieving quality and higher productivity; undertake product development and disseminate the knowledge; supply new and improved designs; arrange necessary credit in conjunction with commercial banks; and assist in supply of raw materials and marketing of products.

(6) To assist in solving the marketing problem, emphasis has been given on marketing plans and study. The government will also formulate purchase policy in favour of the SCI sector to ensure marketing of SCI products.

The SCI sector will also enjoy the following special incentives and facilities:

(7) Financial institutions and commercial banks shall have a separate window for financing small and cottage industries;

(8) The financial institutions and banks should set apart a definite percentage of their resources for the development of SCI;

(9) Debt-equity ratio for SCI shall be 80:20 in order to provide support to small entrepreneurs;

(10) A Small Entrepreneur Credit Guarantee Scheme may be introduced under the joint sponsorship of BSCIC and Sadharan Bima Corporation;

(11) Banking system will arrange necessary fund for sick small industries and for supporting sub-contracting.

7. The 1987-88 Budget

An extensive analysis of Trade and Industrialization Policy (TIP) was done in a three-year-long research project by HIID. A number of 3 to 4-digit manufacturing industries were thoroughly analyzed. The policy implications of this research led the HIID experts to recommend significant reduction in (but not elimination of) all tariffs, conversion of quantity restrictions into ad valorem import duties. and a narrowing of the spread of duties on different products. Since the twin purposes of import duties in Bangladesh. namely raising revenue and import substitution, are still valid, a general weighted mean rate of import duties of approximately 30 percent (as against the erstwhile weighted mean of about 50%) was recommended. The World Bank,using the results of the TIP study, added the weight of its conditions, leveraged under an adjustment loan (SAL), to the earlier trend toward trade liberalization.

The 1987-88 budget is consistent with the earlier trend as well as the World Bank's "conditionality." Import duties were reduced on some groups of commodities, the range of rates was narrowed and lowered a bit, and some quantity restrictions were relaxed. In part as an index of the steady progress toward liberalization of trade, the premium that the WES[5] has enjoyed over the official exchange rate has declined over the past 11 years as follows: 31% in 1977-78 to 29%, 24%, 24%, 14%, 1%, 9%, 13%, 10%, 8%, and 7% (July 1987-88). Source: Econ. Trends (Bangladesh Bank, July 1987). On the whole, the highly inward-looking policy of Bangladesh is gradually inclini toward an outward-oriented approach to its growth.

Neither the 1987-88 budget, nor the World Bank, nor the TIP study, however, made any distinction between small and large sectors. A benign neglect of small enterprises or a more or less equal treatment of unequals seems to continue as before.

Future denationalization was to take the form of public limited companies (PLC). In these companies, the government retains 51% of the unit's shares, 34% of them are offered to private subscribers through stock exchange.[6] while the remainder 15% are reserved for workers of the respective unit. The legal arrangement for this form of companies was prepared in an amendment to the 1972 Nationalization Order (PO27) in early 1987. A beginning was thus made, reminiscing the Malaysian NIP Model to some extent, to convert Bangladesh workers into fledgeling capitalists. The modest 1969 profit-sharing scheme had required nothing of the sort (see Appendix 1A).

8. Certain Related Issues

Finally, a brief discussion of a few issues which bear upon small industries in relation to large enterprises and which are of current concern in the country is in order.

8.1 Labor Policy

Bangladesh is lagging behind its historical partners, Pakistan and India, in progress towards social-security/provident-fund schemes, but is ahead of non-Commonwealth countries in

general in trade unionism. A historical survey of labor legislation of Bangladesh is given as Appendix 1A. The methodology of analyzing endogeneous and policy distortions of labor cost, especially in relation to capital, will be presented in Chapter 2.

BEST AVAILABLE

8.2. Price Control Policy

A number of price control are prevalent in Bangladesh. We will particularly take congnizance of price controls of such intermediate inputs as steel, electricity, gas, and fertilizer. A brief introduction to price controls appears in Appendix 1B.

8.3. A tilt from import substitution of the 1970s toward Export Promotion in the 1980s

Starting in the late 1970s, an export-promotion policy was gradually introduced in Bangladesh, alongside the erstwhile import-substitution policy. As we have seen in the 1982 and 1986 Industrial Policy Acts and the 1987-88 budget, export promotion is now being emphasized while import substitution is being slowly reduced in Bangladesh, although it is still the order of the day. In this subsection, we summarize the major instruments of export-promotion policy currently in operation in Bangladesh.

Import protection creates a bias against export as it produces higher levels of value-added for domestic markets as against export markets, unless matched by commensurate export promotion such as subsidy to exports. It may also discriminate among domestic industries as well as among size-classes of industries. If, for example, the share of exports in total supply of cottage industries were higher than the corresponding share of large scale industries, general import protection (substitution) unaccompanied by equivalent export protection (promotion) to cottage products would hurt the growth of cottage industries.

wash out negative protection due to paying the WES rate otherwise. An LC for 60% of imports, when value added is 25%, would yield an effective rate of protection of (-.10 due to WES premium) (.40 of imports) (.75, being the share of material inputs in output) / (value added .25) = (-.10) (.40)(.75)/ (.25) = -12%, i.e., negative protection of 12%.

(5) The EPZ.--Comparable facilities are provided the enterprises located in the Export Processing Zone (EPZ). They can import their inputs duty-free, but can sell only in the export market. In particular the following facilities may be mentioned. Tax holidays for 5 years, regardless of size, o to 10 years for pioneer promoting type of industries (the pioneering status to be determined by the EPZ Authority); rebate of 50% on income tax after the tax holidays; exemption on income tax on the interest on borrowed capital (including interest of off-shore banks payable on foreign currency loans); exemption of income tax on salary of foreign technicians for 3 years; and other facilities, such as one-stop-service provided by the EPZ Authority.

The main gain to Bangladesh from foreign companies located in the EPZ is employment and workers' wage income plus a minor export in compulsory use by these enterprises of locally-made packing material (which according to the information obtained by talking to foreign manufacturers in the EPZ is about 2% of costs). Against these assets must be put the liability involved in EPZ firms using the Bangladesh quota of exports to the United States. In ultimate effect, the role of the EPZ is not materially different from that of customs bonded warehouses.

(6) Investment incentives for exports and location.--A concessional import duty of 2.5% (no sales tax) on enterprises with a minimum of 70% exports instead, for instance, of a concessional import duty of 20% for industries in developed areas with no exports, is allowed on capital

machinery for industries. The same concession is available to industries in least developed areas, the SCI industries in industrial estates, and industries using 70% or more local raw materials.

(7) Concessional interest rates.--Currently, a subsidized interest rate (one percent lower than otherwise) is available for export credit from nationalized commercial banks and other financing institutions upto 90% of export orders, for short periods. For certain purposes, only 10% interest rate is charged. Accordingly, export credit is available at 9%.

(8) Income tax rebate.--The investors in the EPZ and new investors in developed areas enjoy tax holidays of 5 years. Those in less-developed and least-developed areas enjoy tax holidays of 7 and 9 years respectively. For other firms, income tax rebates on profits from exports range from 20% (for 10-20% export shares) to 60% (for 100% export shares) are available.

(9) Other facilities.--The 1986 industrial policy and recent export/import policy orders have introduced a few other measures promoting exports, industrialization in general, the use of domestic raw materials, capacity-utilization, and the location of industries in less-developed areas. These include concessions on capital gains, depreciation, investment, dividends, royalty, foreign travel, fuel prices, and so forth.

8.4 The debt recovery crisis

Bangladesh has escaped the foreign debt crisis in which several Latin and Central American countries have found themselves mired in the 1980s. The country is, however, suffering from a related debt disease, the internal debt recovery crisis, to which both private and public enterprises have contributed.

The Development Finance Institutions (DFIs), have been the instruments for promoting economic development in this country since Independence. They have seldom had good clients. In the 1970s, their clients were public enterprises (PEs), which ran perennial heavy losses. Their debt-equity ratio rose, on the average, to 85:15.[7] As a consequence, they could not meet their debt obligations. In the 1980s, new owners of denationalized industries have proven even worse clients. The DFIs loan recovery rates deteriorated sharply during the 1980s to below 10 percent in 1986. The recovery rates of commercial banks from small industries have ranged between 10 and 12 percent and are currently estimated in the 15-20 percent range. Foreign donors whose money was loaned to these enterprises also got scorched.

The main reason for the low recovery from the PEs has been their heavy deficits. The causes of default by private enterprises have to be sought, in part, in the speed and scale of denationalization, as discussed earlier, without the necessary information collection and analysis. It is learnt that the original owners, whose enterprises were nationalized in 1971-72, were reluctant to repurchase them with the liabilities accumulated by public managements. But did so, it is alleged, under persuasion by the President who wanted the government to get rid of them. Easy availability of credit (debt-equity ratio could legally go up to as high as 92.5:7.5) enabled them to repossess

these enterprises. Then these powerful families with access to higher-ups found pretexts for not meeting their loan obligations by disputing on both the accuracy of DFI's calculations of borrowers' obligations and for debts incurred during the years of public ownership. Finally, the probable reason for the low recovery by nationalized and commercial banks from small-scale industries in the 1980s is simply the contagion spread by the big fish. The crisis goes on.

The Poverty of establishments

Poverty of families and dwelling units in Bangladesh has received much attention. In this subsection, we discuss a few characteristics of the poverty of permanent establishments/institutions, as revealed by the National Economic Census 1986.

Of the 1.478 million permanent nonagricultural establishments of the country, 0.862 million or 58 percent are kutcha, i.e., their structure is not built of bricks or mortar, but mud, thatch, bamboo, rags, or similar material. About 43 percent of even urban establishments consist of kutcha construction. Among dwelling units, 95 percent in rural areas and 66 percent in urban areas are kutcha.

Only 44.7 percent of nonagricultural establishments in the whole country and 75.2 percent in urban areas use electricity or gas. About 24 percent of establishments in the country and 50 percent in urban areas have tubewell/tapwater facilities. Motorized transport is available to mere 0.292 percent of urban establishments and 0.203 percent of urban dwellings.

Large enterprises predominate in manufacturing industries, finance and insurance, and power industries, employing 28 percent, 3.5 percent, and

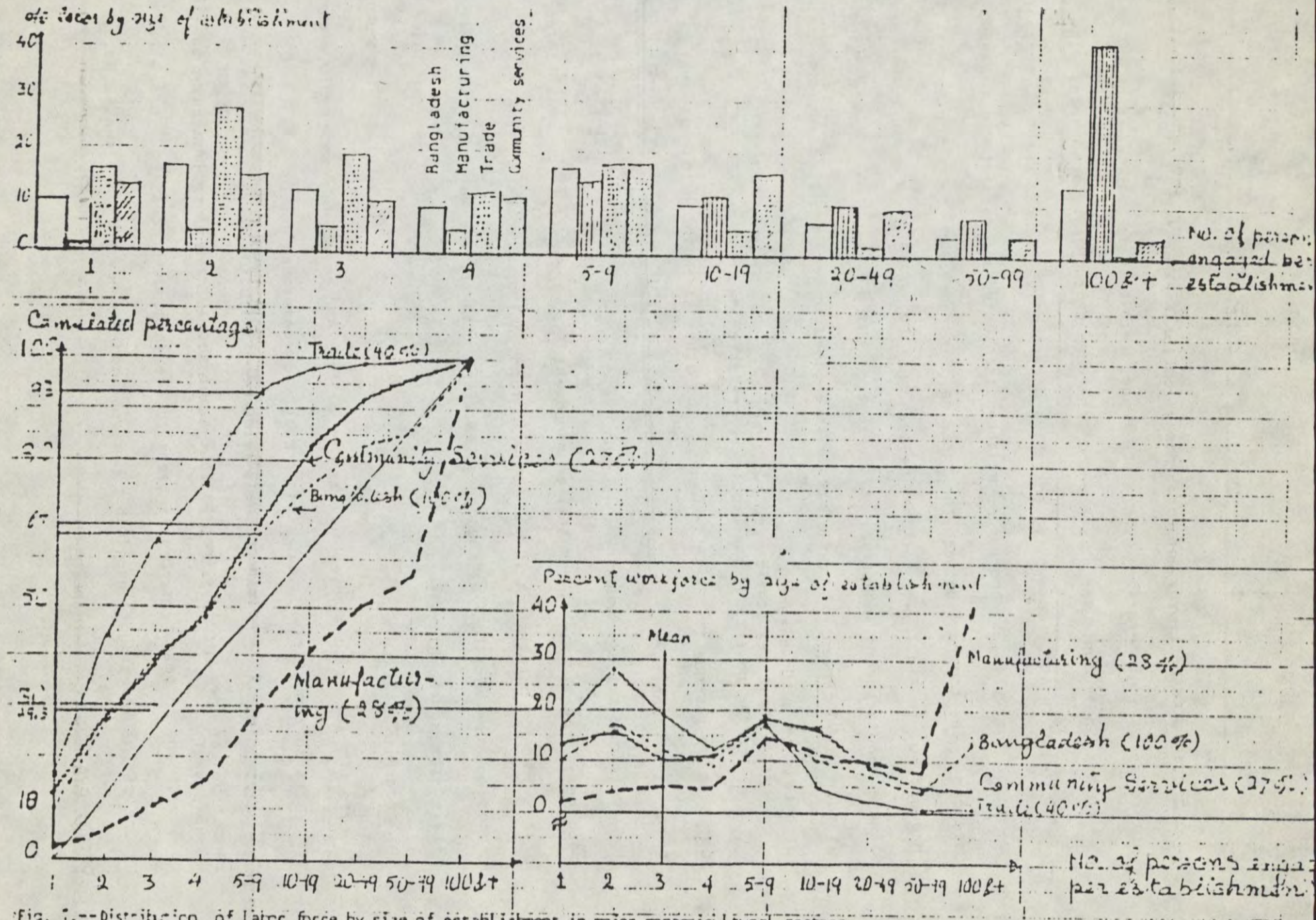

Fig. 7.--Distribution of labor force by size of establishment in major nonagricultural sectors.

Note:- The scale is not uniform. The numbers in parentheses denote percent of total nonagricultural labor force.

Source: Economic Census 1986.

0.5 percent, respectively, of total nonagricultural labor force. Small enterprises conglomerate in "wholesale trade, retail trades, and restaurants," which sector accounts for 40 percent of the non-agricultural work force. The third major sector, "community, social, and personal services," with 27 percent of labor force, is, by and large, equally distributed across small to large sectors. The contrast between the three major nonagricultural sectors is brought out in Fig.1, where it may be seen that 29 percent of the labor force of the manufacturing industries, 67 percent of that of community services, and as much as 93 percent of that of trade is engaged in very small establishments with less than 10 workers.

From these few statistics, two characteristics stand out: One, the poverty of the people is reflected not only by poor dwellings but also by low-quality establishments. The other side of the coin is that the cost of construction ~~for small and cottage industries must be constructed~~ for small and cottage industries must be nominal. Major costs consist of machinery, raw materials, and skilled manpower. Two, the picture of small enterprises in aggregate is not very helpful in formulating policies for their promotion. One must look at subaggregates. For instance, the multiplication of retail stores, the biggest small enterprise of Bangaldesh with 30 percent share in nonagricultural workforce, will hardly increase GNP. The traditional technolog of retail trade is so simple, the entry is so free and easy, and consequently the sector is so competitive, that it is probably overexpanded and overcrowded. Therefore the rate of return to one's resources (including one's own labor) cannot be very remunerative, not to talk about social rate of return. High pay-of to investment in small enterprises seems to lie in goods-processing. This will be one of the investigations of this project when the new economic survey data become available.

9 . Brief assessment of policy changes

As a result of the noted liberalization policy crescendo, particularly since the NIP-1982, Bangladesh has come a long way from the 1970s' control economy to the 1988 free-enterprise economic system: Incentives to private investors and exporters have gradually replaced bureaucratic controls on investment, production, and trade (at least in statutes). Significant progress has taken place in the liberalization of trade. The country has started peeking outward from its erstwhile autarkic inward-looking strategy of economic development. The import-substitution policy, though still quite entrenched, is no longer viewed as a royal road to industrial growth. In addition, numerous export-promotion measures have been put in place.

Incentives have been provided for decentralization of industries and their dispersal to less-and-least-developed areas. Denationalization has reduced the public sector's share of fixed assets in the modern manufacturing sector from 90 percent in 1972 to 40 percent and the number of industrial units from 720 to 160. The stock exchange has been reactivated. Financial and capital markets are functioning in a freer environment: Privatization is being promoted in non-industrial sectors also, for example, marketing of fertilizer

(though progress is slow). All the incentives provided the industry in general apply to small and cottage industries as well. Minor additional incentives, relating mainly to credit availability, were given to small units in the IP-86.

Consistent with the trend towards free enterprise, the planning practice of setting targets for the private sector has been stopped. Instead, the Planning Commission has adopted the French approach of indicative guides to private investors. Investment schedules (lists) are still prepared--for priority industries, industries for foreign investment, and those for the EPZ. But these lists will serve largely as indicators to banks, borrowers, and investors as to where the government planners consider the allocation of resources will be more profitable. The government will not use them as tools of control over private investment.

Despite this shift in policy, the Bangladesh industry is still highly protected. Bureaucratic control is still stifling investment. Whatever evidence is available indicates that the small enterpreneur has still not availed himself of the incentives.

As impressive as the promulgation of a well-thought-out set of instruments of new policies is, the implementation side seems to be weak. Some of the incentives have scarcely been taken advantage of, partly because while they look good on statutes, they have really no substantive operational value. For instance, company income tax rebates in a country in which very little is paid in taxes by individual enterprises may just reflect good intentions. Controlled steel prices and high import duties on the inputs of engineering industries cause a disprotection to small and cottage industries, and have offset much of the fiscal and credit assistance given this sector. Concessionary interest rates and almost duty-free import of machinery cannot

promote labor-using technology nor import-saving exports. The rent-seeking practice facilitated by licensing and similar legislation can hardly be within the reach of the small man or the small enterepreneur. These are speculative inferences. The fact of the matter is that no data have yet been generated to verify the extent to which small enterepreneurs have availed themselves of the parade of incentives and the degree to which investors have responded to various promotional policies. The impact of these incentives remains to be assessed.

This completes the brief survey of industrial policies of the postwar era, particularly since the country's independence in 1971, to identify the place that small industries have occupied or not occupied in the overall process of incentivization. The survey underscores the fact that insofar as statutory facilities are concerned, the small sector has enjoyed, more or less, the same incentives as provided the large sector. Practically, the only differential concession that the small sector has enjoyed in

relation to other sectors is in the form of availability of credit, through the instruments of special window and percentage allotment of credit by banks to small business. That, too, however, came only recently. in June 1986. when the much-acclaimed "top priority" status was assigned this sector, nearly 4 decades after its counterpart across the border in India had started enjoying. Its practical application has still to be seen.

The equal treatment of unequals, small and large sectors, in statutes may have little relationship with the actual situation. For, to what extent a sector can avail of the statutory incentives depends upon its capacity to do so and the complementary inputs it has command over. The capacities and the command over complementary inputs differ disparately between the small fry and the big guy, especially when access to and leverage with bureaucrats is involved. Moreover, some of the results of the expansion of large enterprises due to their avail of incentives may create adverse environment for the growth of small enterprises.

To what extent small, relative to large, enterprises have availed themselves of incentives, and to what consequences, cannot be properly verified until the relevant data become available. Whether or not such data can be generated is being currently debated. as may be seen in Appendix 5A. As a first approximation, therefore, we will use the statutory rates of incentives/disincentives to measure the incidences of various policies by industry, as distinguished from size-classes of industries.

B. A Survey of Existing and On-Going Studies on Small Enterprises

In a recent survey of small enterprises based on research done at the World Bank, Little strikes a pessimistic note about not only the efficiency but also the labor-intensity of small enterprises. The World Bank Studies found "that small firms are not reliably more labor-intensive than their larger counterparts; nor are they consistently more technically efficient in their use of resources" (Little, 1987). Rather than foreclosing further research by considering that the illustrious Oxford professor (one of the best-known consultant economists of LDCs) has said the Last word, however, his conclusion has spurred more research (partly because it is based upon research done for a couple of countries at only one center). Another survey of research done at other centers, for other countries is due. The purpose of this note, however, is a modest one, namely a survey of small-sector studies/projects done or in progress in Bangladesh. Because of the paucity of relevant data and because, as seen in Part A, this sector has not received the promotion in Bangaldesh that its counterparts in the countries covered by Little (India and Colombia) have, this survey cannot, and is not meant to, throw any light on Little's conclusion, which may rather be considered as a hypothesis. A test of it may, however, come in the analysis that will be carried out in this project. The present survey is not even critical. It has a limited purpose. It is essentially an annotated bibliography of the studies done and the data sets generated in this country.

BBR's Small Entrepreneurs Study

An early study on small enterprises and entrepreneurs was done by the Bureau of Business Research (BBR), University of Dhaka (Habibur Rahman, 1979). It was a part of the international collaborative research project on Small Entrepreneurial Development in Asia, sponsored by the Association of Development Research and Training Institute of Asia and the Pacific (ADIPA), and funded by the International Development Research Center (IDRC), Ottawa, Canada. The analysis is based on a survey of 247 operating units in 1977. According to this tudy, 24% of the over six thousand recognized

small industrial units were developed under the sponsorship of BSCIC and Bangladesh Shilpa Bank (BSB). This is, however, not an index of significant public assistance to small industries. The assistance agencies were found to emphasize the increase of numbers more than growth of output, proliferation of enterprises more than entrepreneurs, policy prescription more than implementation, and supporting activities (e.g., long-term finance) to the neglect of stimulatory and sustaining activities (e.g., capacity-utilization and provision of working capital).

A spurt of studies/sample surveys came out in connection with the preparation of the SFYP. At least 4 complementary projects generated large data sets, for the first (and so far the last) time since the early 1960s. Among themselves they almost exhausted the small industrial sector of Bangladesh, namely the handloom industry census for 1978 (Miyan, 1980), rural industries survey for 1981 (BIDS, 1978-81), small industries survey for 1977-78 (BSCIS, 1982), and cottage industries survey for 1980-81 (BSCIS, 1983). They have formed the data bases of several analytical studies since.

The Miyan Study on the handloom industry, 1978

It was a countrywide (except Chittagong Hill Tracts) census of handloom enterprises for 1978. The study found that there were 197,280 handloom units in the country with a total of 437,015 looms, of which only 59% were operative. The rest were idle. The average number of looms per enterprise was estimated at 2.2 and average number of workers perloom 4.3 (of which 42% were hired and 32% were women). The industry produced 347 million yards of cloth per month. The cotton items, sari and lungi, are the two dominant products, accounting for about 80 percent of total output of this industry. A new study on the handloom industry, indeed overall textile industry, is currently in progress under a funding by World Bank at BIDS (Co-ordinator: Prof. Choudhury). The handloom part has almost been completed. The entire study is expected to be ready shortly. One of the preliminary results of Choudhury's study is the high productivity of credit to handloom industry.

The BSCIC surveys on small industries for 1977-78 and cottage industries for 1980-81 and studies based on them

The BSCIC publications consist primarily of the tabulations of data. Information is available on type of product, fixed assets, hired and family workers, value of raw materials, other production costs, and value of output, sales, and services. Small (cottage) industries were defined as privately owned (family-based) manufacturing units with 10 to 19 (not exceeding 19) workers for units using mechanical motive power and 20 or more (maximum of 29) workers in units not using mechanical motive power.

The cottage industries included bidi and sea salt-making units, among other products, but excluded handloom, jamdani, and sericulture industries. The top 7 activities (in terms of units) were found to be tailoring, bamboo and cane products, salt making, fish net making, rice milling, pottery, and wood products. The industry employed about a million workers, and produced a gross value output of about Taka 10b in the survey. As compared to the early 1960s, the growth of relatively more capital-intensive units, e.g., mills, was more pronounced than other units.

The top six activities of the small-industry sector (in terms of numbers of units) were rice mills (51% of all enterprises), bakery, flour mills, light engineering, hosiery, and oil mills. Although the comparisons are not quite conformable, rough evidence in terms of numbers of establishments indicates an annual growth rate, since the early 1960s, of 2.8 percent for small establishments and 2 percent for cottage industries. Thus, though largely left to itself, the SCI sector has not been dormant.[8]

The BIDS studies of rural industries, 1978-81

The comparable data set for rural industries was generated by BIDS during 1978-81 as a part of its Rural Industries Study Project (RISP). This data set has been subjected to an extensive analysis. Its Final Report was published in February, 1981. An entire special issue of The Bangladesh Development Studies was devoted to this study, whose different chapters were summarized in the 7 articles of this issue (Ahmed, ed., 1984).

The survey included both small and cottage industries in rural areas with employment size up to 50 and was done in 11 (out of 465) thanas for a total of 1300 enterprises. It should be of interest to note that the rural cottage industries in 1978-81, in current prices, had capital assets below one hundred takas per worker and produced less than 1000 takas worth of value added per worker. These included: dhenki products; juice gur; shital pati; hogla, bamboo, and coir mats; basketry; bamboo cane, and jute handicrafts; fishing nets and other equipment; reeling yarn; jute and coir ropes; and lime. Aggregate value added of these industries is modest. On the other hand, the value added per worker in small, capital-intensive, rural industries are much larger, namely jute baling (Tk 14933), grain milling (14937), tobacco processing (8,322), saw milling (14003), handsaw timber (3395), bedding material (4242), silk weaving (3127), hosiery (10684), metal handtools (8734), leather processing (1397), plastic products (10407), soap and tooth powder (11368), job printing (8299), and motor vehicle repairing (6739), and welding (9130). (Source: BIDS, 1984, pp. 156-7). These 15 products out of the 65 products of this survey accounted for about 2/3rds of total value added.

Mean value added per worker per year in the former (cottage) group of industries in the reference year was approximately Taka 900. That in small industries Taka 8500. Average annual income per enterprise was estimated to be Taka 3,000 in the cottage group and Taka 30,000 to 60,000 in the small-enterprise group; the estimated marginal products of labor and capital were Taka 1.11 per worker and Taka 0.88 per taka, respectively, in cottage industries and Taka 3.11 per worker and Taka 0.27 per taka, respectively, in small industries. According to this study, thus, it is evident that cottage industries provide at best mere subsistance to its workers (specially see the study by Mahbub Hossain, 1986).

Other studies done on this sector find, more or less, similar results.[9] The productivity in small and cottage industries is low and has not changed significantly since Independence. Neither has it declined as precipitously as in large industries.

Summing up

In the end, it should be mentioned that insofar as policies are concerned, successive 5-year plans since the 1950s have almost ritualistically recognized that small and cottage industries have a very important role to play in the employment and economic development of the country. As regards their practical promotion, that was about all: ritual homage. Little attention has been given in terms of investment, operational policy formulation, technology development,

or institutional building. No department or division for small, cottage or rural industries in the Ministry of Industries or any other ministry has been created. The BSCIC's main energies are spent on its score or so of industrial estates. The newly created Sericulture Board and the Handicom Board have yet to develop into effective institutions. Even where facilities exist on statutes, they may not be taken advantage of for various reasons. For instance, the main concessions that the "top priority" status assigned this sector in the 1986 Industrial Policy consisted of the availability of credit for which purpose banks were required to provide a special "window" and specified percentages of total credit for small enterprises. Statistics indicate that an amount of only Taka 5 crore was disbursed by banks and financial institutions out of Taka 50 crore set aside as the credit disbursement target for 1986-87 for small and cottage industries. Possible reasons, apart from the notorious bureaucratic sloth and administrative complexities, may be that there are few takers.

Thus, whether or not Little's verdict finds support in Bangladesh is difficult to say. A thorough assessment of policies is needed to say anything about it. Since Little's analysis is based on a rather small sample, mainly the experiences of Colombia and India, his conclusion may or may not be robust. It may even be premature, or at best a hypothesis that needs to be tested by more empirical analysis. For instance, in none of the World Bank studies have the effects of policies not specifically enacted to promote small business been carefully analyzed to see whether in their aggregate effect, they might not have hindered the progress of this sector relative to the large sector or whether overall incentives provided large industries might

not be more substantial and more effective than those for small industries. Such an analysis will be done for Bangladesh. Little's own work was done only for India (Little and Mazumdar, 1987), a country with "long-standing policy, unusual among developing countries, of providing special support and protection for small enterprises" (Little, 1987). As has been seen in the survey above, Bangladesh did not provide special support to its small sector until 1986. A comparative assessment of the roles of small industries of the two neighboring members of the SAARC, which we plan to undertake towards the end of this project, should throw some light on this hazy area.

APPENDIX 1A

LABOR POLICY IN BANGLADESH

Labor legislation in Bangladesh owes its origin to the labor laws of British India, which have only marginally been improved upon since the end of the British rule. Social security system is practically non-existent. The provident-fund and compulsory saving system (under which accumulated saving with interest are paid in lumpsum at retirement)— well established in most Commonwealth countries among public employees (including the workers of autonomous and semi-autonomous enterprises), plantation workers and some industries of the organized sector—is in operation for certain groups of workers in Bangladesh. Maternity benefits, compensation for injury and sickness, and similar health benefits have also existed on a rather limited scale since the British days. In the following paragraphs, we summarize the history of labor laws in Bangladesh. Labor legislation from the viewpoint of social security has recently been appraised, with recommendations for additional labor welfare legislation in Bangladesh, by System Development Ltd. (1986)

Workmen's Compensation Act was passed in 1923. It provided compensation for injury at work, sickness, medical care, death grant/survivors' benefits, disablement pension, and similar benefits in selected industries of the organized sector. This act was amended in 1957 and again 1980 to make compensation consistent with changed conditions.

The Trade Union Act of 1926 granted the right to unionize by seven or more workers of any plant. Maternity Benefits Act was passed in 1939, just before the outbreak of World War II.

The same year, Plantation Employees Provident Fund Ordinance, 1939, was issued, which introduced provident fund, for the first time, for workers other than public servants. Certain additional rules about it were issued in 1980.

To assess the progress of social insurance in Bangladesh during the postwar period, it would be useful by way of a comparative view to have a brief look at similar legislation in one or two equally poor countries. India and Pakistan should serve as relevant cases.

The postwar guidelines for minimum standards of social security and other labor-welfare measures for LDCs in different stages of economic development were issued by International Labor Organization (ILO) in 1952 (ILO,1952). Four years before that, within two years after her Independence, India, following the ILO suggestion to that country, adopted the Employees State Insurance Act, 1948, first of its kind in South East Asia. It introduced a compulsory system of social insurance covering health, maternity, and accident benefits for workers. In the same year, India enacted the coal Mines Provident Fund and Bonus Scheme Act, 1948. Four years later India adopted the Employees' Provident Fund Act, 1952, which coincided with ILO's Social Security (Minimum Standards Convention, No. 102, 1952) setting out a framework for low-income countries in different stages of development. The three acts covered major organized sector. Unemployment insurance and old-age pension do not exist yet in the Indian subcontinent, but steps are currently underway in India to introduce these schemes on a limited scale.

The ILO expert team visited Bangladesh in 1952 and again in 1957-58. Its recommendation led to Employees' Social Insurance Ordinance in 1962, which provided benefits to workers and their dependents for sickness, maternity, work injury, and death. The ordinance was implemented in certain areas in West Pakistan, but was deferred in East Pakistan (today's Bangladesh) due to difficulties. Certain regulations about terms of employment, such as sickness benefits, were provided under the Employment and Labor (Standing Orders) Act 1965.

Another ILO mission visited Bangladesh in 1967. Its main recommendations remain unimplemented, but the Companies Profits (Workers Participation) Act, 1968, was passed under which the workers of firms with 100 or more employees and Taka 2 million capital were entitled upto 2.5 percent of profit sharing (depending upon years of service).

The Act was tightened somewhat in the Companies Profits (Workers' Compensation) Rules, 1976. It was further amended in the Companies Profits (Workers' Participation) (Amendment) Ordinance, 1985, when the rate of profit-sharing was raised to 5 percent. Recall also that starting in 1986, newly denationalized industries were to reserve 15 percent of their shares for the respective enterprise's workers. Thus a selected beginning has been made to convert Bangladeshi workers into fledgeling capitalists. Insofar as social insurance is concerned, however, after the independence, the nation seems to have been preoccupied, first, with nationalization (about which workers were happy) and, subsequently, denationalization (about which workers in general seem to be unhappy). In this process, the social security system got pushed back in priority.[10]

Minimum wage legislation has existed since 1961, when two statutes were written: The Minimum Wages Ordinance, 1961, and the (EP) Minimum Wages Rules, 1961. These ordinances merely authorized the government to fix minimum wages in chosen industries/sectors, but minimum wages were actually not fixed until 1973 in hotels and restaurants (amended in 1979, vide the Minimum Wage Rates for Hotel and Restaurants, 1979) and until 1985 for public employees, for whom a minimum wage of Taka 560 was fixed, which is still current with an additional 10 percent dearness allowance.

Bangladesh workers are also relatively behind insofar as labor-management relations are concerned. A part of the reasons for this state is the frequency with which and the duration for which the country has been ruled by military governments since WWII. For military governments have invariably brought statutes restricting some of the basic rights required to promote collective bargaining. For instance, during the 3 years from 1975 to 1978 of the military rule, the number of trade unions declined by 10 percent and the number of trade union workers fell by 8 percent. On the other hand, during the 3 years of civillan rule from 1971 to 1974, the number of unions and unionized members increased by 186 percent and 110 percent, respectively; and during the 4 years of post-military rule from 1977 through 1981, the number of unions and members rose by 20 percent and 29 percent, respectively (Hafiz, 1982. p. A/35).

While military governments of East Pakistan and Bangladesh have in general restricted the right to strike and unionize as well as to collective bargaining, that probably is not a major reason for the lag in progress towards social security and general worker welfare. Rather the lag is, in part, due to practical difficulties. For in a poor country, like Bangladesh, social unemployment insurance is almost out of the question due to high underemployment, illiteracy, low taxable capacity, and other reasons. Even where social

security is feasible (at best only in organized industrial sector), priority goes to immediate returns and short-term risks as against accumulation for old age and survivors' benefits. Bangladesh is, thus, relatively free of those labor laws, which have been considered as a damper on labor-using technology. In comparison to other South Asian countries, for instance India, the position of Bangladesh is summarized by System Development Ltd.(1986) as follows:

	Bangladesh	India
Employment injury benefits	EL	EL/SI
Sickness benefits	EL	EL/SI
Maternity benefits	EL	EL/SI
Old-age security	EL: Tea only	SI
Invalidity insurance	EL: Tea only	SI
Death of breadwinner	EL: Tea only	SI

SI = Social insurance

EL = Employer's liability

The relatively low labor costs due to the absence of social security are, however, offset by certain employment terms.

Firstly, foreign investment has not been particularly encouraged. Thus, after Independence in 1971, foreign investment was first allowed only in public enterprises and was not to exceed 49% of shares. In subsequent years, it was permitted in private ventures, but still not to own majority shares,

which restriction has only recently been lifted. Secondly, the denationalized and divested industries were under legal obligation not to dismiss the previous employees of those firms, which hindered rationalization. Thirdly, trade unionism is relatively strong in Bangladesh and collective bargaining is practiced, which is not an attractive institution to employers. For instance, one of the attractions to foreign employers for locating their plants in the EPZ is the non-unionized environment. Finally, a host of subsidies to capital have increased the attractiveness of capital-intensive, labor-saving technology.

In short, insofar as employers are concerned, labor laws in general are not stringent in Bangladesh and do not increase the cost of labor significantly. Those that exist are confined, apart from tea plantations, mainly to large and medium industrial enterprises. The latter sector also enjoys several subsidies and protection to capital investment. In other words, the potentially expanding large industrial sector, vis-a-vis agricultural and small sectors, enjoys relatively cheaper capital and relatively costlier labor. The data for assistance of various sorts to capital are available and have been incorporated in empirical relations of chapter 2. The corresponding assistance (negative or positive) to labor has been handled by estimating shadow wage by a few categories of labor and relating it to the market wage rate (see Chapter 2).

APPENDIX 1B

PRICE CONTROLS

The final major policy set that discriminates between sectors in respect of investment, production, and employment consists of price controls. Four major areas of price controls may be distinguished: agricultural support prices or procurement prices (and related price-influencing policies, such as food import); intermediate input price controls, for instance, fertilizer, natural gas, cement, cotton yearn, water and electricity prices; consumer-price controls and rationing, for instance, prices of wheat, sugar and rice; and pricing policies for public utilities and similar nationalized industries, such as railway rates, road and water transport charges, postal rates, university fees, and so forth.

The methodology of translating domestic price controls into real effective assistance (positive or negative) corresponds to the scarcity markup for imports subject to quality restrictions. The price-control topic forms the subject matter of a more elaborate study of this project and will be taken up in due course when small enterprises across different macro sectors, such as rural industries versus urban cottage industries, are analyzed.

FOOTNOTES

(Chapter 1)

[1] In FY1986, when GDP in current prices had still not reached the US$ 15 billion mark, total committed aid for the year was US$1.6 billion, disbursed aid was US$1.3 billion, while US$5.2 billion was in the pipeline. With minor wobbles, foreign aid has ranged between 10 to 13% of GDP since 1973. Yet the disbursed outstanding foreign debt is only 40% of GDP and the interest cost on it was about half of one percent of GDP (US$98.4 million as of June 1986). Source: World Bank Report on Bangladesh, Mar 10, 1987, Vol.II.

[2] The Constitution was amended, by the Martial Law Proclamation Order of 1977, from:

"The principles of nationalism, socialism, democracy and secularism. . . shall constitute the fundamental principals of state policy," to read: "The principles of absolute trust and faith in the Almighty Allah, nationalism, democracy and socialism meaning economic and social justice. . . shall constitute the fundamental principles of state policy."

[3] The problems being faced include the continuing dispute between the new private owners of denationalized industries and the public sector about the assumption of liabilities incurred by these industries since nationalization; default on instalment payments (currently about 90 percent payments are overdue) by the buyers of public enterprises; difficulties that banks face due to low rates of recovery from new owners and having to waive some of their accumulated interest; problems that private owners face concerning foreign loans due to exchange rate changes; the 1915 contract laws under which these transactions were made need to be modernized; the same problems relates to the 1960s law relating to the banking business; and similar legal and procedural matters.

[4] The progress in denationalization (the term used in Bangladesh to distinguish the sale of those nationalized industries previously owned by Bangladeshis) and divestment (the term used for the sale of those industries which were taken over by the state when they were abandoned by non-nationals in 1971) may be seen from the following statistics:

Period	Divested	Denationalized	Total
1973-75	154	0	154
1976-81	115	106	221
1982-86	36	50	86
1982-83: Jute and textile		57	57
1986-87: Sold	0	23	23
PLC	0	3	3
Total sold	307	239	544

Source: Ameen (1987, p.88).

[5] The term WES refers to the Wage Earners' Scheme, according to which the remittances of Bangladeshi nationals working abroad (predominantly wage labor that temporarily migrated to the oil-producing Arab countries during the oil boom) were allowed free-market foreign-exchange rate. This rate is determined by auction.

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[6] As of June 30, 1985, 69 Public Limited Companies were listed with Stock Exchange. Their paid-up capital was taka 200 million. The limited role of the stock exchange in Bangladesh may be judged by the low volume of transactions, which in 1984-85 was merely Taka 22 million or just about one million dollars.

[7] The debt-equity ratio of the public sector corporations is given below:

	FY81	FY82	FY83	FY84	FY85	FY86
Debt: Equity Ratio						
BCIC	97:03	81:19	82:18	75:25	80:20	81:19
BSFIC	83:17	82:18	79:21	69:31	83:17	92:08
BSEC	-	98:02	89:11	91:09	93:07	87:13
BJMC	86:14	92:08	84:16	86:14	105:(-05)	141:(-41)
BTMC		114:-14	101:-1	88:12	90:10	89:11
	92:8	86:14	80:20	81:19	87:13	92:08

Source: Malik (1987).

[8] An earlier study on small and cottage industries was done by Ahmed and Ahmed (1979). It was based on secondary data for 1976-77 and a limited field survey and was addressed mainly to measuring output and employment, which magnitudes were estimated to be US$375m (or approximately 6 percent of GDP) and 2.3 million, respectively. While definitions of this sector may differ, the BSCIC reports the following figures for percentage contribution to GDP by small cottage industries in more recent years:

	% Contribution of SCIC
1978-79	3.9
79-80	4.3
81	4.1
82	4.1
83	4.3
84	3.9
84-85	3.8

Source. BSCIC (1986, Table on p.4)

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[9] The background studies for the preparation of the TFYP, done during 1985-86, used largely the same old data which had formed the basis of the corresponding background studies for the SFYP, surveyed in the text above. These were aimed at estimating the size of capital stock, labor force employed, input-output structure, value added, and capital-output ratios.

Their objectives were to identify potential industries in selected upazilas. There is very little in these studies to add to the earlier, 5-year old studies in terms of analysis. Among these, the following are relevant: small and cottage industries by Habibur Rahman (1986), rural industries by BIDS (1987), and trade service by Mahmood, et al., (1987). Two earlier studies on those sectors which are likely to be predominated by small enterprises may also be mentioned, namely, Khan and Siddique (1979) on transportation and Muktadir and Ahmed (1979) on rural construction.

[10] Bangladesh's labor legislation is discussed in detail by Lawyer A.A.Khan (1985).

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