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THE SEMINAR ON REGULATORY CONSTRAINTS TO INDUSTRIAL DEVELOPMENT IN BANGLADESH

SUMMARY OF PROCEEDINGS

Seminar Held On
16 April 1994

POLICY IMPLEMENTATION AND ANALYSIS GROUP (PIAG)
Adamjee Court, Motijheel, Dhaka

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THE SEMINAR ON "REGULATORY CONSTRAINTS TO INDUSTRIAL DEVELOPMENT IN BANGLADESH"

SUMMARY OF PROCEEDINGS

The seminar was held on April 16, 1994 under the auspices of the Ministry of Industries and the Policy Implementation and Analysis Group (PIAG), a USAID-financed project in the Ministry of Industries. It was a day-long workshop divided into an inaugural session and three discussion sessions. The seminar was organized to discuss the PIAG draft report "Regulatory Constraints to Industrial Development in Bangladesh and Recent Deregulations", prepared by the PIAG consultant Dr. Abdur Rab.

The seminar was inaugurated by Chief Guest Mr. A.N.M. Eusuf, Principal Secretary to the Honorable Prime Minister. The inaugural session was chaired by Mr. A.H.M. Abdul Hye, Secretary, Ministry of Industries. The three discussion sessions were chaired respectively by Mr. Mahbubur Rahman, President, the Federation of Bangladesh Chambers of Industry and Commerce (FBCCI), Mr. Kamaluddin Ahmed, Deputy Governor, Bangladesh Bank, and Mr. Latifur Rahman, President of the Metropolitan Chamber of Commerce and Industry (MCCI).

Inaugural Session

Address by Mr. Syed Yusuf Hossain:

This session started with an address of welcome from Mr. Syed Yusuf Hossain, Additional Secretary of the Ministry of Industries and Project Director of the PIAG project. In his address, Mr. Hossain explained the objectives and role of the PIAG project in the ongoing policy reform and policy implementation process, especially in the context of Industrial Policy 1991, which marked a new horizon towards creating a conducive environment for growth. He observed that the PIAG project had been designed to assist the MOI in the task of continuous review of industrial policies and their implementation, in identification of problems and constraints in implementation, and in the process, in evaluation and formulation of new policy recommendations. The project, therefore, represented a significant and serious effort on the part of the Government to improve the policy environment for accelerating industrial and economic development. He further observed that there was need for continuous monitoring and re-assessment of assistance and incentives offered and evaluation of effects of policies on the industrialization process and for determining whether the policy framework of Bangladesh measured up to that of those countries which had become successful and were rapidly developing.

Mr. Hossain further observed that Bangladesh now stood at a crucial juncture of development, where it was imperative that industrialization proceed at a faster rate than in the past to alleviate massive poverty. At this juncture, he noted, Bangladesh needed to compete with many other developing countries in the race for development and for attracting foreign investment. In that context, studies which pointed to the ways whereby the industrialization process could be accelerated were of current and crucial importance to all concerned.

He observed that the study that was being discussed in the seminar had made the points that regulations and controls hindered growth, restrained exports, decreased efficiency of the labor market and in general led to an environment where investment was slow despite very admirable macro-economic management.

He then observed that this seminar was the first in a series which were being planned to identify the critical issues and problems in industrial development and to build a consensus between the Government and the business community for policy reforms.

With these words, he then warmly welcomed the guests and participants of the seminar on behalf the MOI and the PIAG and wished for a fruitful exchange of views.

Address by Dr. Richard Brown:

Dr. Richard Brown, Director of the USAID Mission, while welcoming the opportunity to say a few words, observed that the forum, under the sponsorship of the PIAG project of the MOI, represented a clear indication of the seriousness of both public officials and private sector leaders to improve the investment and business environment in Bangladesh. The forum was timely in that it was supporting the active dialogue taking place on how to increase investment and growth. He observed that the US Government strongly supported the Bangladesh Government's goals of employment creation and poverty reduction and that the same was the organizing principle of USAID strategy in Bangladesh.

Dr. Brown further observed that the manufacturing sector had the greatest potential for increased employment and the key issues to address were how to foster efficient manufacturing activities to get the most employment out of it. It was essential that Bangladesh accelerate its ongoing economic reform and restructuring process to take advantage of a "short window of opportunity" before its world markets were lost to regional competitors and population growth eroded potential gains.

While turning to the subject for discussion in the seminar, Dr. Brown stressed the importance of deregulation reforms to promote private domestic and foreign investment. He remarked that day-to-day regulations facing entrepreneurs were formidable, many of which were carryovers from a period of a centrally planned economy. Such regulations impeded the process of growth, acquisition and mastery of technology. In this context, he cited an example of what deregulation could accomplish. The recent removal of the regulation, in the registration process with the Board of Investment (BOI) that proof be provided of an investment already being in progress, had the almost inconceivable result that more investment was registered in the one month after the removal of the regulation than in the previous three years.

While commending the work done by Dr. Abdur Rab, he wished the workshop discussing his paper to be an important step toward deregulation in Bangladesh.

Opening Remarks by Dr. Ronald P. Black:

Welcoming the distinguished guests to the seminar on behalf of the PIAG project, Dr. Ronald P. Black, Chief Technical Advisor of the project, said that it was a matter of great satisfaction to PIAG to expose Dr. Rab's report to such a knowledgeable and involved group. Explaining the objectives and role of the PIAG project, he observed that the PIAG was envisioned as a Ministry of Industry "think tank" to assist the Ministry in implementing and where necessary formulating policy for stimulating industrial growth through reducing the costs associated with doing business and in general creating an enabling environment. He said, in addition to the Industries Ministry, PIAG could also work with related agencies and organizations concerned with shaping and implementing industrial policy, which also included a close working relationship with the private sector business chambers and associations. He observed that holding this first PIAG seminar in the Metropolitan Chamber auditorium was a symbol of that relationship. As an example of how the PIAG was already having some impact on the process of simplification and elimination of unnecessary regulations and formalities, Dr. Black cited the recent issue of a new circular by the Securities and Exchange Commission (SEC) which eliminated the need for the SEC approval of the transfer of shares of the foreign or joint venture firms. This reform was in direct response to a recommendation in Dr. Rab's paper which was discussed with the Chairman of the SEC upon his kind invitation.

Dr. Black then observed that the seminar gave an opportunity to examine Dr. Rab's report, to share with the participants some of the views and recommendations on deregulation and obtain new inputs for finalization of the report. He hoped that the seminar would contribute to the development of a greater consensus between the public and private sectors to accelerate the development of a vibrant market economy.

He then concluded his remarks with the observation that Dr. Rab's report spanned a wide spectrum of regulatory areas, had provided all concerned with a valuable guide to barriers that were impediments to growth, and a cataloguing of specific actions required to lead to a more congenial business environment.

Paper Presentation by Dr. Abdur Rab:

Dr. Abdur Rab presented the highlights of his study. Speaking about controls on private investment, he said that although according to the current industrial policy there were no controls on private investment except in regulated sectors, controls arose because of non-definition or ill-definition of regulated sectors and lack of transparency and complexity of regulatory procedures as well as because of miscellaneous other reasons, which included (1) ambiguity in industrial policy toward financing of "saturated industries"; (2) regulatory functions performed by industrial promotion agencies, of which the most important was the Board of Investment (BOI); (3) special restrictions applied to foreign investors; (4) restriction on imports of second-hand machinery; (5) weak enforcement of patents and trademark laws; (6) remaining difficulty faced by foreign investors in winding up business; (7) difficulties still remaining in investing in sectors such as power, tele-communications; and (8) difficulties faced with customs. He cited the ban on investment for production of polypropylene bags and many pharmaceutical products and the threatened (but now suspended) ban on the production of polythene shopping bags as examples of cases of inappropriate controls on investment. He observed that the most important reason applied for industrial regulation was consideration of environmental impact of projects. However, which industries needed to be considered for clearance on environmental grounds and the lengthy, complex, and often, costly procedures used to deal with environmental issues created obstacles to private investment. Regarding regulatory functions performed by the BOI, he observed that while the registration process had been simplified and made automatic, there still remained other regulatory functions which needed to be eliminated. Concerning BOI directives to financing institutions about saturated industries, Dr. Rab observed that such directives were inconsistent with a free market control-free investment regime. Dr. Rab then outlined the industry-specific regulations which affected the pharmaceutical, readymade garments and 'gur' industries.

Turning to exchange controls, Dr. Rab pointed out that even after significant recent liberalization of the exchange regime including introduction of convertibility of the taka on current account, there still remained excessive exchange controls . These included (1) remaining restriction on (BOI) approval requirement for) private borrowing from abroad; (2) restriction on reconverting of funds from exporters' foreign currency accounts with retained foreign exchange, if used to meet local expenses; (3) restriction on foreign exchange availability for non-letter of credit (L/C) imports; (4) restriction on cash foreign exchange availability for imports by exporters operating under back-to-back L/C bases; (5) still remaining limits on the access to foreign exchange for personal and business travels; (6) controls on capital transfers; and (7) centralized control on exchange rate management. Dr. Rab observed that the liberalization impact of the taka convertibility was little felt because of the existing remaining exchange controls, including controls on capital transfers, and because the taka remained on a managed float basis. He further remarked that the existing controls were grounded on unfounded fears of abuse of exchange liberalization and capital flight, as the experience of other countries engaging in exchange regime liberalization suggested.

Turning to import controls, he observed that substantial progress had already been made in their elimination and that the remaining controls for trade reasons on 55 four-digit harmonized system code items including 14 pharmaceutical industry-related items deserved to be eliminated soon.

Regarding export controls, he observed that there unnecessarily remained certain restrictions on re-exporting business (i.e. entre pot trade or imports for re-exporting), excessive restrictions on exports of samples and imports of samples for export purposes, ban on exports on consignment basis for non-perishable goods, and export ban and restrictions applied to a number of agricultural and manufactured products including a ban on exports of jute yarn by composite jute mills producing woven jute products and a 30 percent value addition restriction for woven garments in the quota category with value below US $40 per dozen.

With respect to banking regulations, Dr. Rab pointed out that despite considerable financial sector reform and deregulation carried out recently, certain remaining central bank or government controls which required deregulation were: (1) remaining Bangladesh Bank (BB) controls on certain bank loan categories; (2) government directives for credit to the jute sector; and (3) remaining BB-directed interest rate bands for credit to three sectors, agriculture, exports, and small and cottage industries. Dr. Rab further observed that full benefits of financial deregulation were not being realized because of the oligopolistic structure of the banking system with the nationalized commercial banks, which were inefficient, dominating the system. To increase competitiveness in the banking sector, Dr. Rab recommended greater government encouragement of the entry and growth of private banks.

On labor regulations, Dr. Rab observed that the central issues were about how to (1) ensure healthy labor management relations; (2) ensure speedy resolution of labor disputes; (3) remove centralized directed influence on the wage determination process; and (4) ensure effective enforcement of labor laws. He recommended removal of legal deficiencies with respect to employment terms, of weaknesses in trade unionism regulations, and of excessive government intervention in labor disputes to ensure healthy labor-management relations. Among recommendations he made to improve the labor market included those for discontinuation of the current practice of setting public sector wages in disregard of public enterprises' profitability situation, for eschewing the idea of introducing a national minimum wage and for cessation of direct government intervention with trade union bodies outside the legally-prescribed tripartite process.

Finally with regard to general legal reform issues, Dr. Rab first outlined the legal issues that needed to be considered in order to ensure a congenial legal environment for orderly conduct of business activities. He then outlined some of the legal reforms that needed to be carried out or accelerated.

Address by the Chief Guest, Mr. A.N.M. Eusuf:

The Chief Guest, Mr. A.N.M. Eusuf, in his address, appreciated the work done by PIAG. In this context, he observed that it was not simply liberalization of policies which was important but also effective implementation of such liberalized policies. He referred to two other issues covered in the paper: consideration of environmental aspects of projects and the question of saturated industries. Regarding the first issue, he observed that the environmental effects of projects were a genuine concern for the society and such effects would have to be duly taken into account. About the second issue, he noted a need for information about market saturation by potential investors.

Address by the Session Chairman, Mr. A.H.M. Abdul Hye:

The Chairman of this session, Mr. A.H.M. Abdul Hye, explained the major objectives of the PIAG project and those of the other components of the USAID-funded Industrial Promotion Project (IPP). He observed that by producing the current paper on regulatory constraints to industrial development in Bangladesh and holding this seminar, the PIAG was fulfilling part of its major objectives. He observed that efforts for organizing this seminar at an earlier date did not succeed for certain unavoidable reasons. The delay had rendered some observations of the paper out of date. In this connection, he mentioned the ban on the production of polythene shopping bags. The ban had now been kept in abeyance for an indefinite period by a Cabinet decision. Hence the ban was no longer an issue. About the deregulation program proposed in the paper, Mr. Hye observed that the implementation of a program should be carefully designed with appropriate sequencing and timings of the individual reform components.

Mr. Hye then elaborated on the format of the Seminar/Workshop. He explained that the Seminar was divided into three sessions to facilitate focussed discussion on three distinct groups of regulatory areas viz., (1) investment controls and industry-specific regulations, (2) exchange controls, banking regulations, import and export controls; and (3) labor regulations and general legal reform issues. He hoped that comments by the designated discussants would be followed by spontaneous and frank discussion by other participants. He observed that formulating reform programs was a difficult exercise but implementing them was even more difficult. He sought the co-operation of the private sector in the implementation of the various reform programs undertaken.

Before concluding, Mr. Hye appreciated the work already done by the PIAG team and praised the very high quality of papers already produced. He thanked the USAID for their support to the Bangladesh Government on its ongoing efforts for various reform programs in the industrial sector.

Discussion Session 1

INVESTMENT CONTROLS AND INDUSTRY-SPECIFIC REGULATIONS

Opening Remarks by Chairman, Mr. Mahbubur Rahman:

Discussion Session 1 was about Investment Controls and Industry-Specific Regulations. In his opening remarks, the Chairman observed that although certain policy reforms were being announced, complaints were very often heard from private chambers of commerce and industry and other trade bodies that these policies were not in place. The study being discussed was based on extensive interviews and it represented a serious effort to mirror the views of various groups involved in the industrialization process and to identify problems of entrepreneurs and suggest ways of resolving such problems.

Comments by Dr. Zaid Bakht:

Dr. Zaid Bakht, Senior Research Economist, the Bangladesh Institute for Development Studies, a designated discussant, made the following comments:

1. The author should have added to the constraints, listed at the outset, the demand-side problems (e.g., small size of the domestic economy, difficulties of penetrating export markets, etc.) and the prevailing inhospitable law and order situation.

2. The paper did not touch on the system of registration required with the Chief Inspector of Factories under the Factories Act of industrial enterprises employing 10 or more workers, which was a significant source of irritation to the entrepreneurs.

3. While he agreed that the process of registration with the Board of Investment (and similar organizations) should be made both easy and quick, he thought that if it was made automatic, it would compound the problem of monitoring industrial investment. In this regard, Dr. Bakht made a suggestion that provisional registration be deregulated to the chambers of commerce and industry and such registrations be followed by surveys of realized investment conducted jointly by the chambers and the relevant government agencies.

4. The paper also did not cover the pre-investment delay (or other problems) associated with a No Objection Certificate (NOC) required from local authorities for industrial projects not located in public industrial estates.

5. While agreeing with the author that the Government should not guide financial institutions regarding market-saturated industries, he thought that there was still need for supplementing information about projects available with the financial institution in view of their poor project appraisal capabilities.

6. Dr. Bakht strongly endorsed the author's recommendation for removal of production bans. In this regard, he cited the example of how the ban imposed in 1982 on the production of phensydil syrup had led to its wide-scale smuggling from India

and had also caused the social evil of addiction to this drug, while this menace was absent in India where it was produced.

7. While agreeing that foreign and domestic investors should be equally treated, Dr. Bakht suggested that a justification was there for a restriction for foreign investors on production of quota categories of readymade garments unless such garments were meant to be exported to non-quota countries.

Dr. Abdur Rab responded to these comments as follows:

1. The demand-side constraints were not of significance from the point of view of actions that developing countries like Bangladesh needed to be most concerned with for accelerating development.

2. The registration required with the Chief Inspector of Factories was not known to be a serious problem for the entrepreneurs. However, if it was now found to be, it would be incorporated in the final report.

3. A similar observation was valid also with respect to the requirement of an NOC from local authorities for non-public-estate industrial projects. (The site clearance requirement referred to by industrialists and mentioned in the paper might be the same thing.)

4. The automatic registration process which had been just recently introduced in the BOI should not be reversed. The case for making this process simple and automatic and keeping it voluntary overshadowed the need for introducing any element of compulsion in this process to help investment monitoring. The latter problem could be taken care of in other ways.

5. Keeping any trace of discrimination against foreign investors, which contradicted the Foreign Investment Act clause in this regard, was not at all justified, especially in view of Bangladesh's relative failure to attract foreign

investment.

Mr. Charles Byron, Chief Technical Advisor on a project with the BOI, observed that the feedback emanating from the automatic registration process introduced since March 1 had been positive. He sought clarification as to what the author meant by his recommendation that the other regulatory functions still being performed by the BOI should be taken away from it. To this, Dr. Rab replied that his recommendation was for elimination of such regulatory functions and not for transferring them to another government agency. He, however, pointed out that in the case of approving imported input requirements of industrial projects, this function should be confined to the restricted category of imports. Mr. Byron disclosed that the passbook now did not show quantities of inputs which were on the free list. This was introduced in a recent month. Dr. Rab claimed some credit for the PIAG project for this reform. Mr. Byron said that while the PIAG work was to be appreciated the BOI should also be given some credit.

Mr. Abdur Rob Chowdhury, President of the Dhaka Chamber of Commerce and Industry observed that in addition to eliminating regulatory constraints on investment, other problems which should be addressed were difficulties faced by entrepreneurs in getting access to finance from development finance institutions (DFIs) and banks, and in getting reliable consultancy services. The banks were being controlled by the Government and the Bangladesh Bank with top executives of such banks placed there by the Government. Mr. Chowdhury recommended that the Ministry of Industries set up an Advisory Body to look into the problems with the DFIs and this Ministry should take necessary steps to improve consultancy services. He also put up another suggestion: to develop leather industries, the Government should build two separate zones away from the city as is done in other countries.

Mr. Abu Ahmed of IBCS-PRIMAX pleaded for establishment of an industrial and trade information base with an appropriate Government ministry or agency. Information from this could be shared by Government and international agencies.

Mr. Mahbubul Amin Khan, Deputy Governor, Bangladesh Bank observed that some of the findings of the paper had been overtaken by events. He referred to the banking regulations with respect to loans to some industries, post-import financing, transport industries and real estate business and suggested that these were all gone now. Mr. Khan did not think that the problem of investment monitoring should be slighted. He also believed that import substitution industries should not be downplayed. These were important for employment generation. He did not favor the idea of opening up everything. He was concerned about industries which had been financed by the banks. Mr. Khan also mentioned that there was no longer any directed credit, but moral suasion in certain priority areas from the Government. He expressed the view that restriction on hire purchase even for consumer goods was not necessary or desirable. Singer was already doing business on hire purchase basis for its consumer durables. He suggested that there should be specific laws for guiding this business and leasing activities. He maintained that the central bank should exercise prudential controls to safeguard the interests of depositors and in the overall interest of the economy. He also referred to the need for bringing in non-economic issues such as the law and order situation.

Mr. Mahbub Jamil, President of the Foreign Investors' Chamber of Commerce and Industry, observed that registration from the Chief Inspector of Factories was not a difficult problem. However, the problem of having to pay a bribe was there. He mentioned that serious problems being faced were in connection with the VAT administration (in resolving VAT anomalies) and in getting timely response to applications for tax holidays. Mr. Jamil emphasized the need for adhering to the principle of equality of treatment between domestic and foreign investors as professed by the Foreign Investment Act. Some of this Act's clauses had been overtaken by the Investment Policy. An amendment to this Act was necessary but was being delayed. In case of dispute, the previous Act prevailed, not the Investment Policy. He also pointed to the need for establishment of commercial courts for facilitating business in consumer durables on hire purchase basis. Such courts exist in Malayasia.

Mr. Abdus Samad, Member of the Executive Council of the Board of Investment observed that to expect that the BOI should perform as a one-stop service agency was not justified since the BOI was not given that authority and thus was unlike the Sri Lankan BOI. He disclosed that there was now a move on to revise the BOI Act to give it sufficient power.

Dr. Kabir U. Ahmad, Advisor at the Tariff Commission, advocated for synchronization of the rules and incentives for Export Processing Zones (EPZs) and other areas.

Mr. Mahbub Jamil lamented that the very attitude of the bureaucracy was not very helpful. The problem was especially there with the lower echelons of the bureaucracy. The BOI should radically reform itself to perform a promotional role. In Sri Lanka, the BOI officials greet and deal with foreign investors in their hotels. They were not required to visit the BOI office there.

The **Session Chairman** in his concluding remarks made the following observations:

1. There were not only regulatory constraints to investors. The investors faced also other problems.

2. The Government had not been steady and consistent in its policy reforms. He cited the example of private imports of petroleum products permitted by the import policy. But obstruction was created by the Ministry of Energy. The case went to the High Court which upheld the private importer's right. However, the Government had made a retreat from its policy of trade liberalization. By a recent order, such private imports had been made subject to clearance by the Energy Ministry. Such policy reversals shook the confidence of private investors.

3. Policies with respect to tele-communications needed to be changed in order to encourage private investors.

4. The Privatization Board had been established to ostensibly expedite the privatization process. However, with its establishment, the privatization process had been rather slowed. There were also reports that the Board received instructions (from top Government people) to go slow.

5. The law and order situation was a serious problem.

6. The registration process should be hassle-free.

7. The problem with the Chief Inspector of Factories was that that office created unnecessary problems for the entrepreneurs whenever bribes were refused. In this connection, he cited the problem his own establishment faced. There was a similar problem with the Inspector of Boilers.

8. In connection with the treatment for foreign investors, Mr. Rahman opined that it was not fair that they should be allowed to use quota facilities. However, if they were already operating in this business, they should not be restricted.

9. He endorsed the suggestion of Dr. Kabir U. Ahmad that there should be harmonization of rules for EPZ and non-EPZ areas.

10. He did not agree with the suggestion of Mr. Abdur Rob Chowdhury for an Advisory Body to deal with DFI problems.

11. He referred to the need for an amendment of the Foreign Exchange Control Act. In the absence of such an amendment, banks were not always found to go by the Bangladesh Bank circulars.

12. The BOI should have more authoritative role to play for facilitating the access to other services for the investors.

13. The Export Policy should be an executive policy order like the Import Policy. Some of the policies incorporated in the Export Policy like 100 percent tax exemption were not

implemented.

14. The Government should cease intervening in labor disputes.

Discussion Session 2

EXCHANGE CONTROLS, QUANTITATIVE IMPORT REGULATIONS AND IMPORT AND EXPORT CONTROLS

This session was devoted to a discussion of issues in four regulatory areas: exchange controls, quantitative import restrictions, export controls and banking regulations. It was chaired by Mr. Kamaluddin Ahmed, Deputy Governor of the Bangladesh Bank. The Chairman made an opening remark that some of the comments made in the first discussion session dealt with issues of this session.

Comments by Mr. Chaudhury A.K.M. Aminul Haque:

Mr. Chaudhury A.K.M. Aminul Haque, Macro Economist, Financial Sector Reform Program, the first of the designated discussants, then made the following comments:

1. The exchange control regime has been liberalized during the last three years with the abolition of the secondary exchange market, considerable relaxation of exchange restrictions and current-account convertibility of the taka. The recent withdrawal of two restrictions, relating to remittances of foreign exchange for education abroad up to the secondary level and for maintenance of families abroad by the Bangladeshi nationals, has not been mentioned in the paper.

2. He agreed with the author that the remaining restriction on private borrowings from foreign sources needed to be removed.

3. He contended that even in the absence of two-way convertibility, the foreign exchange retention benefit of

exporters was valuable to them as they could use it to meet part of their import needs or foreign exchange expenses or keep it in a term deposit account earning interest comparable to Euro-dollar or Euro-sterling deposit rates at international money centers. Mr. Haque agreed, however, that an examination of potential problems resulting from the absence of two-way convertibility was warranted.

4. While agreeing that access to imports, especially for exporters, should be made as easy as possible, he did not think this required allowing imports more liberally without the backing of letters of credit (L/Cs), which was an internationally recognized practice. The idea of allowing non-L/C imports to "a satisfactory extent" lacked clarity as to what constituted a satisfactory extent. A more reasonable approach would be to simplify L/C procedures and reduce their costs, if these were of any significance to the importers.

5. He thought that foreign exchange restrictions for business and personal travels had been relaxed considerably. The basis of recommending the doubling of the present exchange quotas for travel was not based on any clear rationale. He, however, agreed that the Bangladesh Bank could revise the travel quotas on the basis of examination of cases of requests for foreign exchange in excess of the present quotas.

6. He strongly endorsed the recommendation for withdrawal of the restriction on access to cash foreign exchange for exporters who were importing under back-to-back letters of credit (L/Cs). He cited the large amount of such imports, about US $1.5 billion, covering some two thirds of the total working capital needs of exporters, the higher cost of such imports on deferred payment basis, the limited use of cash foreign exchange under the Export Development Fund, the current favorable foreign exchange reserve situation and the move towards a more liberalized foreign exchange regime as justifications for allowing access to cash foreign exchange for exporters operating under the back-to-back L/C basis. Mr. Haque estimated that a revolving fund of some US $500 million

was needed to allow cash foreign exchange for imports involving a value of US $1.5 billion annually.

7. He endorsed the author's recommendation for removal or further relaxation of remaining foreign exchange controls to render the taka convertibility measure more meaningful. He cited some remaining exchange restrictions such as (1) a limit on the debiting of non-resident taka accounts for various purposes without reporting to the Bangladesh Bank, (2) on excess baggage charges for Bangladeshi nationals, and (3) on gift packets sent abroad. These were all fixed long ago and here not been revised upward.

8. He also commented that deregulations should be at the same time accompanied by procedural simplifications and increased vigilance and monitoring.

9. With respect to quantitative import controls, Mr. Haque observed that there was hardly any scope for disagreement about the need for removal of such controls. However, he thought that it was not easy to ensure quality of drugs simply by putting a ban on the sale of sub-standard drugs. He also remarked that frequent changes in import policy were not desirable. In this context, he cited the example a ban on the imports of eggs which had been removed but was then later reimposed in the face of strong opposition from poultry farms. It was perhaps not expedient to again remove the ban immediately. He also thought there was perhaps need for continuing the existing pre-shipment certification restriction on imports of hatching eggs. He also expressed reservation about the wisdom of removal of quantitative restrictions on combat cloth and second-hand clothing.

10. Mr Haque expressed his general agreement with the author's recommendations for removal of export controls. He thought that at the same time it was necessary to streamline the procedures and formalities faced by exporters. Procedural delays associated with the duty drawback facilities and delays at ports in clearing goods needed to be curtailed.

11. While endorsing the author's recommendation for licensing new private banks to increase competitiveness in the banking sector, Mr. Haque suggested that simultaneous restructuring of the nationalized commercial banks for privatization needed to be undertaken.

12. With respect to the recommendation for lifting of interest rate bands for loans to agriculture, small and cottage industries and exports, he thought that the continuation of the concessionary rates of interest for those priority sectors, at least for some time, was in order. Concessionary interest rate for export financing was used in the East Asian Miracle countries and this was one of the factors which accelerated their export growth.

Comments by Dr. A.K.A. Mubin:

Dr. A.K.A. Mubin, Joint Secretary, Finance Division, Ministry of Finance, the second designated discussant, made the following comments:

1. He first made a general comment that the report was very useful and action-oriented and that various agencies concerned should study the report and take appropriate actions.

2. One area missing in the report which needed to be researched, according to Dr. Mubin, was the problem of access to bank finance, the delays involved and the inability of the banks to appraise loan requests, etc. The banks were found, even in a now liberalized situation, not so responsive to the financing needs of their clientele.

3. With respect to the system of Government-directed credit to the jute sector, Dr. Mubin remarked that this was an interim arrangement linked with the restructuring undertaken by the Government of the jute sector and of a huge bad debt (over Tk. 40 billion) owed by the jute sector to the banking system, which involved an arrangement for loss sharing by both

the Government and the jute sector. Restructuring of this debt was necessary for putting the banking system in order such that it could operate more efficiently on a market-oriented bank-client relationship basis.

4. With regard to the author's recommendation for an expansion of the credit guarantee scheme, he commented that although such a scheme had been in operation for the past four months, the initial response was found to be very marginal. Further research was needed to explore the reasons why the scheme did not seem to have much appeal and what steps were needed to activate it.

5. He remarked that despite the oligopolistic structure of the banking system dominated by the nationalized commercial banks (NCBs), the private banks were found to be less responsive in downward adjustment of interest rates than the NCBs. Dr. Mubin thought that this situation probably called for strengthening of the prudential regulatory system for controlling the banks.

6. In the area of quantitative controls on imports, Dr. Mubin thought that their possible elimination (on trade grounds) was in the final stage of implementation. Citing the example of problems faced by private importers in clearing imported diesel oil, he perceived the need for identification of other constraints as well such as legal constraints and difficulties faced with customs. He also saw a need for simplification of import procedures to be incorporated in the study. A study on import procedures was carried out in the late seventies.

7. According to Dr. Mubin, another element missing in the study was an analysis of changes in effective protection received by industries. The Government was committed to reducing that protection and to that end it had been reducing the import tariffs. Maximum tariff had been reduced to 75 percent. The policy was to reduce the maximum tariff to 45 percent and any tariff protection higher than that would require vetting by the National Tariff Commission (NTC). Dr.

Mubin thought that it would have been useful if Dr. Rab could have also analyzed the capability of the NTC to decide on the appropriate level of tariff protection and on the appropriate period of such protection or, if such capability was missing, how the NTC could be strengthened to do such analyses.

8. He observed that another important area was enforcement of commercial laws, where reforms were proceeding slowly.

9. His final comment was that the study did not sufficiently elaborate on how the convertibility of the taka was meaningless and how it could be made meaningful.

Mr. Abdus Samad, Member of the Executive Council of the Board of Investment raised the problem of access to credit. He suggested that the branch banking system, in which decisions on loan applications were processed at the head offices of the banks, was responsible for the delays faced by clients in getting loans. He also observed that the commercial banks were not used to serve the industrial investors' credit needs and were ill-equipped to do so due to lack of requisite training of the officials. He observed that the project profiles submitted for loans were also often found unworthy to justify risking credit to fund them. The debt equity ratio at 70:30, he remarked, also did not enable all prospective investors to get bank loans because of their inability to put up the requisite equity. Mr. Samad also commented that the rate of interest was not a real problem for industries; the real problem was the delay and harassment entrepreneurs faced with the banks.

Mr. Rashed Maksud Khan, Director, the Dhaka Chamber of Commerce and Industry (DCCI) and Deputy Managing Director, Bengal Fine Ceramics, endorsed the necessity for training bank officials to serve industries. He thought that in providing industrial credit, the NCBs were more helpful than the private banks. The private commercial banks were interested in financing trade and commerce only. The banking procedures were too lengthy. This was because some bank managers were not competent to process loan requests. Hence the training of bank officials was essential.

Turning to interest rates charged by commercial banks, he noted that these were linked with interest rates charged by the Bangladesh Bank. Hence a reduction in commercial bank rates was not possible without a reduction in those charged by the Bangladesh Bank. Mr. Khan also suggested that, to make them more effective, all banks and financial institutions including the DFIs needed to be made autonomous, free from any influence from the Government, as they had been before independence.

Dr. C.A.F. Dowla, Advisor to the DCCI and Economic Editor of the Financial Express, first made a general comment that if controls and regulations were required for the industrial development, the Soviet Union and the Eastern European countries would be the most developed countries of the world. Controls and regulations were not needed. What were needed were some transparent rules and procedures that had to be maintained for industry, business and trade. He then observed that the practice of calculating the interest charges at a compound rate compounded the problem of investors as interest charges became too heavy even before an industry came on stream. Interest needed to be simple and low. He also referred to attempts by the Government to control investments on the pretext of over-saturation as being contradictory to the free market philosophy. He observed that lower-level officials in the bureaucracy were a real problem. They needed to be trained to become private sector development-oriented. He referred to a seminar sponsored last month by the American Embassy, where bureaucracy was identified as the number one problem of this country. Finally he remarked that the exchange rate was not appropriate; it was overvalued and this hurts export industries.

Mr. Mahbub Jamil, President, Foreign Investors' Chamber of Commerce and Industry, observed that the requirement of collateral much in excess of the requested loan (three times the loan amount) was the biggest problem in access to bank finance.

In response to the discussants, **Dr. Rab** observed that he appreciated the illuminating comments and would like to take note of the new points while finalizing the report. He explained that some of the problems raised such as those of access to capital, high interest rates, high utility rates, protection and tariff anomalies, and exchange rate mismanagement could not be dealt with within the framework of the study under discussion, since its purpose was to solely concentrate on regulatory issues as comprehensively as possible. In this connection, however, he mentioned that PIAG had produced a separate paper on exchange rate management policy.

Concluding Remarks by the Session Chairman:

The Session Chairman **Mr. Kamaluddin Ahmed** then made a number of observations. With regard to the interest rate bands for lending to three priority sectors, he observed that these bands did not seem to be a serious problem since most of the interest rates charged by banks were not found to be either near the top or bottom of the bands. However, he disclosed, the Bangladesh Bank was reviewing the need for change in the present policy. Regarding downward inflexibility of interest rates, even after lowering of the bank rates, he remarked that this was partly due to newly imposed prudential regulations to protect against bad debt and also because commercial banks were not supposed to serve industries. With overdue loans accumulating and because of losses incurred in the past, the development financing institutions, Bangladesh Shilpo Bank (BSB), Bangladesh Shilpo Rin Sangstha (BSRS) and Bangladesh Krishi Bank (BKB), had become more conservative, he remarked. The nationalized commercial banks (NCBs) had a large share of loans in priority sectors from where loans could not be recovered. The NCBs were lending to industries, because they were directed by the Government to do so. On the other hand, private banks remained in a safe zone without going in for financing industries.

Referring to the branch banking system in place in Bangladesh, he observed that this was in order as profit-making branches served as cushion for those making losses. Bangladesh could not afford a unitary system allowing bank failures because this would have shaken the confidence in the banking system. Referring to the calculation of interest at a compound rate, he attributed this practice to the fact that commercial loans were basically meant to be on a short-term, 3-month, basis and remarked that the compounding practice did not raise much the overall interest rate payable by the borrowers and hence this problem could not be a major issue. He also observed in this regard that investment in this country was not interest-responsive.

In connection with the policy on private foreign borrowing, Mr. Ahmed observed that the terms that were currently being used for automatic authorization of such borrowing were quite reasonable. About the issue of convertibility of the taka, he observed that the convertibility should not be confused with the free float of the taka; the two were separate things. He further observed that he could not support a free float policy now since the volatility of the exchange rate and/or a possible revaluation of the taka which this policy could lead to did not justify a free float policy at this stage. Regarding the issue of reconvertibility of foreign exchange retention benefits (5 to 10 percent of export earnings), he disclosed that this question was being reviewed by the Bangladesh Bank together with a review of the present size of the retention benefit.

About the case for more liberal imports on a non-letter of credit (L/C) basis, he observed that the L/C requirement was for the benefit of both importers and exporters. This enables them to recover their money in case of default. This policy, however, was not made by the Bangladesh Bank, but by the Ministry of Commerce.

Regarding the current exchange control policy for personal and business trips, he observed that with the further relaxations allowed for business travels as announced by the Bangladesh Bank on 28 March 1994, the exchange restrictions had been sufficiently relaxed.

Discussion Session 3

LABOR REGULATIONS AND GENERAL LEGAL REFORM ISSUES

This session was meant to be devoted to a discussion of the remaining parts the PIAG study, i.e., labor regulations and general legal reform issues. However, the session's discussions were entirely directed to labor issues. It was chaired by Mr. Latifur Rahman, President of the Metropolitan Chamber of Commerce and Industry (MCCI).

Comments by Mr. Anis ud Dowla:

Mr. Anis ud Dowla, Former President of the Employers' Association, Chairman of ACI Limited and Member of the National Labor Law Reform Commission, the first designated discussant, made a general comment that the labor laws of Bangladesh were good but what was lacking was their implementation. He observed that most of the issues raised in the report had been addressed by the Labor Law Reform Commission which, he disclosed, had recently finalized its report. He further disclosed that the Commission, where both employers' and workers' viewpoints were represented, was able to resolve all outstanding contentious issues except one, that relating to the problem of whether outsiders including ex-employees could engage in trade union activity. Worker representatives maintained that they could, while the Commission had recommended that such people could not become members of any trade union. He also disclosed that the National Labor Reform Commission had recommended a three-year moratorium for trade union activity in new industrial enterprises. He expressed satisfaction observing that the Commission had done a very good job and the report completed was a comprehensive piece of legislation which embraced some 42 existing labor law acts or ordinances of the country.

Mr. Dowla strongly endorsed Dr. Rab's covering of the issues of Government intervention in labor issues and of centralized wage determination in public enterprises. With regard to the former issue, he suggested that depoliticization of labor was of paramount importance for improving, the labor-management relations in Bangladesh and for this the Government needed to be persuaded to give up labor politicization. Workers' education would also help in this regard. With respect to the latter issue, he remarked that the current practice of centralized wage determination negated the universally recognized norms of the firms' ability to pay and the workers' productivity.

Mr. Dowla further commented that some of the issues raised in the report were not major ones, such as those relating to denial of the dismissed workers' rights to termination benefits, withdrawal of the curbing of the employers' powers to change service conditions of union executives, and reduction of the excess of remuneration paid on festival days. He observed that while granting of such concessions to the employers were welcome to them, those were not of very material significance to the costs of business. He also thought that introducing labor employment on fixed-term basis rather than giving him a permanent status was not a realistic approach. Finally, he observed that labor laws were not a problem. The real problem that needed to be tackled was that employers were not being allowed to take recourse to the laws in their favor.

Comments by Syed Nizamuddin:

Mr. Syed Nizamuddin, Program Officer, World Bank Resident Mission, the second designated discussant, then presented his comments, which focused on issues relating to wages and termination benefits and their implications for competitiveness of labor costs and employment generation. Strongly supporting the view expressed in Dr. Rab's report, he emphasized that centralized wage determination in the public sector was a major problem; such wage fixation was not only undesirable, it was also not sustainable as it was not consistent with public enterprises' financial performance. Like in India and Pakistan, he suggested, public sector wages should be revised through collective bargaining.

Turning to the current practices of sectoral minimum wage setting by the Minimum Wages Board, for sectors where labor was not sufficiently well organized to be able to bargain collectively, he remarked that while there would continue to be a need for some form of wage protection, the current practices needed to be reviewed as the institutional capacity and analysis on which the current practices were based were weak.

Mr. Nizamuddin also questioned the wisdom of the Bangladesh Export Processing Zones Authority's practice of setting the minimum wage in US dollar terms for industries in the export processing zones (EPZs). Such a practice discriminated against other areas and was also unrelated to the productivity of workers, when their remunerations increased with currency devaluations.

Regarding the proposal for a national minimum wage, Mr. Nizamuddin remarked that such a wage, while was politically appealing, neither necessary nor desirable or useful to labor. India and Sri Lanka had no national minimum wage. Pakistan had introduced a minimum national wage, but the wisdom of this was being seriously questioned by concerned people.

In regard to workers' termination benefits, Mr. Nizamuddin remarked that the severance benefits in Bangladesh with gratuity at a minimum rate of one month's pay per year of service were high compared to those in India and Sri Lanka, where gratuity was calculated at a minimum rate of a half month's pay for every year of service, with a ceiling on the absolute amount in India. He also suggested that the contributory provident fund, which was not yet a statutory requirement in Bangladesh, should not be made so as it would raise the severance costs and affect prospects for employment creation.

Mr. Nizamuddin strongly endorsed the suggestion of the report about the desirability of a provision in the law for fixed-term contracts. The law required that a probationer had to be given a permanent status within a maximum period of six months. He pointed out that it would be highly desirable to provide the employer the flexibility to recruit an employee on a fixed-term contract, which could be periodically renegotiated and renewed. He noted that this would also save the employer the requirement of going through the tedious process of determining the termination benefits at the end of the worker's contract.

Finally, on the question of bilateral agreements between the Government and the Sramik Karmachari Oikya Parishad (SKOP) referred to in the report, Mr. Nizamuddin supported the view that such agreements were undesirable and remarked in this connection that the potential of the forum created for tripartite reviews, the Tripartite Consultative Committee (TCC), was being seriously under-utilized. He suggested that the TCC needed to be reactivated to deal more effectively with labor and employment issues.

Mr. Humayun Shamsul Kabir, Joint Secretary, Ministry of Labor and Manpower (MOLM), explained that recently the Government had begun a number of steps to improve enforcement of labor laws and labor-management relations. He mentioned that among the steps were the following:

1. Submission of proposals prepared by a committee, set up in 1992 by the MOLM, to the Administrative Reforms Commission to upgrade the Department of Labor and the Department of Inspection. The former department, which was responsible for looking after the enforcement of labor laws, maintaining industrial peace and resolving labor disputes, had not been upgraded since 1972.

2. Reactivation of the Tripartite Consultative Committee (TCC) formed with 45 members, 15 each from Government, employers and workers.

3. Formation of a committee by the TCC, with the Secretary of the MOLM as Chairman, to suggest measures to improve industrial relations.

4. Submission to the TCC of two reports on workers' productivity by a Productivity Committee, one for the jute industry and the other for the textile industry.

5. Formation of the Labor Law Reform Commission, in 1992,

which was a tripartite body, and the recent finalization of its report.

6. Amendment, in 1993 of the Industrial Relations Ordinance to give the Chairmen of Labor Courts exclusive power to dispose of cases.

7. Preparation of proposals to strengthen the four Industrial Relations Institutes of the country.

8. Efforts by the Government to strengthen the Minimum Wages Board and the Labor Courts.

On the centralized system of wage fixation for public sector workers, Mr. Kabir remarked that while the decentralized collective bargaining process was an ideal system, there was some political difficulty in suddenly changing the present system which had been in place since 1973. According to him, in a decentralized system, management could be forced by workers to agree to extra benefits, which could not perhaps be extracted in the centralized system.

He disclosed that the Minimum Wages Board had taken up 14 sectors to determine sectoral minimum wages and had finalized proposals for 5 to 6 sectors. On the national minimum wage question, he observed that the Government had not yet given effect to the recommendation of the National Wages and Productivity Commission and would take into consideration the general public opinion about it including the opinion expressed in the seminar.

Dr. Nazmul Hossain of USAID Office of Economics and Enterprise observed that there was a serious dearth of reliable and consistent information over time on labor strikes and disputes and their sources. To improve industrial relations, availability of such information was important, he commented, and suggested that some independent bodies like chambers of commerce and industries could play a useful role in collecting these statistics.

Mr. Shamsuddin Ahmed, a Director of the Dhaka Chamber of Commerce and Industries, alleged that outsiders were brought in by the Labor Department in tripartite talks on labor disputes in his establishment. To this, **Mr. Anis ud Dowla** responded by saying that according to the labor laws, there was no scope for entertaining outsiders in such talks except ex-employees who were part of the collective bargaining agent (CBA). The **Session Chairman** brought the allegation raised by Mr. Shamsuddin to the attention of the representative from the Ministry of Labor and Manpower and requested them to take proper note of the allegation.

Dr. Stuart Callison, Chief of the Office of Economics and Enterprise of USAID, observed that he was concerned about the current minimum wage laws in Bangladesh. He observed that while he understood the politics behind the pressure for minimum wage laws in every country, the trade-off between such laws and employment and poverty reduction goals was very serious for Bangladesh. He noted that raising the income of some 2 to 3 million workers in the formal sector would be at the expense of 42 million informal day laborers.

Dr. Abdur Rab observed, in a brief response to comments made, that he very much appreciated the perceptive and revealing comments. Particularly referring to Mr. Anis ud Dowla's comments, he observed that he was looking forward to seeing how far the Labor Reform Commission's report addressed the outstanding labor issues. Echoing Mr. Callison's concern, he observed that it was very important that wages in Bangladesh were determined through the operation of competitive market forces, which in turn would lead to maximum employment in the country.

Concluding Remarks by the Session Chairman:

The Session Chairman, **Mr. Latifur Rahman**, in his concluding remarks, observed that while recommendations of the report were well thought out, it was gratifying to know that the Labor Law Reform Commission had apparently done its job and addressed most of the labor law issues described in the report with a tripartite consensus. He hoped that if the Commission's recommendations were promptly accepted by the Government, it would resolve some of the burning labor issues.

He agreed with Mr. Anis ud Dowla that in view of lack of a general safety net for workers in Bangladesh, employers needed to adopt a humanitarian approach toward labor. It was, therefore, not necessary for employers to deny the termination benefits to dismissed workers. About the problem of labor militancy, Mr. Rahman remarked, such a problem was often due to inept handling of labor problems by the employer management.

Mr. Rahman further observed that a matter of great concern to the employers was the problem of politicization of labor by the ruling and opposition political parties. Such politicization was easy as the political parties found it convenient to play with the relatively small corps of the formal labor force. He underscored the need for realization at the top that such politicization did great harm to the interests of the economy at large. He remarked that the lack of such realization led to the (illegal) creation of the SKOP with all labor federations bound together. These developments were political in nature. Mr. Rahman again observed that it was encouraging to see that steps had been taken by the Labor Law Reform Commission to address some of these issues and hoped that the Government would implement the Commission's recommendations at an early stage.

Vote of Thanks by Dr. Ronald P. Black

The seminar came to an end with a vote of thanks presented by PIAG's Chief Technical Advisor **Dr. Ronald P. Black.** At the outset he observed that the comments and inputs made by the participants in the seminar would be duly taken into account for possible integration into the final report. He disclosed that in accordance with a suggestion made by Secretary, Ministry of Industries, a paper incorporating the major points and issues discussed and recommendations made in the seminar would be prepared and circulated to the participants for inviting their further reaction. This would be, he said, part of the continuing dialogue which the PIAG project would like to maintain with all concerned and which would hopefully lead to further simplification and, where needed, removal of regulations.

Dr. Black then thanked the Ministry of Industries (MOI) for extending necessary support to the PIAG project for organizing the seminar, the Metropolitan Chamber of Commerce for providing their fine facilities for holding the seminar, and the USAID for its support to PIAG in terms of both funds and wise suggestions. He thanked Mr. A.N.M. Eusuf, Principal Secretary to the Honorable Prime Minister for inaugurating the seminar. He thanked Mr. A.H.M. Abdul Hye, Secretary, the MOI, for chairing the overall seminar and for giving necessary support to the study when it was launched. Dr. Black then thanked Messrs Mahbubur Rahman, Kamaluddin Ahmed and Latifur Rahman for chairing the respective discussion sessions. He expressed his deep appreciation and thanks for the valuable contributions made by the designated discussants and other participants to the workshop. He thanked Mr. Syed Yusuf Hossain, Additional Secretary, MOI and the PIAG Project Director, for giving all necessary logistic support for organizing the seminar. Finally he thanked the PIAG Deputy Project Director Mr. Imdadul Hoque and the PIAG staff for their support to the seminar and the author of the PIAG study, Abdur Rab, for providing the basis for a stimulating day.