**DRAFT**

**Reducing Cost of Doing Business to Spur Domestic and Foreign investment**

*G.M. Khurshid Alam*

**I. Introduction**

**1.1 *Background.*** Bangladesh has been on a transformation path with the manufacturing sector driving exports and job growth resulting in sustained robust average growth in both GDP and in per capita GDP, facilitated by some conducive policy reforms. From here on, the prospects of rapid growth with extensive job creation requires a high-performing and diversified manufacturing sector which will remain, for some time to come, the main driver of growth in Bangladesh.

Bangladesh has continued pursuing that strategic path, and the inclusive growth strategy in the Seventh Five Year Plan, which reflects continuation of the major policy that had been articulated in the Sixth Plan. The cornerstone of this inclusive growth strategy has been a strategy of job creation through employment-intensive and export-oriented manufacturing growth which will be able to absorb the army of additional workers that will continue to enter the labor force consistent with Bangladesh’s demographic transformation. As already factored in the 7th Five Year Plan and the Perspective Plan, private sector will be the driving force in this endeavor for which higher levels of private investments is an absolute necessity. Bangladesh had already attained sustained average growth of 4.8% in the nineties, 5.8% in the period 2001-2010, and 6.3% during 2011-2015 in the current decade. Driven by a rising rate of national savings, the rate of gross domestic investment as a percent of GDP has been on the rise – expanding from a low of 10% of GDP in the 1970s to 28.9% with private investments at 22.1% in FY2015.

Within its medium term macroeconomic framework, the Seventh Plan expects gross investments to reach 34.4% of GDP by FY20 of which private investments are expected to reach 26.6%. While gross investments have been growing, but that has been mainly from higher public sector investments. So there is the challenge of getting higher levels of private investments (both domestic and FDI) so as to attain the levels envisaged under the seventh five-year plan. The slow pace in generating higher levels of private investments indicates that private sector has been facing challenges in policy, regulatory needs, infrastructural and other investment climate related challenges, which need to be redressed.

The Seventh Plan has targeted to attain an average real GDP growth rate of 7.4% and creating good jobs for the pool of unemployed and the new entrants to the job market by increasing the share of employment in the manufacturing sector from 15% to 20%. This increased share of employment is hinging on achieving an average of 10.9% growth in industry over the plan period with manufacturing reaching a growth level of 12.6% in FY 20.

**1.2 Goals and Strategic Vision**

The broad objective of the study isto highlight the main regulatory constraints to private investment, both domestic and foreign, based on available evidence from available data on Bangladesh investment climate and cross-country experiences. The study focuses on strategies for increasing levels of private investment, both domestic and foreign, in light of the projected structural transformation that is envisaged for a rapidly growing economy in the context of globalization. The thrust is on identifying the challenges and opportunities for investments based on analysis of the prevailing investment climate in Bangladesh, and also looks for options and strategies for making improvements. The diagnosis is done on the basis of local and global experiences using the survey data, the Global Competitiveness Index (GCI), the Global Logistic Index (GLI), and Doing Business (DB) index, compiled by the World Economic Forum (WEF), the World Bank, and the International Finance Corporation (IFC) respectively. In this context the “Doing Business” environment and key institutional, regulatory bottlenecks and market structure that impedes private investments in Bangladesh will be looked into, with the objective of drawing out strategies for attracting higher levels of domestic and foreign investments. Based on that diagnosis the paper provides suggestions for policy reforms.

**1.3 The strategic scenarios and targets for moving Bangladesh to trajectory to become a High Income Country (HIC) – the 2041 vision.**

The GED of the Planning Commission has postulated a scenario whereby Bangladesh could traverse to the HIC status around 2041 hinges on the need for Bangladesh to be able achieve its GDP growth target of 8% by FY2020, and then maintain an average growth rate of 8% beyond FY2041. Table 1 below provides a summary of that GED policy scenario. As a result, a key outcome of this plan policy scenario is that Bangladesh could become an UMIC by FY2031; and be on a path to be a HIC around FY 2041. This scenario envisages that Bangladesh’s per capita income would be around USD 5,480 in FY31 and climb to USD 23,302 in FY41, while maintaining 8.3 percent growth rate on an average from FY2016 to FY2046.

These per capita income figures exceed the corresponding thresholds for HIC as defined under the WB guidelines. Indeed, projections by the General Economics Division (GED) of the Bangladesh Planning Commission shows that Bangladesh could cross the UMIC threshold by the target year FY31 and be high income country around FY41. As will be shown later, this income expansion path for UMIC will be quite steep and challenging, and will require not only many policy reforms but also, especially, a massive investment effort (See Figure 8 below).

**Table -1: Summary of Policy Scenario**

| **Key Outcome** | **2030** | **2041** | **2046** |
| --- | --- | --- | --- |
| Extreme poverty | 0.4 | 0.0 | 0 |
| Moderate Poverty | 8.3 | 4.1 | 2.2 |
| Upper Middle Income Country | **√** |  |  |
| High Income Country |  |  | **√** |
| Key Drivers: |  |  |  |
| I/Y ratio | 36.5 | 38.2 | 38.5 |
| Public Investment to GDP | 8.6 | 9.0 | 9.0 |
| Private Investment to GDP | 27.8 | 29.2 | 29.5 |
| Labour force participation | 63.5 | 68.0 | 70.0 |
| Male | 82.0 | 82.2 | 82.2 |
| Female | 44.9 | 53.7 | 57.7 |
| Employed People, In million | 86.2 | 101.2 | 107.5 |
| TFP | 3.4 | 4.3 | 4.4 |
| Capital | 5.3 | 4.6 | 4.8 |
| Labour | 4.1 | 3.6 | 3.4 |
| Export/GDP ratio | 24.4 | 32.5 | 38.2 |
| Remittance/GDP ratio | 6.7 | 5.3 | 5.0 |
| FDI to GDP ratio | 3.8 | 4.2 | 4.4 |
| Public Debt to GDP | 37.1 | 40.2 | 41.5 |
| External | 10.8 | 14.5 | 16.1 |
| Domestic | 16.3 | 25.7 | 25.4 |
| Memorandum Items: |  |  |  |
| Growth rate (%) | 8.2 | 8.4 | 8.5 |
| ICOR | 4.4 | 4.6 | 4.6 |

**Source: GED Projections**

Under this forward looking scenario, Bangladesh economy has also been projected to experience major shifts in its economic structure and the sources of employment generation (Figure 1 and 2 below), with manufacturing having the highest share of GDP (projected to be around 43% in 2041) with services coming down to second position (projected to be around 43% in 2041). During the period most of the employment growth is also projected to be in manufacturing (about 31% of total employment), with employment in service hovering around 43%. The biggest decline, both in terms of GDP hare and employment share is projected to be in the agriculture sector.

|  |  |
| --- | --- |
|  | |
|  |  |
| ***Source: GED projections*** |  |

***Source: GED projections***

***Desired Path to and beyond 2041 – Higher levels of Investments:***  As already indicated above, the two key drivers of this growth will be growth of share of investments (both private and public) and that of exports in the GDP of Bangladesh. The challenge for exports will be the need for its diversification and so there will be necessity of reforms in trade related policy; but it will also require higher levels of private investments particularly FDI in export oriented manufacturing to be able to diversify the exports, bring in technology, and in getting access to markets. Cross-country experience has been showing that there is a positive relationship between investment and GDP growth rate. The positive relationship explains that for economies around the world higher investment leads to higher growth of GDP.

According to the scenario analysis done by GED, Bangladesh’s desired goal of reaching HIC status around 2041 would require it to increase its investment to a minimum of 39 percent of GDP in 2041[[1]](#footnote-1) from nearly 31 percent of GDP in 2017 (Figure 3). The lion’s share of investment would be generated from the private sector (which have been projected to reach 29.2% by 2041). but it would only be possible if planned public investment can create an environment favorable for private investment and foreign direct investment.

***Source: GED Estimate***

**1.4 Lessons from Bangladesh Experience**

Bangladesh economy has been experiencing steady acceleration in economic growth over the last several decades; this pattern continued through out the Sixth Plan and also into the 7th Plan period. Following two decades of low growth during the 1970s and the 1980s, GDP growth in Bangladesh accelerated since the early 1990s, climbing from an average of 4.4% during 1991-95 to 6.4 % in 2011-16 (Figure 4). The growth rate crossed over to 7% in FY2016.

##### Figure 4: 5-Year Average GDP Growth Rates

***Source: Bangladesh Bureau of Statistics***

In per capita terms, growth rate surged from 2.2 % per year to 5.2% over the same periods. The acceleration of per capita GDP during 2010-2016 is truly remarkable and it enabled Bangladesh to cross the threshold of lower middle-income country (LMIC) as defined by the World Bank (Figure 5).

##### Figure 5: Per Capita Income (USD)

***Source: Bangladesh Bureau of Statistics***

***The Rate of Investment – the growth driver.*** Investments and exports have been the key drivers of Bangladesh growth success story. Bangladesh’s development success so far has been accumulation of capital (capital deepening) resulting from rising investments, which has resulted in a structural change of the economy with manufacturing sector becoming increasingly important that has so far positively impacted development of Bangladesh. This is consistent with the growth experiences of East Asia when they started their journey from their low-income stage. The investment rate expanded from a low of 10% of GDP in 1970 grew to 28.9% in 2015. Private investment climbed from a low of 10.6% of GDP in FY1990 to 15.2% in 2000 to 21.6% of GDP in FY2010. In many ways these 20 years transformed Bangladesh from a regulated economy to a private investment-led economy. ***This is an important milestone and lesson-learnt as it demonstrates that private investments respond well to steps that improves ease of doing business, reduces its costs, and brings certainty from any deep policy and institutional reforms.***

On the public investment front, however, the rate declined from 7.8 % to 4.7% between FY2000 and FY2010 owing to weak tax revenue mobilization and growing current expenditures. There was then a reversal of this trend over FY2010-FY2016. Public investment recovered well, growing to 7.6% of GDP in FY2016. The historical growth of investments between FY1990 and FY 2016 is presented below in Fig 6.

##### Figure 6: Growth of Investment (% of GDP)

***Source: Bangladesh Bureau of Statistics***

**2. Some Policy Challenges:**

The rapid growth in private investment rate from 10% of GDP in FY1990 to 22% in FY2010 did not happen by accident. A number of good policies including sound macroeconomic management, trade and investment deregulation, the expansion of infrastructure services and expansion of labor and quality improvements contributed to that effort. A detailed review of these determinants is available in Ahmed (2005; 2006). Sound macroeconomic management has been a hallmark of economic policy making in Bangladesh. Occasional hiccups and deviation from this path were quickly corrected and on average the long-term trend of various macroeconomic management indicators show a facilitating environment for the expansion of private investment. The stability of the macroeconomic environment has been a major enabler of the rapid expansion of private investment (Ahmed 2015).

**Investment deregulation:** In the 1970s and 1980s Bangladesh manufacturing and organized services were characterized by a domination of state-owned enterprises and state controls over prices, investment and external trade. The deregulation process started in the 1980s but gained momentum after 1990. Since then, there has been a major and progressive investment deregulation to boost domestic and foreign investment. The deregulation effort has involved privatization, removal of quantitative restrictions, simplifying business registration process and encouraging foreign investment through relaxation of ownership restrictions.

**Trade liberalization:** Much of the trade liberalization happened during 1990-2005. Although Bangladesh was a late starter compared with other developing countries including in South Asia, the magnitude of liberalization is impressive when measured against the starting point. This involved virtual dismantling of almost all quantitative restrictions on trade, sharp reduction of average trade tariffs and the establishment of the free trade zones (Export Promotion Zones (EPZs)). The hugely positive response of the readymade garments (RMG) sector to trade liberalization and related other policies (such as back-to-back LCs, fiscal incentives and access to concession trade finance) is illustrative of the role trade liberalization in promoting investments, exports, GDP growth and employment.

**Fiscal incentives**: To attract foreign investment and promote domestic investment the Government offers a fairly liberal set of fiscal incentives involving tax holidays, lower income tax rate, accelerated depreciation and low import duties on capital and intermediate goods imports. Exports also enjoy duty drawback benefits. In many ways, the fiscal incentives in regards to exemption of profits or low rates offered to selected sectors (RMG) might be too liberal and an overkill and as such needs to be re-examined to avoid an unnecessary erosion of the tax revenue base.

**Supply of labor and employment policies**: The abundant supply of labor is a major positive contributor to private investment and expansion of manufacturing production and exports, especially in RMG. Low wage cost remains a substantial advantage for Bangladesh that contributes to cost competitiveness in labor-intensive manufacturing such as RMG. Government policy in regards to education and labor markets has played an important facilitating role. Bangladesh labor markets relating to all three major sectors (agriculture, manufacturing and services) work flexibly and the transaction costs of employment in terms of hiring, termination and wage setting are among the lowest in developing countries and certainly within South Asia (Ahmed, 2015). While this flexibility is a big plus, recent developments in the RMG sector suggest that the absence of prudential regulatory norms regarding worker safety and social insurance including coverage of accidents is a serious problem that needs to be corrected.

The above analysis suggests that the returns to good policies can be substantial. But it also raises two questions: first, why the FDI response in Bangladesh has been sluggish in comparison with the dynamic Asian economies; and second what explains the stagnation of the private investment rate over the past few years? The answers to these two questions are inter-related and can be obtained by reviewing the emerging constraints to investment.

**3. Bangladesh Investment trend – the Issues and Challenges:**

***Getting desired higher levels of private investments has been a key challenge.*** While the Bangladesh economy has done well in terms of GDP growth and exports, one negative development is the near stagnation of the private investment effort in recent years. The government to support achieving its overall growth targets had also set private and public investment targets over both 6th FYP and 7th FYP. The 6th FYP had targeted an increase in the investment rate growing from 24% of GDP in FY10 to 32% by FY15. The worrisome factor is that since FY2012, the private investment as a share of GDP has remained virtually flat at around 22% (Figure 7). This is worrisome because the 6th FYP had identified private investment as a major engine of growth and exports, especially in the manufacturing sector.

##### Figure 7: The Private Investment Challenge (% of GDP)

***Source: Bangladesh Bureau of Statistics***

It should be noted that, while the current total investment rate of 29% of GDP has been adequate to sustain the investment needs of the average GDP growth rate of 6-7% overall and 5-6% per capita of the past 6 years; this may not be adequate to take the economy to the next stages of the development path involving sustained 8% overall GDP growth and 7% growth of per capita GDP that will be required to achieve the vision of Higher Income Country (HIC) around 2041. The path will be quite challenging.

As a PRI projection had shown (Figure 8 below), the income expansion path even for Upper Middle-Income Country (UMIC) is steep and requires many policies but especially a massive investment effort. In fact, both public and private investment rate must expand to enable Bangladesh move to the 8% GDP growth path and achieve the target of upper middle income (UMIC) by FY2030. The investment rate needs to go up from the present 29% of GDP to 34% of GDP to achieve 8% growth rate by FY2020 and 35% of GDP by FY2022 to sustain that effort. This substantial expansion in the investment rate is needed partly to accommodate the growing capital intensity of production in Bangladesh and partly to finance the additional 1-2% growth in GDP. As in the past, the momentum has to come from private investment.

##### Figure 8: Transition Path to UMIC (USD)

***Source: Sadiq Ahmed - PRI Projections***

As evident from Fig. 8, the projected transition path will be quite steep and challenging based on what has been achieved so far in investments, particularly private investments. Achieving a 4-5-percentage point of GDP increase in the private investment rate in the next 5 years is not an easy task, especially in view of the stagnation in the investment rate over the previous 5 years. There needs to be substantial changes in the policy and regulatory framework for private investment, with particular emphasis on attracting higher FDI inflows.

***Poor FDI flows have been a stumbling block to raising investment rates.*** A very concerning factor is that the response from foreign direct investment (FDI) has been lack luster (Figure 9). Although FDI flows have picked up recently, reaching $2.3 billion in 2015, this is still much below potential. Total FDI flows in Bangladesh are relatively insignificant in relation to total supply to developing countries (Ahmed and Sattar 2012). For example, as compared with $1.6 billion FDI inflow in Bangladesh in 2013, FDI inflows amounted to $124 billion in China, $29 billion for India, $18 billion for Indonesia and $9 billion for Vietnam.

More recently, as illustrated in Figure 10, FDI flows in 2016 amounted to $139 billion in China, $92 billion for Hong Kong, $50 billion each for Singapore and Brazil, and $42 billion for India (UNCTAD, 2017). These numbers easily dwarf the $ 2 billion or so inflow in Bangladesh. They also indicate the large FDI flows that are still available for developing countries despite prevailing global financial difficulties.

##### Figure 9: Flow of FDI ($ millions)

***Source: Bangladesh Bank***

##### Figure 10: Inflow of FDI 2016 (USD Billion)

***Source: UNCTAD, 2017***

Bangladesh had also adopted several strategies as expressed through the 6th FYP and the 7th FYP to help achieve that goal. Two such initiatives were adaption of the PPP policy and the setting up of Special Economic Zones (SEZs) under the Special Economic Zones Act 2010. Both of these initiatives were expected to help to catalyze higher levels of new private sector investments (including higher levels of FDI) both in manufacturing and exports, and also helping fill up the resource gap needed to build new infrastructure.

***Public investments for facilitating private investments:*** One of the main challenges relating to investment climate and doing business environment in Bangladesh is the huge deficiency in all aspects of quality and also quantity of infrastructure, for which public investments along with PPP investments are absolutely essential. Public investments are critical for facilitating private investments. While it is true for all aspects of public investments it is particularly true for investments in strategic infrastructure like power, energy supply, roads, railway, waterway, ports, and IT related infrastructure. As it will be shown later Bangladesh performs very poorly in terms of infrastructure quality, which negatively impacts its Global Competitive Index (GCI) rankings. All these are extremely important in reducing cost of doing business and that way facilitates higher levels of private investments. There needs to be efficient implementation of public investment through the Annual Development Plan (ADP) along with PPP investments to help Bangladesh reduce cost of doing business and thus improve its rankings in Global Competitive Index (GCI), Global Logistic Index (GLI), the Doing Business (DB) indicators *(to be discussed later*) so as to spur domestic and foreign investments.

While there has been improvement in allocation for public investments through the ADPs, an even bigger challenge is the constant is the lag in providing resources for operation and maintenance (O&M) of the infrastructure that had already been built. However, a very big disappointment has in the inability to mobilize requisite resources through PPP for infrastructure projects. Despite ambitious plans, the PPP strategy has not taken off in any significant shape for a host of reasons including institutional challenges, and the doing business environment itself stymies increased flow of private investments. The net result is a substantial shortfall in public investment rate in comparison with the 6th FYP targets, and is likely to happen during 7th FYP period, if remedial measures are not immediately taken. Unless there is marked improvement in all these indicators and come in line with countries like Korea, China, Vietnam etc. it will be challenging to attain the 2041 goal of transforming into a HIC.

***Higher levels of private investments in manufacturing sector, particularly ready-made garments (RMG), facilitated it in leading the robust GDP growth.***  The underlying growth strategy in the 6th FYP and 7th FYP had aimed at facilitating a faster transformation of the Bangladesh economy away from a primarily agrarian one towards a modern manufacturing and services oriented economy. This has yielded good results for the manufacturing sector in terms of growth in the arena of exports, domestic production, and job creation and its continuous increase in share of the GDP (Fig. 11 and 12 below). The main contributor to this robust growth performance of the manufacturing sector has been investments in the export oriented RMG sector.

The robust manufacturing growth of past decades Bangladesh has also helped in structurally transforming of the economy with share of industry in GDP rising, compensating the decline in the size of agriculture (Fig 11 and 12). Manufacturing, which accounts for 70% of industry and has been driving the structural transformation, will have to continue to lead growth acceleration for many more years to come. At the same time it has to remain globally competitive and ahead of the curve, where a high performing manufacturing sector will have to reach a high level of industrial sophistication meeting internationally recognized standards of product quality within a compliant production environment.

##### Figure 11: Progress with Structural Change

***Source: BBS***

##### Figure 12: Sectoral Growth Trends

***Source: National Accounts, BBS***

In order to measure up to the needs, our manufacturing industry has to shape a course based on the global needs and national realities; but definitely will require higher levels of capital accumulation. The presence of Global Value Chains (GVCs) could provide a mechanism for firms and farms in Bangladesh to access the world market and advanced technologies to reach that higher level of industrial sophistication and meeting internationally recognized standards of product quality within a compliant production environment. These could happen, provided the right policy and institutional support is there and if the investment climate remains conducive for private sector to increase investments (both domestic and FDI). Particularly for accessing world markets and advanced technologies and to cash on the GVC opportunity it will also be critical to have increased levels of manufacturing FDI. The government has been trying to provide support for this through setting up of SEZs.

**3.1 Improving Doing Business Environment – Bangladesh needs to do much better for attracting higher levels of investment**

The two most important determinants for private sector investment are the cost of doing business and the incentive structure. In order to spur private investments (both domestic and FDI), it will be necessary to reduce cost of doing business relative to competing countries, which in turn will provide the necessary returns to entrepreneurs in incentivizing them in taking the long-term risks of investments. This entails not only having in place investor friendly supportive policies, along with strengthened legal, regulatory and other supporting institutions, but also taking specific measures to sort out the challenges that faces investors including infrastructure, logistics, facilitating services, land and skills related challenges. This is what is usually referred to as the prevailing investment climate of country.

*Investment climate* reflects the overall business environment in the country, which not only reduces the cost of doing business but also allows private sector to operate their businesses in a more transparent and hassle free institutional setting. It is important for good investment climate to have in place policy certainty and a non-discriminatory regulatory environment, which in turn gives investors the comfort level to invest. So policy and institutions are at the core of investment climate as much as that of facilitating infrastructure.

Investor surveys like Investment Climate Assessments (ICA) or Doing Business (DB) show that what matters more for investors is the general investment climate and competitiveness of the economy. Long delays in contract enforcement, limited access to serviced land, power and gas shortages and red tape have all become major constraints to investment in Bangladesh. These are what raise cost of doing business in Bangladesh where it features very poorly and very low in almost all the indices. As indicated above primary reason for the lower-than-expected increase in private investment during the SFYP and first two years of 7th FYP has been the continued weakness in the investment climate. While some domestic private investments are coming there has been very little FDI flowing in, particularly in the manufacturing sector. The inability to attract adequate foreign private investment can only be attributed to a poor investment climate, and the better performance of FDI in neighboring countries is a reflection of this.

Capital deepening supported by higher rates of private investments (includes PPP investments in infrastructure) and robust and efficient implementation of public investments will be key driver for Bangladesh to attain its version of attainment of HIC around 2041. As manufacturing and exports will be the key vehicles achieving this visionary goal, all effort should be in ensuring a very robust response to investment needs, both from the private and public sectors. The Government needs to address this challenge much more comprehensively in order to further spur the growth of manufacturing to reach double-digit rate, and critical for this to happen is to bring about substantive improvement in Bangladesh’s *“Investment Climate”.*

**3.2 Improving Investment Climate and Reducing Cost of Doing Business is need for spurring private sector investments:**

***An efficient and supportive regulatory environment a must for improved investment climate:*** The regulatory environment for business can have a determining influence on private investment (World Bank 2004). Laws, regulations and rules are integral part of a country’s governance structure. These are implemented and enforced through a web of institutions. Complex regulations and bureaucratic hurdles tend to increase the transaction costs of doing business and thereby hurt the growth of investment. On the other hand enabling regulations that protect investor interests and simplify business transactions encourage private investment. A report by IFC’s Foreign Investment Advisory Service (FIAS) finds that the biggest problem with regulation in Bangladesh is that existing laws are not applied or enforced properly. Part of the reason for lax enforcement is regulatory capture. The FIAS study points out that very often, the chief ailment is over regulation, and, occasionally, under regulation or poor regulation. Regulations tend to be made without proper social cost and benefit analysis of regulations, and there is no practice of undertaking any Regulatory Impact Assessment (RIA) that takes into account enforcement cost, compliance cost, or the negative externalities arising from new regulation.

In today’s globalized world where capital is fairly mobile, weak domestic investment climate riddled with too many regulations and bureaucratic hurdles will not only adversely affect the inflow of foreign investment but can also cause domestic capital flight to more hospitable investment environment. These impact the Doing Business environment and the related indices where Bangladesh continues to perform poorly, and raises risks for good investors. Making the regulatory environment more business-friendly by improving governance and strengthening institutions will be a pre-requisite for sustained high growth performance of the manufacturing sector necessary for attaining UMIC status, and then moving towards the much desired HIC.

***For attaining higher levels of investments - the markets needs to function efficiently.***

An important outcome of good investment climate is a better functioning market. Effective functioning of markets, governance, and institutions are prerequisite for a vibrant private sector ready to invest at higher levels. Markets depend on a complex array of public institutions that shape the quality and effectiveness of governance, which plays a pivotal role in getting markets to work efficiently. It is critical that governments complement markets, encourage rather than penalize entrepreneurship and competition, uphold the rule of law, and limit bureaucratic harassment and corruption. In short, they should provide the foundation of good governance for harnessing higher levels of investments, which will particularly be needed for the desired manufacturing growth to take place.

***Bangladesh lags behind in different globally accepted indices relating to business environment.*** The prevailing regulatory regime of Bangladesh is to be severely challenging as has been reflected in different global indices including the Global Competitiveness Index (GCI) and the World Bank-IFC published Doing Business (DB) indicators. Review of both the GCI and the DB indicators also point out the deficiency in supportive infrastructure and Logistic facilities when compared to other countries. While inadequate regulations and inadequately functioning institutions raise cost of doing business, so also is inadequacy of supporting infrastructure and logistics. It is important to note that it is a competitive world and it is not just enough to make improvements in all of the above-mentioned constraints, but it is equally important to be ahead of competitors as those countries are also making efforts to improve.

**3.3 Bangladesh Investment Climate in Comparison to some competing Countries.**

In recent years a range of cross- country indicators of investment climate are regularly prepared on an annual cycle by specialized international agencies based on investor surveys. These indicators provide very useful data on the emerging constraints to private investment. While the implications of each constraint will likely vary by countries, the wealth of knowledge available from these global surveys can be productively used to inform policies. These cross-country comparisons are especially useful to understand why some countries are able to attract more FDI inflows than others.

***The Global Competitiveness Index (GCI)*** prepared by the World Economic Forum has now become a fairly standard reference point for assessing the competitiveness of an economy in relation to other countries in the list. The GCI measure is available as a composite index as well as by individual components that comprise the index. The individual components (12) provide fairly in-depth views about the regulatory environment faced by investors in any country as well other factors affecting competiveness including macroeconomic environment, financial services, skills, infrastructure, institutions and technology.

The trend in overall competitiveness of Bangladesh as measured by the GCI in relation to its competitors is illustrated in Figure 13. Although the number of countries covered in the surveys between 2008 and 2017 has changed slightly from 134 to 138, the relative cross-country rankings within a year are not affected. Also, the inter-temporal trend showing relative progress across countries provides useful insights.

##### Figure 13: Global Competitiveness Index (ranking)

***Source: GCI, World Economic Forum (2016-17 and 2008-09)***

The two main messages conveyed by Figure 13 are that: first, the competiveness of the Bangladesh economy relative to competitors remains a serious challenge. China, Indonesia, India, Vietnam and Sri Lanka are much more competitive than Bangladesh. And second, between 2008 and 2017 Bangladesh has made some progress with improving its competitiveness, but China, Indonesia, Vietnam and Sri Lanka have improved faster. As a result, the competitiveness gap with these countries has widened. The one exception in competitiveness performance is Pakistan. In 2008 Pakistan was well ahead of Bangladesh but its performance deteriorated sharply over the past 9 years and had fallen behind Bangladesh in 2016.

An important thing to note is that the better performing countries like Singapore, Malaysia, South Korea, and China have scores 5 and above (Table 2 below). Other catching up countries like India, Vietnam and Thailand had scores above 4. Only Bangladesh and Pakistan in the list below have 3.8 and 3.5 respectively. Bangladesh will have to aim at raising its score to above 5 in the coming years, in order to improve its rankings and make it as competitive as Singapore, South Korea, Malaysia, and China. It should be noted that these are relative rankings and other competitor countries are also striving to increase their scores and rankings. So Bangladesh will have to increase its efforts manifolds to not only catch up but also go over competitors’ scores to be able to attract desired levels of FDI.

**Table 2. Global Competitiveness Index (GCI) 2016**

|  |  |  |
| --- | --- | --- |
|  | **Rank** | **Score** |
| **Bangladesh** | 106 | 3.8 |
| **Singapore** | 2 | 5.8 |
| **Malaysia** | 25 | 5.2 |
| **South Korea** | 26 | 5.0 |
| **China** | 28 | 5.0 |
| **Thailand** | 34 | 4.6 |
| **India** | 39 | 4.5 |
| **Vietnam** | 60 | 4.3 |
| **Pakistan** | 122 | 3.5 |

***Source: Global Competitiveness Report 2016-2017, World Economic Forum***

***Doing Business (DB).*** A big component of the GCI is the regulatory environment as measured by the International Finance Corporation’s (IFC) cost or ease of Doing Business (DB) indicators. The DB indicators are very helpful to measure the progress with deregulation in terms of results on the ground, and not just regulations in the books, and as such they reflect both the regulatory gaps and associated implementation challenges.

The DB indicators provide an overall ease of doing business index ranking as well as rankings for each of the 10 regulatory areas that affect business decisions. The overall DB index for 2017 for Bangladesh and comparators based on 190 countries is indicated in Figure 14. Some interesting results emerge from this comparison. First, despite past progress, the regulatory environment in Bangladesh is substantially less favorable than competitors; it is ranked at a low score of 176 as compared with the worst performing country ranking of 190 for Somalia. Second, all other countries in the comparator list have a relatively better regulatory environment than Bangladesh.

##### Figure 14: Doing Business Rankings 2017 (out of 190)

***Source: IFC Doing Business Database***

The Doing Business challenges becomes more apparent from Table 3 below which gives a breakdown of the different components of the composite overall index. Bangladesh ranks relatively poorly in all the components of the index. Bangladesh will have to address each of the components and needs to better than the competing countries to move ahead in its rankings.

**Table 3. Ease of Doing Business Rankings, 2016**

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | Overall Ranking | Starting a business | Dealing with construction permits | Getting electricity | Registering Property | Getting Credit | Paying taxes | Trading across borders | Enforcing contracts |
| **Bangladesh** | 176 | 122 | 138 | 187 | 185 | 157 | 151 | 173 | 189 |
| **Singapore** | 2 | 6 | 10 | 10 | 19 | 20 | 8 | 41 | 2 |
| **Hong Kong** | 4 | 3 | 5 | 3 | 61 | 20 | 3 | 42 | 21 |
| **South Korea** | 5 | 11 | 31 | 1 | 39 | 44 | 23 | 32 | 1 |
| **China** | 78 | 127 | 177 | 97 | 42 | 62 | 131 | 96 | 5 |
| **Malaysia** | 23 | 112 | 13 | 8 | 40 | 20 | 61 | 60 | 42 |
| **India** | 130 | 155 | 185 | 26 | 138 | 44 | 172 | 143 | 172 |
| **Thailand** | 46 | 78 | 42 | 37 | 68 | 82 | 109 | 56 | 51 |
| **Indonesia** | 91 | 151 | 116 | 49 | 118 | 62 | 104 | 108 | 166 |
| **Vietnam** | 82 | 121 | 24 | 96 | 59 | 32 | 167 | 93 | 69 |
| **Pakistan** | 144 | 141 | 150 | 170 | 169 | 82 | 156 | 172 | 157 |

***Source: Doing Business Report 2017, World Bank***

A comparison of the results illustrated in Figure 13 and Figure 14 shows that while the regulatory environment is an important determinant of the investment climate and competitiveness of an economy, it is only one determinant. It is also important to pay attention to such other factors included in the measurement of GCI as the macroeconomic environment, labor skills, labor market, financial sector, infrastructure, technology, institutions and innovation. Progress in these other areas can compensate for the higher transaction costs of negotiating the regulatory environment while weaknesses in these other areas can strongly offset the regulatory ease of doing business (e.g. Bangladesh versus Pakistan).

***Bangladesh’s DB Rankings worsened between 2010 and 2017.*** An interesting question is how have the DB rankings changed over time? While there are some methodological challenges in such inter-temporal comparisons owing to changes in the number of countries and interpretation of the survey questionnaires, nevertheless the trend in performance is indicative of the relative policy efforts made to address the investment climate issues. Figure 15 shows the changes in relative rankings. It tells a very worrisome story. The rankings suggest a sharp deterioration in the investment climate for the private sector in Bangladesh relative to comparators. In 2010, Bangladesh was ranked at the 119th place out of 183 countries. This ranking worsened sharply over time and fell to 176th place out of 190 countries. All other comparator countries except Pakistan show improvement.

##### Figure 15: Doing Business Rankings, 2010-2017

***Source: IFC (2009); IFC (2016)***

The inescapable conclusion from all of the above is that the overall investment climate for private sector is weak in Bangladesh by both measures (GCI and DB) and has deteriorated, and requires focused attention of the Government, particularly having in place right policies, regulations, and institutions. The Government recognizes the issues and has set up three new institutions – the Bangladesh Investment Development Authority (BIDA), Bangladesh Economic Zones Authority (BEZA), and the PPP Office, all under administrative control of the Prime Ministers Office. However, policy challenges should be handled upfront and the best approach to reforming policies for improving the investment climate is to focus attention on both the regulatory environment as well as the other enablers.

**3.4 Regulatory Challenge to improving DB rankings of Bangladesh**.

Drilling down the composite DB index by its 10 individual components provides substantial insights of where the main regulatory constraints bite most. The Bangladesh 2017 rankings by components are shown in Figure 16. The four top constraints identified by DB survey responders in Bangladesh are enforcing contracts, getting electricity, registering property, and trading across borders respectively. These are followed by getting credit, paying taxes, resolving insolvency, getting construction permits, and starting a business. The ranking in these areas, especially in regard to getting electricity, registering property, and enforcing contracts, puts Bangladesh at the near bottom of the global list of countries. Getting credit, resolving insolvency and paying taxes are also problematic and involve substantial transaction costs. Some additional insights for policy challenges can be gained by looking at how ranking of components have behaved over time.

##### **Figure 16: Bangladesh Key Regulatory Constraints to Private Investment 2017** (Ranking, 190 Countries)

***Source: IFC (2010; 2017)***

Data suggest that the performance worsened for all the 10 indicators, including the three areas where Bangladesh was performing relatively well in 2010 (Figure 17). The most concerning deterioration is in paying taxes; the tax regime has become a serious bottleneck to the investment climate in recent years. There needs to be special focus in instituting major reforms in the overall tax administration with focus not just on revenue collection but also taking into consideration the need of business. In this context not only should there be clarity and certainty of tax policy but also reduce discretionary intervention that makes cost of doing business high.

##### Figure 17: Relative Regulatory Weakening Over Time

***Source: IFC (2010; 2017)***

In some areas like starting business and protecting investors, where Bangladesh had made improvements in 2010, again slid down substantially in 2017. Both these areas also need special attention, particularly to help attract higher levels of FDI. All these also reveal the difficulty in overcoming regulatory challenges and will require continuous monitoring and implementation of necessary regulatory changes.

***Relative Transactions Costs – where Bangladesh could improve?*** The implications of DB 2017 rankings in terms of transaction costs are illustrated in Table 4. The costs are given in terms of the number of procedural requirements, the amount of time involved in meeting the regulatory requirements, and some measure of financial cost of complying with the regulation. In some sense the latter two are more fundamental because what matters to a business enterprise are the transaction costs of complying with regulations in terms of time and money. Ceteris paribus, the lower the compliance cost in terms of procedures and time and money spent, the simpler and more efficient is the underlying regulatory regime.

#### Table 4: Efficiency of the Bangladesh Regulatory Regime 2017

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Regulation/Country Performance** | **Bangladesh** | **China** | **India** | **Indo-**  **nesia** | **Pakis-**  **tan** | **Sri Lanka** | **Viet-**  **nam** | **Best Performer** |
| **1.Starting a business** |  |  |  |  |  |  |  |  |
| **---No. of procedures** | 9 | 9 | 12.9 | 11.2 | 12 | 7 | 9 | 1 |
| **--Time (days)** | 19.5 | 28.9 | 26 | 24.9 | 18 | 9 | 24 | 0.5 |
| **--Cost (% of income per capita)** | 13.8 | 0.7 | 13.8 | 19.4 | 12.4 | 12.2 | 4.6 | 0 |
| **2.Dealing with construction permits** |  |  |  |  |  |  |  |  |
| **--No. of procedures** | 14.2 | 22 | 35.1 | 17 | 15 | 13 | 10 | 7 |
| **--Time (no of days)** | 269 | 244 | 190 | 200 | 264 | 115 | 166 | 28 |
| **--Cost (% of warehouse value)** | 2.7 | 7 | 25.9 | 5.1 | 7 | 0.4 | 0.8 | 0.1 |
| **3. Getting electricity** |  |  |  |  |  |  |  |  |
| **--No. of Procedures** | 9 | 5.5 | 5 | 4.8 | 5.3 | 5 | 5 | 3 |
| **--Time (no. of days)** | 429 | 143 | 46 | 58 | 181 | 100 | 46 | 18 |
| **--Cost (% of income per capita)** | 2861 | 390 | 133.2 | 357 | 1772 | 732 | 1261 | 0 |
| **4. Registering property** |  |  |  |  |  |  |  |  |
| **--No. of procedures** | 8 | 4 | 7 | 5 | 7.7 | 9 | 5 | 1 |
| **--Time (no. of days)** | 244 | 19.5 | 46.8 | 27.4 | 154.8 | 51 | 57.5 | 1 |
| **--Cost (% of property value)** | 7 | 3.4 | 7.7 | 10.8 | 4.6 | 5.1 | 0.6 | 0 |
| **5. Getting credit** |  |  |  |  |  |  |  |  |
| **--Strength of legal rights index (0-12)** | 5 | 4 | 6 | 6 | 3 | 2 | 7 | 12 |
| **--Depth of credit info index (0-8)** | 0 | 8 | 7 | 6 | 7 | 6 | 7 | 8 |
| **--Credit registry coverage (% of adults)** | 0.9 | 91.1 | 0 | 51.8 | 9.4 | 0 | 41.8 | 100 |
| **--Credit bureau coverage (% of adults)** | 0 | 21.3 | 21.4 | 0 | 5.8 | 57.2 | 14.8 | 100 |
| **6. Protecting minority investors** |  |  |  |  |  |  |  |  |
| **--Extent of conflict of interest regulation index (0-10)** | 6.3 | 5 | 6.7 | 5.7 | 6 | 6.7 | 4.3 | 9.3 |
| **--Extent of shareholder governance index (0-10)** | 5 | 4 | 8 | 5.7 | 7.3 | 6 | 6.3 | 8.3 |
| **--Strength of minority investor protection(0-10)** | 5.7 | 4.5 | 7.3 | 5.7 | 6.7 | 6.3 | 5.3 | 8.3 |
| **7. Paying taxes** |  |  |  |  |  |  |  |  |
| **--No. of payments per year** | 33 | 9 | 25 | 43 | 47 | 47 | 31 | 3 |
| **--Time (no. of hours)** | 435 | 259 | 241 | 221 | 311.5 | 179 | 540 | 55 |
| **8.Trading across borders** |  |  |  |  |  |  |  |  |
| **--Time to export: Border compliance (hours)** | 100 | 26 | 106 | 53 | 75 | 43 | 58 | 0 |
| **--Cost to export: Border compliance (USD)** | 408 | 522 | 413 | 254 | 426 | 366 | 309 | 0 |
| **--Time to export: Documentary compliance (hours)** | 147 | 21 | 38 | 61 | 59 | 76 | 50 | 1 |
| **--Cost to export: Documentary compliance (USD)** | 225 | 85 | 92 | 139 | 307 | 58 | 139 | 0 |
| **--Time to import: Border compliance (hours)** | 183 | 92 | 283 | 99 | 129 | 72 | 62 | 0 |
| **--Cost to import: Border compliance (USD)** | 1294 | 777 | 574 | 383 | 957 | 300 | 392 | 0 |
| **--Time to import: Documentary compliance (hours)** | 144 | 66 | 61 | 133 | 147 | 58 | 76 | 1 |
| **--Cost to import: Documentary compliance (USD)** | 370 | 171 | 135 | 164 | 786 | 283 | 183 | 0 |
| **9. Enforcing contracts** |  |  |  |  |  |  |  |  |
| **--Time (days)** | 1442 | 453 | 1420 | 471 | 1071 | 1318 | 400 | 164 |
| **--Cost (% of claim)** | 66.8 | 16.2 | 39.6 | 115.7 | 20.5 | 22.8 | 29 | 9 |
| **10. Resolving insolvency** |  |  |  |  |  |  |  |  |
| **--Time (years)** | 4 | 1.7 | 4.3 | 1.9 | 2.6 | 1.7 | 5 | 0.4 |
| **--Cost (% of estate)** | 8 | 22 | 9 | 21.6 | 4 | 10 | 14.5 | 1 |
| **--Recovery rate ((%)** | 27 | 36.9 | 26 | 31.2 | 43 | 46.2 | 21.6 | 92.9 |
| **--Strength of insolvency framework index (0-16)** | 4 | 11.5 | 6 | 9.5 | 7 | 7 | 7.5 | 15 |

***Source: Doing Business 2017, International Finance Corporation***

As noted, the high transaction costs of compliance with the regulatory regime in the *four areas concerning contract enforcement, getting electricity, registering property and trading across borders* are major contributors to the high cost of doing business ranking and the low inflow of FDI in Bangladesh. In some sense, these four issues are a binding constraint to FDI because while local investors would likely have a way to get through with their local knowledge and connections, the foreign investors will be heavily disadvantaged.

For example, on average it takes 1442 days to enforce a contract and the financial cost of enforcement is as high as 67% of the claim. As compared with this, it takes only 400 days in Vietnam and 453 days in China to enforce a contract; the financial cost is 29% and 16% respectively. The performance gap between Bangladesh and the best performer is commensurately much larger: 164 days to resolve a conflict involving only 9% of the cost of claim. The difficulty of getting access to electricity is equally telling.

It takes 429 days to get access to electricity in Bangladesh as compared with 58 days in Indonesia, 100 days in Sri Lanka, 46 days in India and Vietnam. Additionally the relative cost of getting electricity, measured as percentage of per capita GDP, is much higher in Bangladesh relative to comparators. The performance gap with best practice is huge. Regarding, property registration, Bangladesh takes 244 days while it is only 20 days in China, 27 days in Indonesia and 47 days in India. The transaction costs of resolving insolvency and trading across nations are similarly high in relation to the comparators. Concerning trading across borders, the time it takes complete international trade transactions and the financial cost of complying with the documentary and border clearance requirements are exorbitantly high relative to comparators and especially in relation to the best performer. This is a particularly worrisome result for export diversification.

Finally getting credit is another index where Bangladesh features very poorly. Bangladesh ranked 157 in this category (Figure 16). Bangladesh’s poor performance is a result of having very low scores (Table 4 above) in Depth of Credit information index (score of 0 compared to 8 for China,), Credit Registry Coverage (0.9% of adults versus 91.9% for China), Credit Bureau Coverage (0 % of adults versus 21.3% China).This is particularly challenging for MSME’s to access credit. Higher levels of investments in MSME’s will be important ingredient in Bangladesh’s transformation to HIC and it is here that most jobs can get created.

**3.5 Infrastructure Challenges to Reducing Cost of Doing business:**

The World Economic Forum regularly updates countries position on competitiveness based on several pillars, and infrastructure (transport and energy infrastructure) is determined as a key pillar for factor driven economies like Bangladesh. Comparison of infrastructure among different Asian countries shows that Bangladesh is quite deficient in quality of infrastructure as depicted in Table 5 below.

**Table 5: Infrastructure of GCI 2016-17**

|  |  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- | --- |
|  | **Bangladesh** | **Singapore** | **Malaysia** | **South Korea** | **China** | **Thailand** | **India** | **Vietnam** | **Pakistan** |
| **Infrastructure** | 114 | 2 | 24 | 10 | 42 | 49 | 68 | 79 | 116 |
| **Quality of overall infrastructure** | 120 | 2 | 19 | 14 | 43 | 72 | 51 | 85 | 93 |
| **Quality of roads** | 113 | 2 | 20 | 14 | 39 | 60 | 51 | 89 | 77 |
| **Quality of railroad infrastructure** | 72 | 5 | 15 | 9 | 14 | 77 | 23 | 52 | 53 |
| **Quality of port infrastructure** | 89 | 2 | 17 | 27 | 43 | 65 | 48 | 77 | 84 |
| **Quality of air transport infrastructure** | 115 | 1 | 20 | 21 | 49 | 42 | 63 | 86 | 91 |
| **Quality of electricity supply** | 110 | 2 | 39 | 29 | 58 | 61 | 88 | 85 | 121 |

***Source: Global Competitiveness Report 2016-2017, World Economic Forum***

As evident from Table 5 above, Bangladesh is also way behind all the competitor countries in quality of infrastructure, quality of roads, quality of railroad, quality of port infrastructure, and quality of electricity. Bangladesh is only ahead of Pakistan in quality of electricity. However, that may also be changing with Pakistan making large investments in low cost power generation supported by higher level of investments in transmission and distribution. It is important to note that it is way behind its competing countries like India and Vietnam. This sort of poor quality of infrastructure raises business uncertainty and risks and raises cost of doing business, and as presented above it takes 429 days to get access to electricity in Bangladesh as compared with 58 days in Indonesia, 100 days in Sri Lanka, 46 days in India and Vietnam, and the cost is 2861% of the per capita income (see Table 4 above), which is much higher than all competing countries.

What is also worrisome is that while Bangladesh made some improvement in infrastructure quality in 2013-14, going up to 110 from 130 in 2010-11; it, however, reversed in 2016-17 (Table 6). Bangladesh has slightly come down in its ranking to 114. It is interesting to note that Pakistan, which had been way below Bangladesh in country competitiveness rankings (133 compared to 110 for Bangladesh), has almost caught up with Bangladesh improving it’s ranking to 116 in 2016-17.

**Table 6: GCI Infrastructure Ranking Comparison between the 2010-11 and 2016-17 for Bangladesh**

|  |  |
| --- | --- |
| **Year** | **Global Country Ranking - Infrastructure** |
| 2016 | 114 |
| 2013 | 110 |
| 2010 | 130 |

Source: World Economic Forum, the Global Competitiveness Reports

As Bangladesh embarks its goal to be a HIC around 2041, it must ensure adequate supply of good quality infrastructure, including supply lower cost quality electricity. This will require higher levels of private investments. Bangladesh Investment Development Authority (BIDA) needs to work with the concerned infrastructure related Ministries, Regulators, and Agencies to facilitate necessary investments and also bring in regulatory and procedural changes to reduce costs, particularly getting access to quality electricity. Targets should be set by BIDA just as in the case of DB indices so that Bangladesh can be within the top 30 countries by 2041. So Bangladesh needs to bring more focus in efficient implementation of infrastructure investments, both public and PPP, along with necessary institutional changes relating to implementation, regulation, and policy formulation.

**3.6 The Logistic Challenges – Customs, Ports related processes and infrastructure – Improvement will definitely improve Doing Business and GCI indicators.**

*The export led manufacturing growth will require seamless trade facilitation, for which there has quality trade logistics and adequate investments and procedural and regulatory changes to make necessary improvements in this critical area.* It is evident from Table 7 below that Bangladesh has a overall low ranking (87) as per 2016-17 LPI published by World bank. It is to be noted that the worrisome factor even among the mixed group of countries presented below, Bangladesh is way behind particularly from competing countries like Vietnam, India, and Indonesia. Bangladesh needs to target reaching levels of India and Malaysia in the next 05 years and attain levels of that of South Korea or China in 10 years from now. Since Bangladesh will pursue an export led growth strategy with manufacturing being the dominant sector, it will be most important overcome all the trade logistics related hurdles early on.

**Table 7: Logistics Performance Index (LPI) 2016-17**

|  |  |  |  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| **Country** | **LPI Rank** | **LPI Score** | **Customs** | **Infrastructure** | **International shipments** | **Logistics competence** | **Tracking and Tracing** | **Timeliness** |
| **Bangladesh** | 87 | 2.66 | 2.57 | 2.48 | 2.73 | 2.67 | 2.59 | 2.9 |
| **Singapore** | 5 | 4.14 | 4.18 | 4.2 | 3.96 | 4.09 | 4.05 | 4.4 |
| **South Korea** | 24 | 3.72 | 3.45 | 3.79 | 3.58 | 3.69 | 3.78 | 4.03 |
| **China** | 27 | 3.66 | 3.32 | 3.75 | 3.7 | 3.62 | 3.68 | 3.9 |
| **Malaysia** | 32 | 3.43 | 3.17 | 3.45 | 3.48 | 3.34 | 3.46 | 3.65 |
| **India** | 35 | 3.42 | 3.17 | 3.34 | 3.36 | 3.39 | 3.52 | 3.74 |
| **Thailand** | 45 | 3.26 | 3.11 | 3.12 | 3.37 | 3.14 | 3.2 | 3.56 |
| **Indonesia** | 63 | 2.98 | 2.69 | 2.65 | 2.9 | 3 | 3.19 | 3.46 |
| **Vietnam** | 64 | 2.98 | 2.75 | 2.7 | 3.12 | 2.88 | 2.84 | 3.5 |
| **Pakistan** | 68 | 2.92 | 2.66 | 2.7 | 2.93 | 2.82 | 2.91 | 3.48 |

***Source: Logistics Performance Index (LPI) 2016, World Bank***

If we look at the breakdown of scores as presented in Table 7 above, we find Bangladesh behind all countries listed in the table in each of the categories. It is also apparent that for Bangladesh to improve the situation in each of the above categories there has to marked improvements in Customs and Port related efficiency. This, of course includes regulatory, procedural, and related infrastructure related efficiency.

Improving Customs and port efficiency could also positively impact Bangladesh’s Doing Business rankings as this will help in improving on Trade Across Border Index. Research (Djankov, Freund and Pham 2010. Doing Business 2014) has found that for each additional day that a product is delayed before being shipped, trade volume falls by more than 1%. As reported in Doing Business report, globally the most common feature of trade facilitation reforms in all regions has been the introduction or improvement of electronic submission and processing of customs declarations. Improving customs administration and enhancing port procedures were the second and third most common features. The introduction or improvement of risk-based inspection systems has also facilitated trade. As reported in Doing Business 2014, Economies are virtually linking traders and agencies involved in trade and transport through electronic single windows, and successfully implemented in many countries.

To shed light on the bureaucratic and logistical hindrances facing traders, Doing Business measures the time and cost (excluding tariffs) of exporting and importing a standard containerized cargo by sea transport and the number of documents needed to complete the transaction. The indicators cover documentation requirements and procedures at customs and other regulatory agencies as well as at ports. They also cover logistical aspects, including the time and cost of inland transport between the largest business city and the main port used by traders. Of the 4 components of trade covered by Doing Business— document preparation, port and terminal handling, customs clearance and inland transport—the 2 biggest obstacles for traders in low-ranking economies are document preparation and inland transport because of administrative hurdles and poor infrastructure. It is easier, less time-consuming and cheaper to trade in economies following good practices. The logistic challenge that Bangladesh faces as reflected by its LGI ranking also gets reflected through the Enabling Trade Index presented in the Global Enabling Trade Report 2016 of the World Economic Forum

It is apparent from Table 8 below that Bangladesh is also low-level performer in the Enabling Trade Index. The only segment it does well is *“Foreign market Access’* where it has a high rank of 12 and a score above 5. It also shows that the Enabling Trade Index is low for Bangladesh because its Customs’ and Port related services is of poorer quality relative to other countries of the world. This conclusion is supported by all the other data that has been presented in this paper.

**Table 8: Enabling Trade Index of Bangladesh, 2016**

|  |  |  |
| --- | --- | --- |
|  | Rank | Score |
| **Domestic market access** | 127 | 3.4 |
| **Foreign market access** | 12 | 5.3 |
| **Efficiency and transparency of border administration** | 130 | 3 |
| **Availability and quality of transport infrastructure** | 109 | 2.7 |
| **Availability and quality of transport services** | 100 | 3.5 |
| **Availability and use of ICTs** | 112 | 3.1 |
| **Operating Environment** | 128 | 3.5 |

***Source: Global Enabling Trade Report 2016, World Economic Forum***

Bangladesh has, of course, undertaken lots of reform measures in improving Customs Administration including regulatory, infrastructure, procedural reforms and using of digital technology and automation. While this has helped Bangladesh, evidenced by the growth in its volume of global trade, further trade facilitation related reforms improvement would be required given that its competitors are reforming. Among other things, these trade facilitation reforms should include further improvement of electronic submission and processing of customs declarations, and the improvement of risk-based inspection systems. Besides, there will also have to be improvement of customs administration.

***Chittagong port performance raises cost of doing business.*** Bangladesh has not been able to get full benefits of the Customs Administration reforms that had already taken place because of port related infrastructural bottlenecks. Bangladesh lags behind in both the indices. As shown in Figure 18, Chittagong port has very high turnaround time (4.26 days). It takes almost 1.70 more days than even neighboring Kolkata port. This automatically raises port related costs. This has to change and effort needs to be made to bring it at least to Colombo port level. At the same Chittagong port Throughput in 2015 was only 2.02 million of TEU compared to 36.54 million TEUs for Shanghai. Bangladesh’s Throughput needs to reach Shanghai level by 2041 (Figure 19)

**Figure 18: Turnaround Times for Selected Ports, 2016**

***Source: Ministry of Shipping, Government of India; Chittagong Port Authority;***

***Sri Lanka Ports Authority; Marine Department, Hong Kong***

**Figure 19: Global Port Throughput 2015 (in millions of TEUs)**

***Source: Lloyd’s List Maritime Intelligence***

Bangladesh will have to urgently address the Port related infrastructure constraints including road access issues. In addition, enhancing port procedures capacity will also have undertaken, and moving towards automation with proper interface with Customs and other logistic areas will have to be ensured. With the rising volume of trade that will continue to accompany the rising incomes that Bangladesh traverses on its desired path to HIC, there will be need for additional port facilities. The Government is in the process of setting up a deep-sea port. This agenda needs to move ahead most urgently.

BIDA will have to work with both Customs and Port Authorities and their controlling Ministries in identifying procedural and regulatory steps/measures for urgent reforms and also facilitate private investments in related infrastructure through PPPs, particularly in improving capacity of Chittagong port in the short to medium term, and the new deep sea port in the longer run.

**3.7 Modernizing Land Administration and setting up of Economic Zones can lead to reduction of Cost of Doing Business – *its impact through reducing time in registering properties, getting building permit, and reducing land related case loads allowing courts more time for contract enforcement.***

Bangladesh is a land-constrained country and has to cater to the different competing demands on land for housing, food, communication, and business needs. Land is also the most valuable asset and a leading constraint to investments as has been reflected in different surveys. With efficient land management we could see improvements in three of the DB indicators – enforcing contracts, registering property, and dealing construction permits – where Bangladesh performs very poorly as had already been shown above.

The courts are overloaded with cases that originate form disputes relating to title and registration. Land ownership/title related cases burdens the court system with the impact that on average it takes 1442 days to enforce a contract and the financial cost of enforcement is as high as 67% of the claim, compared to only 400 days in Vietnam and 453 days in China to enforce a contract; the financial cost being 29% and 16% respectively. If this burden could be reduced then the courts could focus more in quick dispensation of commercial disputes and enforcing contracts, as would be expected when country moves to higher levels of development.

The land titling related issue also makes property registration a long drawn process. Bangladesh takes 244 days to register property while it is only 20 days in China, 27 days in Indonesia and 47 days in India. Access to industrial land for manufacturing is made difficult by complexity in the process and time taken to register properties – this also has implications on getting building permits in shorter time.

Because of the challenges relating to land title it becomes very difficult for entrepreneurs to purchase land. This is even more challenging for foreign investors. So proper policies and regulatory measures needs to be in place that puts in place an efficient land market that is able to cater to the alternate needs, including the growing demand for land to set up manufacturing and logistics related industry. Since land touches every aspect of development and the lives of its people it needs to be handled with special emphasis so that objectives of Bangladesh’s development goal of reaching HIC status around 2041.

***Complex land related regulatory system that requires streamlining to reduce cost of doing business:*** The land related problems are institutional, procedural, and regulatory; which results in an inefficient land market and the resultant doing business index related challenges. There are three institutions – Land Survey office, Land Revenue office and Sub-Registrar office -, administered by two separate Ministries, that are involved in the, settlement, titling, revenue collection, transfer and registration process.

Land related complications arise because the Land records may be updated: (i) as a result of land surveys (via the Settlement Officer); (ii) (via the sub- registrar’s office) registering of deeds of sale; and (iii) through inheritance (through AC land office). Each of these units has their own time frame of completing their individual tasks, which can be a cause for inadequate transparency when dealing with the citizen. Efficiency and transparency of land market will depend on how well coordinated are the functioning among each of the three institutions in dealing with the processes involved in land transfer and those in updating the land titles and land survey, which are all linked to each other; and the outcomes are dependent on efficiency of all. The diversity of ways in which land records may be updated, and the problems associated with each give rise to numerous disputes and also proliferation of land related civil and criminal cases, and thus raises the cost of doing business.

The regulatory system pertaining to land administration is, therefore, complex that calls for simplification and streamlining for land markets to operate efficiently and transparently. While there needs to be full review followed by reforms of the institutional structures, it will be important to use all aspects of digital technology to ensure that record of rights is established in digital form. This can then be used immediately for registration with waiting for long time prevalent at the moment. The Registration process should also be linked digitally so that interaction with officials declines. This has been done in other South Asian countries, including and India and Pakistan, which has similar land administration system and so should be taken up urgently.

These alone will not be enough as the cadastral survey process and the appeal process are themselves also lengthy as stated earlier. Digitization of survey should be come simplar and less time consuming as satellite based mapping technology is available. Similarly the scope for reducing Appeal time and steps needs to be looked into and reduced. There is process for review and rectification but the appeal process could take a long time and also costly. Where a decision relating to the recording of land title is disputed, the appeals process starts at the lowest rung of the ladder and then moves progressively upwards until the appellants and other interested parties either accept the judgment given or lack the resources to proceed further. There is definitely scope for improvement here if necessary regulatory steps and institutional changes are brought in backed up by use of technology.

***Land Zoning could overcome the land constraint challenge, and also support sustainable development goals.*** As a step towards having a more efficient land will be the need for land zoning. Zoning is an essential tool in successful urban planning. Maps divide communities into different zones based on the types of uses allowed—such as residential, commercial, industrial, public buildings, parks and green areas. Land zoning regulations can provide a useful framework for investors and developers by specifying the most appropriate location for their projects, given that the infrastructure, connectivity, energy, and environmental concerns get regulated upfront. This can therefore facilitate in easing up the decision of the investor to invest and move forward with the process of applying and getting building construction permit and start construction of factory building or warehouse in the shortest possible time, leading to more efficient and less costly construction permitting systems. Any improvement in this will also improve rankings in DB and GCI indicators.

**3.8 Economic Zones in Bangladesh as an immediate measure to reduce Cost of Doing Business in a limited demarcated territory – The proposed One Stop Service (OSS) can quickly be implemented.**

Many countries, to address the investment climate and better business environment issues, have successfully used Economic Zones as a catalyst for investment; but the rationale for their development differs between developing and developed countries. For developing countries, the Zones have traditionally had both a policy/regulatory and an infrastructure rationale. [[2]](#footnote-2) On the policy/regulatory side, it includes measures meant to boost investment competitiveness and reduce business entry and operating costs, which can be a useful tool as part of an overall economic growth strategy to enhance industry competitiveness and attract investments, particularly foreign direct investment (FDI)[[3]](#footnote-3). On the infrastructure side it can plan providing right type of infrastructure within a limited area maximizing on economies of scale.

Given the time and challenges to quick implementation of not only regulatory and procedural reforms, but also overcoming quickly the challenges related to land administration, the government has rightly embarked in setting up economic zones with increased involvement of the private sector in setting up zones, and with government facilitating that process through regulatory support, access to land and infrastructure where needed.

The Special Economic Zones (SEZs) can not only help pilot regulatory/institutional reforms that improves business environment and reduces cost of doing business and reduces infrastructure bottlenecks, but also give unhindered access to serviceable land. Providing single window service like One Stop service (OSS) is a way to reducing policy/regulatory hassles to investors, as it can conveniently be rolled out and implemented in the limited territory of economic zones. It can thus act as a catalyst for domestic and foreign investments to invest in a more business friendly environment. The investments, including FDI, could reach the desired levels (e.g. what is being stipulated in the 7th FYP) with efficient implementation of the SEZ including having in place policies, regulations, and the necessary infrastructure fully in place for investors feel comfortable to invest.

This will provide much needed time and space to undertake all the reforms discussed above relating to reducing cost of doing business across the country. Over long term the focus should be to learn from SEZ experience and improve the investment climate and regulatory oversight throughout the country.

***Land Acquisition Related Policies may be a challenge to setting up of SEZs:*** Government’s declared policy of setting up of economic zones is likely to require land acquisition. A very difficult issue is that related to land acquisition, which become necessary for development purpose and which also increases use of land for non-agriculture needs. Laws in Bangladesh do not distinguish between processes governing the acquisition of farmland and urban lands. While the Industrial Policy of Bangladesh addresses the potential conflicts emerging from uses of fertile farmland for industrial purposes, there are no effective mechanisms to ensure the application of the principles put forth in the policy. It creates a challenge when large footprint projects are to be implemented in green-field areas, industrial estates, special economic zones or export processing zones. The legal instrument for expropriating lands for public purposes is the “Land Acquisition and Requisition of Immovable Property Ordinance, 1982”. Besides, the resettlement policy of Bangladesh is not adequate. Therefore, policy that facilitates a comprehensive and modern technique of resettlement needs to be adopted in order to smoothen the process of acquiring land. However, critical to even having a better land acquisition process will depend on having in place a well functioning transparent land market.

**3.9 Improving Access to Credit could raise investments in MSMEs*.***

International experience suggests that a part of the solution to the diversification of manufacturing production and exports, and to higher-income job creation outside agriculture and unorganized services lies in revamping and spurring the growth of micro and small and medium enterprises (MSME) in manufacturing and services. In the World Bank’s Ease of Doing Business 2017’s ranking for ‘Getting Credit’, Bangladesh is ranked at 157, way behind Malaysia (20), Vietnam (32), and India (44).

Bangladesh MSME sector has not been growing as expected and the financial market is failing to cater fully to the needs of the MSMEs including among others access to finance. While there are definitional problems, there is no doubt that however defined MSMEs are a substantial source of economic activity in Bangladesh. Yet, available evidence suggests they lack dynamism. While there are many factors that constrain its performance, access to organized finance is a critical constraint. The main challenges faced by banks for financing MSMEs are poor quality of collateral, inadequate documentation, and improper business plans. With relatively high interest rates for SME lending, stringent collateral and guarantee requirements might be a critical barrier to SME access to finance. Banks, on their part, tend to be less flexible about the collateral requirement in the case of the SMEs as they perceive SME loan to be more risky and the cost of monitoring and supervision of small loans to be higher. Banks also tend to hesitate to provide credit for new borrowers and in most cases business experience of 2 or more years is needed for SMEs to access bank credit.

In recognition of the financing constraint, the Government in recent years has focused considerable attention to MSME finances to boost its potential role. Despite substantial expansion of microfinance and credit from banks, non-bank financial enterprises and specialized refinancing windows, total access to financial services is still low relative to the size and needs of the MSME sector, especially in the rural areas. The high cost of financial products (including the cost of microfinance institutions (MFIs)’ products) has regularly been highlighted as a major hurdle in accessing financial services.

Weak financial infrastructure is a key impediment to the development of the MSME financing ecosystem in Bangladesh. There are policy and regulatory constraints including the absence of start-up capital options, inadequate lending instruments that cater to various financial and risk management situations, high cost of doing business, and the dominance of fixed-asset based collateral requirements for SMEs. As evident from Table 4 above, the low rank for Bangladesh in getting credit access are its very low scores in its Depth of Credit Information index (score of 0 compared to 8 for China,), Credit Registry Coverage (0.9% of adults versus 91.9% for China), Credit Bureau Coverage (0 % of adults versus 21.3% China).This is particularly challenging for MSME’s to access credit, as it limits the availability of credit, particularly to its small and lower end of the medium enterprise segments, as they are unlikely to be in the credit bureau or credit registry coverage, thereby raising the cost of lending to these enterprises thus reducing access to credit. Here lies a major regulatory challenge of setting Registry so that need for providing physical collateral would diminish for smaller sized loans.

Within the MSME sector, startups with limited operating histories face particularly challenging environment in accessing financing. Startups have the potential to create jobs in emerging and innovative industries if they can obtain the funds they need to grow. Due to institutional factors, banks are not well positioned to address their financial needs. However, entities such as seed funds, angel investors, venture capitalists, accelerators and growth equity firms can play this role. The pre-bank startup-financing ecosystem in Bangladesh is nonetheless, nascent, with a limited number of formal investors focusing on startups.

One issue that becomes apparent is that there needs to be reduction in costs of delivery of financial services in order to increase accessibility of those not being served by the formal financial system. One solution is increased use of technology in providing financial services through what is known as Fintech solutions. Bangladesh has entered in a limited way through opening up mobile financial services (MFS), but more dynamic policies and regulatory reforms needs to be undertaken so that Bangladesh can keep up with the technology revolution.

**3.10 Institutional, Regulatory structures affecting business environment – the role Bangladesh Investment Development Authority (BIDA), and Bangladesh Economic Zones Authority (BEZA).**

A host of public and private institutions and agencies in Bangladesh are involved with the business related regulatory environment and the investment climate in which manufacturing enterprises operate. It is apparent from the review of DB and the GCI indicators that there needs to be changes/reforms in a number of areas and institutions. One of the critical challenges that business faces is the time it takes to get electric connections. There have been efforts to increase electricity generation but there are gaps in transmission and distribution needs. It is particularly important to note there are three areas where there has been deterioration of Bangladesh’s position (Figure 17 above).

The business regulatory environment is impacted by a complex institutional structure comprising multiple Ministries and Department’s and agencies under them. While focus of all Ministries is on development of the country, they are stuck by their individual goals and strategies, which may not be supportive of each other’s goals. For example while Ministry of Commerce is supposed to in charge of ensuring a more business friendly trading environment, it is the national Board of Revenue (NBR) under ministry of Finance which has final say on setting tariffs, though *de jure* the Tariff Commission under Ministry of Commerce is supposed to be key player in this. The NBR is driven by its strategy of meeting revenue targets which many a times runs counter to the Ministry of Commerce’s goal of trade promotion and trade facilitation. There is then the Ministry of Industries with many of the regulatory bodies affecting manufacturing working under it. These include agencies bike boiler inspection, BSTI. The issue is Ministry of Industries (MoI) is also in charge of some of the public sector manufacturing units (SOEs) like Fertilizer and Steel products. A lot of the decisions of MoI are driven by their focus on SOEs, which may not be amicable for private industry. The complexity within manufacturing further increases because for Jute and Textiles there is a separate Ministry and for pharmaceuticals it is the Ministry of Health.

While different sectors within manufacturing may have different special regulatory needs, the overall business regulatory needs are same for all industry. The structural problem that Bangladesh has been facing is that there is no exclusive Ministry for private industry. All these Ministries have agencies/corporations under them that continue to be in business. The Ministries are much more driven by policy and institutional support to protect the SOEs under them. Even beyond policies, the Ministries sometimes play the role of regulator. This is a problem as it fails to separate policy making from regulations and service delivery. In the case of telecommunication sector this had happened and we saw strong FDI flow into this sector.

Given the difficulty with the multiplicity of institutions that in some way linked to business environment through both policy and regulatory interface and its impact on private investments, the government has in more recent times have set up some institutions to promote and facilitate private investments. Among them, two of the institutions are important as they are directly working to reduce cost of doing business and reducing regulatory hassles. These two institutions are Bangladesh Investment Development Authority (BIDA) and the Bangladesh Special Economic Zones Authority (BEZA). Both these institutions are under the administrative control of the Prime Ministers Office, with their governing Boards chaired by the Honorable Prime Minister.

***Bangladesh Investment Development Authority (BIDA).*** Bangladesh Government formed BIDA by amalgamating the former Board of Investment (BOI) and the Privatization Commission. This has institutionally strengthened BIDA because besides undertaking steps to simplify different procedural steps for business registration and other tasks along with promotional work for bringing in new investments, it also now has assets of SOEs that it inherited from the PC. These assets sit on valuable land, which is identified as a key constraint.

BIDA has taken on itself the very important task of moving forward the necessary regulatory reforms that will help bring transparency while it also embarked on making institutional changes backed by an Act to provide one-stop service to investors. BIDA being the nodal agency for promoting investments in the country will have to undertake the coordinating role of working with Ministries to ensure that the one-stop service window works. BIDA is the agency for leading and coordinating the process of bringing in necessary regulatory and institutional reforms that will reduce cost of doing business in Bangladesh. BIDA has already embarked on the task improving Bangladesh’s DB ranking and come into par with competing countries. This is a laudable goal and should be pursued in coordination with the concerned Ministries and agencies.

This task will get easier if adequate infrastructure supply is available to meet demand. Improving infrastructure supply like power, energy, road and rail communications, ports will help raise GCI rankings. Here BIDA as support to the Government Ministries can provide promotional role of getting more private sector investments through PPPs and IPPs in energy supply, power generation and transmission, ports and logistics, express toll-road construction. BIDA could be the institutional link between the Ministries and PPP office. An important task the BIDA can perform is working with Land and Law Ministries in getting digitization of all land related records and processing, along with working out a zoning system across the country to clearly delineate land for agriculture, forestry, fisheries, industry, infrastructure and urban needs. This alone could unbundle lot of the hassles allow entrepreneurs to take informed investment decisions.

BIDA has closed SOEs in its portfolio, which needs to be transformed into productive assets. BIDA could learn from BEPZA’s success in converting lossmaking SOE’s into successful EPZs in a short period of time.Government had handed over two loss making closed State Owned Enterprises (Adamjee Jute mills and the Chittagong Steel mills) to BEPZA to convert to EPZs. BEPZA quickly moved in and set up the Adamjee EPZ and Karnapuly EPZ. When Adamjee was closed it was making annual loss of over Taka 100 crore each year and it had 25,000 permanent/temporarily employed. Besides, both the SOEs had huge debt with the state owned banks and the power company (PDB).

Today Adamjee EPZ has 61 foreign and domestic owned private export oriented enterprises. It has 51,114 *(expected to go over 100,000 once all the enterprise construction is complete),* direct employments as of December 2016; and during FY 16 exported goods worth US$ 563 Million *(expected to go over US$ 1 billion annually once all the enterprises are fully constructed*), with cumulative exports since its inception, i.e. FY 06 to FY 16, reaching US$ 2.25 billion.

There is an even better story in the case of Karnaphuly EPZ (formerly Chittagong Steel Mills) where 53 enterprises are operating with employment reaching 66,731 as of December 2016 *(expected to go over 100,000 once all the enterprise construction is complete)*; and during FY 16 exported goods worth US$ 823 Million *(expected to go over US$ 1 billion annually once all the enterprises are fully constructed*), with cumulative exports since its inception, i.e. FY 08 to FY 16, reaching US$ 2.93 billion. As an option BIDA could consider working with BEPZA in converting a few of these SOEs into EPZs, before it undertakes a broader strategic plan for using these assets. Since BIDA is moving forward with implementing one-stop shop for all approvals, these converted SOEs could help BIDA pilot and test implementation, before rolling out across the country.

***Bangladesh Economic Zones Authority (BEZA*).** Recognizing the importance of zoning and urban planning, Bangladesh has adopted zoning systems and the Government has enacted Economic Zone Act in 2010, and under it Bangladesh Economic Zone Authority (BEZA) has been established. The Act provides legal basis for the establishment of economic zones in all potential areas including backward and underdeveloped regions with a view to encouraging rapid economic development through industrialization. The expectation is that under the new SEZ paradigm, with a regulatory authority in place, there will be quick implementation of new Zones so that local firms can harness spill-over impact from Foreign Direct Investment (FDI), and in the process additional investment can be encouraged within value chains, more local products procured and better linkages could be established between firms and educational institutions (easily available skilled manpower is important for success of SEZs). The Act also has provisions for private and PPP based zones, and has provisions adaptation to required environmental and social practices through rules, streamlined regulations, and institutional setup. It will allow the Government to develop and pilot an approach that is less reliant on Government subsidies, while leveraging comparative advantages and private sector capability wherever possible.

Successful development of SEZ can be expected to provide investors confidence invest and bring in in new technology and produce to take advantage of the GVC using Bangladesh’s comparative and competitive advantages. The Act promotes Economic Zones in the Private sector, Government led EZs or in a combination. The mandate of the BEZA allows it to identify local potential zones, acquire lands and build the zones with necessary facilities. BEZA may seek public-Private Partnership (PPP) to build and effective utilization of such zones. While Economic Zone Act 2010 provides a more organized use of land for industry and urban growth, it also provides an opportunity to bring a better balance with agriculture land use by restricting Economic Zone land in areas, which are less suitable for agriculture and also land, that is productive for agriculture.

BEZA’s vision is to develop 30,000 hectares of land for SEZs, establish 100 SEZs across the country in the next 15 years with an employment target of 10 million. Meanwhile, BEZA has promulgated the policies and rules pertaining to setting of SEZs and has 25 areas for providing One Stop Service (OSS) to investors. These 25 areas includes approval of investment proposal, different permits, permission for utility connection, NOC for off-shore banking, Certificate of Incorporation, TIN and VAT registration, building permit, visa, work permit, environment clearance, Customs Clearance etc. These are laudable steps and address some of the core daunting doing business and logistics challenges facing investors, particularly foreign investors wanting to invest in Bangladesh. All these procedural and regulatory reforms that BEZA has undertaken should become operational within next one year.

According to its Annual Report 2016 and other documents, BEZA has by now approved 74 Economic Zones. Of these, 54 zones are to be developed in PPP mode, 20 will be privately developed zones under license from BEZA. Meanwhile BEZA has already initiated issuing of licenses to private SEZs. There has been MOUs between governments have been signed for setting country specific SEZs. Two Zones in Mongla (in Khulna) and Kushtia will be India specific zones and one zone in Anwara in Chittagong will be a Chinese specific zone. All these are very positive steps. The challenge will be for BEZA to go through a steep learning curve, develop its institutional capacity, and move this process forward in a transparent way so that investors find it conducive. The planned one-stop service for which Law has been drafted could be more easily implemented in SEZs, for which necessary BEZA capacity should be in place.

However, given the regulatory environment prevailing in Bangladesh, especially institutional capacity, it needs to be implemented carefully lest the privately licensed zones change course and there is inadequate oversight to effectively enforce regulatory compliance. The caution is because Bangladesh is a land-poor country and land market speculation is an issue. Besides, any rapid proliferation of private zones can also place significant, unanticipated costs on governments, especially in terms of offsite infrastructure and facilities, as exemplified by the Dominican Republic, and more recently the Philippines and Vietnam[[4]](#footnote-4).

***Setting up SEZs automatically does not make them successful.*** To a great extent, the fate of zone initiatives gets determined from the outset, by the choices made in the establishment of policy frameworks, incentive packages, and various other provisions and bureaucratic procedures. *The experience suggests that maximizing the benefits of zones depends on the degree to which they are integrated with their host economies and the overall trade and investment reform agenda. In particular, when zones are designed to pilot legal and regulatory reforms within a planned policy framework, they are more likely to reach their objectives[[5]](#footnote-5).* The success of zones is also critically linked to how they are developed, managed, regulated, and where **located.**

***Learning from Bangladesh Export Processing Zone (BEPZA) experience.*** It should be noted that Bangladesh has already long experience in setting up successful export processing zones through BEPZA. While BEZA is a relatively new organization, it can learn from BEPZA’s experience. The first issue is location of Zones. The most successful EPZs are in the Chittagong and Dhaka regions. This becomes apparent when we see that the Karnaphuly EPZ in Chittagong and the Adamjee EPZ in Narayanganj (greater Dhaka), which were last EPZs built by BEPZA, have already surpassed in terms of employment, investments, and exports compared to EPZs in other regions which were set up much earlier. BEZA has undertaken an ambitious target of implementing 100 SEZs in the country in the coming years. While the goal is appreciated there needs to be a cautious approach in selecting the first few zones which should be based on feasibility and at the right location. Successful implementation of the first two or three SEZs will send positive signal to the world heralding Bangladesh as a competitive destination for investments. Given the limited capacity, BEZA needs to prioritize and put focus on getting the first two or three zones fully operational, along with necessary one-stop service in place at the shortest possible time. Another area of BEPZA experience that could help BEZA are the PPP contracts that they have successfully implemented. BEPZA, to ensure 24/7 quality power supply, innovatively implemented PPPs in power generation, and for ensuring environmentally sustainability used PPPs to build Effluent Treatment Plants (ETPs), and water treatment and supply of quality water in CEPZ and DEPZ.

**4. Reform Priorities – Policy, Institutional, and Regulatory - The way forward**

The relative stagnation in the private investment rate despite very favorable macroeconomic performance and robust economic growth are indicative of the private investor concerns with the business environment that has made progress but falls short considerably in relation to other countries. The deregulation process seems to have slowed down after 2010, and has become a critical challenge to having an enabling business environment, which is being reflected through the very poor outcomes in all the different global indices that had been earlier discussed. This process now needs total revamping now that Bangladesh has set up BIDA.

BIDA could start with addressing constraints affecting all the 10 Doing Business (DB) indicators that make Bangladesh ranking so low. However, the priority will have to be top six constraints identified in the IFC survey on ease of doing business in Bangladesh for 2016. While addressing the DB identified constraints it will also be important to address the infrastructure related constraints like easy and certain access to electricity, good quality transport infrastructure, and highly efficient ports. These will directly impact in improving performance of getting electricity and trading across border indicators as well as help improve Bangladesh’s GCI and GLI indices. A very important reform will be that related to land administration and working of an efficient land market. It has potential to help improve Doing Business rankings in three areas – enforcing contracts, registering property, and facilitating construction permit. As had been discussed earlier having well functioning land market would ease issuing of building permits; and if land related cases decline the courts will have more time for commercial cases and so enforcing of commercial contracts can gain momentum.

Since Bangladesh is substantially lagging behind in attracting FDI relative to comparator countries like China, Hong Kong, India, Vietnam and Singapore, policy reforms should focus on resolving issues that affect both domestic and foreign private investors. It is important to note that the reform agenda is large and priorities have to be set. The reform process should be seen as a continuous process that should be reviewed annually to assess progress and identify new issues.

## 4.1 Simplifying regulations and improving implementation – BIDA needs to anchor and steer the process.

Despite past efforts to deregulate the business rules of operation, regulatory constraints remain serious in many areas and implementation is an even bigger problem. While it is understandable that improvements in the civil service is a long drawn process, several practical steps can be taken to alleviate the concerns without any major overhaul of the civil service. Government has already set up BIDA and BEZA as institutions to alleviate doing business challenges. BIDA which has been tasked with improving global Doing Business ranking of Bangladesh by facilitating policy, regulatory, and process changes should as priority undertake review of all regulations, processes, and policies negatively affecting business environment, and take measures to improve Bangladesh’s rankings GCI, DB, and GLI. More specifically some of the actions are as follows.

* A high-powered business deregulation task force needs to be established with representation from the private sector to overhaul the entire regulatory regime with a view to abolishing all regulations that constrain investment and ensuring that prudential regulations required to protect public interest are business friendly. BIDA could be the Secretariat for the task force. It should be a continuous process where with BIDA acting as the Secretariat, and prioritize policies, regulations, rules, and procedures that needs most urgent attention and facilitate implementing the changes. It should undertake periodic Regulatory Impact Assessments (RIA) to determine which regulations and policies need amendments or abrogation.
* BIDA needs to set up specific targets and monitoring mechanisms to attain higher levels of GCI, DB, and GLI indices. It will require good coordination with different Ministries and agencies to be able to come up with positions where investor surveys will show the positive developments.
* BIDA will have to work with both Customs and Port Authorities and their controlling Ministries in identifying procedural and regulatory steps/measures for urgent reforms and also facilitate private investments in related infrastructure through PPPs, particularly in improving capacity of Chittagong port in the short to medium term, and the new deep sea port in the longer run.
* BIDA should set up a “*doable”* mechanism for instituting the proposed one stop service (OSS). It will be very important to gain confidence of investors about OSS. OSS needs to be cautiously approached with realism in time frames promised for delivery of particular services.
* Government should take care to ensure the predictability of policies and avoid frequent changes that could hurt investment choices. This is particularly important in the case tax and tariff policies where periodic certainty must be ensured to allow investors to decide on taking risks.
* Public administration capacity prevents proper implementation of rules and regulations, especially in the areas of Drug Administration, environmental clearances, and testing labs. Along with efforts to strengthen these agencies, outsourcing options to private sources may be examined.
* All clearance and licensing agencies must be digitized with online applications and approvals. Service standards for clearance/licensing lead times should be established.
* Discretionary application of rules/regulations by bureaucracy should be avoided through political oversight at the Minister level.

## 4.2 Improving the tax regime for business.

The business sector is mindful that paying a fair share of taxes is a national obligation. It is therefore committed to working cooperatively with the government to help increase the revenue performance of the tax system. However, the tax system must be business friendly rather than averse to the development of the business sector. A strong private sector has been the engine of growth in Bangladesh. As private sector grows total GDP also grows that helps tax revenues. The main challenge for NBR is to increase the tax base to bring in more enterprises that are out of the tax net either because they are in the informal sector or because they are able to take advantage of the loopholes in the tax laws. The global experience is that high corporate tax rates discourage investment and encourage tax avoidance. Similarly, too many tax exemptions to any one sector leads to unfair competition and discourages diversification. Based on results of different IFC surveys and also on the basis some feedback form business groups the following reform options are proposed which can be have very positive impact in improving DB indicator and raise Bangladesh’s ranking.

* There needs to be rationalization of the income and corporate tax rates to make it competitive with comparator countries. The government needs to consider lowering maximum corporate tax rate could to around 25% over a three year period (35%; 30%, 25%) to be in line with more competitive economies like Malaysia (22%-24%), Thailand (20%) and Singapore (17%).
* The tax laws, rules and regulations must be simplified and streamlined and made consistent with good international practices. NBR should consult business sector in this task. For the short term, several specific actions can be taken: (i) withdraw the 20% withholding tax on technology service providers; (ii) remove the NBR pre-determined gross profit level set for the footwear industry and assess tax on actual profit; (iv) make the income tax refund process more streamlined (like VAT return) and excess tax payment should be refunded in designated company’s bank account within 30 days from assessment completion; and (v) withdraw the minimum tax provision for loss making companies.
* A simplified low-tax regime will eliminate the need for expensive tax holidays and tax exemptions. But when these are provided, these must be done in a simple non-discretionary way.
* The NBR needs to transform to a tax service agency rather than a tax-policing agency with professional staff and service orientation.
* The interface between NBR staff and corporate staff should be minimized through digitized transactions.
* Dispute resolution mechanism including ADR must be made more efficient and effective.

## 4.3 Addressing the infrastructure problem.

Despite considerable new investments in power generation and transport, business responses show that supply of infrastructure services and trade logistics, especially port services, are of major concern. Several steps can be taken in the short term.

* Bangladesh needs to build multimodal transport network backed up high quality express roads, higher speed double track railway, and accessible and efficient river transport system backed by efficient container and cargo handling at designated places. It will facilitate trade and will help raise the DB, GLI and GCI indices for Bangladesh. In this context all highways connecting to Chittagong port should have access controlled express lanes immediately implemented.
* Ensure long term supply of gas, other energy, and power supply. Urgently complete implementation of LNG imports and ensure effective availability to all industries, particularly to SEZs by 2019/2020. Implement the Power sector Master plan diligently and on time. The plan should be that there should be enough along with quality transmission, and distribution back up to ensure that all industries coming on line from 2020 onwards are given connection certainty within reasonably declared time. After 2025 this should be automatic on demand. This measure will raise Bangladesh’s ranking on the electricity related DB, GCI indices.
* Meanwhile, adopt a fair and equitable gas connection policy for business enterprises, rather than on an ad-hoc policy based on personal connections. In this regard, enterprises that were given gas connection commitments prior to new investments /expansion programmes (e.g. the example of Jalalabad Gas Co, cited earlier) must be provided with gas connections to avoid large financial loses.
* Public utilities, e.g. DESCO, Titas Gas, WASA, REB, etc.) must adopt a proper policy for supplying timely and quality services with well-defined service standards. The transaction costs in terms of time and money must be reduced in line with good international practice, published and monitored.
* All utility services should be digitized so that personal interface is not needed.
* Improve the turnaround time of ships as Chittagong port faces congestion affecting trade facilitation. There is urgent need to increase handling capacity of the ports and also recruiting necessary manpower. The target should be to reach the level of Colombo in both Turn-Around time and Throughput by 2022. This will improve Bangladesh’s DB, GCI and GLI rankings.
* Accelerate implementation of the Deep seaport so that the Throughput of Bangladesh can be at par with ports like Shanghai. Use private investments through PPPs, particularly in improving capacity of Chittagong port in the short to medium term, and building the new deep-sea port in the longer run.
* The Dhaka airport’s cargo handling facility needs to be improved urgently. A possible solution is to outsource the airport cargo handling services to the private sector and appoint the Civil Aviation Authority as a regulatory body.
* For ensuring road safety, the Bangladesh Road Transport Authority (BRTA) needs to reintroduce mandatory installation of speed governors in trucks and buses to control their speed and enforce it through the routine fitness test.
* Revive use of railway for transporting tea from Sylhet Division to Chittagong for auction, thereby reducing pressure on Sylhet-Chittagong road connection.

Additional measures are necessary over the medium term.

* The service quality in all land, air and sea ports need substantial upgrading through investments in port facilities, digitization and better staffing.
* Connectivity from Chittagong Port to factory-gate service could be substantially improved by developing the inland water and rail services.
* Establish a new Inland Container Depot (ICD) in the proposed site of Dhirasram in Tongi to ease the pressure on Kamlapur ICD and its connecting roads.
* The waste management and disposal service for manufacturing enterprises needs urgent attention with possible PPP solutions.
* Over the longer term much higher investments in infrastructure will be needed. Public sector alone cannot deliver this. The PPP initiative is dormant and must be energized by over-hauling the institution with internationally trained experts and a well thought out enabling framework learning from international good practices.
* China, Japan and Korea have substantial capacity and funding to develop large infrastructure projects on a turnkey basis. The government should look into this carefully.

## 4.4 Strengthening land administration

The long delays and high cost of land procurement are reflective of another binding constraint to private investment: the availability of land for manufacturing enterprises. The land market is very inefficient in view of weak land ownership data, lack of computerization of land records, poor zoning laws, and high transaction cost. On top, population pressure and rapid urbanization have contributed to a growing scarcity of urban land. As land prices have sky rocketed so have land disputes and various forms of corruption including land grabbing.

* Computerize all land ownership data.
* As priority complete cadastral survey using digital and satellite technology and digital record of rights of all land in greater Dhaka (includes Gazipur, Narayanganj, Narsingdhi, Manikganj, Munshiganj, and Tangail Districts) and greater Chittagong (includes Cox’s bazar District).
* Work with Ministry of Land and other concerned Ministries in comprehensive Zoning the whole of Bangladesh, starting as priority greater Dhaka and Chittagong.
* Undertake regulatory reforms to simplify land transactions and registration and reduce the cost of land registration in terms of both time and finances.
* Implement institutional reforms to improve land administration and record keeping.

**4.5 Make all necessary policies, rules, and procedures including proposed One Stop Service (OSS) fully operational for SEZs in the short run.**

The government has recognized this constraint and has responded by developing SEZs. This is an excellent initiative. However, the process of completing SEZs in a shape that such that they land can be immediately used for productive purposes is fairly long. Also, the demand for land far outstrips the SEZ plans. So, measures will have to be taken to both fast-track the completion of SEZ projects as well as to develop the land market to facilitate efficient private land transactions. A range of policy actions are needed here including:

* BEZA should immediately operationalize its OSS, given that it will be much easy to implement within each SEZ.
* Ensure timely supply of necessary social and economic infrastructure to enable quick completion of SEZs. In addition to supply of road connectivity, electricity, gas and water supply, schooling facilities also need to be provided to enable worker and family relocation to SEZs
* BEZA should complete the Mirershai SEZ within its stipulated time and ensure that at least one anchor investor (e.g. Samsung or Toyota type global brand) sets factory there within 2020, followed by another by 2023. In between other industry could be set up.
* Ensure that Chinese and India specific Anwara, Kushtia, and Mongla SEZs be up and running within 2020.
* The success of BEZA will greatly depend on its capacity to manage implementation of PPP based zones. It needs to work closely with PPP Office for it. Besides, it should find ways of leveraging BEPZA experience in not only Zone development but also the PPPs implemented by them in their EPZs.
* Since BIDA has SOE assets in its control it could work with BEPZA or BEZA to develop these as economic Zones. BEPZA’s experience in successfully converting two SOEs into EPZs can be used.
* Facilitate private investments in SEZs to provide land for domestic and foreign private investors, including simplifying the clearance procedures and ensuring that these clearances are provided without inordinate delays, and ensuring timely infrastructure supply to the private EZs.
* Revisit the restrictions on agricultural land holdings to facilitate commercial agriculture for agro-processing industries
* Strengthen enforcement of zoning laws. This is a serious problem causing haphazard growth of commercial enterprises in residential areas that has contributed to severe traffic jams and law and order problems.
* Given the difficulty in building new institutions and also having different institutions (BEZA, BEPZA, HTPA, Private EPZ Cell, BSCIC) pursuing the same goal under different paradigms, it would be optimum for a country like Bangladesh to have one Authority regulating the entire zone development program, be it private, public, or PPP. One challenge will be to separate regulatory authority from development of public funded zones.

## 4.6 Lowering the cost of trading across borders

With increasing integration with the global economy the cost of trading across borders for both imports and exports have a determining influence on the global competitiveness of the Bangladesh economy. Bangladesh has done well to eliminate most export duties. It has also abolished most quantitative restrictions on imports and reduced import duties. Yet, owing to a complex system of supplementary and regulatory duties (SRDs), overall trade protection is high and there is a huge anti-export bias of the trade regime. While Bangladesh has tended to address this concern by allowing duty-free imports for a few large export products, especially RMG, through the bonded warehouse system and has established a duty drawback system for exporters, feedback from business sector showed that there are problems with the implementation of these measures. Importantly, the complexities of the tariff and SRD system and their uneven application create many problems for business. Additionally, the customs administration process involves high transaction costs. Given these concerns, several policy measures can be taken to lower the cost of trading across borders.

* Establish a customs tariff reform commission drawing from officers from the NBR, the and the finance and commerce ministries as well as outside experts and representatives from private business to develop a comprehensive reform proposal that seeks to simplify the customs tariff regime and substantially reduce its anti-export bias.
* Computerize all import/export clearance processes.
* Improve customs clearance facilities in all land ports.
* As in the case of RMG, allow bonded warehousing facility for all export industries. Like RMG the warehousing should also be allowed on 60 KM radius similar to bond facility for all other export oriented industries. Also, the renewal of bond license and Utilization Declaration (UD) should be brought under similar footing as that provided to RMG through BGMEA. Where Customs certification is needed for renewal, this should be done within 7 days since they already have all data on imports and usage.

## 4.7 Improving Access to Credit to MSMEs

The financial infrastructure in Bangladesh needs to be studied to identify specific bottlenecks to higher levels of MSME financing. Given the discussions earlier on getting credit challenges that constrains the doing business environment particularly for small and lower end of the medium segments of MSMEs some actionable recommendations are suggested below to address the deficiencies.

* *There needs to be in place the infrastructure to have in place a continuously expanding and easy access to high quality credit information*, and the private sector can play a role in the credit information market – as an example the telephone companies have large database on which could be used if proper policies are adopted. As discussed earlier, the low rank for Bangladesh in getting credit access are its very low scores in its Depth of Credit Information index, Credit Registry Coverage index, and Credit Bureau Coverage index.
* *Bangladesh needs to introduce secured transactions regime by enacting necessary laws so as to* enable lending against movable collateral and help reduce the financial sector’s reliance on fixed assets as collateral. This is very important as weakness in the credit information system causes the scheduled banks to tend to be less flexible about the collateral requirement in the case of the SMEs as they perceive SME loan to be more risky and the cost of monitoring and supervision of small loans to be higher. The stringent collateral and guarantee requirement practices of the banks makes SME lending rates relatively higher, thus acting as a barrier SMEs to access credit.
* Policies and regulatory changes need to be brought so the mobile financial services are able to go beyond the present scope and move to a digital financial regime provide different financial services that will make access to finance to small and the lower end of the medium enterprises easy. Bangladesh should draw on international experiences in East Africa (mainly Kenya), India, China and elsewhere and put in place various Fintech enabled SME financing business models. It needs to put in place the policy and regulatory actions that are necessary to allow these business models to flourish while mitigating risks to financial integrity, stability and investor protection.

## 4.8 Improving the legal framework for contract enforcement and solvency

The total FDI inflows into Bangladesh are a mere $2 billion as compared with a total supply of $600 billion for all developing countries. While the dynamic East Asian economies of China, Hong Kong and Singapore have led the way for the developing countries in attracting FDI, India and Vietnam are also doing well. Armed with low-cost labor and good macroeconomic management, Bangladesh has tremendous potential to attract FDI. The investment climate improvement measures noted above should have a positive impact on this. Additional, foreign investors are very particular in paying attention to certain aspects of the legal framework, including contract enforcement and resolving business insolvency. The IFC ease of doing business have identified these two issues as the biggest investor concerns, especially for foreign investors. So, it is imperative to modernize the regulatory framework for private investment, especially for foreign investors, through proper policy actions in these two areas.

A number of actions are recommended.

* As a first step, the Law Ministry should check the adequacy of these two important enabling regulations in light of international good practice. Based on that review, appropriate steps have to be taken to streamline and strengthen the related regulations.
* Secondly, the government should ensure that adequate administrative and legal procedures are in place to enforce the sound implementation of these regulations. The government can learn from the experience of good practice examples how business disputes are resolved and how bankruptcy proceedings are implemented internationally. This review can then inform what actions are needed to enforce proper implementation, including whether there is a need for separate legal entities to resolve business disputes in a timely manner and with minimum transaction costs.

**5. Conclusion.** Over the next two decades, the regulatory regime will have to reach a transparency level that will provide certainty to the entrepreneur to undertake investment risks similar to the more developed countries now. During this period the focus should make institutions and regulatory agencies impacting doing business environment to become world class and fully digitized. In this context some of those key institutions which should be leading the way are Tax Administration, Customs Administration, VAT Administration, Land Titling Administration, Land Registration, Department of Environment, Registrar of Joint Stock Companies, BIDA, BEZA. At the same time there has to be zoned development and backed by adequate and high quality infrastructure.

1. ESCAP (2017), estimated Bangladesh would need to investment $ 10 billion only to cover the huge infrastructure gap between 2015 and 2030. This investment would however increase GDP by about 3.94 percentage points implying annual addition to GDP growth of 0.26 percent only from this source. This scenario also includes USD 33 billion investments for Delta projects. [↑](#footnote-ref-1)
2. FIAS Report on SEZs [↑](#footnote-ref-2)
3. Jin Wang, London School of Economics Job market Paper Version of November 2009 – The Economic Impact of Special Economic Zones: Evidence from Chinese Municipalities. *His research concluded that, the SEZ related policy package, including private property rights protection, tax breaks and land use policy, increases per capita municipal FDI by 58% in the form of foreign-invested and export oriented industrial enterprises. The report also found out it increased municipal foreign owned capital stock and did not crowd out domestic capital (and investment), and showed that it helped bring in more advanced technology and increased municipality TFP growth by 0.6 percentage points.* [↑](#footnote-ref-3)
4. Special Economic Zones, World Bank [↑](#footnote-ref-4)
5. FIAS Report, April 2008 [↑](#footnote-ref-5)