

# BANGLADESH POVERTY: THE NEED FOR A "BIG PUSH"

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## ABSTRACT

Bangladesh has agreed to meet certain *poverty reduction* targets by 2005, involving both the economic and social aspects of poverty. The prospects for meeting these targets are examined. It is shown that the social goals are on their way to being met, but the chances of reaching the income poverty targets with current policies are slim. The long-run growth rate must be raised and this requires focusing upon the long-run, and upon economics, narrowly considered, to a much greater extent than is currently done. Export-led growth will not be adequate. Entrepreneurship and infrastructures will have key roles to play, as will family planning. Simple but far-reaching institutional changes, such as computerizing land records are needed. Poverty reduction requires a return to income growth as the primary object of policy.

### Introduction and Thesis

This essay takes poverty reduction as the primary goal of current economic policy in Bangladesh and asks if the Government of Bangladesh (GOB) will meet the poverty reduction goals it has committed itself to; if not, what are the most acceptable options? The consequences are not just economic. While Bangladesh has often gained attention as a "Test case of Development", recent events have also noted the example of Bangladesh as a bulwark against political extremism. The State Department has already praised Bangladesh as a 'moderate Muslim democracy', but if the projected poverty and population growth continues, extremism is being provided a fertile ground. It should also be noted that Bangladesh is an ethnic and religious 'border state'. Immediately to its east are peoples who differ both in ethnicity and religion; even those areas currently part of India were historically under the influence of the Burmese, and some of these people have been in revolt for decades. Once there is turbulence, it is not easy to predict the outcome. The economic development of Bangladesh is not just in the interest of the Bangladeshi's.

This essay is also concerned, as part of the inevitable process of deciding practical policy, with setting orders of magnitude for the various aspects of poverty. That poverty is a hydra headed monster is one of the truisms of our day. Which head should we tackle first? And how can we keep the other heads of the monster at bay? Given the targets to be achieved, it will be argued that the only relevant poverty measures to be *actively* implemented involve income growth, supplemented by a renewed attention to family planning. There are many other desirable goals, but they are all more readily tackled or are already on the way to being met. It may seem to be taking a step back in time, but this makes the problem of poverty *primarily* an economic one, in the narrow sense.

It will be argued that some vision of the long run must come to dominate economic thinking since both the GOB and the donors have been overly occupied with the short-run. This makes floods and cyclones, political turmoil and global recession--- survival till the next crisis-- the only future! It fails to instill hope, the first requirement of good policy. This paper will argue that the magnitude of the problems facing Bangladesh is such that only a 'big push' will be adequate if poverty is to be reduced. The usual categories of agriculture, industry and services do not throw new light on policy, and export-led growth seems unlikely. Rather, the emphasis should be on institutional changes that foster *entrepreneurship* and on *infrastructures*. The measures needed for these goals are straightforward and relatively simple. Once the long run is seen as being stable, the short-run will cease to agitate us.

A word on references and supporting material: The published scholarly literature on Bangladesh is so dated as to be useless for most policy decisions<sup>1</sup>. As a result, working papers and reports as well as the Internet are the most useful way to get to the relevant facts. Brevity requires a minimum of data, tables and graphs---but I have tried to provide full references for each item. Having worked constantly on Bangladesh since 1996, including two sabbaticals in Dhaka, several views are just the result of accumulated experience. For all these reasons, the paper will read as being more opinionated than it is meant to be<sup>2</sup>. There is simply not enough space to justify all opinions and I chose those I consider to be central for exposition.

It is convenient to begin with the multiple goals the GOB has committed itself to, and then to summarize the main theses of this paper. The Partnership Agreement on Poverty Reduction, (hereafter PA), between the GOB and the Asian Development Bank

(ADB) lists the achievement of the following seven goals as desirable by 2005: These are: 1) Reduce by 25 per cent the proportion of people living below the poverty line. 2) A 50% reduction in the proportion of children 6-10 not attending school. 3) Eliminate gender disparity in access to basic education. 4) 20% reduction in the proportion of children under 5 who are malnourished. 5) Reduce maternal mortality by 35 per cent; 6) Reduce infant and child mortality by 30 per cent; 7) 50% reduction in the proportion of women of appropriate age not having access to reproductive health services. Which of these goals have been met so far and what is the likelihood of meeting the targets under current policies? If some goals are not going to be reached, what should be done?

The first goal is to reduce the poverty count by 25 per cent by getting GDP to grow rapidly. The goal set is ambitious as this is much higher than the historical trend of poverty reduction achieved hitherto. The empirical estimates of past poverty reduction suggest that a GDP growth rate of about 10 per cent is needed for the PA goals to be reached. Whether such growth is feasible is a difficult question to answer and will occupy much of the paper. But let us look at the social goals before providing an overview of the main thesis.

The remaining goals of the PA, from the second to the seventh, deal with Education and Health, or the Social Sector. There are no theoretical grounds for assessing the impact of income on say, gender equality, so the extrapolation of current trends is taken as the basic method for studying these issues. Bangladesh made encouraging progress in social development during the last decade. Between 1992 and 1998, the country's Human Development Index (HDI) increased by 49 percent along with improvements in key social indicators.<sup>3</sup> *At current rates of progress, all the social goals set for 2005 appear to be achievable.* For example, the GOB has made very notable gains in extending education and in making it more equally accessible to girls. This is true of all the other social indicators of poverty.

One can argue that perhaps the standards for health and education should have been set higher, but that is not only a different question, it is one that is perhaps irrelevant in view of the deficient economic growth and the stalemate over family planning. Indeed, the omission of family planning as an explicit goal in the PA is a serious lacuna. The failure of *total fertility rates* (TFR) to come down further means that the population may grow beyond 250 millions, instead of stabilizing at 200 million. And this in a country with

55,000 square miles! High population growth can easily negate the effects of greater GDP growth. Population estimates also influence proposed spending requirements in Education and health. On every ground, it is urged that family planning be urgently drawn directly into the agenda of the PA.

The current Government, elected in October 2001, faced several budgetary and foreign exchange crises. The World Bank was firm about not increasing aid unless *state owned enterprises* (SOE's) are privatized and corruption is curbed. The losses from SOE's are enormous---about Taka 30 billion in the last fiscal year. But simply dismantling SOE's will increase unemployment in a sector where labor is strongly organized. Without suggesting concrete alternatives, how can a Government move? As for corruption, simply urging that it be ended is idle sermonizing. What is needed is a nuanced approach that develops concrete alternatives. Unless people have hope for the future, they will continue to maximize their short-run individual payoff---because this is what their individual self-interest tells them to do.

What can we learn from the immediate past that will help to sharply increase the growth rate? There has been good progress in agriculture, industry has been relatively static, and the service sector has provided background support for both employment and income. What are the prospects of any or all of these sectors providing the thrust for a significantly higher growth rate of GDP?

Agriculture is dominated by the production of crops, and this sector is unlikely to be such a leading thrust sector. It is highly dependent upon the weather, the demand for crops is inelastic and increasing portions of the output of agriculture consists of non-farm output, whose potential is more properly considered under small and cottage industry. Agri-processing may have potential, but this can be realized only with more favorable exchange rates. Industry has not shown dynamism so far and *foreign direct investment* (FDI) has not been forthcoming in requisite amounts. Services have mostly been a residual catchall, and, given the low levels of skill and literacy, this is likely to continue. These cautionary statements are supported by a direct study of some prominent sectors, particularly those that bear on export-led growth.

If domestic entrepreneurship is to be provided a secure base from which to operate, even as it seeks to spread its wings internationally, domestic economic performance has to be sustained at a high level while the bases for international competitiveness develop.

This requires a sustained thrust towards pro poor economic growth in the domestic economy. It is not just a question of raising incomes. Thus, gas exports will not do the job because of the highly capitalized production technology and the absence of linkages.

Infrastructures have been shown to have a significant impact upon incomes and to reduce poverty. However, the marginal impact of additional infrastructure under the current system appears to have noticeable diminishing returns. Most new poverty is urban poverty. This suggests that a scheme to 'capture' the growing urban poverty in secondary towns or rural areas through investment in infrastructure is likely to be the most promising avenue for sustaining a high growth rate of GDP and the simultaneous reduction of poverty. The growth of secondary towns and of market areas in the form of *growth centers* (GCs) has long been an item of the agenda of the GOB and it has received substantial donor support in this endeavor. It is suggested that this thrust be taken to its logical conclusion and the introduction of *compact townships* (CTs or dense rural settlements with modern infrastructure) be supported in selected areas.<sup>4</sup> With the background of a large infrastructure program providing the promise of employment and secure utilities and transport, the seeds of entrepreneurial efforts need to be nourished by policy. Entrepreneurs will have to find profitable opportunities by themselves, but they need the rule of law and finances to exploit these. Sound governance is a prime requisite for stimulating the high levels of growth desired, and it will be argued in what follows that if an infrastructure program (whether involving CTs or some other concept) of the desired magnitude is adopted, this will alone provide much of the stimulus for good governance. The next item on the agenda, after infrastructural programs is the provision of credit: Institutional changes, such as those involving land records and sales, will at once reduce the litigation arising from land disputes, and provide individuals with collateral they can use for investment funds. The success of the garments industry shows that Bangladesh does not lack for entrepreneurship. The challenge is to provide for the entry of fresh new blood and to enable current entrepreneurs to aspire to higher accomplishments.

### **Growth for Poverty Reduction**

The first item on the agenda in the PA relates to poverty. The Bangladesh economy has raised its growth rate from 4 per cent in the 1980's to just under 5 per cent in the 1990's. In the second half of the 1990's the growth rate has remained at or above 5 per cent. The decades of growth since the

independence of Bangladesh in 1971 have reduced the incidence of poverty from over 70 per cent in 1973 to 47 per cent in 1996. It is estimated to have come down to below 44 per cent in 2000. This reduction has been general over geographical regions, even though poverty is slightly higher in rural areas, and it is noteworthy that the poverty decline of the latter half of the 1990's was not accompanied by worsening income distribution (ADB 2000). We can consider the feasibility of achieving the PA goal by extrapolating from the past which, however, does not give much ground for optimism. If we look at the impact of currently achieved rates of growth on poverty reduction, and extrapolate them into the future, we find the following. Using the calorie intake method, the past rate of poverty reduction, between 1996 and 1999, was 1.7 per cent annually; while the rate required to achieve the PA target is 4.7 per cent--virtually a tripling of the growth rate!<sup>5</sup> Finding ways to increase the growth rate of per capita GDP is the first priority in achieving the goal of reducing poverty.

Two facts could make the task somewhat easier. First, the impact of income growth on poverty--what is technically called the poverty elasticity--is significantly higher for agriculture and rural areas than for urban, industrial ones: the available figures suggest a pro-poor policy based upon rural areas and upon agriculture. Secondly, all the poverty reduction elasticities have been calculated for per capita growth rates and hence all of them depend upon population growth rates. If population grows at a slower rate, more poverty reduction is achieved. While the subsequent argument is framed largely in terms of the growth rate, this does not mean that the poverty elasticities should be considered rigid. Indeed, we can use higher poverty elasticities as an alternative to higher growth rates, or better yet, in conjunction with them.

Growth for poverty reduction differs from ordinary economic growth precisely because it examines how an increase in income will affect poverty. Gas exports for example are a much discussed policy in Bangladesh. Gas exports are being considered to provide (a) the foreign exchange to pay for the contractual obligations to the International Oil Companies, (b) resources for the development of downstream industries in the sector, and (c) cushion for the balance of payments. While these are all desirable in themselves, they do not bear directly on the reduction of poverty; indeed, given the capital-intensity and high skills needed in this industry, the direct impact on poverty will be small in relation to the expenditures.

Since per capita growth necessarily requires a consideration of population growth, it is as well to note an inexplicable lacuna in the goals set by the PA: the role of family planning.<sup>6</sup> The failure of fertility to continue declining, even if replacement fertility is attained in the next decade, means that the final size of the Bangladesh population is projected to rise to over 260 million, or double the present size. Why has the sharp decline in fertility of the previous decade has reached a plateau? The *Strategic Directions for Bangladesh National Family Planning*<sup>7</sup> found that 50% of non-users of family planning did wish to use contraception. Why has there been such limited success in reaching them?

While the consequences of static fertility rates are grave, the problem itself is amenable to analysis. Indonesia also had a plateau in its fertility decline. This was an 'expected' outcome because the initial emphasis of its population program was on easy distribution methods. The contraceptive mix currently used in Bangladesh needs to be reviewed—sterilization, IUD and injectables need more emphasis (according to the officials at the World Bank, Aid Memoirs have been saying this since 1993.) But progress has stalled since 1995. It seems to be largely a management issue.<sup>8</sup> Currently, doctors are under the Directorate of Health while Maternal Health is under the Directorate of Family Planning. There is an uneasy unification at the lower (Thana) level but it is separated again at higher levels, leading to adversarial relations between two complementary parts of the health program. Because of the partial implementation of the sector-wide approach, (following the Cairo Population conference guidelines), the system of home visits by family planning workers has been facing a stop-go status, without putting in place any alternative system of community-based health clinics. This is a good example of how an otherwise well-meaning plan can go astray because of lack of ownership and good governance. These problems do not need more money for a solution; they need more carefully crafted decisions.

### **Short-run Strains, Long-run Impasse**

The overall stability of the macroeconomy is quite good. While my principal argument deals with the long-run, a brief glance at the short run issues of 2001 will be useful to provide a perspective in which to view Bangladesh's economic policy. High growth in agriculture had led to a high growth rate for the economy as a whole: about 5.7 % for 2000. Gross savings rates had increased from 16.7% in 1995 to

21.3 % in 2000. Inflation had been contained to the low single digits despite an increase to 8.9 % in 1999 due to the floods. Inflation was low between 1996 and 2000 as the government exercised restraint in borrowing, revenue collection improved, with an annual increase of 15% and good agricultural harvests have contained the most volatile aspect of costs. In 2001 the early macroeconomic trends appeared very promising. The index of industrial production rose by 11 percent, compared to the similar period of the previous year. A continuation would give rise to the highest annual growth in industrial production since 1994-95. Similarly, export earnings registered a 16 percent annual growth in the first three quarters of 2001, compared with 8 percent growth during 1999-2000.<sup>9</sup>

These favorable indicators hid some deeper strains. Government expenditures increased in 2001 while tax collections did not keep pace. To further sustain the SOE's, despite their losses, the Government borrowed large amounts and injected much liquidity into the financial system. Combined with the non-performing loans of the banking system over 40% and the low levels of foreign exchange this has made for a fragile financial framework within which the macroeconomy has to operate. The excellent export growth of as much as 25 per cent between July and December of 2000 slowed down considerably in 2001 and the global slowdown, combined with unrest at home, produced further sharp declines.

The major area of weakness was the low and declining level of foreign exchange reserves, which currently stands at about \$1 billion. Of greater concern, foreign remittances, somewhat inexplicably, became virtually stagnant after having grown rapidly in the previous years. The errors and omissions item in the foreign accounts has grown considerably, suggesting capital flight, and foreign aid disbursements have declined sharply. Hence the usual means of increasing foreign exchange reserves are not at hand.

A spending spree from the development budget just before the election (Jan-May 2001), raised Government borrowing sharply, thereby posing risk to external balance and macroeconomic stability. The Government financed a large fiscal deficit from domestic sources. As a result, the interest burden on Government debt is rising sharply. Despite the recent increase in efficiency of revenue collection, Bangladesh has one of the lowest tax/GDP ratios in the world, so the interest burden on the debt will start crowding out investment in other sectors. It has been widely noted that a lack of fiscal discipline was the

main underlying cause of the above short-run problems. The short term requires budgets that are more balanced, more oriented to development, combined with a competitive alignment of exchange rates to promote exports.

These macroeconomic strains have been contained, despite some loud grumbling from the Finance Minister about the high-handedness of the donors. Assuming short run problems can be similarly managed in the future, how will the pattern of growth exhibited till 2001 affect poverty reduction? The policy of the "Washington Consensus" is being followed, but is it enough? Shahid Alam has shown how those who followed the "approved" policies did not grow as fast as those that showed nationalistic aspirations and Leah Greenfield has made the same point by historical analysis in a very recent book.<sup>10</sup> The simple extrapolation done above suggests that more than just the 6-7 per cent growth proposed by some donors is needed, demanding as it already appears. How is this growth to be achieved? After reviewing the performance of specific sectors such as agriculture, industry and services, it will be suggested that none of these—or exports such as garments or information technology—will suffice to provide the basis for such rapid growth. Therefore, the critical thrust must come from infrastructures.

The excellent performance of agriculture in recent years has been a pleasant surprise. Agriculture has been the leading sector of growth, achieving self-sufficiency in rice and producing a record 25 million tons. While agriculture grew at a slow average of 1.6 per cent in the first half of the nineties, it picked up considerably in the latter half, from 3.2 per cent in the 1998 to 6.4 per cent in 2000. What has accounted for this remarkable performance and can it be expected to continue? Why has the cautious pessimism of the World Bank (2000) been mistaken? The weather has been unusually favorable, something that cannot be extrapolated. Even the severe floods of 1998 were followed by a bumper harvest and did not affect the trend. There has been adequate supply of key agricultural inputs such as fertilizer, seeds and diesel, at stable prices. The Government had also reduced the import duty on a variety of agricultural equipment such as power tillers. By such means the inputs to agriculture have been kept within readily calculable reach of the farmers. On the output side, procurement prices have been slowly increased, from Tk 1100 to Tk 1250 for Aman and from 1125 to 1300 for Boro and from 750 to 880 for wheat, thus providing farmers the right incentives to use the higher productive inputs. To enable marketing and planning, agricultural credit was provided much more

freely. Overall, agricultural policy has been consistent, coordinated and steady. The question is, how long will the gains continue? We typically distinguish between reaching one's production capabilities and being able to expand them. By easing input supply, raising output prices and enabling credit, the farmers have been able to reach their potential; now it is time to expand the farmer's frontiers, something normally beyond the capacity of individual farmers. The success in crop production has been the most noted feature of agriculture. However, the demand for crops is inelastic and studies suggest that the fertility of land is decreasing.<sup>11</sup> Furthermore, crops are very dependent upon the weather, so it is too much of a gamble to rely upon traditional agriculture as a thrust sector.<sup>12</sup> Hence further progress in agriculture has to come from non-crop sources, particularly agri-processing which seek out high value and high quality products. According to the World Bank, this is most affected by having competitive exchange rates.

Industry, on the other hand, has been sluggish. While Industry grew at 7.5 per cent in the first half of the nineties, it has now slowed down to 5.6 per cent from a high of 8.3 per cent in 1998. This lackluster performance has been attributed to a "slowdown in the pace of implementing sector specific reforms, severe infrastructure bottlenecks, especially of power and ports, social and political unrest, and weak corporate governance."<sup>13</sup> The weakness of the financial sector, especially the high percentage of non-performing loans, has been a staple of all commentaries upon the Bangladesh economy. Under these circumstances, it is hardly surprising that foreign investors have also been deterred from investing in Bangladesh. While the pattern of import growth in 2001, with capital machinery and industrial raw materials playing a big role, suggests a good rebound, the problems of the financial sector and of governance remain.

It is convenient here to note that the service sector, which is now the bulk of the economy, provides a vital source of employment. What is misnamed the 'informal' sector is actually a hotbed of indigenous entrepreneurship, which is why it has been subsumed within 'entrepreneurship' in a later section and is not treated separately. There are about 570,000 establishments in the 'informal' sector and they employ over 70 per cent of the manufacturing labor force. Of equal significance is the fact that the landless rural population, which consists about 26 per cent of the total number of households, spends almost as much time in non-agricultural activities as in agricultural ones—48per cent labor days in non-

agriculture versus 52 per cent in agriculture.<sup>14</sup>

### **Export-led Growth?**

A great deal of hope is placed in popular discussion upon the beneficial effects of liberalization and globalization. While international markets are probably the most fruitful source of demand over time, there are few grounds for relying heavily on this avenue. As this may sound unduly negative, it is worth considering some specifics. We can consider the prospects for continued entrepreneurial success in two popular sectors, Ready Made Garments (RMG) and Information Technology (IT), and the prospects of expanding into India, the most promising market for Bangladesh.

There is no doubt that the first two decades of RMG in Bangladesh have been a grand success. Bangladeshi entrepreneurs have convincingly shown that they are capable of utilizing profitable opportunities in the world market. Presently, the industry occupies the enviable position of being the largest manufacturing and export business in the country, employing nearly 2 million workers, 90 percent of whom are women. The response of the industry to a natural disaster is revealing. The floods that affected Bangladesh between July and September 1998 were among the worst natural disasters impacting the people and the economy of Bangladesh in recent history. The 1998 floods directly impacted thirty million people for three long months. The negative shock to the economy reduced GDP growth significantly<sup>15</sup> and created a crisis for the tightly scheduled export industry; but the industry and the individual firms responded creatively. As a result, exports were steady, in terms of both value and volume, during the July-August 1998 period when the country was in the grips of widespread flooding; production and export capacity were also minimally impacted by the floods. This is a remarkable achievement.

The share of apparel products in total exports has steadily risen for several years. In both absolute and relative terms, the industry dominates the modern economy of Bangladesh. In addition, the positive sociological, demographic, political and economic impact of 1.5 million workers employed in the manufacturing sector is huge. The knitwear sector has been especially dynamic in recent years. Given the fact that the market for knitwear exports is unprotected by quotas, this bodes well for the post MFA future of the industry. Unfortunately, other potentially promising exports from Bangladesh—leather, jute goods, and frozen foods—have not fared

as well over this period. This has accentuated the already narrow export base of the country and is a matter of concern. Limitations of Bangladeshi entrepreneurship are seen in the fact that the large buying houses in Dhaka are now controlled by Indians and Sri Lankans. Originally many Bangladesh firms had direct contracts but they could not maintain the quality or the schedule. Now that a backward linkage industry has gained a foothold, it is asking for protection. The biggest threat to exports, which in practice means the RMG industry, comes from the financial sector, which is characterized by a weak banking sector with little transparency or central bank control. Elements of crony capitalism and moral hazard are certainly present in Bangladesh, especially in the nationalized banking sector and in credit markets.<sup>16</sup> According to a World Bank-Asian Development Bank report, the financial sector in Bangladesh remains fragile with 33 percent of the portfolios of the nationalized commercial banks (NCBs) and domestic private banks in the non-performing category.<sup>17</sup> Notwithstanding the fifty billion taka of taxpayer money that was used to re-capitalize the NCBs in the early 1990s, the system-wide capital inadequacy today is very large since the default rate, which was over 40 per cent in 1999 is still at about 35 per cent. This situation could cause the entire banking system to collapse under foreign or domestic shock. One important lesson from the East Asian crisis is that moral hazard and the resulting financial panic can be very costly for an economy, even when the fundamentals are sound. Other potential hazards include an overvaluation of the taka compared to the currency of its competitors. Despite the repeated devaluation in the recent past, according to the World Bank, the taka had remained overvalued in real terms. This could undermine the long-term competitiveness of the industry. It is too soon to know the effects of the recent float of the taka. Finally, in the year 2004, under the Uruguay Round Agreement on textiles and clothing, MFA quotas will be phased out. Bangladesh will lose its preferential access to its most important markets and will have to compete with India, China and other apparel exporters in a truly global competitive environment. Many apparel firms in Bangladesh are not ready for this change, although the more efficient larger firms that have diversified their products and markets are expected to do well in the post MFA world. These limitations are being stated only to remind us that the RMG will be struggling to keep up with past success, and cannot be relied upon as the source of the additional thrust needed to boost the growth rate to ten per cent.

The limited entry of Bangladeshi entrepreneurs into the higher end of the value chain—which involves

marketing abroad—is a limitation that could be usefully tackled if Bangladeshi products could readily penetrate the nearest foreign markets and thus gain the experience and self-confidence that would enable them to try for the global consumer. This requires a closer look at the Indian market, where trade is supposed to be on a level playing field. The balance of trade between Bangladesh and India has been greatly in favor of India. Not surprisingly, the continual growth in the India-Bangladesh trade gap has taken large political dimensions in Bangladesh. Despite several formal and informal bilateral and multilateral meetings on regional cooperation and opening its economy, the impression in Bangladesh is that Indian politicians and bureaucrats have steadfastly discouraged imports of finished products from Bangladesh. A study of the disaggregated pattern of import sources shows that Indian exports to Bangladesh are largely of import substituting nature.<sup>18</sup> They serve to help Bangladesh's overall trade flows and preserve the value of the Taka. It is not so much India's imports into Bangladesh that call for explanation as the lackluster Bangladeshi exports into India. The Bangladeshi entrepreneurs urge that it is not just their own limitations but also the persistent bureaucratic hassle imposed by Indian officials that limits their perception of India as a market.

The 'policy' of building a surplus in trade with Bangladesh has continued despite shifts in political power and a move towards liberalization at the center in India. Bangladeshi policymakers have reluctantly come to realize that trade with India now is not on a level playing field. This partly explains the resistance to selling natural gas to India and providing new road access to Bangladeshi ports for Indian products. Throughout Bangladesh, there is a general perception of Indian commercial imperialism. This is true not just in Bangladesh media but is supported by those with no axe to grind, such as the eminent diplomat Mukchund Dubey, who said "Unfortunately, the most natural and easily accessible market, India, still remains by and large closed to Bangladesh. India is following a short-sighted, niggardly and over-cautious incremental approach towards opening up its market to imports from Bangladesh. A Bangladesh request to grant duty-free access on a non-reciprocal basis for a list of 25 product groups has been under consideration for more than two years now...This is also despite the fact that among external suppliers, India has been the biggest beneficiary of Bangladesh's policy of trade liberalization."<sup>19</sup> Indian imports are undoubtedly valuable to Bangladesh. However, at present, it seems that Bangladeshi exporters are unfairly limited by bureaucrats and businesses in India. This strategy is essentially short

sighted since much more than trade is involved in these economic relations. Bangladeshi entrepreneurs must be able to look upon the subcontinent as one market. The government of Bangladesh can help change current stagnant viewpoint by nurturing exports to India and by working at the political level to achieve a fair playing field for such exports. However, the onus of reform lies on the Indian side. The Indian politicians and bureaucrats must rise to the challenge of exercising benevolent dominance and make a genuine attempt to ease the flow of goods from the Bangladesh side. Whether they have an interest in doing so is a question yet to be answered. As always, the enlightened sections in the Indian business community can help foster this change in strategy.

The phrase 'Information Technology' has acquired something of the aura of a silver bullet among the LDCs. For any LDC to succeed in such a strategy it has to establish a comparative advantage. This is precisely what is hard to do in a world of globalized trade where everyone, from Venezuela to Vietnam, is aware of a new profit opportunity. In other words, there are no longer gains from secure export markets, such as Taiwan and South Korea enjoyed for awhile, both because of their special relationship with the United States and because they were first-comers in exploiting the 'export first' strategy. However, it is only repeating the obvious to state that no one eats, wears, or lives in software. Information Technology is worthwhile either directly, as in the production of software, or indirectly, when it increases the efficiency of other production processes. Many enterprising individuals have started obtaining code writing contracts and training low level workers in the skills necessary for such tasks. Soon Bangladeshis will be joining Indians in Silicon Valley in the army of temporary workers who do software on contract basis. The question is whether the impact will be of sufficient magnitude.

Three facts stood out in India's favor in her recent rise to prominence in IT. First, India's educational system, specially in the sciences and mathematics, is second to none in quality; secondly, a legacy of British rule is that India is fluent in English, the primary language for IT in global business; and thirdly, that significant numbers of Indians were already in prominent positions in the US business world and were looking for ways to help the motherland. To state these reasons is to understand why Bangladesh should not hope for too much success in direct production of IT wares. Bangladesh lacks the educated manpower, both in quantity and quality, to make a significant thrust in, say, software;

Bangladesh has spent a decade neglecting English as a language and hence many graduates lack the understanding of idiom so essential to communication with a potential client; and Bangladeshi managers in the upper echelons of the corporate west is a very recent and still rare phenomenon. These reasons limit the quantitative gains to Bangladesh in Information Technology even if it could obtain the requisite contracts.<sup>20</sup>

Since neither agriculture, nor industry, nor exports appear able and willing to bear the burden of raising the growth rate to ten per cent, some other means must be found. It is argued that this consists of enabling domestic entrepreneurship to grow and for infrastructure programs to be initiated that will immediately stimulate domestic demand and support the eventual entry into world markets.

### **Entrepreneurship**

In view of the stagnation of heavy industry, the first step is to examine the potential of smaller manufacturing units. Small and Medium Enterprises (SMEs) can play a critical role in bringing economic development and reducing poverty in developing economies. *The role of Small and Medium Enterprises in generating pro poor economic growth will be clear from the fact that such enterprises are usually labor intensive, easy to enter (and exit) and have low capital requirements.* They are the most fertile breeding ground for future entrepreneurs. In view of their potential, this is a sector worth describing briefly. In Bangladesh, where small means 10-50 workers and medium 51-99 workers constitute over 80 percent of manufacturing establishments, SMEs provide backward and forward linkages with micro and large enterprises, and form part of core business activities. The bulk of SMEs are small in size (89 percent), many of which overlap with micro and cottage type of activities, while 11 percent are medium enterprises. Most SMEs are located in major cities and in peri-urban areas, are very varied in their activities, and were involved in 209 types of manufacturing activities out of 213 at the 3-digit level. Two major industrial categories combined – food, beverage and tobacco manufacturing (33 percent) and textile and leather production (20 percent) – comprise over half of SMEs.<sup>21</sup> From the ISS data, share of SME (defined as 10-100 workers) relative to their larger cohorts (more than 100 workers) shows that SMEs make up for 85 percent of the establishments; they have 48 percent of the fixed capital, 33 per cent of the gross investment and 40 per cent of the sales. Significantly, the Net value added and returns to capital for SMEs are 37 percent and 43 percent respectively of the total value of

private manufacturing units.

Subcontracting between large and small firms is a pattern common to most developing countries and has been particularly significant in Japan. Such networks are usually a good sign since they not only enlarge the pool of skilled labor and entrepreneurship, but are also capable of fairly complicated and delicate production operations. An important development over the last decade has been the emergence of a small number of large firms, with a large number of small firms which feed the larger ones through subcontract arrangements (JOBS, February 1998). The larger units identify the marketing chain, and expect the smaller units to focus on production. This behavior is common in footwear and the readymade garments sub-sectors.

A recent World Bank study (November 1999) concludes that the majority of manufacturing enterprises have experienced efficiency gains, or positive total (factor) productivity growth between 1992-93 and 1997-98, averaging 29 percent over a five-year period or 5 percent annually. The small and medium sized firms, as well as the large firms, enjoyed improvements in Total Factor Productivity (i.e. better use of all inputs) but failed to close the gap with the best practice firms in terms of technical efficiency. In other words, this sector shows great vitality and potential. Perhaps the major impediments to realizing it's full potential is the existence of significant transaction costs, both in setting up and in continuing operations..

For example, the procedure for setting up a formal sector enterprise is lengthy and can be cumbersome. Multiple licenses, approvals or permits are required. The business registration process entails obtaining a trade license. According to the Factories Act 1965, all manufacturing enterprises employing 10 or more workers are required to register with the Office of the Chief Inspector of Factories and Establishments. The Chief Inspector is expected to monitor the safety and working conditions at the factory sites. Registration with the Joint Stock Company is mandatory for all private limited companies. SMEs engaged in import, production of goods or services, and are subject to Value Added Taxation (VAT), are required to obtain a VAT registration. SMEs are required to obtain Tax Payers Identification Number (TIN) at the time of (a) opening a letter of credit for the purpose of import; or (b) renewal of a trade license; and (c) submission of tender documents for purpose of supply of goods or services, execution of a contract or for rendering of services. A clearance from the Department of Environment is required of all manufacturing

enterprise, ensuring that anti-pollution and safety measures are adhered to. This listing is not exhaustive, but demonstrates how many governmental agencies a business establishment has to encounter in order to start a business. Smaller enterprises are particularly more frustrated by such lengthy processes as they often do not have the resources or expertise to comprehend, much less comply, with the procedures.

Poor governance discourages business in general. For example, the amount of time that businesses have to spend as well as the side payments they have to make to complete any simple transaction—such as getting a passport, registering a land title, obtaining a building permit, obtaining utility connections or a phone connection or licenses—are enormous (Table 4.2).

Businesses in Bangladesh have to face corruption in every phase of operation—from obtaining a trade license to performing day-to-day business activities to expanding a business. Apart from all these legal requirements, another aspect of poor governance is that entrepreneurs have to pay monthly tolls to local

mastaans (hoodlums) simply to maintain steady production as well as in expanding a business.

Very small firms, say with less than 10 workers, are hardly worth anyone's time, whether it be the tax collector or the local gangster. This keeps them somewhat insulated from illegal payments. Small firms are vulnerable to 'bandits', and not strong enough to buy security, which large firms can arrange. Large firms thus end up with less illegal payments per unit of production. Figure 4.2 shows that a small firm poised for growth, at point b, faces the highest per unit cost of corruption: hardly the best way to be a catalyst for economic growth!

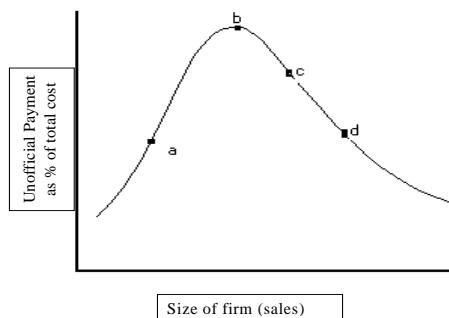
Some simple forms of discrimination against SMEs are probably unintended. Currently, an individual, if sufficiently wealthy, has to pay a wealth tax but a company (the usual legal form of a large business entity) is not required to pay the wealth tax. Since small enterprises usually take the form of sole proprietorship, they become liable for wealth taxes on their business capital. Thus, the fiscal policy of Bangladesh does not extend much support to SMEs. It has to be recognized that both Japan and Taiwan made much use of these small but flexible production

Table 4.2: The Hidden Cost of Service

Service	Standard Time	Waiting	Informal Payment for Faster Service
High Tension Electricity Connection			Taka 100,000-150,000
Low Tension Electricity Connection			Taka 10,000-15,000
Gas	3 months		Taka 40,000
Water	3-4 months		Taka 14,000-20,000
Phone	10-12 years		Taka 50,000-70,000
Trade License for a Garments Factory	1 year		Taka 5,000-8,000

Source: Government That Works, Reforming the Public Sector, The World Bank, 1996

Figure 4.2: Unofficial Fees as a share of Total Production Cost by Firm



Source: Data International, 1999. The Small and Medium Enterprise Sector in Bangladesh.

units during periods of rapid growth. Despite the discouraging growth rates available for the SMEs it is this sector that has the greatest potential for advancing pro-poor economic growth.

Credit and working capital have consistently remained major bottlenecks to industrial growth in Bangladesh. Availability of electricity is also ranked close to credit as a serious problem. Unlike India, utility rates in Bangladesh are the same for both large enterprises and SMEs, usually too high for the smaller enterprises. A recent survey shows that finance and marketing assistance are the two highest-ranked support services desired by entrepreneurs. The SMEs can also use guidance from accounting and management. Stable utility supplies at predictable rates and government policies aimed at promoting SMEs are looked for, but the sorts of training and consultancy support so often offered are not much in demand. What is more critical is enhancing quality through improved technology. Efforts to improve quality, not just the introduction of new products, are vital as this will give access to export markets and make local outputs serve as import substitutes.

Given the seriousness of the credit constraint, the Government can make wealth more usable. In technical terms, it can 'liquefy' existing wealth, by allowing more transparent and transferable forms of property. Land and housing are at present the 'sinkholes' of accumulation. The GOB and the donors have been trying for a decade to implement change. The land management system has been characterized as 'dysfunctional' in an ADB study while the World Bank Legal and Judicial Capacity building project characterized the judicial system as follows: "The system lacks transparency, accountability and the capacity to plan and manage its own affairs; it limits access and is inequitable and, perhaps most vexing, it is subject to excessive delays." The document goes on to ask for reform of the land laws, as above, and to seek alternative judicial systems.<sup>22</sup>

The roots of entrepreneurship need to be fed by enabling people to use their own capital more freely and for the financial system to aid those who are resourceful with the funds to take on new challenges. Bangladeshi society is much like England in the 18<sup>th</sup> century, where family loyalty took precedence over other obligations; hence the freeing of family wealth is the first source of liquid capital for potential entrepreneurs. Land and housing, the two most potent ways of obtaining capital and the legal framework, can be enormously enabling here. The medium term goals for achieving the desired income growth should

be:

- Lower taxes selectively so that tax revenues are increased and entrepreneurs are not harassed.
- Liquefy wealth so as to increase the capital available for investment

The current Government is explicitly committed to taking itself out of business; what needs to be done to implement the two proposals above is neither complex nor costly.

### **Infrastructures**

The process of nurturing entrepreneurship, both for domestic and foreign markets, may take some time to bear fruit. In particular, the changes in governance may require several years to become effective. In the intervening period, poverty reduction must continue and the people prepared for the challenges facing a new generation of entrepreneurs. The other major task is to pull the social framework together while growth accelerates, and to provide the new generations with the facilities to continue growth. There are two broad methods for reducing poverty. The first is to arrange for income growth; this is an indirect way of reducing poverty, but it is perhaps most effective in the long run. The second is to raise the capabilities of the poor through health and education and then rely on an enabling environment to help the poor escape poverty. Or poverty can be directly addressed by targeted employment such as provided by microcredit; or income transfers can be used to provide a social safety net. Before going on to direct policies which will sustain a high rate of growth, it is worth noting the possible impact of the two direct measures frequently used to influence economic growth towards the poor: Microcredit and targeted programs.

Microcredit programs of public sector agencies promote income and employment opportunities along with training and other support activities. The Bangladesh Rural Development Board (BRDB) disbursed more than Tk. 10 billion as microcredit to 1.6 million beneficiaries during 1991-1998. Microcredit is also distributed by different Government ministries, departments and agencies (estimated at Tk. 20 billion until 1999/00).<sup>23</sup> The Nationalized Commercial Banks (NCBs) channel microcredit, the cumulative disbursement being Tk. 47 billion till 1999. Microcredit is very good at pulling the very poorest out of extreme poverty, but as it reaches those in higher incomes it loses effectiveness. *It is excellent at poverty alleviation; it*

*is not an instrument of continued economic growth.*<sup>24</sup>

The same comment applies to the aid provided to specifically targeted groups. Much good is done, but what next? Thus, the share of food grains distributed under the programs in the Public Food Distribution System (PFDS) rose from less than 40 per cent in the early 1990s to over 80 per cent in the late 1990s (GOB 2000). The programs largely attract the vulnerable poor due to self-targeting nature. The temporary and seasonal nature of the programs, however, limits their ability to generate sustainable incomes for the poor. In infrastructure development projects, not only do the poor benefit from participation in construction and maintenance activities, it is the poorest who appear to gain the most. Thus, infrastructure needs to be examined more carefully for its effectiveness.

Infrastructures not only benefit the poor directly, but, through the provision of education, health and electricity, enable the poor to enrich themselves over time. The following facts are of fundamental importance in this regard. Ahmed and Hossain, based on data on the most- and least-developed villages in Bangladesh, estimate the provision of good infrastructure could result in the average household income rising 33%. Specifically, income from agriculture increased by 24%, from livestock and fisheries by 78%, and from daily wages by almost 100%. Income from business and industries, however, rose by only 17 percent. The distribution of the increases revealed that the functionally landless and small farmers gained a larger share of the increase from crops, wages, and livestock and fishers, while the large landowners captured the smaller increase in business and industries. Another recent study indicated that, on average, the incomes of households in villages with good roads and electricity are around 13 percent higher than those of their counterparts in villages with underdeveloped infrastructure.<sup>25</sup> This suggests significant diminishing returns to infrastructure under the current pattern of provision and indicates the need for new approaches to infrastructure development.<sup>26</sup>

One has to absorb the magnitude of the problem facing Bangladesh in order to appreciate why new approaches should be tried out. The most striking reason is employment. By 2020 another 45 million people will be added to the population and another 50 million to the labor force! If we remember that Bangladesh was formed in 1971 in the land that was a new country in 1947, it is clear that we will have to employ *another* East Pakistan in 20 years! In 40 years we will have to employ another 80 million—or

*another* Bangladesh!

In order to fully understand why a new system for providing infrastructure has so much potential, one has to know that Bangladesh is one of the very few countries without nucleated villages. What is called a village is almost always a dispersed collection of homes brought together on paper for administrative purposes. The high productivity of infrastructure arises from economies of scale in production and in distribution; however, providing infrastructure under the current pattern of housing makes use of neither of these economic characteristics. People locate where they please and the Government promises to bring roads and electricity to them. It sounds like a really backwards approach, especially since the Government cannot afford to keep such promises. Populism is a convenient way to get votes but a poor bargain for the economy.

The situation with rural roads is particularly vexing. Bangladesh is a land-scarce country, a fact that scarcely needs repetition. Due to its topography, soils and floods, road building costs in Bangladesh are among the highest in the world. One would think that Bangladesh would economize on rural roads. Yet Bangladesh has the highest density of rural roads in the world.<sup>27</sup> What is this due to, if not the dispersed village homesteads? The facts suggest stressing rural and agricultural development; infrastructures will provide employment, slow urban growth, and assist the growth of rural manufacturing and agro-processing. Most of the world is familiar with the susceptibility of Bangladesh to floods and cyclones—to these, arsenic has become a threat for some 60 million Bangladeshis. Simply in order to meet these natural hazards in a cost-effective manner, people need to be placed in more dense living quarters anyway. All the goals come together by using Compact Townships (CTs).<sup>28</sup>

A Compact Township is an agglomeration of houses, hospitals, schools, markets, rural industries and local governmental units that provide all basic services to a population of about 20,000. It is to be largely self-governing and, once the government provides the enabling laws and demonstrates the concept with some pilot projects, substantially self financing. The size is small enough for traffic within the CT to be of non-motorized variety and for motorized traffic to be thus isolated from the CT itself. The CT will thus be well connected to markets yet environmentally friendly. As the size is small enough to provide effective protection from floods, the CT's will permit Bangladesh to do with many fewer embankments and thus encourage the re-emergence of a wetlands

environment, as well as serve to stimulate the renewal of freshwater fisheries. The general idea of a CT is simply a combination of integrated rural development with the idea of a growth pole, or its spatial equivalent, a growth center. The principal difference lies in the conjoined scale, scope, and purpose of the CT.

The optimistic scenario has population stabilize at 200 million by 2040. Let us assume the larger urban areas will accommodate 60 million people by 2050, over double the current level. If infrastructure is provided, and moving into the CT is voluntary, perhaps 20 million people will choose to continue to stay in their present homes; to house and provide opportunities for the remaining 120 million will need some 6000 CTs over the next 50 years. If we build 150 CTs a year this will take 40 years. If we assume that each CT is built over a two-year span, an average of 300 CTs will be in process each year. Employment will average 4000 per CT: a total of 1,200,000. I have been unable to find figures for employment multipliers, but if this is around 2 then the CTs will employ so many people that we will see something like a labor shortage! Hope is the best contraceptive and steady employment gives the most hope. So, the best single argument for CTs is that they will provide for full employment, that this will in itself reduce population growth rates, and provide the best prospects for future economic development. In addition, the CT can be provided with flood proofing, water can be cleansed of arsenic, small industries can be provided with power and telecommunications, and the community can be provided with web portals for education, business and health services.

All moves into the CT s will be voluntary. No force will be used. The only inducement will be an indirect one. No Government can be asked to support that which is beyond its means. It can be asked to provide education and health, but only in an affordable way. Those who choose to move into the CTs will have easy access to education, health, banking, family planning etc. Those who do not so move are still eligible for such benefits, but it will be much harder for them to gain access.

This brings up the all important question of financing. The important point to bear in mind is that all the benefits proposed such as education or health are no innovations. These promises have already been made to the people. The expenditures upon them are due. The real question is: How can we effectively do what has already been promised? The exact numbers I provide below are not of primary significance, only the orders of magnitude are.<sup>29</sup>

At current costs, with modest flats for each household, each CT requires about \$30 million for its construction.<sup>30</sup> Can we finance a reasonably large number of pilot CTs? To suggest feasibility, let us consider the savings in roads, electricity and marketing that will arise from the CT s. One will not have the obligation to take electric lines into the interior at Government cost, smaller village roads can be left in an unfinished state and preserve the environment and the countryside. Using data from the Local Government Office (LGED) and the Rural Electrification Board, a preliminary analysis conducted in 1999 suggested a potential savings of \$4.5 billion. This money can be used to initiate the process of developing pilot CTs, about 150 of them. Redirecting expenditures from their current pattern allows a nationwide trial for at least three years; the difference between the two patterns of expenditures—the current one of taking infrastructure to the people and that of inviting people to the infrastructure—is that the CTs look directly to the future and hold out more hope than the current scheme.

If the initial trials show promise, but donor aid is not forthcoming, the challenge of deficit financing or borrowing from abroad has to be faced. Such infrastructure investment is worthwhile because it is a precondition for future growth. Suppose it leads to higher inflation and a greater role for the state. While balanced budgets and low inflation are undoubtedly best, if the goal is economic growth, let us remember the following: There is no evidence that moderately high inflation, say 25%, will adversely affect growth; there is much evidence that infrastructure investment "crowds-in" private investment; and that a sustainable budget deficit can be maintained through the growth dividend of infrastructure investment. So financing the CTs should not be an issue for the short run when funds can be diverted from less productive uses, and, if the trials show promise, in the long run, since borrowing and deficit financing are both legitimate means to provide infrastructure.<sup>31</sup>

There will be many ancillary benefits. Consider some possibilities in physical planning. There are some 68,000 villages and 13,817,000 households in rural Bangladesh with .07 acres of homestead per household. There are a total of 1,949,000 ponds. Suppose only 80% of the villagers agree to enter the CTs, thereby 10,000,000 households will free up about .05 acres each, (since they need .02 acres each in the CT s), this will save 500,000 acres for fruits and vegetables. Similarly, we free up about 1,500,000 ponds available for scientific fisheries instead of homestead use. What large implications can this have

for nutrition, micro-nutrients, and the general health of the populace?

In summary, the first item on the agenda is a growth rate of ten per cent. In the long run, such growth can only come from a vibrant entrepreneurial class. It is entrepreneurship that must lead the way in a market economy. But domestic entrepreneurship can just as easily be stifled as fostered by uninhibited competition. The goal is to stimulate entrepreneurship mostly in those areas where all competition is local, such as non-tradables, and let this serve as a breeding ground of hope for the future.

### **Social Sectors: Stated Targets Being Met**

There is no doubt that social facets of poverty, such as education and health, are of primary importance. Both are amenable to increased expenditures; the difference lies in health being available to people even without any programs, public or private, while education has to be provided for people to acquire. In other words, health programs try to save us from harm, while education tries to raise us to a new level. They are closely linked however. Without good health, we cannot be effectively educated, without education we cannot appreciate many health preserving measures or raise our incomes to ensure future health. The economic gains are relatively greater for poor people, who are typically most handicapped by ill health, even in the short run; in the long-run, education assume equal importance in sustaining economic growth.<sup>32</sup> Bangladesh has increased spending on social sectors in recent years and real budget expenditures on social sectors have increased faster than the total. However, since this reallocation has taken place during a time when public investment was curtailed in directly productive sectors (manufacturing and irrigation in crop agriculture) and many agricultural subsidies were withdrawn, such fiscal adjustments are no longer available. It seems both fortuitous and convenient that, simply carrying out current policies, with no necessary additional expenditures on either education or health, will be a satisfactory way of achieving the desired goals of poverty reduction.

**Education:** Education receives the highest priority in public social spending. This is justified by the argument that education is both a consumption good, contributing directly to the well-being of those who attain it, and an investment good, in that it contributes human capital for future production. Educational facilities for both primary and secondary levels have expanded rapidly since the mid-1980s. The number of primary schools increased by more than 50%,

enrollment expanded by 75%, and gender disparity declined. Similar trends are noticed for secondary education, with the number of schools increasing by 55% and enrolment by 138%. The number of colleges increased by nearly five times with more than a five-fold increase in the number of students. Bangladesh has three important achievements in basic education: increase in adult literacy rate, narrowing down of gender gap, and expansion of primary school enrolment rate. If we look at the indicators proposed in the PA, it is easy to be complacent about pro-poor economic growth in Bangladesh. Between 1997 and 1999 the enrolment rate has increased by 4 per cent. This is already halfway to the desired goal. As for gender equity in enrolment, since net female enrolments are 95.6% and male net enrolments are 96% there is no statistical reason for believing that gender disparity in education still continues.

The GOB has been more open to including NGOs since the 1980s. The NGOs have experimented with a variety of delivery mechanisms to cater to the basic educational needs of the poor. NGO schools currently enroll around 8% of the total primary school enrolment. These efforts, in particular BRAC schools, have gained international attention. Since the early 1990s, the Government has also allowed more mainstream primary schools to be setup by NGO's. This fruitful partnership between the GOB and the NGOs can do with further strengthening.<sup>33</sup>

There are several potential sources of increased efficiency which should be explored extending thoughts to increased spending: First, the growth of salaries in the education budget needs to be contained. More careful monitoring of educational expenses seems vital. This will increase teachers' productivity through complementary measures (e.g. reducing absenteeism, increasing the teaching load, and rationalizing the recruitment process to attract well-trained teachers). The potential efficiency gains can be seen from the fact that the number of hours of classroom teaching per year is 444 in Bangladesh as against 1235 in China and 1100 in Indonesia; in grades 3 to 5, 47% of scheduled classes are not held. The primary school curriculum, which should take three years to complete, requires five years on average. This wastes students' time as well as their parents' investment. Only 37.8% of participants at secondary level complete the education cycle.<sup>34</sup> While the Government's Primary Education Development Program (1997-2002) aims to focus on many of these critical areas, the latest budget gives much emphasis on teachers' salaries at the expense of training, supervision, and facilities.

Second, higher education needs to take a back seat. Public spending per student is low in any case; indeed Bangladesh spends only half as much per capita on education as India or Pakistan, and one-third that of Sri Lanka; it is especially so in primary education, where public spending per student at primary level is around US \$13 which is one of the lowest in the world. On the other hand, 95% of expenditures of public universities, where the students generally come from well-off families, are borne by the Government. Third, technical education, now a small part of the budget, deserves support; but, as it is in the interest of the entrepreneurial class to foster such skills, they should be encouraged (by providing tax-free status to such social investment, for example) to provide a skills development fund to expand technical and vocational education. The potential for distance learning and IT education are areas still being explored.

**Health:** The goals here are malnutrition, infant and child mortality and maternal mortality. Drastic reductions have occurred in infant mortality rates (IMR) since 1990 (119) through 1999 (58); similarly child mortality rates have been reduced significantly from 1990 (106) through 1999 (89). If we take the cheap solution of extrapolating these reductions in a straight line, the desired goals are met. Maternal mortality decreases are also apparently being met, but since there is disagreement on the data, I will not press this point. The accepted measure for monitoring acute malnutrition is weight-for-age, as it is more sensitive to rapid changes in food availability, etc. The latest data show a dramatic decline in both severe and moderate malnutrition among children less than five years of age.<sup>35</sup> The decline between early 1997 and early 2000, was from 20.6% to 13.1% for severe, and from 56.3 to 47.8% for moderate malnutrition. So, most of the decline was among severely malnourished children. Again a simple extrapolation shows the desired goals being met. Of course, future changes may not be linear, but since we have no real idea how they will go, this is a good working hypothesis.

The simple straight-line extrapolations will be reinforced by income growth. Thus, in a sample of 58 developing countries, a 10% increase in income per capita, all else being equal, reduced infant and child mortality rates by between 2.0 and 3.5 percent and increased life expectancy by a month. If the income growth targets are met, this alone will provide gains in infant and maternal mortality of about 20 and 35 per cent respectively by 2005. So the policy suggestion is: "Continue the current policy thrust. If doubts arise, do a rapid assessment. If the goals are

not being reached, target new programs directly at the hardcore poor. At the margin, the hardcore poor are twice as helped by each dollar, so this will double the effect of each dollar spent." This strategy has an excellent chance of still reaching the goals of the Poverty reduction Agreement by 2005.

The results of the latest CIET survey (1998-2000:) suggest that gender equity in access to health services is not so much a general concern as one limited to specific issues:

- ◆ Gender is apparently not a factor in the choice of service used: 56% of government health service users are female, and 56% of private health service users are female. Some 60% of family members, ill but not using any service, are also female;
- ◆ There is no difference between male and female service users in their likelihood of paying extra money to the health worker(s), or paying unofficial registration fees;
- ◆ Nearly all women (94%) who received any antenatal care for pregnancies in the last five years rated the quality of the service they received as 'good', irrespective of area of residence, service providers, literacy, age and economic status.

Instead of pouring new money into health programs in order to meet the goals of the poverty reduction program, the following facts suggest that large gains are feasible quite cheaply with just some targeted expenditure on awareness.<sup>36</sup> People need to know just how important it is, as a practical matter, to secure health services and to know how and where to obtain them:

#### *Considering pregnancies*

- In the last five years, 59% of women had at least one antenatal care (ANC) visit and 54% had at least one visit in the first 6 months of pregnancy. Among those who received ANC, the median number of visit estimated was 1.7, which was very low compared to the recommended 4 or more. Is it ignorance of its importance, or some other factor, which is responsible for the low levels of ANC?

#### *About child health*

- Child mortality (2-4) remains higher among girls; moreover this mortality differential has not reduced during 1998-2000 This stems from differences in child care:
- Following the very rapid increases in immunisation rates in the late 1980s, levels have essentially reached a plateau recently.

Immunisation rates were slightly higher for male than female children (56% vs. 52%).

- A complementary BCC strategy targeted to mothers with low education is also needed in view of the high drop-out rates from DPT1-3, and the low coverage of measles vaccine in these areas and in children of poor, and uneducated mothers.

*And finally, regarding malnutrition*

- Some 50% of the households suffering from malnutrition have adequate food. The underlying causes of malnutrition, therefore, tend to be associated not just with food security but with behavior, social attitudes, and a lack of understanding and knowledge of nutritional needs.<sup>37</sup>

### Conclusion

Poverty reduction involves gains in income, education and health among its many facets. This paper has argued that current policy should focus all its efforts upon reaching the income growth target. This involves stimulating entrepreneurship, providing enabling laws, building infrastructure and keeping the macro framework stable by 'balancing' budgets and 'floating' exchange rates. The other goals of education and health will, in all probability, be met just by effectively implementing current policies. In particular, given the constraints, the emphasis on increased allocations for education and health is perhaps overmuch: *The emphasis throughout should be on rearranging existing expenditures and maximizing efficient utilization.* What is most important in these sectors now is the quality and composition of public investment. A simple but telling measure suggesting what can be gained lies in the fact that, of the 46 ADB projects evaluated, only 37% were classified as 'generally successful', compared with an ADB average of 54%.<sup>38</sup> Just attaining the average ADB success rate would imply a 50% improvement!

Now we turn to income growth, as this is really the hard policy question. The popular suggestion of export-led growth is not really tenable. Readymade garments (RMG) have provided sterling examples of dynamic entrepreneurship. However, a harsher international environment has now replaced the initially favorable international conditions and the RMG sector will be pressed to stave off collapse, let alone keep up its past rate of growth. Information Technology (IT) has made a good start, but Bangladesh lacks both the educational base at home and the expatriate contacts abroad for it to rely upon IT as a major player in the near future. The

diversified successes of SMEs, which helped countries such as Taiwan, are few, since the SMEs are hit by weak governance at home and by increased intensity of international competition. Globalization has provided a stimulus to a few industries, which have weathered the initial storm and become internationally competitive. A closer look at the pattern of trade with India, the nearest and most potentially most promising trade partner, shows that export gains are likely to be modest. This is unfortunate as India is the best ground for testing out Bangladeshi entrepreneurship. India imposes several non-tariff barriers and the Bangladeshi entrepreneur still lacks the expertise to look upon the Indian sub-continent as one market and plan accordingly.

Donors' insistence on imposing balanced budgets and the like is correct, but quite inadequate. The demand side must come *slightly* ahead of the supply side because people are spurred on by hope. Exports are good, but no one can rely on them. SOEs are a big loss, but since much skilled manpower and bureaucracy is needed to engage in devolution of government, why not ease them into new jobs? Simply firing people is not a good option, either economically or politically. The error of the donors lies in two basic points, one analytical and the other institutional. Analytically, donors underplay the importance of demand. For example, banks in Bangladesh have been able to raise interest rates because of the purely temporary stimulus given by Ramadan. Institutionally, donors overemphasize the possibility of spontaneous entrepreneurship if the 'preconditions are right'.

To provide for the needed income growth, aggregate demand needs to be boosted to increase employment directly, as, in a chain of multiplier effects, does investment. The way to achieve this goal is by heavy concentration of domestic infrastructure. Since most poverty is rural and since infrastructure is vital to economic growth, the GOB should redirect infrastructure support to *growth centers* and *rural settlements*. Such massive investments will be most productive, i.e., will not get swallowed in corruption, if accompanied by good governance. Good governance supports the poor with access to those public services essential for their well-being and for which they have a right to, and is vital to encouraging the latent entrepreneurial talents of individuals so that they will be able succeed economically and foster economic growth. It has been well stated that, "Lack of good governance is perhaps the single most important impediment to accelerating the pace of poverty reduction in Bangladesh. Since effective and efficient delivery of public services matters most to

the poor, weak governance hurts them disproportionately.”<sup>39</sup> Administratively, good governance will be best achieved if there is a simultaneous devolution of financial authority to municipal and local governments.

In conclusion, it has to be reiterated that the primary goal for poverty reduction must remain economic growth. A careful re-examination of the East Asian Miracle (Quibria 2002) shows that the social sector indicators in these miracle countries were low *prior to and during* the initial periods of rapid growth. Once rapid growth has been induced, the people themselves form the strongest lobby for good health and quality education. In other words, given the constraints and endowments facing Bangladesh, economic growth at 10 per cent is the most pro-poor outcome Bangladesh can aim for.

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The following is a selection of recent papers/reports available on the Web. I am grateful to Arif Al-Mamun for the detailed references.

*IRBD FY2003 Interim Report*

[http://www.cpd-bangladesh.org/fy03\\_interim%20report.PDF](http://www.cpd-bangladesh.org/fy03_interim%20report.PDF)

*IMF Concludes 2003 Article IV Consultation with Bangladesh*; July 11, 2003

<http://www.imf.org/external/np/sec/pn/2003/pn0384.htm>

*Bangladesh: Statistical Appendix; Country Report No. 03/194*; July 11, 2003

<http://www.imf.org/external/pubs/ft/scr/2003/cr03194.pdf>

Centre for Policy Dialogue

*Competitiveness Environment in Bangladesh 2003 and Global Competitiveness Report 2003-04*

[http://www.cpd-bangladesh.org/gcr\\_press.PDF](http://www.cpd-bangladesh.org/gcr_press.PDF)

CPD Dialogue Paper

*Exchange Rate Policy of Bangladesh – Not Floating Does Not Mean Sinking*

By Dr. Mirza Azizul Islam; January 02, 2003

[http://www.cpd-bangladesh.org/dp\\_020103.PDF](http://www.cpd-bangladesh.org/dp_020103.PDF)

*Achieving Replacement Level Fertility in Bangladesh: Challenges and Prospects*

Professor M Ataharul Islam, Professor M Mazharul Islam and Professor Nitai Chakraborty

<http://www.cpd-bangladesh.org/cunfpa18.htm>

### Endnotes

<sup>1</sup> With the possible exception of those from the Center for Policy Dialogue. A two page summary of this argument appeared in the July 2003 issue of The Executive Times.

<sup>2</sup> As an expatriate, I will often use ‘we’ for policies suggested to the GOB

<sup>3</sup> Despite these improvements, both performance indicators and levels of public spending are still low compared to most South Asian countries.

<sup>4</sup> Such settlements may be dictated in arsenic ravaged areas in any case, because of the need to provide safe water.

<sup>5</sup> Even if we use the Cost of Basic Needs (CBN) method, we find the past rate of poverty reduction to be 2.5 per cent, which still requires an increase in the growth rate of almost 90 per cent. For a valuable review of poverty in the mid-90's, see Khan and Sen (2001).

<sup>6</sup> The 1999/2000 survey produced an estimated national TFR of 3.3. That level of fertility would be expected to give a Crude Birth Rate of around 27 per 1,000 depending on the age structure of the population, especially of women of reproductive age. The Crude Death Rate is around 7 or 8 per 1000. The net effect is about one child above the GoB target of replacement fertility by 2005.

<sup>7</sup> Ministry of Health, Dhaka, 1996

<sup>8</sup> The changed efficacy seems to have little to do with the sector wide approach of HPSP per se. Initially Family Planning works well as vertical project, FPHP, but with time it requires an integrated approach.

<sup>9</sup> For good reviews of the Macroeconomy which point out both data deficiencies as well as open questions, see Bhattacharya(2000) and Khan (2001)

<sup>10</sup> Shahid Alam, Poverty from the Wealth of Nations, (MacMillan,2000). Leah Greenfield, The Spirit of Capitalism,(Harvard,2003)

<sup>11</sup> World Bank 2000.

<sup>12</sup> The subsidies given for both fertilizer and for electricity are somewhat inexplicable. It may be easier to attain Food self sufficiency by buying from abroad and storing the grain rather than growing it at home.

<sup>13</sup> Country Assistance Plan, 2000, p1

<sup>14</sup> Mahmud,2001, pp12,20

<sup>15</sup> Quddus and Rashid (2000)

<sup>16</sup> Akhter Hossain and Salim Rashid, “Financial Sector Reform,” in M.G. Quibria (edited) The Bangladesh Economy in Transition, Oxford, Delhi, 1997, 221-274.

<sup>17</sup> The World Bank and The Asian Development Bank, Bangladesh, Economic Trends and the Policy Agenda, May 1998, 15-16.

<sup>18</sup> Table 5 in Rahman and Rahman, 2001. More details are to be found in Molla, Quddus and Rashid (2003)

<sup>19</sup> The Hindu, March 28, 2001. In November 2001, the Indian Government has reintroduced charges of dumping against batteries---one of the few manufactured goods Bangladesh can export to India.

<sup>20</sup> Quddus and Rashid (2000)

<sup>21</sup> This section relies on an unpublished ADB report of Najmul Hossain who notes that the database for dealing with SME's is weak and information on changes within the sector is spotty.

<sup>22</sup> The Janakantha ,May 6, 2001, states as its headline that over 80 per cent of litigation is land related.

<sup>23</sup> Implementing microcredit programs by almost every ministry and their agencies, as well as the NGO's, has become a cottage industry. See GOB 2000.

<sup>24</sup> This is contentious, but the Wall Street Journal piece on the Grameen bank (Nov 27 2001) points out many of the limitations of micro-credit. For a scholarly query see Basher (2001)

<sup>25</sup> Sen,2000,p12

<sup>26</sup> The GOB does have a rural infrastructure program at present, which supports the building and maintenance of rural roads, bridges and culverts; small scale irrigation structure; development of trading facilities in rural markets; and creation of trading network. The details are spelled out in the Mid Term Review of the Fifth Five Year Plan. It has been claimed by the previous Prime Minister (Daily Star, May3,p11) that even this limited effort at providing housing and accompanying infrastructure has halted the creation of urban slums.

<sup>27</sup> Bangladesh Rural Infrastructure Strategy Study (World Bank, 1997).

<sup>28</sup> The following section summarises an elaborate discussion that extends through two issues of Asian Affairs.(nos 1 and 2, 2000) It will be best to start the CT's as a Pilot project on reclaimed (khas) lands or in arsenic affected areas or in cyclonic belts.

<sup>29</sup> Albeit on a smaller scale, such plans have been drawn up for countries like India and Italy. For a valuable review, see Rosenstein Rodan (1981)

<sup>30</sup> This calculation excludes the cost of land. As the CT's are to be in rural areas, the cost of land will be a small part of the total. I am grateful to officers of the construction companies, Concord and ShelTech, for information, as well as faculty in the Civil Engineering department.

<sup>31</sup> For evidence of the positive impact of building expenditures upon growth see Wen (2001)

<sup>32</sup> The following sections rely on unpublished ADB reports by Haider (Health) and Mujeri (Social Sector).

<sup>33</sup> Excellence in the overall trend however masks several persistent weaknesses. In particular the low quality of education and the wastage of resources through high dropout and repetition rates give most concern for the future. Despite recent increases, Public expenditures on education in Bangladesh are low compared to other developing Asian countries and averaged around 2 per cent of GDP in the 1990s. The fruitful partnership with NGO's has promise for the future. Planning Commission 2000.

<sup>34</sup> See World Bank (1999).

<sup>35</sup> Demographic and Health Survey 1999/2000

<sup>36</sup> The fact that the targets will be met should not to suggest a rosy picture of the Health Sector. Access for the poor can be quite limited. The recently conducted Mid-Term Review (MTR) of Fifth Project HPSP that of NGOs .It makes a sufficient case for intervention to observe that, for several selected health indicators, the poorest 20% and the richest 20% differ by as nearly one hundred per cent ! Demographic and Health Survey 1996/97 P39.

<sup>37</sup> The general framework has been well stated in the ADB Report for Health Sector Reform in Asia and the Pacific (1999) (see pp106 and 107). It states that for each illness we need to know a) What are the relative costs of prevention vs cure? b) What are the relative costs of Traditional vs Non-Traditional approaches? This section draws on an interview with Mr G S Kang of the World Bank

<sup>38</sup> Country Operating Strategy, ADB,p8.

<sup>39</sup> Country Assistance Plan, ADB,p24. , Since poor households cannot evade the pervasive influence of Government, what does such contact cost them in their daily lives? Siddiqi (2000) examined 3117 households and concluded that, on an average, such families paid an estimated average cost of corruption

and misgovernance of TK 1501.83; about two-thirds, or TK 1001.5, is due to corruption, and the rest is due to misgovernance.

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