

Clare E. Humphrey

*Privatization in
Bangladesh*

*Economic Transition
in a Poor Country*



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South and Southeast Asia*

Privatization in Bangladesh

Economic Transition
in a Poor Country

Clare E. Humphrey

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*To Nizam Uddin Ahmed,
friend, colleague, and trail guide
along a treacherous path*

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The field research in Bangladesh was carried out in two phases, August-December 1986 and February-March 1987. The first draft of the study was written in Washington, D.C., over several months in the spring and early summer of 1987. After a lengthy review by the Center and USAID, in Washington and Dhaka, comments were sent to me in mid-October in Accra, Ghana, where I was serving on another assignment. Some revisions were made in Washington in late 1987, and a specially tailored executive summary with recommendations was submitted for the consideration of the government of Bangladesh in December 1987.

Several professional friends and colleagues, who had read and commented on the original study, urged me to consider publication. A two-month consulting assignment in Nepal intervened. That consultancy involved advising the cabinet and the King on the privatization of the state tea corporation. The intriguing experience of the Nepal assignment, coupled with my earlier study on Taiwan's pioneering divestiture of several large state enterprises, prompted me to take another look at the Bangladesh report as a useful case study. The job of collecting additional material and editing, revising, and updat-

ing the original study was accomplished in the spring and summer of 1988.

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Clare E. Humphrey
Washington, D.C.

Contents

<i>Acknowledgments</i>	ix
1 Introduction	1
Notes, 6	
2 Privatization—An Overview	7
How to Approach Privatization: Ten Propositions and Caveats, 8	
Why Privatize? 9	
Privatization in Traditional Societies, 13	
Types of SOEs Suitable for Privatization, 15	
Types of Privatization, 15	
Notes, 18	
3 The Prelude—Colonialism, Partition, Liberation, and Nationalization	19
The British Period (1757–1947), 20	
The Pakistan Period (1947–1971), 21	
Liberation and Nationalization—the Mujib Period (1971–1975), 28	
Notes, 39	
4 The First Phase (1975–1981)	46
The Zia Government, 46	
Revised Investment Policy of 1975, 47	
“Privatization” of the Commercial Sector, 50	
The Industrial Sector and the Public/Private Mix, 52	
Summary of the Zia Period (1975–1981), 56	
Notes, 59	

5	The Second Phase (1982-1988)	63
	New Industrial Policy of 1982, 65	
	Reorganization and Revitalization of the Public Enterprise System, 74	
	Privatization and Private Sector Development Since NIP-'82, 77	
	Industrial Policy of 1986 and the "51-49 Plan," 85	
	Privatization in Bangladesh—A Recap, 91	
	Notes, 92	
6	The Private Sector's Performance	98
	Notes on the Bangladesh Business Community, 100	
	Interaction With the Government and the Public Enterprises, 106	
	The Volatile Labor Question—The Dilemma of Unemployment in a Poor Country, 113	
	The Traditional Tests—Management and the Bottom Line, 118	
	Profit and Loss in Jute and Textiles, 124	
	Privatization of Fertilizer Distribution, 127	
	Summary, 129	
	Notes, 131	
7	The Public Sector's Performance	136
	Politics and the Decision-making Process, 137	
	Comparison With Taiwan's Privatization Program, 141	
	Implementation of Privatization Policy, 144	
	The Public/Private Mix, 145	
	Foreign Investment, 147	
	Donor Agencies and Private Sector Development, 148	
	Improvement of the Public Enterprise System, 150	
	Selling Shares of Public Enterprises— the 51-49 Plan, 152	
	The Future of Privatization in Bangladesh, 155	
	Notes, 157	
8	Conclusions and Recommendations	160
	Conclusions, 160	
	Recommendations, 163	
	Notes, 178	

<i>List of Acronyms and Abbreviations</i>	179
<i>Bibliography</i>	183
<i>Appendix A: Divested Industrial Enterprises</i>	205
<i>Appendix B: State-Owned Enterprises</i>	252
<i>Appendix C: Survey Questionnaire for Privatized Enterprises</i>	258
<i>Appendix D: Terms and Conditions for Transfer of Ownership of Privatized Jute Mills</i>	261
<i>Index</i>	267
<i>About the Author</i>	275

1

Introduction

This study of privatization in Bangladesh has been undertaken for two reasons. First, privatization is increasingly recognized as a legitimate and effective tool for economic transformation and development. In fact, some observers believe that privatization may be one of the most important trends in economic development in the coming decade.

Second, Bangladesh has been chosen for this study both because it is a country with monumental social and economic development problems, and because it has divested more state-owned enterprises (SOEs) than any other less developed country (LDC). The convergence of these factors makes a study of privatization in Bangladesh appropriate and, hopefully, valuable to observers and practitioners concerned with economic development, social change, and modernization in the Third World.

Country after country has come to the conclusion, albeit some reluctantly and belatedly, that the private sector functions more effectively than the public sector. At the minimum, privatization is a way to tap the energy and resourcefulness of the private sector, while reducing government losses and budget drains.

As a consequence, there has been a gradual, but widespread movement to transfer government assets and functions to the private sector, thereby dismantling some of the state enterprises and state control systems so painstakingly constructed during the 1950s, '60s, and early '70s.

Privatization transactions have covered a wide spectrum of geo-

graphic and economic sectors in a variety of countries at vastly different stages of development. A representative sampling could include:¹

- telecommunications in the United Kingdom and Italy
- airlines in Singapore, Niger, and Malaysia
- banks in Chile, Bangladesh, and the Philippines
- fisheries in Kenya and Somalia
- mining in Taiwan and Togo
- aluminum in Costa Rica
- hotels in Mexico, Sierra Leone, and Jamaica
- oil and petrochemicals in South Korea and the United Kingdom
- fertilizer and seed distribution in Senegal
- paper manufacturing in Thailand and Taiwan
- tool manufacturing in the Ivory Coast
- rice and flour milling in Pakistan
- cement in Turkey and Taiwan
- jute and textile mills in Bangladesh
- port authority and container terminal in Malaysia
- sugar in Uganda and Jamaica
- bus systems in Sri Lanka and Argentina
- holding companies in Brazil
- auto manufacture/assembly in Spain, Mozambique, and Mexico
- road supervision and construction in India and Bolivia
- prisons in the United States
- food processing in Mali, Zaire, and Turkey
- bicycle and scooter manufacturing in India
- forestry in Ecuador

This listing is illustrative, but not all-inclusive; it has been included to provide some sense of the diversity of privatization activities. The procedural approaches and privatization techniques employed in these transactions have been equally varied.

One of the more encouraging aspects of the privatization picture in the Third World is that the impetus for much of the activity has originated from the LDCs themselves, rather than from aid-donor countries attempting to shove western free-enterprise down their throats.

Of course, there has been some donor pressure to which aid-dependent countries have prudently responded. But in many instances, beleaguered LDC governments have come to officials of developed countries and said in effect, "We've got a problem. Our state enterprises are floundering; but we don't know what to do about it. Please give us some guidance on how to extricate ourselves from this di-

lemma." While such a scenario indicates the presence of problems, it demonstrates a healthier attitude and greater commitment than mendacity.

Considering the great amount of privatization activity that has taken place, it is surprising that no in-depth study of one country's privatization effort has been carried out. There have been a number of worldwide surveys of privatization transactions and several procedural "how to" manuals. However, most existing studies (with a few outstanding exceptions) have been concerned with technical rather than policy issues.

Additionally, most studies have been transaction-oriented, aimed at the enterprises being privatized. Less attention has been given to analyzing the overall national scene and the underlying forces and factors—social, historical, political, and cultural, as well as economic—that influence development, government decisions and privatization programs. Some observers believe that useful lessons can be gleaned from a comprehensive study of one country's overall experience with privatization and the conditions and issues surrounding it. What is needed is one country's privatization story, as completely as it is possible to tell it, and this is the prime motivation behind the present study.

Why Bangladesh? Partly because more public enterprises have been divested there than in any other country—a total of 1,076. The 609 of these that were in the industrial sector will be the focal point of our investigations. This stupendous statistical record prompted such a recognized authority as Elliot Berg to rhapsodically refer to Bangladesh as one of two "champion performers in the world of privatization or divestiture."² One of the main thrusts of this study will be to determine if this accolade is deserved.

But it is not only the sheer number of Bangladesh's privatization transactions that provides useful insights into the complexities of privatization there or anywhere else. I shall leave to the concluding chapter an evaluation of whether quantity equates with quality. Other statistics and features are equally compelling for drawing the thoughtful observer to Bangladesh.

For one thing, Bangladesh is somewhat atypical in that the majority of its many privatization transactions have been divestitures. In contrast to the popular conception, divestiture is not the most often used method of privatization. It is, on the contrary, one of the least often used, mainly because of the financial and political complexities and pitfalls involved in implementing it. On the other hand, analysis of these very difficulties in the Bangladesh context can provide meaningful insights.

Most readers who pick up this study are probably already familiar with Bangladesh's situation. But for those who are approaching this study because of their interest in privatization, rather than any particular knowledge of Bangladesh, a few notes might be in order.³

Bangladesh covers an area of 55,598 square miles. This is slightly smaller than Iowa, which ranks 25th among American states. But instead of Iowa's comfortable population of about 3 million, Bangladesh is jammed with 107 million souls, most of whom live in abject poverty and squalor.

The average per capita income is \$150 per year, and perhaps 80 percent of the population live below that. Even the lowest cost of living framework cannot make that into a living wage. Annual population increase is averaging 2.5 percent. Life expectancy is improving, but is still only around age 50. Health and nutrition figures are sobering. Literacy is estimated at 24 percent, but only 10 percent for women.

Although blessed with a rich cultural heritage that has produced some of South Asia's greatest poets and writers, the area we now call Bangladesh has had a checkered history. It has suffered in debilitating succession from British colonialism and exploitation; an unequal partnership with Pakistan resulting in a bloody fratricidal war of liberation, followed by two coups complete with presidential assassinations; an unsuccessful experiment with socialism which featured nationalization of the industrial sector; and political and economic instability that has continued to the present day.

In addition, the Bengalis have been plagued with the disruption and factionalism normally associated with an impoverished, conservative society in the throes of traumatic change. Traditional ways appear inadequate for the challenges of late twentieth century society, but no new system of values and practices has arisen to replace them. Islam is the only cultural shield and solace against an otherwise hostile environment.

Economically, East Bengal cum East Pakistan cum Bangladesh has always been a backwater area, dominated, alternately, by Calcutta, London, or Karachi. Bangladesh has been called an "international basket case" for more than a decade. It is the poorest large country in the world. The economy is heavily agricultural, and the population is rural and conservative. Agricultural output and productivity are increasing, but relatively inelastic. Natural gas is the only plentiful natural resource.

Infrastructure is inadequate. Topography dictates transportation. More produce and people are transported on the many rivers than on roads and railroads combined. The extensive river system and the

agricultural economy as a whole are vulnerable to annual flooding during the monsoon season. Rampant deforestation has increased erosion and the danger of flooding. A few years ago, a tidal wave and consequent flooding wiped out 300,000 people at a single stroke.

Industry, while currently only about 15 percent of gross domestic product (GDP), is increasing. It offers the best hope for economic progress, employment expansion and better income distribution. One of the many tragedies of Bangladesh's situation is that its leading industry and foreign exchange earner, jute, is an industry that is slowly dying due to competition from synthetic fibers.

The work force is unskilled and unmotivated except for survival. The fledgling management group, while expanding and improving professionally, is still more attuned to trade and commerce than industry and to the demands of familial rather than corporate enterprise.

In view of all of the adverse factors present in Bangladesh, it is amazing that any progress has been made, but it has. Almost all of the gains have been registered in the private sector. The pervasive but inertial state enterprise system continues to lose money. A mixed, broader-based, more diverse and balanced economy is emerging, but the process is agonizingly slow and painful.

Privatization has been at the center of the process and the accompanying controversy. The recent economic history of Bangladesh cannot be analyzed properly without an understanding of the issues surrounding privatization. Conversely, Bangladesh has had to confront, at one time or another, and in one form or another, almost every problem faced by LDCs trying to get out of the bog of economic stagnation. The fact that Bangladesh's circumstances have been especially stark only makes it a more suitable case study. If privatization can assist in generating positive and substantial benefits to Bangladesh's troubled economy, the lessons can be adapted and applied elsewhere.

With this in mind, the approach throughout this study has been to consider several basic questions related to the process of privatization.

These basic questions fall into two categories: six questions designed to analyze the Bangladesh experience; and six which stress self-analysis for those concerned with development problems of other lands.

Questions to Ponder About the Bangladesh Case

- What did they do?
- What were the conditions that prompted them to do it?

- What were their short-range objectives and strategies?
- What were their long-range objectives and strategies?
- What did they accomplish, and how?
- Where did they fail, and why?

Questions for Other Countries to Ponder About Their Own Situations

- What do we want to accomplish in the long run?
- What do we want to accomplish in the short run?
- What is our plan of action?
- What factors will most affect our efforts, both positively and negatively?
- What can we adapt from the Bangladesh experience?
- What must we do differently, and why?

This approach may seem simplistic to some, but it strikes to the core of our purpose. Each factor, each step in the process of privatization, should be scrutinized through the prism of these and similar questions. Such application, done with thoughtfulness, candor, and consistency can transform this study from a document to be read into a tool to be used.

We shall come back to these questions at the end of the study as a reflective exercise during our final evaluation.

Notes

1. This listing has been compiled from a variety of periodical, scholarly and official sources. In a number of the economic categories listed here, there has been activity in other countries besides the ones mentioned.

2. Stated in a speech presented at a Conference on Privatization, held in Washington, D.C., in February 1986 under the sponsorship of the U.S. Agency for International Development (USAID). The other country is Chile. Berg further stated that they "are far and away the leaders of the divestiture parade in the less developed world." *ibid.*

3. The figures that follow came from a number of sources, but mainly from *Statistical Pocket Book of Bangladesh—1986* (Dhaka, Bangladesh Bureau of Statistics, 12/2/86), and from several publications of the World Bank.

2

Privatization—An Overview

The principal purpose of this study is to document and analyze Bangladesh's extraordinary experiment with privatization of the industrial sector of its "modern" economy and, to a lesser extent, of commercial, financial, and agri-business institutions and activities as well. The preoccupation of the study will, therefore, be with what has actually been taking place in Bangladesh. But if this exercise is to be useful to those both inside and outside of Bangladesh who are grappling with the complexities, potentialities, and pitfalls of privatization, we should first devote some attention to certain salient features of and basic questions related to the privatization process. Chapter 1 offered a few descriptive notes on the scope of privatization around the world. This chapter attempts to provide some understanding of the nature of the phenomenon.

This chapter will present a brief overview of some distinctive aspects of privatization, which, while a relatively new phenomenon on the development scene, has attracted worldwide attention and occasioned heated debate in recent years. This overview is not intended to be an in-depth theoretical or technical discourse on privatization, but rather a brief exposition of a few important, practical issues that one should bear in mind when approaching the study of any country's privatization situation. This overview can serve as a logical framework for my analysis of Bangladesh's privatization policies and programs.

The reader will not be burdened with the usual pedantic, meticulous "definition of privatization." We will assume that the audience

to which this study is addressed already has a relatively well-developed perception of what privatization amounts to and what it involves. Therefore, it will suffice to say that the term “privatization” will be used in this study in its widest possible sense, i.e., the replacement of government institutions or activities with those of the private sector.

How to Approach Privatization: Ten Propositions and Caveats

The following is a set of general thoughts to keep in mind while reading this study. These thoughts do not constitute a comprehensive conceptual framework for the subject, but they have influenced how this study was approached and structured. They do represent the author’s viewpoint or bias, but should be taken as a point of departure rather than a subjective, ideological argument. They will be analyzed, clarified, and elaborated upon in various ways in subsequent sections of this chapter and throughout the rest of the study.

1. Privatization is often more influenced by political issues than by strictly economic considerations.

2. Privatization and divestiture are not synonymous. Divestiture is only one type of privatization, and is perhaps one of the least attractive and least utilized methods. There are “many roads to privatization,” just as there are to its counterpart, socialism.

3. Privatization is too often associated primarily with questions of equity, particularly in developed countries; but privatization of a *function* or *service* can, at times, be just as important. A good illustration of this has been the privatization of fertilizer distribution in Bangladesh.

4. One should approach this subject from the standpoint of privatization of an *economy*, not merely the unloading of inefficient, money-losing state enterprises. Privatization should be undertaken to develop viable enterprises and a more vibrant economy, not simply to cut state-owned enterprise (SOE) losses or reduce government deficits.

5. A government’s privatization policy will be ineffective unless it is preceded by a well thought-out plan with clearly defined long-range objectives, backed up with will and commitment, and implemented through an effort that is comprehensive, coordinated, and consistent.

6. Privatization of state enterprises will accomplish little without parallel government-sponsored policies and programs to en-