

## **Manufacturing Sector**

For sustained growth and poverty reduction, the Government would pursue a globally competitive industrialization strategy dictated by the dynamic comparative advantage of the country. This means an employment-intensive industrialization with emphasis on small and medium enterprises (SMEs) and export-oriented industries.

The pace and level of manufacturing growth in the past was slow: the share of manufacturing in GDP increased to around 16 per cent in 2000/01 from 13 per cent in 1989/90 indicating a growth rate of less than 7 per cent per year. The performance of both large/medium and small scale industries was similar. Manufacturing growth remains narrowly based with only a few industries (e.g. readymade garments) spearheading recent growth. While trade liberalization measures in the early 1990s provided easier access to imported raw materials particularly for small industries, several factors e.g. increased imports of competing products due to lowering of tariffs, illegal imports from India encouraged by unfavorable movement in Bangladesh's exchange rate vis-a-vis Indian rupee, dislocations caused by natural and manmade factors, and deterioration in the overall investment climate led to a slow and fluctuating manufacturing growth. Total manufacturing investment remained at around 1.4 per cent of GDP in the late 1990s.

The foreign direct investment (FDI) flow into the manufacturing sector is small. Foreign investment in Export Processing Zones (EPZs) accounted for less than 10 per cent of total manufacturing investment in the 1990s. Bulk of the investments in the EPZs went into garments, textiles, footwear and other labor-intensive industries with little in high-tech industries. The FDI outside of the EPZs went mostly into gas and power sub-sectors. The limited size of the domestic market and lack of a facilitating environment discouraged the inflow of FDI into manufacturing industry outside the EPZs.

Slow manufacturing growth and the emergence of industrial sickness in the past had many roots. The problems relate to deficiencies in industrial finance, slow pace of privatization of public sector enterprises, mixed impact of rapid trade liberalization, lack of a competitive exchange rate policy, discriminatory fiscal incentives, and the persistence of a legal and regulatory framework that is characterized by pervasive, archaic and unnecessary laws, vague and discretionary regulations, and flawed and weak enforcement. Infrastructure bottlenecks e.g. inadequate transport, power, telecommunications, ports and other facilities, lack of investment-friendly labor relations and procedural complexities make setting of viable industrial enterprises very costly in the country.

The Government's efforts to accelerate manufacturing growth and increase its poverty reduction role would emphasize several elements. For the privatization program, a firm timetable would be set to assert the Government's political will and send clear signals to those who oppose the program. Necessary measures would be taken to reduce social costs of labor adjustment through appropriate safety-nets and help retrenched workers to reintegrate into the labor market. With a vibrant and dynamic private sector as the principal actor, the Industrial Policy 1999 envisages that Bangladesh will have a sizable industrial sector within a decade contributing at least 25 per cent to the GDP and employing 20 per cent of the labor force. Similarly, a Jute Policy is being

adopted to ensure a desired level of jute production, promote diversified use of jute, and increase the use of environment-friendly jute products. The Jute Diversification Promotion Centre (JDPC) has been set up to identify and exploit new technology for production of diversified jute goods in the private sector through providing technology, training, market research and finance. The efforts to increase the productivity of both raw jute and jute goods production would be intensified further to expand employment opportunities and generate economic activities in the country.

**Trade Policy Reform:** For proper pacing and sequencing of trade policy reform, the Government would announce well in advance planned changes in trade policy and help relax supply-side bottlenecks through complementary reform measures. For curtailing illegal imports, trade infrastructure will be improved and measures will be taken to eliminate the flow of remittances through the *hundi* channel. A competitive exchange rate policy will be followed to restore the balance in bilateral exchange rate with major export competing countries and discourage the inflow of legal and illegal imports.

**Legal and Regulatory Framework:** The legal and regulatory framework would be streamlined in several respects e.g. contract enforcement and dispute resolution, bankruptcy and labor laws, copyright protection, land titling and transfer procedures. The regulatory requirements would be streamlined through coordination among relevant agencies so that the One Stop Service of the Board of Investment (BOI) could help complete all requirements within a specified time. The capacity of the BOI would also be strengthened. These, along with measures to improve the law and order situation and create a congenial legal environment, would assure prospective investors, both domestic and foreign, that there is adequate legal protection to legitimate business.

**Industrial Finance and Fiscal Incentives:** To meet the demand for term loan financing, the Government would revitalize the non-banking financial institutions including investment companies and the stock market by enhancing their capacity to mobilize funds and creating enabling conditions for their operation as quasi-commercial banks. Along with necessary financial sector reform and new institutional initiatives, best practice methods of investment financing will be developed.

For developing the capital market, greater transparency and accountability of the stock exchanges would be ensured. The Central Depository System (CDS) would be speedily introduced and the stock exchanges would be strengthened by updating the rules and regulations along with measures to facilitate surveillance and enforce compliance of rules.

Fiscal incentives to export industries would be rationalized along with adopting a more appropriate definition of export industries and effective measures to stimulate backward linkages. The prevailing system of duty drawback would be simplified and the cash compensation scheme would be replaced by appropriate measures consistent with WTO regulations to ensure competitiveness of domestic export industries.

The ongoing process of reforming customs and improvements in VAT and income tax administration would be accelerated and sustained through appropriate reorganization of the

National Board of Revenue (NBR). The customs reform would be extended to cover all agencies at sea, air and inland cargo terminals to ensure speedy import and export clearance. The problems relating to pre-shipment inspection (PSI) would be resolved to ensure effective implementation of the system.

***Skill and Technology Upgradation:*** Skill and technology upgradation will be geared to achieve several objectives e.g., diversifying the industrial base and the export sector, meeting the enhanced health, sanitary and phytosanitary standards of the exportables in the post-WTO era, attracting FDI in high-tech industries, and complementing trade liberalization through adequate supply response. The Government would enhance investments in vocational training systems and make them more relevant to current needs of the industrial sector. The efficiency of public technical training institutions would be increased through in-factory skill upgradation and training activities. Technology acquisition, adaptation and upgradation would be given priority to ensure competitiveness in manufacturing and export sectors.

***Capacity Building and Industrial Support Services:*** The institutional capacity to provide quality support services will be enhanced. The Government would revamp the industrial statistics wing of the BBS to generate consistent data on manufacturing sector. The capacity of the WTO cell of the Ministry of Commerce would be enhanced through reorganization and an autonomous Foreign Trade Institute with links to the private sector would be established. The Government would undertake appropriate reorganization to ensure strong leadership, autonomy and professional capacity of the agencies serving manufacturing and business such as Board of Investment (BOI), Bangladesh Small and Cottage Industries Corporation (BSCIC), Bangladesh Standards and Testing Institution (BSTI), Export Promotion Bureau (EPB), Bangladesh Tariff Commission (BTC), National Board of Revenue (NBR) and Office of Patents, Designs and Trademarks.

***ICT and Export Oriented Industries:*** The ICT sector is yet to take-off in Bangladesh and its growth is painfully slow mainly due to poor informatics infrastructure. The Government would emphasize three areas for developing the ICT sector: (i) improvements of telecommunication infrastructure; (ii) rationalization of BTTB's monopoly and regulatory roles; and (iii) human resource development in the ICT sector.

For ensuring competitiveness of Bangladesh's readymade garments (RMG) sector after 2005, setting up of backward linkage industries would be encouraged based on careful assessment of the long-term viability of different segments. The Government would address other factors that also influence competitiveness e.g., skill upgradation and training of workers, better management practices, adoption of better technology and improved maintenance of machineries and equipment, better working conditions, power failures and political unrests, law and order situation, corruption and procedural complexities, port congestion and delays in port clearance, and problems of export finance.

With high potential of agro-based industries for both exports and import substitution, the Government's policy support would cover several areas e.g. infrastructure development for

transportation and preservation of perishables; acquisition and adaptation of improved technologies and upgradation of local skills; preferential import of related input and equipment; development of intermediate industries such as packaging, bottling and printing; extension of air cargo facilities, rationalization of air freight charges, and expansion of cooling and storage facilities at export points.

***Developing Small and Medium Enterprises:*** The development of small and medium enterprises (SMEs) would be the key element in pro-poor manufacturing growth. Creating a vibrant SME sector would require pro-active policies beyond removal of policy biases due to their persisting structural weaknesses. These include: increased public investment in SMEs in areas of training, extension, research and market promotion; provision of finance and preferential fiscal measures; legal reforms to expand and simplify the use of non-real estate security for facilitating access to institutional finance; and implementation of an effective credit guarantee scheme.

The Government would adopt a consistent set of definitions for various size categories of enterprises so that the current anomaly (e.g. between BBS and NBR) is removed. Despite attempts to provide access through targeted lending, actual delivery of institutional credit to SMEs remained grossly inadequate due to several factors e.g. lengthy and cumbersome loan application process, inadequate capability of financial institutions for proper project evaluation, pre-occupation with fixed asset ownership as collateral, and lack of proper autonomy and accountability of financial institutions resulting in inflexibility, inefficiency, political interventions and corruption.

For addressing credit problems, the Government would introduce reforms in financial and fiscal sectors. The financial institutions would be encouraged to seek deposit relationship with small entrepreneurs and use cash flow rather than asset ownership as the criterion for creditworthiness. An expanded credit guarantee scheme would be used to support the policy. By removing existing discriminations (e.g. in VAT, wealth tax and provisions for tax holiday), the fiscal policy would be tailored to provide support to SMEs. For creating a conducive business environment, laws and regulations and policies related to SMEs would be improved; incentives to develop institutional network to support SMEs e.g. financial and credit guarantee institutions, business development services, training, technology, information and advocacy services would be provided; and the ability and involvement of the stakeholders in planning and policy/program implementation would be increased. The access to resources by SMEs would be enhanced through several means like creating incentives for financial institutions to support SMEs and micro-enterprises along with expanded role of the NGOs, expanding sources of financing through viable schemes such as loan guarantee, venture capital, and promoting leasing industry; improving management capacity of institutions providing business development services, strengthening training institutions and their networking; and reorienting and restructuring government training agencies to create stronger links with SMEs. The Government would implement programs to improve knowledge, entrepreneurship, and productivity of SMEs and support new entrepreneurs (business start-up). The Government's overall approach would be to remove unnecessary regulatory barriers and simplify required laws and regulations since the impact of regulations falls unevenly on the SMEs compared with their large-scale counterparts.