INVITATION TO A DIALOGUE

The public and private sectors: two sides of same coin

Rehman Sobhan, *Star Guest Columnist*

Bangladesh's private sector is all pervasive. Every farmer, streetside vendor, even the young men who smuggle in goods from Bangkok through what is known as 'flying business' are part of an active private sector. The *Dolai Khal* entrepreneurs, the handloom, the handloom weavers, the village *Karigars*, have all demonstrated considerable enterprise, in raising capital, accessing market opportunities, innovating, making profits and reinvesting this for expansion of capacity. We do not hear of defaults from these entrepreneurs or complaints of sickness. This class is rarely vocal, do not take full page ads in the newspapers to register their grievances and do not participate in seminars at the Sonargaon Hotel. They go about their business taking the market as given, the government as either irrelevant or an enemy which can do them harm but rarely do them good. It is the misfortune of our economy that this numerous, hardworking and creative constituency has received little adademic recognition, remains invisible to the policy makers and donors and has no advocates in our political arena.

What we have instead are a vocal and officially patronised class of entrepreneurs who are distinguished from the *Dolai Khal* enterprises by the fact that they have access to institutional credit and are more dependent on changes in macro and micro policy interventions of the government to influence their fortunes. Obviously there is a size dimension to this class. Such entrepreneurs own what are known as modern industries, mechanised, based on imported capital and technology. Their very size however drives them to institutional sources of credit for both investment and working capital. Even if they possess sufficient liquidity, and many do, they are less inclined to risk their own equity and expect to turn to institutional sources to assume the risk taking functions.

The intimate linkage between this numerically small, highly visible and politically influential class of entrepreneurs and the public sector institutions which serve them is what sets them apart from the hundreds of thousands of small entrepreneurs. The relevant dividing line in Bangladesh is thus not between the public sector and the private sector, which remains little more than abstract categories, but between a small class of people who control, operate and benefit from the state and a vast constituency of private enterprises which operate without reference to the state and prosper inspite of rather than because of the government.

The goal of public policy thus has to aim at transforming the performance of both the public and the private sector. This means more than just raising the profitability of some loss making public and private enterprises. It means the redirection of the entire system of governance away from a regulation oriented *babu raj*, which obstructs rather than stimulates both public and private enterprise, towards production-oriented system committed to promoting efficiency, real transparency in distributing public resources and full accountability for its use.

The growth of this small class of metropolitan based entrepreneurs is itself hardly undesirable and is an inevitable part of the process of industrialisation, technological progress and globalisation of the market. We cannot forever depend on handloom cloth, or machine shops with old lathes but have to keep abreast of modern technology if we are to be internationally competitive.

To the extent that our entrepreneurial class evolves from small industry or the trading and professional classes, taking risks, invest equity and grow by learning and doing, they can and indeed have established viable and potentially dynamic enterprises. The growth of the garment industry is a good case in point where the size of the investment has in most cases been within the managerial competence of the investor and the debt leverage has not been excessive.

The default crisis

The problem seems to have arisen whenever entrep-reneurs seek to move beyond their resources and experience. This inevitably means borrowing from the DFIs. Most such larger enterprises are set up by first generation industrialist, who either do not have or are unwilling to risk their own capital. Most such investment projects thus begin life with a heavy debt liability. In theory the DFIs are expected to provide 70 per cent of the projects investment. In practice DFI financing could cover 100 per cent or 120 per cent of the necessary capital. This is managed through over-estimating the cost of the investment and the value of the owner's pledged assets in the loan application to the DFI. Through discrete over invoicing of the imported equipment, a healthy nest egg can be accumulated abroad by the prospective borrower. However if an enterprise borrows Tk 5 crore to import machinery but actually imports only Tk 4 crore of machinery, they still have to repay the Tk 5 crore to the DFI but with a productive capacity of only Tk 4 crore from which to generate the pay back for the loan.

As a result many enterprises are condemned from birth to default unless the enterprises are particularly profitable.

Obviously the scope for defaulting with such impunity on their loans to the DFI is only possible through the connivance and incompetenee of the machinery of government and to some extent the donors. It is worth recollecting that the seeds of the present default crisis were sown in the period 1977-82 when the World Bank, Asian Development Bank and KFW Bank of Germany indiscriminately pushed loans to the private sector through the Shilpa Bank (BSB) and Shilpa Rin Sangstha (BSRS). The managers of these banks were put under heavy pressure to disburse loans so that the donors could step up their lending.

Whilst loan processing in these DFIs was always a long drawn out process due to both the inefficiency and malfeasance of the officers, much of the delay lay in the fact that projects were poorly conceived, often unviable and their sponsors had limited credit worthiness. These defects were often overcome through the telephonic intervention of ministers and key officials who pressured bank officials to approve loans against their better judgement. Once it become evident that both the donors and the higher level policy makers were indifferent to the actual bank ability of the investment project, bank officials felt free to become active collaborators in clearing unfeasible projects in exchange for some worthwhile material inducement.

The over-capitalised and leveragiged enterprise faced further problems in keeping their enterprises viable in the face of changing policies and market conditions, insufficient domestic demand due to weak growth, and tensions on the labour front. These problems were compounded by the indifference of the GOB to the mounting debt crisis due to the operational failures of enterprises and weak debt recovery of the DFIs. The accumulated debt liability through interest and penal interest thus became a problem in its own right.

The climate of default spread from the DFIs to the NCBs to such institutions as the Krishi Bank. Once it became known that the government was unwilling or unable to enforce recovery and could be pressured to ease the debt burden, even the more efficient debt service clients deteriorated in their repayment performance so that the size and rate of the default aggravated over the years.

Donor responses

The donors belatedly awoke to the default crisis and in 1985 suspended all disbursements and new loans to the DFIs until the GOB could improve recovery and reform the institutions. But the defaults on the DFIs had been compounded by defaults to the nationalised commercial banks (NCB). Thus when the World Bank negotiated the Financial Sector credit with the Ershad government in 1988 it attached severe conditionalities to the loan, relating to debt recovery.

To enforce recovery it was the World Bank who introduced the provision for publishing the defaulters list and wanted the GOB to circulate their names to all bankers so as to deny defaulters further loans. The present Finance Minister, who has been somewhat unfairly castigated by the business community for enforcing these severe measures, was in fact only honouring the commitments made by his predecessors to the World Bank under the provisions of the Financial Sector credit.

As things stand today the default both to the DFIs and the NCBs have reached unmanageable proportions due to the compounding of the interest liability. The DFIs show no sign of being able to recover their outstanding dues so that lending by the donors to the DFIs remains suspended even today, seven and half years after the original suspension. As a consequence, lending by the DFIs for new projects remains low and in turn new investment by the private sector remain low.

In the 1986-91 period, coinciding with the 1986 Revised Industrial Policy, real manufacturing investment has

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remained stagnant. This suggests that unless the DFIs resume lending, the scope for a surge in new investments in the private sector is limited. Some donors, such as ADB, have tried to get round this impasse by lending directly to private enterprises. But scope for this is limited by the very intensive loan appraisal procedures of the multilateral banks who, if they assume the risk of the loan, want to be sure that their loan is not defaulted.

We will thus have to first diagnose the sources of the illness infecting the industrial sector and put in place a recovery plan to improve the health of already sick industries in both the private and public sector. This will require more basic solutions which address both the malaise afflicting the whole economy and the crisis of governance. The tensions on the labour front and the deterioration in law and order are merely symptoms of this wider crisis.

None of these expedients nor the government industrial policy reforms in 1982-1986 and in 1991 have done much to stimulate private investment in industry. Businessmen still remain reluctant to risk their own equity, because, they argue, the deterioration in worker management-relations, the unfavourable law and order situation and above all exposure to an uncertain external market regime aggravated by liberal imports, both illicit and due to policy reforms, do not guarantee them enough security for assuring a return on their investment. This investment pessimism in the private sector is no doubt reinforced by the mounting liabilities of the borrowers from the DFIs and NCBs and the fact that 4500 enterprises are now claiming to be sick and in need of some government sponsored debt relief.

Improving the health of the private sector

Can a poor country such as Bangladesh afford to have the cream of its private sector languishing in a state of sickness, with little new investment taking place, factories closed or operating at low capacity and debts to the DFIs and NCBs mounting by the week? When we see that the public enterprises are equally sick, we must come to terms with the fact that Bangladesh is suffering from a systemic crisis which will not be resolved by silly polemics about the limitations of the public and private sector or by simplistic conditionalities imposed by the World Bank and Asian Development Bank about promoting privatisation and import liberalisation as the panacea to our chronic maladies. Import liberalisation is adding to the sickness of the industrial sector. Privatisation of this sickness will thus do nothing to rescue us from the industrial stagnation which has affected the Bangladesh economy over the last five or seven years.

The *Dolai Khal* entrepreneurs, the handloom weavers, the village *karigars* have all demonstrated considerable enterprise, in raising capital, accessing market opportunities, innovating, making profits and reinvesting this for expansion of capacity... It is the misfortune of our economy that this numerous, hardworking and creative constituency has received little academic recognition, remains invisible to policy makers and donors and has no advocates in our political arena.

Improving the health of the private and public sector is thus of considerably more importance today than to indulge in theoretical discourses about changing the boundaries between the public and private sector. The fact that over 50 per cent of the 690 public enterprises privatised since 1974 are today closed is evidence enough that privatisation is hardly a solution to a deeper economic crisis.

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Bangladesh cannot afford an underperforming private sector anymore than it can afford a loss making public sector. Both institutions have been set up with public funds so that their poor performance is not just a private loss but is a national loss. This national loss has to be measured in terms of the various alternative uses for these resources such as primary schools and healthcare, irrigation, credit to the poor. The fact that the overwhelming majority of the working poor in whose name aid is mobilised from the donors do not have access to DFI or NCB loans means that access to these loans has been a form of discretionary political patronage available to the GOB which has enabled a few thousand families to prosper.

To thus first condone and then write down debt liabilities is seen by the lakhs of small private enterprises, the large numbers of poor borrowers from Grameen Bank who have regularly serviced 98 per cent of their loans or the millions of small farmers paying higher fertilizer prices due to the World Banks desubsidisation policy, as a further demonstration of the skewed system of priorities of the GOB towards the already affluent classes. The government thus has to enforce credit discipline for generating resources for underwriting new private investment, for enforcing a competitive economy and for restoring a sense of social justice in its development agenda. We thus need to find creative solutions to the default crisis which reactivates production without perpetuating a default culture and can widen the network of institutional credit to the small entrepreneurs without infecting them with the disease of credit indiscipline.

The goal of public policy thus has to aim at transforming the performance of both the public and the private sector. This means more than just raising the profitability of some loss making public and private enterprises. It means the redirection of the entire system of governance away from a regulation oriented *babu raj*, which obstructs rather than stimulates both public and private enterprise, towards production-oriented system committed to promoting efficiency, real transparency in distributing public resources and full accountability for its use. It means a transformation in the culture of the private sector through policies and commitment of resources which reward the risk taker, the innovator, the producer and build a competitive climate where the market rather than discretionary patronage to the influential, differentiates the gainers and losers.

How are we to realise this transformation which has eluded us for two decades? There are no ready made answers. The problem is political and touchs the very essence of a democratic system. It should thus be the primary task of the political parties to address these issues.

Such a dialogue may address, inter alia, such issues as the reasons for poor performance in the public and private sector, policies and institutions to improve both allocative efficiency and the performance of existing institutions, finding a creative solution to the default crisis, the features of a long term industrialisation strategy, the division of responsibility between the public and private sector to realise the industrialisation strategy, mechanisms for ensuring accountability and transparency in the use of public resources in both the public and private sector, the appropriate institutional mechanisms to bring about mutual cooperation between the public and private sector and the workers, measures to reach out to and stimulate the enterprise of the non-patronised entrepreneurial class and to integrate them into the development design. Such broad issues would need to be broken down into a series of even more specific issues for discussion. Out of such a dialogue we may hope to conscientise the political activists and the public about the need for the the design of an agenda to transform the performance of the public and the private sector.

EC devalues Portuguese, Spanish currencies

BRUSSELS, Nov 22: European Community finance chiefs devalued the Spanish and Portuguese currencies by six per cent early Sunday in the latest attempt to clam chaos in currency markets, reports AP.

The move, the third realignment of European currencies in two months, was announced after an 11-hour meeting of the EC's Monetary Committee, a panel of central bank directors and treasury officials.

The devaluations of the Spanish peseta and Portuguese escudo do not alter their values against the dollar. The change takes effect Monday.

Devaluation makes a country's exports cheaper and tends to boost its economy, but imports become more expensive which can fuel inflation. The peseta was devalued by five per cent on Sept 17.

The turmoil has thrown into doubt the ability of the EC to achieve its goals of establishing a common currency and single central bank by the end of the decade.

In Madrid, Finance Minister Carlos Solchaga said Spain requested a further reduction of the peseta's value to restore confidence in the currency and boost the nation's slowing economy.

Portugal followed suit to keep its exports competitive with products from Spain and Britain, its main trading partners.

The realignment Sunday comes two months after the worst upheaval in the 13-year history of the European Monetary System, which was established to limit fluctuations among EC currencies and pave the way for a single currency in the 12-nation bloc.

On Sept 14, the Italian lira was devalued by seven per cent and Germany cut it's key lending rate.

But this failed to restore

Paris may not necessarily exercise veto power

French PM rejects EC-US accord

PARIS, Nov 22: Premier Pierre Beregovy on Saturday called a landmark farm agreement between the European Community and the United States "unacceptable," but stopped short of threatening an immediate French veto, reports AP.

"It constitutes a grave threat to European agriculture, and not only for French agriculture," Beregovoy said.

He said there would be "difficult negotiations" ahead, indicating that France would not necessarily exercise a veto to scrap the accord.

Some leading conservative lawmakers and farmers, however, urged an immediate government veto.

Beregovoy and Agriculture Minister Jean-Pierre Soisson urged French farmers, who have held angry demonstrations in the past week aimed at the Socialist government and the United States, to restrain themselves from violence.

A McDonald's restaurant was forced to close Saturday night in Amiens, about 100 kilometers (60 miles) north of Paris after some 100 protesting farmers tried to enter the fast-food restaurant. The farmers remained outside, shooting off firecrackers and affixing posters to the windows, but no major damage was reported.

In Lille, north of Amiens, about 20 farmers burned hay in front of another McDonald's and took away meals for their children.

Earlier in the week, farmers had entered a McDonald's and stomped on hamburgers as a symbolic protest against America. France, the EC's leading agricultural producer, had long blocked an agreement with the United States as detrimental to its farmers.

No farmers' protests were reported Saturday, although the Peasant Confederation representing small-scale farmer added to call for a massive demonstration Wednesday in front of the National Assembly, which debates the long-stalled world trade negotiations that day.

Beregovoy used harsh words to describe his reaction. "Based on the information I currently have at hand, I judge this project unacceptable, and it will not be accepted," he said in a statement released by the Prime Minister's office.

But he added, "We have before us thus difficult negotiations," suggesting that France will seek a more favourable version of the accord through talks.

"We have good sense on our side: Europe cannot reform its common agricultural policy in May only to dismantle it in November, " he said.

EC President Jacques Delors, who is French and is thought to have presidential aspirations, declined to express an opinion until a final trade pact is reached in Geneva.

Jacques Chirac, leader of the main conservative opposition group, the Rally for the Republic, Saturday repeated his party's call to scrap the agreement. "The government has no choice but to (Veto) an accord that seriously harms the interests of farmers," he said.

Philippe de Villiers, a prominent lawmaker from the Conservative Union for French Democracy, agreed that "The president of the republic should make it known that France will exercise its veto in Brussels." He said the accord "betrays the interests of France."

France's Communist Party, which often sides with the Socialists on vote calls, said Friday that the veto should be used to "say no to the American diktat."

Asia welcomes the deal

An undated AFP report says: Asia generally welcome the new farm export subsidies agreement between the United States and Europe, with Japan raising the only criticism, fearing its implications on their rice import ban.

Japanese Prime Minister Kiichi Miyazawa said the agreement was "welcome," but added there would be no change in Japan's opposition to a proposal that its lift a ban on rice imports and instead levy high tariffs that should be reduced gradually.

He also pointed to the French objections to the agreement, pending approval by European Community member nations. "We need to watch developments in the French parliament," he told reporters at his official residence.

Japanese caution contrasted with the reaction of New Zealand's political leaders and farming representatives who hailed the agreement Saturday as an exceptionally good deal that would have a major impact on the country's economy.

G-15 urges greater Third World links

DAKAR, Nov 22: Leaders of the G 15 group of developing countries, meeting in Dakar for a three-day summit, called for greater cooperation between countries in the developing world and better relations with the industrialised North, reports AFP.

Opening the third G 15 summit, Senegalese President Abdou Diouf also urged the international community to mobilise to bring an end to the conflicts in Somalia, Liberia , Bosnia-Herjegovina and Angola, which were endangering world stability.

He spoke, also, of the injustices committed against other peoples, such as the Palestinians and people in South Africa.

He said "the countries of the North" had a "role to play in construction of our common future."

He said the financial capital, technology and knowledge of the industrialised North were indispensable if the developing countries were to fulfil their potential and called for increased South-South cooperation, which would help create a world in which interdependence would prevail.

DAKAR: Zimbabwe President Robert Mugabe (L), Indonesian President Suharto (C) and Senegale President Abdou Diouf (R) attend the 3rd G-15 summit November 21 here. The meeting of the leaders of the Group 15 will end November 23. — AFP/UNB photo

Acting Brazilian President Itamar Franco, speaking on behalf of the countries of Latin America, said democracy and development were the words which best described the aspirations of people in those countries.

He urged respect for the 'free opinion of Angolan voters" and called on the international community to condemn all attempts to achieve a solution by force in Angola.

There had been a deterioration in the economic relationship between North and South, Franco said. "The developing countries have opened their markets but, because of northern protectionism, they have not been obtaining reciprocal benefits."

Indian Prime Minister Narashima Rao called for a "global partnership between North and South."

Egyptian president Hosni Mubarak said the South needed to have realistic aims, and move forward in stages toward cooperation with the North.

G 15, comprising Algeria, Argentina, Brazil, Egypt, India, Indonesia, Jamaica, Malaysia, Mexico, Nigeria, Peru, Senegal, Venezuela, Yugoslavia and Zimbabwe, was founded in 1989.

Top US business executives see continued weakness in economy

WASHINGTON : Top executives from major US corporations expect the economy to limp long this year and to show little improvement in 1993.

"The economy has continued the same halting and sluggish performance that has prevailed throughout the recovery," the Business Council said October 8.

The slow growth is project to keep unemployment high and inflation low, the Council said. Meanwhile, a projected slowdown in the economies of major US trading partners is

US interest rates and boosting the value of the US dollar in foreign currency markets, according to the forecast.

The Business Council, which meets twice annually, consists of the heads of the largest US corporations. The forecast is put together by a panel of 18 corporate economists.

US economic output is projected to rise two per cent in the second half of 1992, about the same as in the first half of the year but a full percentage point below what was expected in the forecast presented in May. The consensus forecast is

than forecast are greater than the chances that it will be stronger, the Business Council report said.

The Business Council forecast was echoed by the separate "Blue Chip" survey of 52 private economists, released October 9, projecting 2.7 per cent growth in GDP next year.

Of the 18 economists, 10 see no difference in terms of growth prospects through next year under Clinton administration, while 8 believe growth may be somewhat higher under Clinton. Eleven of the 18 believe the federal budget deficit will be higher if Clinton

"At these levels, the deficits are approximately 5.5 per cent of the nation's total gross domestic product, the highest ratio for any two-year period since the 1940s," the economists said.

The panel said the industrial production is still not back to its pre-recession high, and is not now expected to regain that level until early in 1993.

"Within this overall environment, no major sector is viewed as likely to turn in a truly strong performance," the Business Council said. But the housing sector is projected to

pressed levels. But the growth in consumer spending — projected to average 2.6 per cent during the four quarters of 1993 — would still be only about three fourths as fast as the average growth over the past 30 years and well below the pace typical during recoveries.

The Business Council economists see some slight further easing in inflationary pressures, projecting consumer prices to rise about 3.25 per cent during 1993.

The panel forecasts corporate profits climbing 15 per

It expects the unemployment rate to remain around 7.5 per cent through the spring of 1993 and then drop to 7 per cent at the end of next year.

The economists said they expect the Federal Reserve, the US central bank, to continue to ease monetary policy if the economy remains sluggish and some fiscal stimulus to be enacted sometime next spring, regardless of which candidate wins the presidency.

A majority of the panel see some tightening of monetary policy by the middle of next year.

"Even the highest growth rate now expected for this year is only two per cent in Japan," it said.

This will dampen US exports, which are projected to grow, on average, by only 2.1 per cent in 1992 while imports to good and services climb by 5.7 per cent.

Despite the widening trade deficit, the Council concludes that US products will remain globally competitive because of the low level of the dollar.

"The recent particularly low levels of the dollar are not likely to be sustained, and some rebound against the