

Readymade Garments Industry Developing Backward Linkage to Face the Challenges of 2005

by Professor Hafiz G A Siddiqi

An enabling environment must exist. The law and order necessary to operate the industry must be maintained. Mustanism, hartals, illegal trade unionism, etc. leading to stoppage of work at ports, transport movement, etc. must not be allowed to disrupt the normal operation of the industry. Infrastructural bottlenecks must be removed.

GIVEN The investment needs and future uncertainty, one can safely conclude that Bangladesh will not be able to invest Tk 21,000 crore (twenty one thousand crore) to develop the total capacities in the backward linkage industries required to meet the demand of RMG in 2005. To be self-sufficient in the production of export quality yarn and fabrics is neither necessary nor feasible.

However, it is necessary to make the RMG industry more competitive than it is now because the post MFA world market will create new challenges for Bangladesh.

One such possible challenge will be that the traditional sources of supply will shrink which may adversely affect the RMG industry of Bangladesh. For example, the supply of cheap cotton, yarn and fabrics from India, China and Pakistan will decrease because they will first use their surplus cotton, yarn and fabrics to manufacture garments to create new value addition and earn more foreign exchange by exporting them. (This will be possible due to the phasing out of MFA).

Therefore, Bangladesh must try to reduce its dependence as much as it can on foreign sources for yarn and fabrics by increasing its capacity to produce that much of yarn and fabrics which our traditional suppliers will refuse to supply because they themselves will be using them for the production of garments.

This means Bangladesh must create a certain amount of new capacity to spin yarn, weave cloth and process gray fabrics. It will still continue to partly depend on imported yarn and fabrics as do Hong Kong and Singapore. This should not create a serious problem for Bangladesh to remain competitive in the world market after 2004.

It is unlikely that our traditional suppliers will stop exporting cotton or yarn or fabrics completely by diverting all these resources to the produc-

tion of garments. This will go against their comparative advantages. Our traditional suppliers particularly India, Pakistan, China and Thailand which are at a relatively higher stage of development and are richer compared to Bangladesh will in the near future move to the production of high-technology higher-value items where return on investment will be much higher than that in RMG. The garment industry being migratory in nature will continue to thrive in a country like Bangladesh as long as labour remains cheap. Therefore, for Bangladesh, the sources of supply of cotton, yarn and fabrics will not completely dry out.

This means that the RMG industry needs to be integrated only partly; a limited number of composite mills, a larger number of independent spinning mills and processing units may be established.

But investment in these sectors will not be viable unless the government reforms its policies of financial support. The cost of financing the linkage projects must be brought down as was done by India and other countries during the initial period of developing their textile sector. The cash incentives should continue. In addition, long term loan must be available at reasonable interest rates. Although the current nominal rates are around 12 per cent, the actual cost of fund to the entrepreneurs amounts to some 20 to 22 per cent after various adjustments. This is quite high a rate which will discourage investment in this sector. The commercial banks need not maximize their profits at the

cost of the RMG sector. The government may direct the banks to make reasonable profit (not as much as they can squeeze from the market) and lower the interest rates for RMG sector substantially, say to 6 to 7 per cent. It does not mean that the bank should not take necessary precaution against possible defaulters.

Debt-Equity Ratio: Investment in backward linkage industries, particularly in composite mills is quite large. As indicated in the main text, the entrepreneurs will need equity capital from financial institutions. Currently a 50:50 debt-equity ratio is enforced. To encourage investment in this sector the government should lower the ratio to a reasonable level, say, 80:20.

Creation of Special Equity Fund: As stated earlier, if all the backward linkage industries a spinning, weaving, dyeing, printing and processing are to be developed by 2004 a total of Tk 21,000 crore will be needed as equity fund. The government should create a Special Fund of at least Tk 15,000 crore to provide equity capital to those sound entrepreneurs who can come up with 20 per cent equity. It may be mentioned here that similar supports are available in many countries including India.

Human Resource Development: The floor workers, supervisors and production managers in general are not properly trained. This is true of spinning, weaving, dyeing, processing and garment manufacturing. Bangladesh must improve substantially both labour

productivity and managerial efficiency. Human resource development must be given high priority otherwise equity support and concessional rates of interest will not be of much help. The quality of yarn and fabrics in addition to design and making of the garments must be of high standard. The competitors of Bangladesh, namely, Hong Kong, India, Sri Lanka and others have established special training institutes. For example, the Institute of Textile and Clothing at Hong Kong Polytechnic University offers three-year diploma programmes in the relevant fields. The BGMEA should discuss with universities, particularly private universities and finance introduction of modern courses which will enhance the skills of production workers of the spinning mills, weaving mills, processing units and garment factories. It must be reiterated that the quality of the product and delivery services, including marketing will finally determine the fate of the RMG industry after 2004.

Diversification of Product and Market: The importance of product and market diversification has already been emphasized. So far Bangladesh did not need much marketing efforts because most of the firms have been working as sub-contractors. But to remain competitive in the post MFA world market, the number of the independent firms must increase from the current level of 8 per cent to at least 30 per cent. These firms must be able to identify, through market research, new market segments (new products including). Both India and Sri

Lanka are implementing this strategy. By successfully exporting non-quota items, Bangladeshi entrepreneurs have demonstrated that they can get into new markets. Therefore, there is no reason for unnecessary panic about post MFA market when competition will increase. Assuming that adequate government support will be available, the important thing is that Bangladeshi entrepreneurs emphasise the quality of the products, product diversification and aggressive marketing.

Market Access: As a member of WTO, Bangladesh must insist to have duty free access to such large markets as India, Japan and China. There are many new types of garments (it needs research to identify the specific market segments) which Bangladesh can produce with the support of the new backward linkage facilities and serve these markets. As one of the 48 least developed countries of the world, Bangladesh should resort to the Provisions of WTO which entitle Bangladesh to have non-reciprocal market access to such countries as mentioned above. If Bangladesh can get into the markets of Japan, India, ASEAN countries and China, it will not have problem in maintaining its leadership in RMG exports after 2004. However, the success will mostly depend on how efficiently Bangladesh conducts its business/economic diplomacy.

Above all, an enabling environment must exist. The law and order necessary to operate the industry must be maintained. Mustanism, hartals, illegal trade unionism, etc. leading to stoppage of work at ports, transport movement, etc. must not be allowed to disrupt the normal operation of the industry. Infrastructural bottlenecks must be removed. The image of Bangladesh must further improve. Bangladesh must gain confidence of the investors, local and foreign.

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IN MEMORIAM

Dewan Mohammad Azraf

by Abdur Rahim

A legend in his lifetime National Professor Dewan Mohammad Azraf passed away in Dhaka on November 1, leaving a vacuum in the intellectual field of Bangladesh. Renowned philosopher and dedicated educationist Dewan Azraf was the founder Principal of Abujar Gifari College in Dhaka Author of 40 books on different subjects, specially on Islam and philosophy, he was a grandson of spiritual poet Hasan Raja of Sylhet.

tions including Islamic Foundation and Dr Mohammad Shahidullah Smriti Samity. Dewan Azraf died at the ripe old age of 94. But it is unfortunate that he did not get his due honour at the fag end of his life



A scholar of rare qualities, Dewan Azraf had dedicated his life in the teaching profession and was engaged in popularising philosophy through his writings and deliberations in different seminars and symposia. An authority in Islamic philosophy Dewan Azraf was also well-versed in Pali and Sanskrit. A former Professor of Philosophy and Islamic Studies in the Dhaka University, he was later honoured as a National Professor during the regime of Late president Ziaur Rahman. He lived a very humble life in his old age.

He was also awarded Ekushey and Shadinata Padak, besides many other awards from various organisations including Islamic Foundation and Dr Mohammad Shahidullah Smriti Samity.

and he had to suffer from financial problems. It is alleged that he did not get proper attention from the government when he fell critically ill. Wellwishers and admirers of the late National Professor had

called upon the government to send the ailing philosopher abroad for treatment. A national daily reported that not even a medical board was formed for this great man whereas writers of lesser calibre get much more care and government patronage in such case.

The general people and the opposition party leaders, have, however, shown due respect to the departed soul since the government party leaders worth the name were conspicuous by their absence in Janaza also. It is said that the greatness of a nation is judged by the honour they show to the great sons of the soil. Dewan Azraf is gone but his contribution towards our philosophy, literature and culture will remain alive and the indebted nation will remember him for ever. No monuments are required to be erected to keep the memory of Dewan Azraf alive; with the passage of time monuments may perish but intellectual contribution lasts for eternity.

That such intellectuals as upheld the cause of freedom of expression have ignored the great soul of the soil even in his death is a shame to the nation. Let his soul rest in peace.

Dr Habibuz Zaman

by Shahabuddin Mahtab

"It is not enough merely to exist. It is not enough, I am earning enough to support my family. I do my work well. I am a good father, husband, churchgoer.

That is all very well. But you must do something. Seek always to do some good, somewhere. Every man has to seek his own way to realize his true worth. You must give some time to your fellow men. Even if it is a little thing, do something for those who need help, something for which you get no pay, but privilege of doing it. For remember you do not live in a world all your own. Your brothers are here too."

— Dr Albert Schweitzer.

abroad (USA, UK). His only son was born in the USA, and is now a doctor in Virginia. Both his daughters, are in North America. His wife Jahannara Zaman, lives here in Gulshan, Dhaka.



Dr Zaman was a Fulbright Scholar, a WHO fellow, and again, a Nuffield Foundation Fellow. In the matter of fellow-

ships, he was also a Fellow of the Royal College of Pathologists and a Certified Pathologist (USA). His seminal contribution in the field of medical education was the training of forty histo-pathologists, while he was working at the Jinnah Postgraduate Medical Centre, Karachi (1960-70). As Director, Medical Education in Bangladesh (1972), he helped in the establishment of the College of Physicians and Surgeons. In the seventies and eighties (till 1987) he served as Advisor of the WHO at the South-East Asia Regional Office, New Delhi.

On return to Dhaka after retirement, he mostly spent his time in his study overlooking a garden, in writing, both in the areas of medicine and memoirs. His recent publication "70 Years in a Shaky Subcontinent" (Janus Publishing Co Ltd, London) is a collection of such memoirs events that he passed through and observed. A large part of his time was spent in voluntary service (1987-99). A genial and friendly person, he was a gentleman par excellence. His last wish was to rest in peace.

Project Finance

Providing Mechanism to Avert Bankruptcy

by Dr. M. Fouzul Kabir Khan

Project finance deals involve great amount of due diligence on bankability of the projects to ensure that the project produces the desired output and the cash flow generated by the project is enough to pay all debts.

PROJECT Finance is a relatively new concept in this country. The term itself is misleading as it literally implies the financing of projects in general. In fact, project finance refers to a particular method of financing projects. Broadly, debt in a typical project may be financed through two different methods, namely: corporate finance and project finance. Under corporate finance the lending decision is based on the overall financial condition of the borrower including its corporate balance sheet. Even if the project to which loan has been given is not performing well the lenders can still expect to get paid if the corporate entity as a whole remains healthy. In case of project finance the lending decision is primarily based on the evaluation of the project and the special purpose vehicle (project company) created to implement the project. The source of debt repayment is limited to project's assets and mainly to its cash flows. Therefore, project finance is usually on a non-recourse or limited recourse basis implying that project sponsor's assets outside the project are not offered as security for debt repayment. Corporate finance on the other hand is often based on full recourse, meaning that all corporate and sponsor's assets are at stake for repayment of debt.

Project finance techniques are used mainly in capital-intensive projects characterised by highly leveraged debt. Previously the use of the technique was limited to mining, oil and gas development and similar extraction activities. In recent years, project finance is also being used in financing of infrastructures and other similar activities. In Asia alone, infrastructure projects worth US \$ 500 billion were financed using project finance technique. In Bangladesh, several capital-intensive projects in power generation and a container port are

in the process of being financed using this technique.

The recent popularity of project finance is due to several factors. From the sponsor's viewpoint it allows them to mobilise large amount of debt to implement capital intensive projects. It permits them to do so with relatively small equity contributions and without exposing their corporate balance sheet. In a typical project finance deal debt-equity ratio could be 4:1 or even higher. From the lenders' perspective it allows them to focus their due diligence on project intrinsics without bothering about the details of corporate health. Project finance deals have also become possible because of financial and legal innovations involving identification, mitigation and allocation of project risks among various participants of the project.

Project finance deals are structured around a number of simple premises. Firstly, a project must have predictable and robust cash flow that would enable repayment of all debts plus a fair return on equity over a reasonable period of time. Secondly, each major project risk has to be allocated to the party that is in the best position to absorb such risk. Finally, there have to be legally enforceable contractual arrangements including provisions of events of default, liquidated damages, lenders' step-in rights and other security that create conditions for project participants to abide by the contract. In the ultimate analysis project finance is based on cash flows. That is why it is often euphemistically said that there are three important things to remember in project finance: cash flows, cash flows, and cash flows!

The key features of project finance deals are discussed below.

Date-certain fixed-price construction contracts: Most important risk in any project is construction delay and cost overrun. Therefore, lenders in a project finance deal always insist on date-certain fixed-price construction contracts. Such contracts must also lay down the various milestones for construction completion that lenders would monitor with the help of independent engineers. Such contracts not only ensure completion of the project on time but also help in planning the infusion of funds into the project. The construction contractor has to agree to provide an agreed sum of liquidated damages for the failure on its part to achieve critical milestones. Based on the construction contractor's undertaking the sponsors provide similar completion guarantees to the government/agencies.

Disbursement of funds and agent bank: The lenders in project finance deals would make sure that the funds lent to the project are used exclusively for the purpose of the project and are not diverted to other use. Therefore, lenders would agree with the sponsors on the project costs and a disbursement schedule based on independent engineer's review of the construction contract and other project documents. Thereafter, lenders would appoint an agent bank that would receive both equity and debt as per agreed disbursement schedule and using these funds, would make payments to contractors and suppliers and other similar parties.

Definite off-take and input supply arrangements: Usually

project finance deals are structured around some kind of definite off-take arrangements for project's output. These contracts generally take the form of take-or-pay contracts under which the off-taker guarantees to pay for making capacity available irrespective of whether or not the output is actually dispatched or used. Usually such capacity payments are adequate to service all debt and ensure a reasonable return on equity. Power Purchase Agreement, common in power generation projects, is an example of take-or-pay contract. In addition to capacity payments the off-taker is also required to make usage payments (e.g. energy payments) in proportion to the output actually used. In addition to off-take arrangements project finance deals are often characterised by fuel input supply contracts. Fuel Supply Agreement, common in power generation projects, is an example of such an arrangement.

Revenue cascade and use of escrow accounts: Lenders in project finance deals maintain strict vigilance on accrual and use of project revenues. Sponsors have to agree to channel project revenues into an escrow account and to set up a hierarchy of payments from such accounts. Again the agent bank referred to previously would administer the inflow and outflow of funds according to an agreed cascade pattern. The first charge from the account would be the agreed expenses required to run the project (e.g. organisation & management expenses), followed by any government dues and senior debt service payments. This is followed by payments to sponsors like subordinated debt

service, technical services fee, dividends etc. The latter payments can be made only after the priority payment obligations are met.

Credit enhancements by third parties: When lenders consider bilateral commitments made by project participants under various project agreements as inadequate, the lenders may require credit enhancements from third parties. For example, a bank with good credit rating may be asked to open letters of credit confirming infusion of equity by project's sponsors. Other examples of credit enhancements include various insurance, warranties and partial risk guarantee (PRG). Recent debate regarding IDA partial risk guarantee for AES Haripur project illustrates the use of credit enhancements in project finance deals. Under the proposed PRG, commercial banks would lend to the project in exchange of a guarantee that in the event of failure of the project company to service the debt, IDA will make the debt service payments. IDA in turn would require an indemnity agreement with the government before issuing such guarantee to the commercial banks.

Lender's step-in rights: In project finance deals both the sponsors and the government are required to inform the lenders if the project goes wrong in any significant way because of failure of one or more of the participants to fulfil their obligations. Examples of such situation would include failure to achieve any key construction milestones and/or payment defaults. In such a situation the lenders have a right to step in to revive the project by infusion of funds and even by bringing in a new operator. Various project agreements recognise such rights of the lenders.

Security: As mentioned earlier, project finance deals are structured on limited/non-recourse basis. Therefore, lenders have stringent security requirements under this arrangement. The standard security package would include all of project's assets including mortgage on immovable properties, hypothecation on movable properties, assignment of project revenues, all project contracts and insurance.

Project finance deals involve great amount of due diligence on bankability of the projects to ensure that the project produces the desired output and the cash flow generated by the project is enough to pay all debts. It also involves evolving mechanisms to ensure that project funds are exclusively used for designated purposes and use of project revenues based on the agreed revenue cascade with repayment of senior debt as a high priority. It also requires weaving of contractual framework that would provide right incentives to the project participants to work in the best long-term interest of the project. Finally, it also needs to provide a mechanism for the lenders to correct the situation through direct intervention if something is grossly wrong with the project well ahead of time so that bankruptcy and liquidation could be averted.

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Racism Dies Hard!

We Want a "White Waiter" and a "White Teacher"

by Lal Salam

RECENTLY, the American press has been carrying stories about Bangladeshis as "model minorities", working hard to realize the American Dream. However, not all the stories are quite so positive. This week, two incidents reminded us of the dark side of the dream. In both cases, stereotypes about Bangladeshi immigrants were used in shameful manifestations of racism.

The first incident involved 22-year-old Kabir, a computer science student at Wichita State University and a popular waiter at nearby "Chili's" restaurant. A 50-year-old couple were waiting for dinner when Kabir came to take their orders. As Kabir started telling them about a special contest "Chili's" was holding, the lady interrupted: "We don't want to hear about a... contest!"

Before Kabir could regain his composure, the lady (and there could be no doubt at this point as to what kind of a lady she was) continued, "We would like a white waiter."

If this were New York, one of two things would have happened: either Kabir would have thrown them out, or the manager of the restaurant would have done the same. But this being Kansas, a white waitress intervened (you might call her Dorothy from Oz) and a badly hurt Kabir walked away. The couple asked if "Dorothy" was going to be their waitress. She said yes and they were visibly pleased.

Kabir's co-workers were furious, but the two managers on duty decided "not to make a scene". Later, when the Wichita Eagle newspaper contacted him, general manager Sean McLachlan, defended the decision:

"Maybe they were racist and ignorant, but I think it was best that we avoided some kind of scene or trouble because of our other guests. We have to be concerned about all our guests. In 14 years in this business, and four as a manager, I've never heard of this happening before. It's unfortunate there are people like that out there."

share Sean's sense of caution. In an outraged article, reporter Bob Getz wrote:

"Myself, I think it's unfortunate that McLachlan didn't toss these sorry racists out of the restaurant. And instead of worrying about making a scene, making so much commotion that even the customers in the restaurant's most distant corner knew exactly why these people were getting the old heave-ho."

When reached for comment, Kabir sounded a conciliatory note:

"I love to work at Chili's. I work my butt off. But I enjoy it. I've never had anything like that happen to me before. Yes, I felt really bad. I was very frustrated. But I didn't react. It happened very suddenly and surprised me."

In another corner of the country, Mohammad Matur Rahman was in anything but a conciliatory mood. Unlike 22-year-old Kabir, 50-year-old Rahman was determined to make as much fuss as possible. A Chemistry instructor at Grand Rapids Community College, Rahman was fired from his \$62,000-a-year position a year after he started work. In a lawsuit against the College, Rahman's lawyers argued that he was discriminated against because of his Bangladeshi accent and nationality.

Rahman told reporters that: "It's because of my nationality that many of the students have been manipulated to complain against me." Named in the lawsuit were science instructor Tom Neils, former acting Dean Roberta Schrader and former acting head of physical science, Leslie Edmondson. The lawsuit alleged "severe emotional distress, lost wages and benefits, embarrassment, as well as impaired earning capacity."

Rahman has been a U.S. citizen for several years. A former teacher in Bangladesh, he taught at various small colleges in the US before being hired as a Chemistry instructor at his present job in August 1998. The papers filed with the

court argue that Tom Neils was afraid from Rahman from his first day.

"Even before (Rahman) began teaching in Grand Rapids, Defendant Tom Neils... began questioning (Rahman) about his salary schedule. Dr. Neils made it very clear that he was not pleased that (Rahman) started at a higher salary than he (Neils) was currently being paid."

"I was treated like a foreigner (by Neils)" said Rahman to reporters.

When contacted by the Grand Rapids Press newspaper, Dr. Neils vehemently denied the accusations:

"I did nothing wrong. I'm not jealous. I'm not anything. Somehow there was a huge misunderstanding between what I said and how he interpreted it... I don't understand why I'm being sued in the first place. I'm not mad at him."

A month after he was hired, Leslie Edmondson said students started to complain about Rahman's accent. Lawyers for Matur Rahman stated that he had been working to fix this problem: "(Rahman) stated that he would attempt to raise his voice and speak more clearly. He is aware that he has an accent and he is continuously trying to improve his accent."

After this meeting, Rahman alleged that Edmondson actively began looking for information against him:

"They were asking the students behind my back to get as many complaints as they could from the students. They completely interfered with my instructions and tried to do things to make me look ineffective."

Dean Roberta Schrader later told Rahman that "I paid tuition to come to GRCC. I want to be taught by white faculty, no matter what."

When the case comes to court, I hope Rahman's lawyers will remember to ask this:

If being White and speaking English without an accent were the two main criteria, how many immigrants would have succeeded in America over the last century?

