Is LDC graduation a panacea?

Selim Raihan

Bangladesh has successfully met all three criteria for LDC graduation in the first review in March 2018. It is expected that Bangladesh will be able to meet the graduation criteria in the second review in 2021 and will finally graduate from the LDC status in 2024. Benefits of graduation from the LDC status are cited to include an improved country-image and higher rating for investment by international rating agencies which may attract larger foreign direct investment. However, there are a number of risk factors for Bangladesh associated with its graduation from the LDC status. Simulation results from the global dynamic general equilibrium model suggest that the loss of preferences in the markets of European Union, Canada, Australia, Japan, India and China in 2027 (the year which will mark the end of preferences for Bangladesh if the country can officially graduate from the LDC status in 2024) might lead to an annual reduction in total exports of Bangladesh by 11% which would be equivalent to around US$ 6 billion given the current projection of growth in exports. Also, many of the exemptions of WTO provisions, including the cut in tariff and subsidies and adherence to intellectual property rights (especially for pharmaceuticals sector), which are currently enjoyed by Bangladesh as an LDC, will no longer be available after 2027. Furthermore, as Bangladesh has already graduated from the World Bank’s ‘low-income’ category to ‘lower-middle income’ category, the scope for loans at lower interest rates would be limited. It is important to mention here that much of the aforementioned prospective benefits is not ‘automatic’ as the country has to work quite a lot to materialize those benefits. In contrast, almost all of the possible losses would be ‘automatic’ as soon as the country graduates from the LDC status. Therefore, the country has to prepare itself over the next 9 years to counter these losses. In order to have a better understanding of Bangladesh’s progress in the per capita Gross National Income (GNI) in a cross-country context over the period between 1980 and 2016, we have created a scatter plot for 140 countries (excluding the high-income countries). The horizontal and vertical axes show the log of GNI per capita in 1980 and 2016 respectively. The larger dot shows Bangladesh’s position in 1980 and 2016. It is clear that Bangladesh was able to increase its per capita GNI from US$ 206 (log value of 5.33) in 1980 to US$ 1433 (log value of 7.23) in 2016.
Navigating the labyrinths of the deals' world: State-business relationship in Bangladesh

Mirza Hassan and Selim Raihan

For many economists, Bangladesh case is a paradox since such steady and reasonably high growth took place in the context of ‘bad’ or ‘weak’ governance. The fundamental assumption of this view is that standard ‘good governance institutions’ or ‘market enhancing governance institutions’ are pre-conditions for a high and sustained growth rate in the economy. Market-enhancing governance institutions enable the market to be efficient since these reduce transaction costs, guarantee credible commitment of the state through the establishment of formal and universal property rights, and allow an efficient enforcement of contracts. In contrast, we argue that the existing trend in growth rate has been possible in Bangladesh (despite lacking in or weaknesses of many of the market-enhancing institutions) since a reasonably robust form of ‘growth-enhancing governance’, characterized by de facto rent sharing (across political divides), political elites’ ability to separate economic and political rents (based on contingent needs), and (more critically) a largely ordered deals’ (explained below) environment (irrespective of being open, closed or semi-closed in various sectors of the economy), has created the enabling conditions (de facto credible commitment of the state, transactional certainty etc, which are critically important to the private market actors) for economic growth to take place.

In contrast to ‘Rules’ environment (formal law-based governance whereby state-business interactions are governed by impersonal transactions and universal enforcement) ‘Deals’ environment is characterized by an informal and personalized transaction and selective enforcement. Deals environments can be again divided into several dimensions: whether deals, once negotiated, are honored (ordered) or not honored (disordered); and whether deals are widely available (open) or limited to an elite (closed). Ordered deals are deals that, once negotiated between business actors and state officials, are honored. Barring a few years after the independence, Bangladeshi state has been staunchly pro-business. But it manifested major syndromes of a ‘soft state’, diverging in implementations of pro-business reforms, especially related to privatization and relaxing bureaucratic control over business through regulatory reforms. A combination of external pressure (by the World Bank and IMF) and domestic politics since the late 1970s, being dominated by pro-market elites—both politicians and technocrats, created enabling space for the state to formulate and adopt business-friendly regulatory and economic policies. Such meta/macro level features of elite political settlement largely shaped the meso level deals world and structured the state-business relations, during the earlier phases of growth acceleration.

A clearly discernible shift in the deals environment occurred during the late 1970s —from a largely closed and disordered (governing the processes of nationalization of industries, allocations of permits and licenses, uncertainty with the land reform, adjudication of property rights etc) one to an increasingly open and ordered one. In its drive to create new entrepreneurs and to bolster the private sector led industrial growth, the state followed a de facto extremely lax form of regulatory governance in sanctioning industrial loans from specialized publicly owned banks that led to massive loan default. Such ‘primitive accumulation’ strategy was, in general, based oncronyism, to a limited extent (for a few politically connected and partisan business actors), but mainly based on open deals (for the multitude of business individuals with no political identity). The latter category generated a pro-active form of market-led corruption (unsolicited bribing of officials by the entrepreneurs) as well as massive rent-seeking, mainly by bank officials, but also by officials of the relevant ministries and the process was largely governed by an ordered form of deals (transactional certainty). Such nature of rent management led to the emergence of RMG sector at the end decade of the 1970s as well as the creation of indigenous entrepreneurs, especially in the RMG sector. Such entrepreneurs, to a very limited number, were also created through the disinvestment of publicly owned industries. During the 1980s, closed but ordered deals can be observed to cover a diverse set of economic activities—granting of license and permits for export and import and large construction projects but not necessarily setting up of industries. The governance of industrial loan sanctioning and privatization of nationalized industries continued to be largely characterized by a mix of cronynis (in greater form) and open-ordered deals. Such mode of state-business relations resulted in the creation of a significant number of local entrepreneurs (especially rapid increases of RMG factory owners) and capital formation in the private sector; which perhaps, to some extent, explain the growth acceleration, albeit weak in nature, that one notices during that decade. The competitive democratic political phase (1991-2013) saw a complex evolution of the deals environment, possibly due to the relatively newer forms of rent management in the economy—a complex mix of monopolistic but pre-dominantly duopolistic rent allocations (sharing rents across the political divide). Following such de facto rent management practice, direct access to state resources/privileges (permit, license, leases etc) tended to be predominantly closed and ordered in nature and individual’s political identity critically mattered here. But even in these closed domains of businesses, market actors with wrong political identity (or no political affiliation as in the case of the majority of businesses) were also able to partner with political insiders to access state resources. Such strategic practice of the firms, in effect, transformed closed deals into an open deal to a large extent. Syndication of business firms (alliance of firms owned by ruling and opposition party actors along with non-partisan business) was another popular strategy used by the business, particularly at the sub-national levels (district and small towns), to access state resources (construction of public buildings, roads etc), which considerably opened up an otherwise politically important closed deal space. Also rent allocations, during the competitive political phase, became more centralized particularly in relations to the critical domains of the economy (power sector mainly but also large infrastructure, to some extent). Centralization of rent allocations, in the Bangladesh case, implied closed deals but not necessarily disordered. Decentralized rent allocations, hardly seen in the critical domains of economy, tended to be largely governed by a stable and predictable network of actors and consequently ordered. It should be noted that ordered deals environment provides predictability and reduce uncertainty only for players who are willing to play by the de facto rules of the game. Foreign investors who cannot take recourse to informalities (due to legal restrictions imposed by the countries of origin) or domestic business who would like to play only by the formal rules may not be able to navigate through the system or find it largely closed and disordered.

The competitive political phase ended in Bangladesh in 2013. What emerged after that, in the political domain, can be called as the dominant party system. The first thing to note is that one of the features of de facto rent management, the practice of rent sharing across the political divide, seems to have altered to a certain extent. There has been a steep rise in crony capitalist practices with the advent of the dominant party politics, although a steady increase of this has also been observed during the later years of the competitive period. Print media has exposed numerous unscrupulous cases in the banking sector, by politically connected businesses. Licensing of private banks has also been subjected to an obvious form of crony capitalism. The extent of rent-seeking seems to have changed considerably. Perhaps with the exceptions of a few critical sectors of the economy such as power (especially in relation to large plants) and very large infrastructure projects, state-business transactions have now been subjected to increasing numbers of rent-seekers (more politicians, government officials, police, regulatory agents etc), which has added to the investment costs. The mode of rent-seeking has also changed from the previous relatively centralized form to an increasingly decentralized one (again critical domains of the economy—large power plants or infrastructure are still mostly subject to centralized rent allocation process). This has been an inevitable consequence of increases in the number of rent-seekers. The business now has to engage with rent-seekers with veto power at various points down the bureaucratic hierarchies. Although there are anxieties among business actors regarding the current political situation, still this settlement has provided, since 2014, a form of political stability that contributed, among other factors, to the reasonably high and stable growth rates in recent years.

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**Book review by Dr. Syed Akhtar Mahmood**

Dr. Syed Akhtar Mahmood is Lead Private Sector Specialist in the Macroeconomics, Trade and Investment Global Practice of the World Bank Group (WBG). He acted as Global Lead for Business Regulations and is now leading the Good Regulatory Practices program of the WBG. Dr. Mahmood has worked on privatization and state-owned enterprise reforms in the former socialist economies of Eastern Europe and Central Asia and Africa, and on private sector development issues in various regions of the world. Dr. Mahmood is also interested in the mechanics of policy reforms, including political economy, institutional and incentive issues in government, and stakeholder engagement. He earned his D.PhiL. in Economics from the University of Oxford in 1989. His publications include *The Political Economy of Development Policy Change* (with Gustav Ranis), Blackwell 1991.


Syed Akhtar Mahmood

About a decade and a half ago, Professor Nurul Islam, the eminent Bangladeshi economist, gave us “Bangladesh - The Making of a Nation: An Economist’s Tale”. From the unique vantage point of an economist who sometimes saw things from a distance but often was at the center of action, Professor Islam provided a fascinating account of Bangladesh’s struggle for autonomy and independence during the 1950s and 1960s, and, then in the early seventies, its efforts to rebuild the economy and put in place a sound machinery for administration and economic management. Coming from a perceptive observer who was also an active participant in the making of a nation, this was an invaluable contribution to the literature on how nations are “made”.

But how are the men and women who help make a nation, themselves “made”? What shapes their thinking, world view, social commitment, dedication to professional rigor, values and norms, sense of duty, and ability to navigate the minefields of politics, bureaucracies and international relations? What prepares them for the leadership roles that they assume one day, not ordinary leadership within a mature, stable nation but the more challenging one involved in making and shaping a young nation? And since leaders are also human beings, what human weaknesses might they be afflicted by? How do these weaknesses emerge and how do they affect their work and effectiveness?

Anyone interested in these questions would be happy to learn about Professor Islam’s latest gift to us, his memoirs titled “An Odyssey: The Journey of My Life”. Published in October 2017, this book of 275 pages, which Professor Islam says should be read as a complement to his earlier book, is a narrative of his life starting from his childhood in Chittagong, Bangladesh’s second largest city, and ending thousands of miles away in Washington, D.C., his home for the past three decades. From Chittagong to Washington, with Dhaka, Karachi, Oxford, Rome, Cambridge (Massachusetts) and New Haven in between, this has been a fascinating journey with ups and downs - an Odyssey no doubt!

But why did Professor Islam write this book - not an easy thing to do for someone just short of entering the tenth decade of his life? "Why should I write this book", he had once asked me, "why would anyone want to read it? This question, partly philosophical, partly reflecting a concern about Bangladeshi’s apathy to history, perhaps also a reflection of modesty, was thrown at me one day as I was giving him a ride to his office in Washington D.C. As an emeritus fellow of the International Food Policy Research Institute (IFPRI), he has an office in D.C., close to mine. We also live in the same suburb in Maryland, adjacent to America’s capital. These rides have been a source of stimulating conversation and great learning for me, providing windows into Professor Islam’s personality and feelings that would otherwise remain elusive.

My answer to Prof. Islam’s question was simple. There are very few Bangladeshis, perhaps none, who have been an academic, an institutional builder, a close associate of the political leadership who led a country to independence, a high-level policy maker during challenging times, an international civil servant and a respected player in global academia. The accumulated experience of such a person is an invaluable asset that should be shared with the generations to come.

I had a question too. How frank was he willing to be - frank about what he saw, but also frank about himself? “At this age, I have nothing to hold back” Professor Islam had assured me. He has kept his promise. The reader gets a taste right up front. He writes in the preface, “It is often said that a memoir is like a mirror in which the author likes to see himself. Therefore, there is a possibility of not seeing what he does not like to see and thus memoirs may not be entirely objective. Most of all individuals have biases – that is human nature. Therefore, I hope that my possible biases would be set against the biases of others to enable the readers to reach their own conclusions”. Indeed, readers should reach their own conclusions. Thanks to Professor Islam’s rich and frank narrative, those would be informed conclusions.

It is said that the experiences of one’s childhood and youth often leave a lasting impression, for good or bad. In chapter 1, on his childhood, Professor Islam talks about his highly disciplined teacher-father who, every evening, would sit down with his son, sacrificing his only leisure time, asking the young Nurul Islam to go over systematically all topics covered in his studies that day, while cross-examining him rigorously. Prof Islam writes about its impact, “This method of learning taught me something else for the rest of my life. Before I embarked on a new chapter or a new topic, I was to go over my mind whatever I had learned from my studies up to that moment about this and related subjects. This enabled me to refresh my memory on whatever I had learned so far and link it to what I was going to study next. I found that it was indeed a strong pedagogical device”.

Perhaps this childhood experience is at root of the high preparedness with which Prof. Islam would approach things later in his life, whether his exams at Harvard where he obtained a Ph.D. (chapter 2), his dealings with the establishment-dominated board of the Pakistan Institute of Development Economies of which he was the first head (chapter 4), his briefing to the World Bank President, Robert McNamara, during 1971 (chapter 4), his negotiations with both his colleagues in government and external players as head of Bangladesh’s Planning Commission (chapter 5) or his dealings with various governments during his decade-long stint as an Assistant Director General of FAO (chapter 6). People who make a nation are people with discipline!

During 1971, as he lobbied hard in the US to gain support for Bangladesh’s independence war, the renowned economist Holis Chenery, then Chief Economist of the World Bank, offered Professor Islam the newly created job of Director of the Development Research Center of the World Bank. As he was preparing to accept the offer, perhaps also a recognition of his achievement, he was made the first person from the developing world to become a Director at the World Bank, Bangladesh became independent. Sheikh Mujibur Rahman asked him to head the newly independent country’s first planning commission. It was an offer that he could not refuse.

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Chapter 5 tells the story of his days at the Planning Commission. His earlier book provides details of the policy issues addressed by the Commission; in this book Professor Islam gives us a glimpse of the happenings behind the scenes. Particularly illuminating is his frank discussion of the tensions between the technocrats at the Commission and the bureaucrats in the government, who resented the unique power and status given to the former, unlike anything they were accustomed to in the Pakistan days. The politicians too, excepting the Prime Minister, also resented the power given to the technocrats. This narrative provides us with very useful insights into the outsider-insider game in governments.

At the end, the technocrats lost out. Perhaps Professor Islam and his team devoted much of their energy to the technical aspects of their work, hoping that the support of the top leader of the country, to whom they had unfettered access, and the integrity of their technical work would see them through. Perhaps they should have paid more attention to playing the bureaucratic and political machinery. Perhaps they forgot that those who strive to make a nation also need to play such games. Professor Islam may not have networked enough within the first Bangladesh government but he did utilize the very rich set of networks he enjoyed internationally. We get many glimpses of this, whether during his work to set up the Pakistan Institute of Development Economics, which quickly became one of the best think-tanks in the developing world in the sixties, or in his efforts to rally the support of influential US players during the independence war and global support for Bangladesh's reconstruciton and development after independence. A particularly insightful section of the book talks about his engagement in the early seventies, with Indian policy makers, many of whom were known to him from before. A reminder that those who make nations also make networks!

We end where we began – his childhood. In the first chapter, Professor Islam tells the poignant story of how a serious eye ailment handicapped him as he prepared for his high school exam – he was in pain, unable to read himself and needing to have books read out to him. His family and he were unsure he could sit for his exams.

The young Nurul Islam ended up topping this highly competitive, province-wide examination – an outcome that he believes, "could not but be an act of God’s infinite mercy in response to our fervent prayers". Those who make a nation are also men of faith!

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