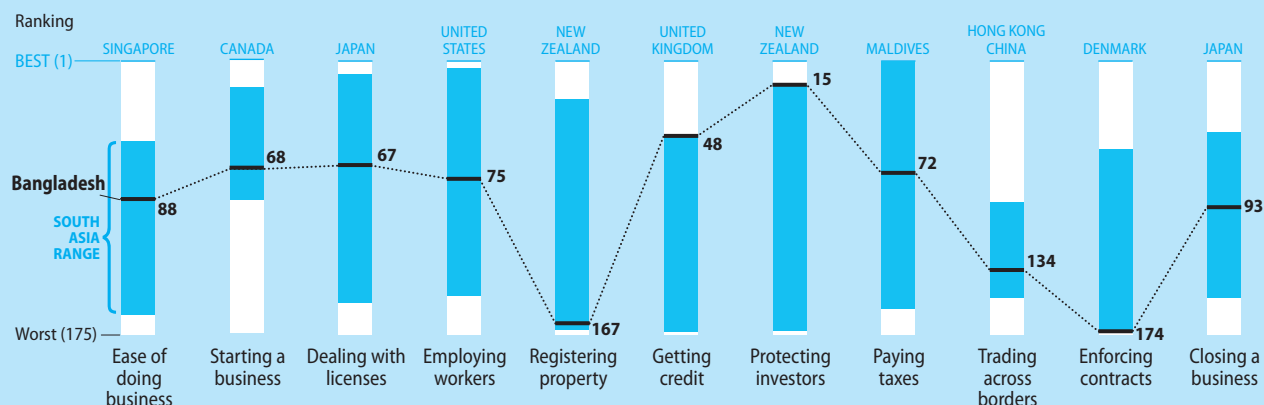


COUNTRY PROFILE

BANGLADESH Ranked 3rd in South Asia, following the Maldives and Pakistan.

Starting a business

Entrepreneurs in Bangladesh do not need to put up any minimum capital to start a business, but that is about all the relief they get. Bangladesh has a worldwide rank of 68 on the ease of starting a business. The process requires 8 procedures taking 37 days at a cost of 88% of income per capita—a decline from 94% in 2005. Within the region, only Bhutan and India make start-up more burdensome. The greatest obstacle is cost, which is higher in Bangladesh than in any other South Asian country. Only Nepal (where start-up costs 79% of income per capita), Afghanistan (67%) and India (74%) are in a comparable league. Elsewhere in the region it takes less than 22% of income per capita to start a business (table 2.2).

Within Bangladesh start-up takes 30 days in both Khulna and Bogra and 37 days in Dhaka and Chittagong. While all entrepreneurs have to complete all 8 procedures, the cost of starting a business in Bogra, Khulna and Chittagong (62% of income per capita in each case) is lower than in the capital city, Dhaka (88%).

TABLE 2.2

Starting a business in South Asia

| Country ranked by ease of starting a business | Procedures (number) | Time (days) | Cost (% of income per capita) | Min. capital (% of income per capita) |
|---|---------------------|-------------|-------------------------------|---------------------------------------|
| Afghanistan | 3 | 8 | 67 | 0 |
| Maldives | 5 | 13 | 18 | 7 |
| Sri Lanka | 8 | 50 | 9 | 0 |
| Nepal | 7 | 31 | 79 | 0 |
| Pakistan | 11 | 24 | 21 | 0 |
| Bangladesh | 8 | 37 | 88 | 0 |
| Bhutan | 10 | 62 | 17 | 0 |
| India | 11 | 35 | 74 | 0 |

Source: *Doing Business* database

What to reform

Company registration at the Registrar of Joint Stock Companies takes 2 weeks compared to 3 days in Pakistan. A project is underway to automate the Registrar of Joint Stock Companies and streamline the registration process. This is a good opportunity to reduce registration fees. By simplifying the registration process, administrative expenses can be cut. And lower registration fees will encourage more entrepreneurs to register their businesses formally. Costs can be reduced further by making the use of lawyers optional, as in Pakistan and Nepal. To ensure the legality of the documents, standardized documents can be introduced. This also makes the registrar's job easier and reduces the rejection rate of applications.

Further reforms can target delays. Registration with tax authorities requires 2 procedures, i.e. registering with the tax authority and registering for value added tax (VAT). These can be pursued simultaneously with the longer taking 9 days. In Sri Lanka, which requires only one tax registration procedure, the time is 2 days. Bangladesh can speed things in other areas as well. For example, although the database of company names was computerized in 2003, it still takes 5 days to verify the uniqueness of a name. In Pakistan, it takes only 24 hours.

TABLE 2.3

Subnational rankings on the ease of doing business in Bangladesh

- 1 Dhaka
- 2 Chittagong
- 3 Khulna
- 4 Bogra

Note: The rankings for all cities are benchmarked to April 2006 and reported in Appendix III. The ease of doing business averages rankings across the 10 topics covered in *Doing Business*. This excludes variables such as macroeconomic policy, quality of infrastructure, currency volatility, investor perceptions, or crime rates.

Source: *Doing Business* database.

Dealing with licenses

Registration is only the beginning. Businesses then need to obtain an array of permits and licenses to begin operating—a cumbersome process in Bangladesh. As an example it takes 13 procedures and 185 days to obtain the permits and licenses to build a warehouse. While the number of procedures is comparable to the OECD average (14 steps), and better than the regional average (16 steps), the time to complete the warehouse licensing process (185 days) is more than a month longer than the OECD average of 150 days. While the cost of licensing (272% of income per capita) is almost three times the per capita income, and much higher than the OECD average of 72%, it is lower than the regional average of 376%, which includes Pakistan's cost of 973% and 606% for India. The three most burdensome steps are obtaining project clearance from the Department of Environment (30 days, costing on average \$400), obtaining project clearance and the building permit from the City Development Authority (75 days, costing \$70) and obtaining a power connection (40 days, costing from \$100 to \$1,000 depending on the project size).

Obtaining a license in Chittagong and Bogra, especially in the pre-construction period, requires more procedures (in total 15 and 14 procedures, respectively) but less time (150 and 146 days, respectively) compared with Dhaka (13 procedures in 185 days). The cost of licensing in terms of percentage of income per capita is the highest in Dhaka (272%), more than twice as much as in Chittagong (128%), Khulna (104%) or Bogra (115%), mainly because of the cost of obtaining facilities from utilities authorities (about \$760) and a \$400 fee to obtain project clearance from the Environment Department in Dhaka.

What to reform

A recent World Bank Group Foreign Investment Advisory Service (FIAS) review of the environmental clearance process concluded that delays in the processing of environmental clearance certificates (ECCs) can be reduced by improving the capacity of inspectors and technical officers. The lack of trained staff, plus deficiencies in the legal framework and corrupt practices, also means that businesses often get clearance without putting in place an adequate environmental management system. Although all industries are required to have an ECC, a large majority is operating without such certificates. In brief, well-meaning businesses are harassed while the goal of environmental protection is often unrealized. A similar review should be conducted of the procedures at the City Development

Authority, the Rajdhani Unnayan Kartripakkha (RAJUK), and those for obtaining a power connection.

Other reforms are underway and require continued implementation. The Board of Investment recently introduced e-government processes that allow online tracking of various approval requests. This has resulted in some reduction in time needed to obtain approvals. The Bangladesh Export Processing Zones Authority (BEPZA) is introducing e-government in its work to facilitate online clearances and other investor services. These projects need to be sustained and replicated in other government agencies. Strict time limits in licensing combined with a silence-is-consent rule—where the authorization is automatically given after a specific period of time passes—can further reduce delays.

Employing workers

Bangladesh scores among the best in the region and ranks 75th worldwide on the ease of employing workers. There is no variation for all indicators of employing workers at the sub-national level because the same national employment regulations apply throughout the country. The cost of hiring is zero—there are no social security taxes or payroll taxes associated with hiring a new employee. By contrast, in India, Pakistan and Sri Lanka the cost of hiring ranges between 12 and 17% of salary. It is also relatively easy to fire a worker in Bangladesh. Employers are not required to obtain approval from a third party before dismissing one redundant worker or even for collective dismissal. There is no legal requirement to retrain or replace workers prior to dismissal. Only 1 month's notice is required and there is no legally mandated penalty for redundancy dismissal. Severance payments can be costly though, amounting to 47 weeks. The rigidity of hours worked is also quite low in Bangladesh. Until recently, trade union activity was not allowed within export processing zones. The government has recently enacted a law allowing limited trade union activities in the export processing zones.

What to reform

While by regional standards Bangladesh boasts fairly flexible employment laws and regulations, it could nevertheless work to increase flexibility. Bangladesh's total firing costs, at 51 weeks' wages, are high. Decreasing the cost of firing would make it easier for employers to hire workers when there is a rise demand, because employers would be less fearful of burdensome firing costs in the event of an economic downturn.

Bangladesh could also benefit from loosening its restrictions on weekend work. Under the Factories Act of 1965 if an employer wishes to have an employee work on a weekly holiday, the employer must, first, give notice to an inspector of this intention and, then, display a notice to the same effect in the workplace. This process can be simplified. The same goes for restrictions on redundancy. In Bangladesh an employer must send copies of redundancy notices to an inspection official. Streamlining the employment process makes it simpler for businesses to respond to shifts in the market, and reducing bureaucracy would lower their costs of operation.

In September 2006 the government passed a new labor law. The effects of this new law can be expected to be felt in the coming year.

Registering property

Bangladesh has a worldwide rank of 167 on the ease of registering property, among the worst global rankings by any South Asian country on any of the *Doing Business* indicators. It takes 8 procedures and 425 days to register property. By contrast in Nepal 3 procedures are required and in Pakistan and India, 6. Sri Lanka also has 8 procedures—but the process there takes only 63 days. The cost of registering property is also high in Bangladesh, at 10.5% of the property value compared to a regional average of 5%.

The longest delay is in registering the property at the municipal deed registry office, which takes between 180 and 540 days. The buyer may obtain a certified registration document within a week, but obtaining the original certificate may require about 6 months to 1½ years, or even up to 2 years in some cases. By contrast, in Sri Lanka it takes only 36 days to register at the land registry. In Pakistan, 38 days. In Nepal, it takes only 1 to 2 days for registration of the deed at the land revenue office and issuance of a new title certificate. Obtaining the permission from the municipality office, the RAJUK, to transfer property ownership, one of the early steps in the process, adds 60 days to the process in Bangladesh. Verification of the record of rights from the land revenue office adds another 15 to 60 days.

The ease of registering property varies by city. While there are seven common registration procedures throughout the country, for the land being developed by City Development Authority (for instance, RAJUK's development of model towns in Gulshan, Banani, Baridhara, Uttara and the Nikunja Residential Area) one additional step is required—obtaining permission from

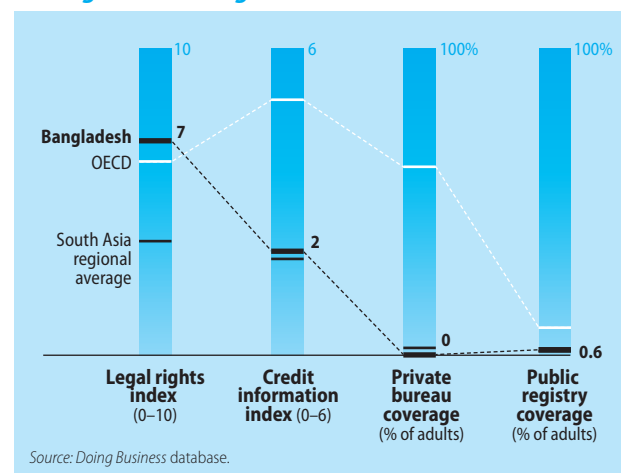
the City Development Authority to transfer ownership of the property—which makes the registration process in Dhaka lengthier and costlier than in the rest of the country. In the case of Bogra and Chittagong it takes 391 days and costs 10% of property value and in Khulna it takes 373 days and costs 9% of property value, compared to Dhaka (425 days and 10.5% of property value).

What to reform

Reforms to make property registration easier have started. A Land Registration Act came into force on July 1, 2005. It will help reduce false and multiple registrations of land. Registration fees were also cut by 1%, although they remain high overall at 10.5%. A pilot project to computerize land records has been completed in the Demra thana of the Dhaka district. Title deed requirements are being simplified—with the title, the location of the land and the map on a single page and all other documents in a backup database. The government is moving ahead in replicating the pilot model in phases in other thanas (Upa-Zillas) of the country under a public-private partnership.

Simple reforms can also have a big impact. Bangladesh can encourage formal property transactions by further reducing the registration fees and stamp duties, which cost 3% and 5%, respectively, of the property value. By contrast, in Pakistan the stamp duty is 3% and registration fee is 1% of the property value. In Sri Lanka, there is no separate registration fee; it is subsumed within a stamp duty set at 4% of the property value. In India, while the stamp duty is 5% of property value, the registration fee is only 1%. Typically reductions in fees lead to more revenues, as more properties are registered and with less underreporting of property values.

FIGURE 2.2
Getting credit in Bangladesh



Getting credit

Bangladesh ranks 48th worldwide and ahead of the South Asian average on the ease of getting credit. There is no regional variation within Bangladesh. Although no private credit bureau operates, a public credit registry functions reasonably well. Bangladesh scores 2 out of 6 on the credit information index—at the same level as Nepal but behind Pakistan, India and Sri Lanka. With a score of 7 out of 10, Bangladesh is the top performer in the region on the index of legal rights for borrowers and lenders, higher than the OECD average of 6 (figure 2.2). This high score is in large part a result of the Money Loan Court Act of 2003. The reform significantly sped foreclosure on collateral by introducing summary proceedings and allowing credit institutions to sell collateral by public auction after giving due notice to the defaulting debtors.

Further improvements are needed. It is estimated that 6 million households in the middle category (small businesses, and small and marginal farmers), are too poor for the formal banking sector and too rich for the traditional microfinance sector. Only 7% of one million potentially eligible small businesses are currently served by the banking sector. Private commercial banks cannot profitably serve this missing middle segment because they do not have the appropriate products and processes to reach it. For example, a typical application for a small business loan requires up to 29 steps, 9 meetings with the client and over 50 different documents totaling 200 pages. Such cumbersome procedures make it very expensive for banks to lend money to small businesses. At the same time margins in the private banking sector are still sufficiently high that banks neither have to look for new markets nor invest in developing new products and technologies.

What to reform

Bangladesh can expand access to credit by further improving the ease of taking and enforcing collateral. Reforms to the existing secured transactions laws can expand the pool of assets that can be used as collateral to enable every physical and juridical entity to securely pledge all types of assets. Moreover, enforcement of collateral requires further streamlining. The Money Loan Court Act's reform to allow creditors to sell collateral without a trial is a great step forward. But the major bottleneck lies in cumbersome procedures for selling collateral through public auctions. Allowing for private, licensed enforcement and auction agents would significantly speed recovery of collateral.

Lenders are also more likely to extend credit when they can accurately assess borrower risk. The government can encourage more effective sharing of credit information by: supporting the computerization of the credit registry; making available at least 2 years of historical data; expanding the registry's coverage to include information on loans under \$800; and extending the credit registry to cover information from microfinance institutions and non-financial institutions, such as utilities, retailers and trade creditors. Finally, Bangladesh can change its laws to allow private institutions to provide credit information services. While it is unlikely that such an industry would immediately flourish, private credit bureaus are generally more effective at serving lenders than public registries. Allowing them to form in Bangladesh can be an important element in the move from a relationship-based economy to a relationship-neutral economy.

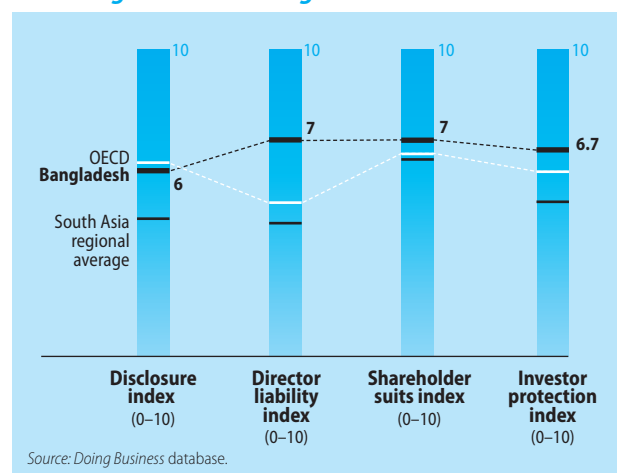
In the short to medium term, access to finance for small businesses can be expanded, and technical assistance to financial institutions can help them develop credit products for small businesses. Bank portfolios should be expanded outside the largest two metropolitan centers, which currently account for the vast majority of financial intermediation.

Protecting investors

Bangladesh has a global rank of 15 on the protecting investors indicator—the top performer in the South Asia region. As the indicator examines areas governed by national legislation in Bangladesh, there are no differences at the sub-national level. Bangladesh performs particularly well in the director liability index and shareholder

FIGURE 2.3

Protecting investors in Bangladesh



suits index, which measure the ease with which an investor can take directors and controlling shareholders to court—and win—for violations of their duties to the company. Bangladesh also scores well in the disclosure index and the investor protection index. On all four indices, Bangladesh scores above the regional average and higher even than the OECD average, except on the disclosure index (figure 2.3). There were no revisions to the investor protection regulations between 2005 and 2006.

What to reform

Investors in Bangladesh may be able to sue directors quite easily, but they are unlikely to learn of the mismanagement in the first place. Disclosure requirements surrounding large, related-party transactions are weak. Bangladesh can improve transparency by requiring immediate public disclosure of large transactions involving company insiders. It could also mandate external review of such transactions—either by an independent auditor or the stock exchange—shining more light on transactions involving conflicts of interest.

Paying taxes

Bangladesh ranks 72nd worldwide on the paying taxes indicator. A typical business makes only 17 tax payments per year, compared with 61 in Sri Lanka, 59 in India and 47 in Pakistan. However, the time needed to comply with tax rules is very high, at 400 hours, compared with 264 in India and 274 in Bhutan. At 40.3% of commercial profits, the total tax burden is still relatively high although below the regional average of 45.1% and OECD average of 47.8%. In Nepal, for example, the total tax burden is only 32.8% of commercial profits.

What to reform

Bangladesh needs to accelerate the implementation of reforms to simplify tax compliance. The National Board of Revenue has launched a medium-term strategy to improve tax administration. In November 2003, the Large Taxpayer Unit (LTU) for income tax was restructured (taxpayer services, revenue collection, accounting, audit, and enforcement). It was also given the responsibility for collecting withholding taxes. Steps were taken to strengthen filing and payment procedures, improve detection of stop-filers, increase capacity for audits and introduce computerization of certain LTU operations. And an LTU for VAT was set up in October 2004.

The government can also encourage compliance by reducing tax rates to more moderate levels. Corporate in-

come tax in Bangladesh accounts for the bulk of total tax revenues, and at 37.5% is the highest in the region. Such high rates encourage tax evasion. Revenues can be maintained or even increased if the tax rate is decreased along with broadening the tax base. A pre-announced program of reductions in customs duties and, especially, para-tariffs to bring Bangladesh in line with the developing country average within 5 years would give industry a clear signal and allow companies to plan their investments.

Trading across borders

Bangladesh ranks 134th on the ease of trading across borders, well below the regional average. It takes 16 documents and 57 days to import, the second longest time among the South Asian countries after Afghanistan with 88 days. Exporters are relatively better off, requiring 7 documents and 35 days, comparable to Nepal (44 days) and Bhutan (39 days). The key export sector—garments, which account for nearly three-fourths of exports—can clear exports much faster. Even imports meant for the garments sectors clear much faster than average. In Bangladesh the total cost to import totals \$1,287 per container, cheaper than Afghanistan (\$2,100), Nepal (\$1,800) and Bhutan (\$1,950), but more expensive than Sri Lanka (\$789) and Pakistan (\$1,005), and comparable to India (\$1,244). The cheapest port at which to import is Dhaka, at \$829 per container, while the most expensive is Bogra (\$979). It is cheapest to export from Chittagong (\$553) due to its proximity to a seaport, and the costliest to export from Dhaka (\$607).

What to reform

The government has recently taken a number of initiatives to improve the environment for trading across borders. Customs procedures were streamlined by introducing the ASYCUDA++ system, which involves electronic processing and tracking of files. A one-stop service was introduced at the Chittagong port to facilitate port- and customs-related paperwork. However, the infrastructure of both sea and land ports requires improvement. Further investment in port equipment and streamlining of processes is needed, in particular on the import side. Trading across borders could be made easier by first reducing documentary requirements. For instance the requirement for import licenses and consular certification of documents originating from abroad could be abolished. Bangladesh could also reduce many of the fees related to imports.

Enforcing contracts

Enforcing a contract in Bangladesh is the most cumbersome of all countries in the region. It requires 50 procedures and about 4 years (1,442 days) to enforce a contract, compared to 20 procedures and 837 days in Sri Lanka (figure 2.4). Costs amount to 46% of the claim, compared to 21% in Sri Lanka.

Though there is little difference among the various cities of Bangladesh in terms of the procedures for enforcing contracts, Dhaka is the most expensive (46% of claim) due to the high attorney fees and takes the second longest time (1,442 days). It is comparatively less expensive in Bogra and Khulna (about 40% of claim) due to lower attorney fees, but takes the longest in Bogra (1,790 days), due to a 4-month delay in filing the lawsuit, as opposed to only a week in Dhaka.

The government introduced major reforms in the Civil Procedure Code in 2003. Delays are showing signs of improvement, but the reforms have yet to give the desired results. Two recent reforms have improved the judicial system. The Money Loan Court Act of 2003 set up a special court to deal exclusively with loan defaults exceeding 5 lakhs, prescribed time limits for granting judgments and imposed restrictions on appeals.

What to reform

Bangladeshi entrepreneurs will benefit from further implementation and extension of the current reforms. Case management pilot programs in 5 districts have given judges a more active role in determining the pace of cases. The project cuts short the serving of notice,

implements a courier service, imposes time limits and creates a central filing system. These pilot programs should be extended to other courts. Enforcing contracts can be sped further by computerizing and linking the courts' databases. The current system of double filing cases at the central register and at the court of original jurisdiction is inefficient. Developing specialization in commercial disputes by training judges is also important for unlogging the courts.

Closing a business

Bangladesh is in 3rd place among its South Asian counterparts when it comes to the ease of closing a business—after Pakistan and Sri Lanka—and 93rd place worldwide. It takes 4 years to go through bankruptcy proceedings, significantly lower than the 10 years it takes in India. But that is little comfort as global best practice is 0.4 years (Ireland) and regional best practice is 2 years (Sri Lanka). The cost of insolvency is 8% of the estate value and the recovery rate for claimants is 25%.

While in Dhaka it takes 4 years to go through bankruptcy proceedings with a cost of 8% of the estate value, there have been less than 60 bankruptcy cases in Chittagong, Khulna and Bogra in the last 20 years. Therefore these cities score “no practice” on the *Doing Business* closing a business indicator.

What to reform

Efficient bankruptcy procedures increase the amount that creditors recover from insolvent firms. They cause credit markets to expand and investments to rise. Bangladesh can best improve insolvency proceedings by focusing on efficient foreclosure and liquidation proceedings. Bankruptcy should allow for a fast process whereby creditors can decide on the highest value procedure. The process should also give qualified insolvency managers incentives to follow quickly the most efficient procedure. Regardless of whether a firm enters foreclosure, liquidation or reorganization, the administrator should be able to sell the business as a going concern so that the new owners keep the intrinsic value of the operating business and not just the assets. Bangladesh can also improve the efficiency of bankruptcy by eliminating criminal liability for managers who allow a company to become insolvent. Such managers are forbidden from entering into a corporate position for almost 7 years. This discourages entrepreneurship. It also dissuades companies from starting bankruptcy proceedings early enough to save the company.

FIGURE 2.4

Lengthy delays in enforcing contracts

