How flexible are the financial services to the export sector in Bangladesh

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Abstract

The paper makes an attempt to critically analyze the different financial problems encountered by exporters in Bangladesh, particularly in the context of post-MFA phase-out of Apparel export, which accounts for three-quarters of Bangladesh's total exports of Bangladesh. The paper also highlights practical solutions to those problems to improve the quality of services provided by banks and other financial institutions. The paper further analyzes the operational problems of banks and other financial institutions that have a direct negative impact on the export sector, in particular on SMEs. Possible solutions to those constraints are also recommended. Primary data have been collected from a survey of 37 exporters, 12 banks and 5 non-bank financial institutions (NBFIs). The data have also been collected from a number of secondary sources. Officials of various regulatory authorities have been interviewed to identify the initiatives undertaken by them to address the financial problems of exporters.

1. Background

During the 1980s and 1990s, policy focus in Bangladesh shifted to trade as the engine of growth and the key to development. This was in the backdrop of significant increase in the national income of many developing countries through export led growth. The Government of Bangladesh also initiated several policy

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measures at the macroeconomic as well as the microeconomic level to boost foreign currency earnings through a diversified portfolio of exports. These policy initiatives however, required massive changes in the mindset of individuals and institutions for effecting a transition from a control mode to a liberalized mode. The completion of the Uruguay Round and the establishment of the WTO facilitated the transition. It also brought to the fore core issues affecting performance. Bangladesh was faced as much with the problem of market access as with the need for diversification of its export basket. The response essentially rested on trade facilitation. Banking and financial services for the export sector was central to this facilitation – for addressing issues of efficiency as well as expansion and diversification of export. Hence, the priority focuses on the efficiency and effectiveness of banking and financial services for exporters.

This has become all the more imperative in the changed context of the Multi-Fiber Agreement (MFA) phase out at the end of 2004. In the post-MFA phase, the most important export sub-sector (RMG) contributing three-quarters of the total export earnings will probably be badly affected. The Government of Bangladesh played an instrumental role in facilitating the phenomenal growth of RMG sector by providing various incentives. It now will have to play similar positive role in facing the post- MFA challenge. It particularly has to focus sharply on both infrastructure development to reduce lead time and as well as reduction of cost of doing business so that exporting firms remains competitive vis-à-vis well organized Chinese or Indian exporters.

However, It has been observed in a study (International Business & Technical Consultants, Inc, Bangladesh Export Diversification Project - BDXDPD, 2003) that inadequate access to bank finance by exporters, high cost of financing and lengthy procedures are the major constraints to the expansion of the export sector. At least 90% of the exporters faced the problem according to this study. In addition, the study indicated that sectors like shrimp, agriculture and light engineering considered inadequate financing as a major constraint to their expansion. A number of initiatives were under taken in the meantime to enhance the efficiency of the banking system to cater to the demands of exporters. There has been, however, no in-depth analysis of the impact of these initiatives on the export sector in general or on service delivery on the part of banks and financial institutions. In this backdrop the paper makes an attempt to examine the operational problems of banks and other financial institutions that have a direct negative impact on the export sector.

2. Objectives of the paper

The objectives of the paper are

- to analyze the current financial environment under which the exporters operate and to identify critical financial factors impeding the desired growth of the export sector.
- to evaluate the current practices followed by different financial institutions (Fls) in financing the exporters and to identify critical procedural and legal obstacles that restrict and/or discourage the Fls from providing all the necessary financial support and services to the exporters.
- to identify other sources of finance for the export sector and assess the current practices and importance of the informal sector in providing financial support to the export sector.
- to make specific recommendations of feasible measures to remove the constraints and to identify critical success factors for the development of an effective banking and financial system for the export sector.

3. Methodology

Primary data have been collected from a survey of 37 exporters, 12 banks and 5 non-bank financial institutions (NBFIs) through both open-ended questionnaires and informal interviews. The data have also been collected from a number of secondary sources. Officials of various regulatory authorities have been interviewed to identify the initiatives undertaken by them to address the financial problems of exporters. A detailed survey was also conducted for identifying other sources of finance and financial services available to the exporters. Interviews have been conducted with the management of Dhaka and Chittagong Stock Exchanges for evaluating their responsiveness to the financial needs of the exporters and their liquidity position. Various government bodies have also been interviewed for identifying the critical issues surrounding informal money markets, such as overseas facilities, counter trade, Non-Resident Bangladeshis (NRBs), private funding from established Bangladeshi and foreign companies, ‘sleeping’ equity partners, etc. Policies of Government on Foreign Direct Investments (FDIs) and their cost and effectiveness have also been analyzed.

4. Banking and Financial Services: an overview

4.1 Financial support and services required by exporters

The most important aspect of export is the financial involvement of the exporters and the role of institutional finance. Ordinarily, exporters require a wide range of banking/credit facilities at the pre-shipment and post-shipment stages. Besides, they operate in the highly competitive area of international commerce, and as such, these facilities need to be made available at competitive rates. Exporters require finance for the procurement and/or manufacture of goods for export. Where goods are shipped on credit terms, they look towards the banks/financial institutions for finance against export bills/deferred terms of payment. Finance apart, the exporters need banking services to collect export bills, convert export bills into local currency and eliminate exchange risk. The exporters also need other ancillary services to meet the terms of many commercial contracts and collect information about financial standing and business integrity of foreign buyers, foreign markets etc. Availability of these services to the exporters at the right time, in adequate volume and on reasonable terms, therefore, is essential for developing and expanding exports.

4.2 Current financial environment under which the exporters operate

The exporters in Bangladesh meet their financial requirement mainly from institutional sources. The commercial banks are the single important source of their institutional finance. In their export financing operations, the commercial banks (CBs) are assisted by the Bangladesh Bank (the central bank), the Sadharan Bima Corporation (SBC) and other non-bank financial institutions (NBFIs). The Bangladesh Bank (BB) provides refinance at concesssional rate of interest and operates various export promotional schemes of the government. The Sadharan Bima Corporation, through its Export Credit Guarantee Department (ECGD) issues insurance policies to cover risks involved in export and provides guarantee facilities to enable the commercial banks to allow finance flexibly to the exporting community. The non-bank financial institutions (NBFIs) extend term loans and do not provide any working capital facility. The NBFIs are of course, not substitutes for banks and are not in a position to provide banking and other ancillary services needed by the exporters. Efficient and effective banking and financial services therefore, play a vital role in promoting foreign trade, particularly in giving a push to exports.

Of these commercial banks that are Authorized Dealers (ADs) in foreign exchange are the actual bankers to the exporting community in Bangladesh .The total number of authorized dealers catering to the exporters' need is as under:

Table 1 shows that the sources of bank finance and services for the exporters are centralized in Dhaka and Chittagong.

Bangladesh Bank is the central bank of the country. It is the Regulatory Body of all banks and financial institutions. It controls the foreign exchange transactions and co-ordinates the import/export activity of the country. The major roles that Bangladesh Bank plays in financing export are provided in the box below.

Table 1: City wise numbers of Authorized Dealers

Dhaka	Chittagong	Khulna	Rajshahi	Sylhet	Barishal	Others	Total
354	139	51	32	32	7	32	647
55%	21%	8%	5%	5%	1%	5%	100%

Source: Bangladesh Bank

4.3 Financial support and services provided by the banks

A summary of the various banking and financial services provided to the exporters is given below:

4.3.1 Providing settlement mechanism

The commercial banks in Bangladesh (particularly the Nationalized Commercial Banks (NCBs) and Foreign Commercial Banks (FCBs) equipped, as they are, with a large net-work of branches/correspondent banks abroad are placed in an ideal position to assist both established exporters and the new exporters. The Private Commercial Bank (PCBs), with less international exposure, are not in an ideal position to provide settlement mechanism.

4.3.2 Providing export finance

Export finance refers to the credit extended to the exporters for financing their transactions. It includes finance for assembling of raw materials and manufacturing into goods for export and the finance for the deferred payment to exporter. Short-term credit provided by the banks is of two types: 'pre-shipment finance' commonly known as 'packing credit' and 'post-shipment finance'.[1]

1 Packing credit refers to any loan to an exporter for financing the purchase, processing, manufacturing or packing of goods meant for export orders. Post-shipment credit means any loan or advance granted or any credit provided by an institution to an exporter of goods from Bangladesh from the date of extending the credit after shipment of the goods to the date of realization of the export proceeds, and includes any loan or advance granted to an exporter, in consideration of, or on the security of, any drawback or any cash payment by way of incentive.

Box 1 Bangladesh Bank's role in exports financing

- Issuance of AD license: Bangladesh Bank (BB) has issued Authorized Dealer (AD) license in favour of 647 branches of CBs all over the country. Among them 354 (55%) ADs are in Dhaka City. 139 (21%) ADs are in Chittagong city and the remaining ones are located in other major business centers of the country.
- Refinancing for the commercial banks against export finance.
- Implementation and maintenance of Cash Subsidy (CS) accounts declared by Government of Bangladesh (GOB). [GOB allocates CS from its annual budget, which the Bangladesh Bank disburses through the commercial banks. Two departments of BB are involved in handling of CS. Banking Regulation and Policy Department (BRPD) announces the policy and issues circular and the Currency Management Department makes the disbursement. During the year 2003, BB disbursed Tk. 823 billion against CS among the exporters.]
- Implementation of the schemes initiated by GOB for expediting the country's export business. [BB announces policies related to the admissible uses of exporters retention quota and international credit cards. BB controls and monitors the implementation of schemes and maintains the statistical data of the schemes.]
- Bangladesh Bank closely monitors interest rate on export finance charged by commercial banks.

4.3.3 Existing Financial Schemes, Facilities, Subsidies offered to the Exporters

The existing packages of schemes and facilities subsidies offered to exporters are shown in the following figure. Details are at annex.

Figure 1
Government Schemes and Facilities

SCHEMES

1. Foreign Exchange Retention quota for exporters.
2. International Credit Card issued against retention quota for exporters.
2. Credit Guarantee Insurance Scheme.

FACILITIES/SUBSIDIES

1. Duty Draw Back
2. Cash Subsidy
3. Bonded Warehouse
4. Export Development Fund
5. Equity Entrepreneurship Fund
6. Income Tax Rebate
7. Freight Rebate
8. Export Promotion Bureau's (EPB) Export Promotion Fund

Table 2 : Financial support and services provided by banks

Sl #	Banking services	Nature of services.
1	Payment settlement mechanism	• Banks collect/negotiate the documentary and other bills drawn upon the overseas buyers. • Banks also buy the proceeds of the foreign currency bills, on spot or forward basis, as the case may be, in order to eliminate the exchange risk.
2	Export Finance	• Pre-shipment credit. • Post-shipment credit. • Financing of export under deferred payment terms. • Finance against collection of export bills. • Finance against export incentives.
3	Other services	• In order to meet the terms of many commercial contracts, exporters need tender guarantees when tenders are submitted, followed by performance guarantees for the successful tender(s). • Information about financial standing and business integrity of foreign buyers, foreign markets etc.

4.3.3.1 Foreign Exchange Retention Quota for Exporters

Under this scheme merchandise exporters are entitled to maintain a certain percentage of foreign exchange in their F/C accounts out of the repatriated fob value of their export. The following table shows the admissible quota and recent initiative taken by the government:

4.3.3.2 International Credit Card against Retention Quota

International Credit Cards may be issued against retention quota in favor of up to 3 top-level executives of an exporting firm/organization holding retention quota Foreign Currency Account (FCA). The international credit card is useable for business travel only.[2]

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[2] At present the following banks are issuing International Credit Cards:

1. Standard Chartered Bank
2. American Express Bank
3. National Bank Ltd
4. Prime Bank Ltd.

The following banks have applied for permission to issue international credit cards:

1. Premier Bank Ltd.
2. Eastern Bank Ltd.
3. National credit and Commerce bank Ltd.

(Source: Bangladesh Bank)

4.3.3.3 Export Credit Guarantee Insurance in Bangladesh

Sadharan Bima Corporation administers the scheme to deal with credit risk associated with export trade. Under this, Export Finance (Pre-Shipment) Guarantee provides guarantee to the financing banks or financial institutions to the extent of 75% of the total amount of loss suffered due to insolvency of the exporter or non-payment of the loan by the exporter after four months from the due date of payment. The Export Finance (Post-Shipment) Guarantee is provided to banks or financial institutions to the extent of 75% of the total amount of loss suffered due insolvency of the exporter or non-payment of the loan by the exporter after four months from the due date of payment.

The guarantees are issued for a period of one year and are renewable on request of the lending banks and financial institutions. The premium is 0.05% per month on the highest amount outstanding at any time in each calendar month.

A Comprehensive Guarantee provides protection to exporters against overseas commercial as well as political risks.

It covers 85% of loss caused by commercial risks and 95% of loss caused for political risks and is issued for one year and renewable at the option of the insured. The premium rate varies from 0.125% to 0.65% for exports made against Letter of Credit (LC) and 0.40% to 2.00% for transactions under contracts.

Table 3 : Foreign Exchange Retention Quota for Exporters

Si No.	Exporters by Sector	Admissible Quota In % of net repatriated Free on Board (FOB) value	
		As on 18-1-03	Recent initiative
01.	Merchandise Exporters	40%	Increased to 50% from 19-01-03
02.	Low domestic value added products like POL products including Naphtha, Furnace oil, Bitumen, Readymade Garments of imported fabrics, Electronics goods	7.5%	Increased to 10% from 19-01-03
03.	Computer Software and Data Entry/Processing Service Export	40%	Increased to 50% from 19-01-03
04.	Service Exporters	5% of their repatriated income	a) Business travel abroad. b) Deposit in renewable time deposits account.

4.3.3.4 Duty Draw Back[3]

An exporter of manufactured products is entitled to draw back the value of the customs duties, sales tax, etc. already paid on the importation of raw materials used in the production or manufacture of the export products.[4]

Currently, there are three methods of duty drawback, viz.:

- Duty draw back on actual export
- Notional payment of duty.
- Duty draw back at flat rate for realizing draw back.

4.3.3.5 Cash Subsidy

The following table summarizes the product/sector wise entitlement of cash subsidy (CS).

There are many cases of malpractice in cash subsidy. There have been extensive abuse of the facilities by certain groups of exporters who have taken away several billion Taka mostly against advance payment of T.T. Consequently, the government has discontinued cash subsidy against T.T.

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3 Procedure for claiming duty drawback:
For the purpose of claiming duty drawback, the exporter is required to file a drawback-shipping bill in the prescribed Format as required alongwith necessary declaration. Supporting documents required for processing the claim:

a. Triplicate of the shipping bill
b. Copy of the Bank Certified Invoices
c. Copy of Bill of Lading/Airway Bill
d. Freight and Insurance Certificate
e. Copy of the contract or L/C
f. Worksheet showing the drawback amount claimed
g. Transshipment certificate where applicable
h. Blank acknowledgement card in duplicate

4 Duty drawback disbursed during the last three years

Taka in million

Sl No.	Particulars	1999-2000		2000-2001		2001-2002		2002-2003		Remarks
		Budget	Dis.	Budget	Dis.	Budget	Dis.	Budget	Dis.	
01	Duty draw back		160.00 **98.41	*62.10	146.43 **88.38	*59.21	172.02 **32.42	*96.05	199.00 **498.34	*547.10

(Source: Statement collected from Bangladesh Bank)
*Given by Bangladesh Bank, ** Given by DEDO

Table 4: Product / Sector wise entitlement of Cash subsidy (CS)

Sl No.	Product/ Sector	Cash Subsidy admissible in % of net repatriated fob value	Procedure/terms and conditions
01.	Agriculture, Agro Product	a) (Vegetable, Fruits /Agro processing) 25% for export local Agro Product (vegetable) and Agro Processing industries b) 25% for export of fresh fruits[5]	a) CS is released after repatriation of export proceeds in foreign currency. ADs must submit the CS application of exporters to Bangladesh Bank within 180 days after credit of export proceeds to their Nostro Account abroad. b) Export proceeds realized through banking channel against documents drawn under L/C is considered for CS. c) Recently Bangladesh bank has amended the condition and allowed export proceeds realized in banking channel through documents drawn against export contract to be considered for cash incentives[6]
02.	Frozen Shrimp and other Fishes Export	c) 10% for export of 100% local product[7]	1. CS is released after repatriation of export proceeds in foreign currency. ADs must submit the CS application of exporters to Bangladesh Bank within 180 days after credit the export proceeds to their concerned Nostro Account abroad. 2. Export proceeds realized in banking channel through documents drawn after export against L/C opened through banks is considered for CS.
03.	Local Textile Product	d) 15% up to June 2003 e) 10% for fiscal year 2003-04 f) 05% for fiscal year 2004-05 g) No cash subsidy after June 2005[8]	h) CS is considered for repatriated export proceeds against documents drawn under L/C. Cash incentive is also considered against documentary collection through banks after export h) CS is payable through banking instrument and priority is given to ensure adjustments of installment of Term Loan & working capital finance,
04.	Jute & Jute Goods	5% for shipment upto June 2003[9]	Jute mills after shipment submit the application for CS with relevant documents to negotiating AD. ADs release the cash subsidy determining the net fob value after repatriation of export proceeds.

5 BB FE circular No. 12 date: 2-11-2002.

6 BB Circular Letter No: FEPD(com) 291/ krishi pannya/niti/ 2003 –401 date: 15-04-2003

7 BB FE circular No. 23 date: 12-12-2002.

8 BB FE circular No. 10 date: 05-06-2002.

9 BB FE circular No. 19 date: 12-08-2002.

05.	Light Engineering By-cycle	15% for export with minimum 40% value addition. Admissible for shipment upto June 2005[10]	CS is released after repatriation of export proceeds in foreign currency. ADs must submit the cash subsidy application of the exporters to Bangladesh Bank within 180 days after credit the export proceeds to their concerned Nostro Account abroad. ii. CS is admissible only against the export against L/C.
06.	Bone crust	15% for local product[11]	CS is released after repatriation of export proceeds in foreign currency. ADs must submit cash subsidy application of the exporters to Bangladesh Bank within 180 days after credit the export proceeds to their concerned Nostro Account abroad. ii. CS is admissible only against the export against L/C.
07.	Hogla, Straw, Wastage of Sugarcane	a) 15% for use of local product more than 80% b) 10% for use of local product of more than 50%[12]	CS is released after repatriation of export proceeds in foreign currency. ADs must submit CS application of exporters to Bangladesh Bank within 180 days after credit of export proceeds to their concerned Nostro Account abroad. ii. CS is admissible only against export against L/C.
08.	a) Leather goods	15% for use of local product This will be admissible upto June 30, 2005[13].	CS is released after repatriation of export proceeds in FC. ADs must submit the cash subsidy application of the exporters to Bangladesh Bank within 180 days after credit of the export proceeds to their concerned Nostro Account abroad. CS is admissible only against the export against L/C.

4.3.3.6 Bonded warehouse

a. Bonded warehouse has generated special enthusiasm among the import-led export oriented industries. Bonded warehouse provides storage facilities for imported goods under the control of the Customs. Since bonded goods are not released for consumption, duty is not collected immediately on such goods.

b. Bonded warehouse warrants are transferable. They are however, not negotiable. This means that while the holder can transfer the title of

10 BB FE circular No.27 date: 12-12-2002.

11 BB FE circular No. 12 date: 12-12-2003.

12 BB FE circular No. 26 date: 12-12-2002.

13 BB FE circular No. 15 dates: 18-07-2002.

these goods to the transferee, the transferee takes this subject to all the defects and liabilities attached to the original holder. In foreign countries, certificate of licensed warehouse are fully accepted as security against advances.

c. Bond License remains valid for one year from the date of issue and the license is renewable subject to satisfactory performance. The bondholder applies to the Dept. of Customs in printed form 2 months before the expiry date with necessary papers.

For change of lien bank, the license holder is required to apply to the Dept. of Customs with import/export performance with the existing lien bank.

4.3.3.7 Export Development Fund[14]

The Export Development Fund (EDF) has been created for sustaining export drive and the long-term development of non- traditional export by

(a) assuring continued availability of foreign exchange to meet the import requirements of non- traditional exporters, particularly newer exporters;

(b) encouraging foreign suppliers, overseas confirming houses, and foreign commercial banks to provide short – term credit lines to Bangladeshi exporters; and

(c) complementing other export development policies, such as improved access to duty-free imported inputs and to promote non-traditional exports, diversify exports, and encourage higher value added exports.

(d) ensuring availability of foreign exchange to exporters to finance their imported inputs requirements. This is expected to act as a stimulus to private sector export production and marketing effort, and to encourage investments in market development as well as plant and equipment necessary to expand export capacity.

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14 Export Development Fund (EDF) has been created jointly by the International Development Agency (IDA) and the Government of Bangladesh (GOB) for financing imports of raw materials and spare parts of export oriented manufacturers in order to diversify export and to promote and encourage non-traditional and higher value added export. The fund is utilized by the commercial banks for financing exporters to the maximum of 70% of the export L/C at an interest rate of 1% above London Inter bank Offer Rate (LIBOR). The fund is owned by GOB and managed by Bangladesh Bank. Bangladesh Bank provides a spread of 3.5% to the financing commercial banks on their advances to the new non- traditional exporters and a spread of 2.5% on all other advances rediscounted with EDF.

The object of providing this fund is to gradually eliminate structural and regulatory constraints to financing of imported inputs required for export manufacturing, so that the need for a separate EDF will be eliminated in due course.

Participating Financial Institutions

All scheduled commercial banks may allow lending to eligible non-traditional exporters and avail of the facilities of the EDF. The financing banks will utilize their foreign exchange positions and obtain refinance from Bangladesh Bank on first come first served basis. They will disburse directly to foreign or domestic suppliers to enable the eligible exporters to use EDF. The commercial banks will assign the export proceeds to EDF after using the fund.

Eligibility

Direct and indirect non-traditional exporters (firms, individuals or partnership) exporting goods other jute and jute goods (excluding jute carpets) and tea, (excluding consumer packaged tea and tea bags) and high domestic content (with 30% value addition or more) ready-made garment exporters are eligible for EDF to the maximum extent of 70% of the value of export L/C[15]

4.3.3.8 Equity Entrepreneurship Fund (EEF)

Bangladesh bank has introduced EEF[16] in order to support fledging and risky new projects; especially software and food/agro based processing industry. EEF fund has so far sanctioned Tk.840 million[17] in the two sectors and Bangladesh Bank has earmarked Tk.3 billion for the fiscal year 2002-2003[18] Main features of Equity Entrepreneurship Fund are as follows:

1. EEF provides finance to the software and food processing and agro-based industries.
2. Fund is available up to 49% of the combined capital of the project, which shall not exceed 33.33 percent of the total project cost. If the project is not

[15] Loan disbursed under EDF in the last three years is give below:

Year	Amount in million US$	Amount in million Taka	Increase/decrease
1999-2000	105.15	6098.70	
2000-2001	137.75	7989.50	31%
2001-2002	136.54	7919.32	(0.9%)

leveraged, the contribution of EEF may go up to 49 percentage of the total cost.

3. The total cost of the project shall be minimum of Tk. 10 million (inclusive of net working capital).
4. The finance may be disbursed through all the scheduled banks and the Industrial Promotion and Development Company Limited (IPDC).

Export promotion fund of EPB

Export Promotion Bureau of Bangladesh (EPB) and Janata Bank signed an Memorandum of Understanding (MOU) to extend financial support to Information and Communication Technology (ICT) and handicraft exporters. Initially EPB placed a fund for Tk. 50 million for this purpose, which increased to about Tk. 80 million. Janata Bank realises service charge @ 2.5% for itself and interest of 4.50% for EPB of loan amount[19]:

4.4 NBFIs in export financing[20]

There are 19 non-bank financial institutions in operation in Bangladesh. Among them five have been interviewed during field survey. The financing products of the NBFIs are:

a. Loan
b. Lease.

16 BB EEF Circular No. 06

17 Byron, Rejaul karim, and Zahidul Haq (2003: 33:4) The Daily Star: Entrepreneurship fund finds way in 12 schemes, June 29,2003

18 http://www.Bangladesh-bank .organisation/about/dept/eefu/eefu.html

19 Number of projects and amount financed under EPB

Agro-processing companies		Software companies	
No	Amount Sanctioned	No	Amount Sanctioned
27	Tk. 1555.3 million	6	Tk. 93.91 million

20 Non-banking financial institutions (NBFI) are those institutions which (i) give loans or advances for industry, commerce, agriculture or housing or (ii) carry on business of the underwriting or acquisition of, or investment or re-investment in, shares, stock, bonds, debentures or debenture stock or securities issued by the Government or any local authority or (iii) carry on business of hire purchase transactions including leasing of machinery or equipment or (iv) finance venture capital and includes merchant bank, at a premium but does not include a loan to a company or other body corporate upon terms involving the issue of debentures or other securities.

The NBFIs are extending term finance for installation of capital machinery and construction of factory building. They do not provide working capital finance.

Table 5: Sources of funds of NBFIs

Sources of fund	Rate of interest
Local commercial Banks	11% to 13%
Loan from Foreign agencies	LIBOR+3%

4.4.1 Utilization procedure of Foreign Currency (FCY) by NBFIs:

FCY funds received from abroad against foreign credit lines are kept deposited by NBFIs in foreign currency with local banks as cash collateral. Interest earned on such deposit is transferred to the company by these banks. Overdraft facilities at hundred percent equivalent Takas are obtained from the banks at much lower rates than market rates. The overdrafts are utilized for funding both long term and short-term investments. In this way, it is possible to enjoy long term fund facility at lower rates.

Table 6 : Lending Rate of NBFIs

Products	Rate of interest
Lease	15% to 18%
Short term loan	15% to 16%
Long term loan	15% to 18%

4.4.2 Contributions of NBFIs in export financing:

Field survey reveals that NBFIs are extending financial support to all potential sectors like textile and Ready Made Garments (RMG), food and allied products, agro based industries, leather, ICT etc. The national investment figures of their contributions to the exporters/export-oriented industries however are not available.[21]

It has been observed from the study that the banks and financial institutions are not maintaining any separate statistical data set for credit/finance offered to the

21 FIs /NBFIs' financial support to exporters in the last 5 years:

exporters in different type of product. There is no monitoring and budgetary system in the financial institutions for export credit either. Bangladesh Bank also has no special monitoring system in place for this sector. The concerned individuals/ bodies/ authorities are more interested in the export earnings rather than export credit/ finance. They are only looking after the export earnings rather than investment in the export sector. In other words, there is void in strategic planning for this sector.

No investment in export is shown separately in their annual reports.

The NBFIs provide their service at the doorsteps of the investors. The response time is very short as shown in the following table.

The lending rate of NBFIs is higher than that of NCBs and PCBs. Although, borrowers still prefer to borrow from the NBFIs. This is because of their quality service and simple procedure and for non-existence of trade union activities.

NBFIs are extending long-term financial support, which is not defined as export credit by Bangladesh Bank. They do not provide working capital or any other banking services to the exporters and are not substitutes for banks. The mainstream banking sector can learn important lessons from them, particularly with regard to quick service.

Table 7 : Response time for different of Project

Sl	Nature of job	Response time
1	Green field projects proposals	4-6 weeks
2	Projects expansion proposals	4 weeks maximum
3	Existing clients with satisfactory performance	1 week.
4	Regular correspondences (balance confirmation, liability position etc)	1 working day

4.5 Venture Capital for exporters

Equity capital in fledging and risky business is known as venture capital and it is provided by specialist venture capital firms, wealthy individual, and specialist firm and investment institutions such as pension fund. It usually implies involvement by a venture capitalist in the management of client enterprise since the success of a new company depends on the efforts its managers put in. Furthermore, venture capitalists can ensure better utilization of their investment by participating in the management of the new companies. In broad terms, venture vapital is the investment of long-term finance where the venture capitalist earns his/her return primarily in the form of capital gain.

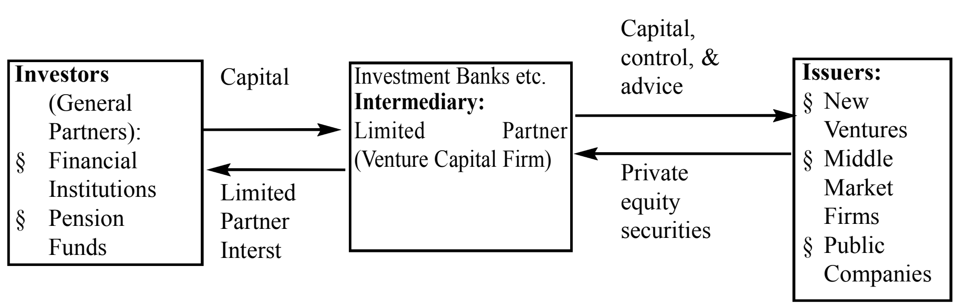
4.5.1 Features of venture capital

Venture financing is actual or potential equity participation through direct purchase of shares, options, or convertible securities. The objective is to make capital gains by selling off the investment once the enterprise becomes profitable. It is a long-term investment. Venture Capital Firms (VCFs) need to wait for a long period, say 5-10 years, to make large profit (Pandey (1999)). It ensures continuing participation of the venture capitalist in the management of the entrepreneur's business. The hand-on management approach helps him/her to protect and enhance his/her investment by actively involving and supporting entrepreneur. More than finance, the venture capitalist gives his/ her marketing, technology, planning and management skill to the new firm.

4.5.2 Venture Capital in Bangladesh

There are a number of thrust sectors in Bangladesh that have significant potential to grow but are also fraught with risks. Venture capital can make the enterprises profitable through flexible financing and appropriately guiding their expanding businesses. Agro-processing industries, IT (software), light engineering,

Figure 2 : A simple structure of organized private equity market



handicrafts, leather and leather products, garment industries with capital upto Tk. 50 million etc. are a few among the potential sectors of venture capital financing.

4.5.3 Government and Private Initiatives for Venture Capital

4.5.3.1 Government Initiative

Bangladesh Bank has already introduced EEF[22] in order to support risky new projects; especially software and food/agro based processing industry. EEF fund

[22] EEF circular no.6 dated June 24, 2002 of Bangladesh Bank

has so far sanctioned Tk. 840 million[23] in the two sectors and the Bank has earmarked Tk.3000 million for the fiscal year 2002-2003[24].

Features of Equity Entrepreneurship Fund of Bangladesh Bank:

1. EEF provides finance to the software and food processing and agro-based industries.
2. Fund is available up to 49% of the combined capital of the project not exceeding 33.33 percent of the total project cost.
3. The total cost of the project shall be minimum of Tk. 5 million (inclusive of net working capital)[25]
4. Finance may be disbursed through all the scheduled banks and the Industrial Promotion and Development Company Limited (IPDC).
5. The fund is available only during the time of start-up and the loan applicant is registered as a private limited company.
6. Companies registered after 1st January, 1997 shall be regarded as new companies and will be eligible for finance.
7. Subsidiary companies of an established company are also eligible for getting the finance
8. Non-Resident Bangladeshi sponsors are given priority.
9. The investment is made in the form of equity and the projects are required to issue ordinary share certificates in name of the Government
10. The supervising financial institutions (FI) of EEF represents the Government in the Board of Directors of the financed companies and also monitors the business activities of the project on a regular basis.
11. The Supervising FIs are entitled to have 25% of the dividend earned by EEF.

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23 Byron, Rejaul karim, and Zahidul Haq (2003: 33:4) The Daily Star: Entrepreneurship fund finds way in 12 schemes, June 29,2003

24 http://www.Bangladesh-bank .organisation/about/dept/eefu/eefu.html

25 EEF Circular NO. 12 dated April 17,2003 of Bangladesh Bank

4.5.3.2 Private Organizations in Venture Capital Financing

Grameen Fund:

Grameen Fund is a sister concern of Grameen Bank providing venture capital to the risky-technology oriented enterprises which are otherwise deprived of finance from the conventional sources. Grameen Fund was incorporated as non-profit organization in 1994. They invest the capital gain in risky technology oriented ventures.[26]

BASIC Bank

BASIC Bank took initiative for providing venture capital for different companies with earmarked capital of Tk. 30 million[27] from the profit. However, it has not yet been made operational.

VANIK Bangladesh Limited

VANIK has conducted market survey to introduce venture capital in Bangladesh and trained some of their officials as well. Due to change in ownership, they could not introduce venture capital finance in Bangladesh.[28]

5. Other sources of export finance

In addition to banks and NBFIs, several other sources, both formal and informal, provide finance for exporters. Informal money lending has been a common centuries old practice across the sub-continent. The newly evolved sources include overseas facility and venture capital as well as factoring services.

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26 Major objectives of the Grameen Fund:

- Participate in the majority of equity capital in companies trying to innovate in various sectors that hold promise for future growth, having direct or indirect impact on poverty alleviation.
- Provides loans, equity or both, to risky firms using untested technology and / or producing untested but innovative products; both for existing companies for balancing, modernization or expansion
- Assist in management buy-in or buy-out of existing companies needing financial and management support, provided that such companies activities/product bring direct and/or indirect benefit to the poor.
- Promote or develop enterprises having prospects for export and for import substitution that will use indigenous raw materials, provide extensive employment to the poor and /or help upgrade the skills of the rural or urban poor.

27 Executive Interview with the Management of BASIC Bank

28 Informal Interview with Mr. Mahmudul Bari, Assistant Vice President, Merchant Banking, VANIK.

5.1 Informal Money Market

It is a widely known fact that informal moneylenders charge usurious rates of interest from rural borrowers who primarily take loan for crop cultivation, purchase of bullocks etc. With rapid urbanization, informal money lending is widely practiced in industrial areas and cities of Bangladesh.

Study reveals that exporters of certain sectors borrow from other sources; namely:

i) Relatives/friends: Terms and conditions of repayment of loan differ widely.
ii) Moneylenders: Terms and conditions of their loans are more or less similar. They charge high interest rates, usually 10% per month.
iii) Traders cum moneylenders: Yarn traders for example, sell yarn etc. to the knit garment exporters on credit and charge interest @ 4%-5%.

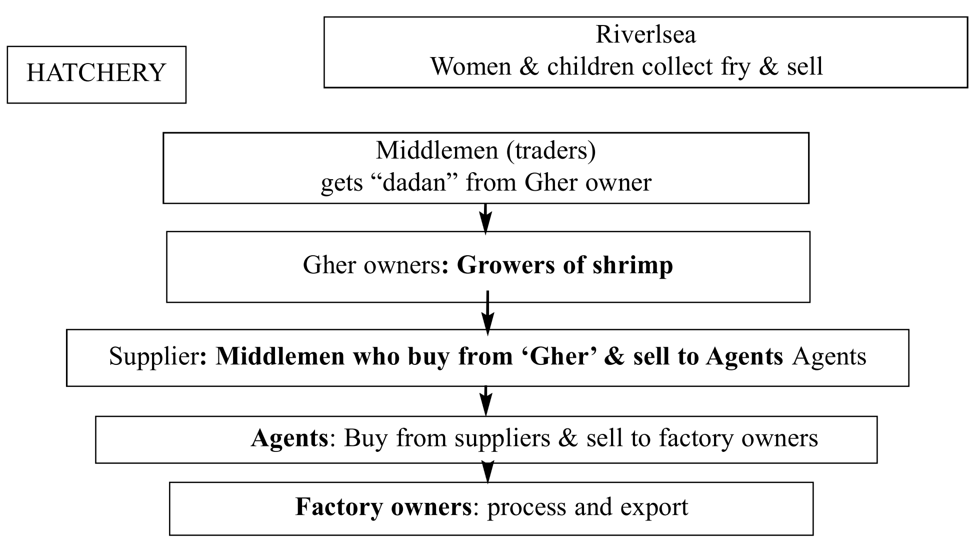
5.2 The sectors borrowing from other informal sources are:
- Frozen Food: Shrimp

There are five tiers shown below to support the export-oriented shrimp industry

Hatchery and shrimp factories get bank finance and they do not need to borrow from informal sources.

Middlemen, 'Gher' owners, suppliers and agents sometimes get bank finance in the form of Cash Credit (H) against collateral security of real estate. Many of them borrow from local money lenders at monthly interest of 5% to 8% and in some areas, the monthly lending rate is 15% - 8%. In rare instances, the factory owners borrow from informal sources.

Figure 3 :



- Handicrafts

There are a large number of handicraft items produced in different areas of the country, mostly by family members. Exporters make advance ("*dadan*") to the artisans for procurement of raw materials to ensure supply of high standard and quality products. Organized institutional finance for the producers is very limited.

- Vegetables

Vegetable exporters make advance payment (dadan) to the growers to ensure production and supply of vegetables of required quality and standard. The growers normally do not get institutional finance.

- Garments

A large number of knitwear garment exporters having capital of Tk. 10 million to Tk. 20 million with a workforce of 150-300 borrow from the local money lender at a monthly interest of Tk. 10000 per month plus brokerage of Tk. 1,000 for borrowing Tk. 1,00,000. They are compelled to take such loans when they fail to get urgent bank finance due to stock-lots and/or to avoid further stock lot. Sometimes they also borrow from the traders cum moneylenders who sell yarn etc. on credit at market price and charge interest @ 4% to 5% per month and the loans are utilised for:

- Lifting yarn under quota from the local mills.
- Providing L/C margin of the importers of commercial banks when they fail to arrange it from their own source.
- Meeting the shortage of margin for availing cash credit (pledge) limit sanctioned by the commercial banks.
- Payment of salary and wages of worker.

5.3 Factoring Services[29]

5.3.1 Factoring Sevices in Bangladesh: Prospects & Potential

Bangladesh is a developing country. Factoring will be of great assistance to the entire industrial and trading sector. Factoring will be specially helpful for the

[29] Factoring is a device of transforming a non-productive, inactive asset (i.e. book debts) into productive asset (viz. Cash) by selling book debts (receivables) to a company that specialises in book debt collection and administration. It is a popular mechanism of managing, financing and collecting receivables. The arrangement between the client and the factor primarily depends upon the needs of the clients. This could be either financial or sales ledger administration or collection of book debts or credit risk coverage etc. or all together. The type of factoring arrangement concluded at a given time depends upon client needs, nature and volume of client's business and financial strength, type of business, cost of services etc. Factoring is now universally accepted as vital to the financial needs of particularly small and medium sized business. Factoring has become well-established in developing countries as well as in those that are highly industrialized. In South Asian, India and Sri Lanka have already launched its service. In Sri Lanka, factoring is now accepted as a useful financing service. In India also, factoring is gaining acceptance in the business community.

development of SMEs in Bangladesh. Small and Medium-sized Enterprise (SMEs) suffer from the lack of adequate bank finance, because of reluctance on the part of banks against book debts of SMEs.[30] Furthermore, factoring could be a supplementary financial service with the existing financial services provided by banks. The commercial banks are over burdened with huge amount of non-performing assets. There is a good prospect for setting up of factoring companies for taking over the non-performing assets of Tk. 26,000 crore of the commercial banks.

5.4 Counter Trade[30]

5.4.1 Counter Trade in Bangladesh

Bangladesh has undertaken different initiatives to start counter trade arrangements with different countries. The objective of starting counter-trade in Bangladesh is to reduce trade deficit and to reduce pressure on foreign currency reserve. In the initial stage, Bangladesh has established trade relationship with three countries viz. Myanmar, Thailand and Indonesia. If potential counter trade relationship brings fruitful results, Bangladesh will go for such arrangements with other regional countries in phases.

5.4.2 Overseas facility

Both bankers and exporters reported that some industries have been set- up with imported capital machineries funded by non-resident Bangladeshi (NRB). Furthermore, it was also reported that machineries and raw materials are often imported with undisclosed funds through under invoicing funded by the "sleeping equity partners" in and outside the Export Processing Zone (EPZ). However, with a significant overseas population, overseas facility remains an attractive source of finance for many exporters.

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30 The following reasons are cited for this:

- SMEs do not maintain a proper accounting system and therefore banks are unable to verify the accuracy of book debts.
- Most SMEs are organized in as proprietary or partnership firms and thus are not required to have audited accounts. Banks cannot put much reliance on unaudited accounts.
- Most SMEs have poor credit management. They have inadequate and inefficient systems of book debt collection. Thus, the incidence of bad debt losses is high in the case of SME sector.
- SMEs have a tendency of slackening their effort of collecting book debts once banks have financed their book debts.
- SMEs are not in a position to provide sufficient collateral security.

5.5 Role of Stock Exchange

Dhaka Stock Exchange (DSE) and Chittagong Stock Exchange (CSE) are non-profit organizations.[31] They work as intermediaries between investors and companies. They help the companies to raise capital through initial public offering. They perform the valuable secondary function of buying and selling their securities. Since the stock exchanges are not lending or borrowing institutions, DSE and CSE do not have any provision to maintain liquidity. At present, there is good market liquidity to attract investment for all types of companies including the emerging export enterprises. They do not have any scope to extend special help to the exporters. They help investors in getting their shares liquidated through their enlisted brokers.[32] It has been observed from the daily price index published by the DSE and CSE, that most stocks are traded at half the price of face value, which indicates that they have not been able to regain the confidence of general investors despite recent positive initiatives undertaken by Security and Exchange Commission (SEC).[33] Until the full confidence is regained it will not be meaningful to expect DSE and CSE to come forward to assist exporters in need of finance.

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31 Exceutive Interview with the Dhaka Stock Exchange and PRO of Chittagong Stock Exchange 5. Box 4.1 Background of DSE and CSE

32 Dhaka Stock Exchange was incorporated in 19 54. As on 30th June, 2001 there were 244 securities listed with DSE and the total issued capital of all listed securities was Tk.32, 227 million and market capitalization was Tk.72, 168 million . On the other hand, The Chittagong Stock Exchange (CSE) was r egistered as a public limited company in April 1995. As on 30th June, 2001 there were 171 securities listed with CSE and issued capital of all securities was Tk.27,350 million. Total market capitalization of all securities of CSE as on 30th June 2001 stood at Tk.62,820 million Form July 1996, the market index of Dhaka and Chittagong Stock exchange started increasing and it continued till the market collapsed in Nov 1996. Thousands of new and small investors who knew very little about the stock market suf fered most. Following the debacle of 1996, Securities and Exchange Commission (SEC) seeks comment from the DSE/CSE whenever they receive any application from companies intending to float their shares in public.

While sending comments to SEC, DSE/CSE ens ures that the company has a good track record and sound performance in the previous three years. On the basis of DSE/CSE's comments, SEC accepts the proposal only if found satisfactory. Comments are incorporated with the prospectus.

33 Dhaka Stock Exchange: (September 2003), Monthly Review: Dhaka

5.6 Role of Export Promotion Bureau

The Export Promotion Bureau was established by the then Pakistan Government as a Department of the Ministry of Commerce. Subsequently, it was re-organized as a semi-autonomous body for promoting export of Bangladeshi products by a Presidential Order in 1977. The Head Office of EPB is in Dhaka and three regional offices are situated in Chitagong, Khulna, and Rajshahi.

5.6.1 The functions of EPB are[34]

- Adoption of dynamic policy and program measures for active promotion of exports;
- Co-ordination of export development efforts at various levels;
- Co-ordination and monitoring of national export performance and progress;
- Carrying out of promotional activities in product and supply development;
- Exploration of markets abroad;
- Collection and dissemination of trade information;
- Organization of participation in international trade and export fairs abroad;
- Imparting of training for HRD;
- Conducting of studies, surveys, research etc on products and markets;
- Administering and monitoring of RMG quota.

Table 8 : Loan from EPB's Export Promotion Fund

Name of the Companies	Amount Sanctioned	Amount Disbursed	Present Outstanding
Information Communication Technology			
Data Soft	Tk. 25 lac	Tk. 25 lac	Nil
The Decode	Tk. 50 Lac	Tk. 50 lac.	Tk. 35
H a n d i c r a f t			
Craft International	Tk. 5 Lac	Under Process	-
Prianka Banarashi	Tk.5 Lac	Under Process	-

Source: EPB

34 EPB, "What it is, What it does" published by Trade Information Center of EPB, Dhaka

5.6.2 Activities and Contribution of EPB in Export

5.6.2.1 Export promotion fund of EPB

EPB has signed an MOU with Janata Bank for disbursing loan from Export Promotion Fund to ICT and handicraft exporters. It allocated Tk.40 million for ICT and Tk. 10 million for handicraft exporters.

5.6.2.2 Country of Origin Certificate & trade license

The Certificate of country of origin is a very important document used in international trade finance. In Bangladesh, EPB issues six different types of certificates of origin. They also issue trade license for textile and visa for the textile exporters to the USA.

5.6.2.3 Trade Fair

EPB arranges different types of trade fairs in Bangladesh and other countries for promotion of exportable goods. EPB also helps different Bangladeshi companies to participate in international trade fairs abroad to create market for Bangladeshi products. In 2001-2002, EPB participated in 22 different trade fairs and organized 4 single country exhibitions.

Box 2: Country of Origin Certificate issued by Bangladeshi Company

Generalized System of Preference (GSP): It is issued for 15 different EU countries and 14 developed countries including USA, one of the major importers of Bangladeshi goods.

South Asian Preferential Trade Agreement (SAPTA)*: It is issued for the SAARC member Countries such as Sri Lanaka, India, Maldives, Pakistan, Bhutan and Nepal.

Bankot Agreement*: This country of origin certificate is issued for China, Srilanka, Korea and India.

GSTP(Global System of Trade Preference): It is issued for the Group of 77 member country

Annex-3 : It is exclusively for Mexico

KPT(Korea Preferential Trade): It is used exclusively for Korea**.**

*Bangladesh is a the member of SAPTA & Bang ot Agreement

5.6.2.4 Publications on Export[35]

Export Promotion Bureau Publishes different types of printed materials on export for home and abroad. Printed publications are circulated to Bangladesh Missions abroad, concerned Ministries, Government Departments, National and International Trade Organizations, Trade Associations, Chambers of Commerce, and leading exporters.

Trade Information Center (TIC)

Trade information Center (TIC) is a commercial library of Export Promotion Bureau. There are 9677 books/publications and 72 international and national periodicals preserved in the TIC at present. Day-to-day activities of Trade Information Center (ITC) have been computerized and includes the following database:

- Database "TICL" contains books available in the Library.
- "COM" database contains information on local exporting companies. It is the export directory with detailed information.
- Database "PREIO" contains journals/ periodicals available in the TIC.
- CD-ROM "PATAS" contains statistical Information on export and import of 71 countries.

6. Issues and recommendations

Heretofore, a broad overview has been presented of extensive spread of financing services that are currently available for exporters. The study has identified several critical issues that affect the efficiency of these services as well as act as impediments to export. They are given below along with their recommendations.

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[35] List of Publications published during the year 2001-2002 is given below:

1. Bangladesh Export Statistics 2000-2001;
2. Brochures and Posters on International Trade Fairs/Single Country Exhibitions held abroad;
3. Quarterly Trade Information Journal;
4. Folder on National Export Training Program;
5. Folder and Poster on Dhaka International Trade Fair (DITF) 2002;
6. Directory on DITF 2002;
7. Souvenir on DITF 2002;
8. Application form for Pavilion/Stall of DITF 2002;

Source: Annual Report 2001-2002 of EPB

6.1 Impediments to export – issues and recommendations

6.1.1 Banking related impediments

Issue: Centralisation of Business Power

1. NCBs take a long time to communicate decisions on application for financial support from new clients. According to the Business Delegation Power of NCBs & PCBs[36], the sanction of Long Term Project Finance is approved by the Head Office/Board of Directors in most of the banks, irrespective of the collateral issue[37]

2. In the case of shrimp culture, finance is treated as rural finance. Since all frozen food exporting organizations are situated in Chittagong and Khulna, obtaining finance from the bank becomes very time consuming and lengthy.

Recommendations

Short Term

1. CBs may be advised to delegate the sanctioning power of long term project finance for setting up the backward linkage industries to the field level as per

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36 The above information is available from the 'delegation of business power' of the following banks reviewed:

NCBs

1. Sonali Bank
2. Janata Bank
3. Agrani Bank
4. Rupali Bank Ltd.

PCBs

1. IFIC Bank Ltd.
2. Prime Bank Ltd.
3. National Credit and Commerce Bank Ltd.
4. Mercantile Bank Ltd.

Islami Banks

1. Social Investment Bank Ltd.
2. Al-Arafa Islami Bank Ltd.

The following commercial banks informed that they do not have delegated business power:

1. Dhaka Bank Limited
2. Dutch Bangla Bank Limited
3. United Commercial Bank Limited.

37 According to the Delegation of Business Power of NCBs & PCBs, the sanction of Long Term Project Loan is centralized at Head Office/Board of Directors, while the sanctioning power of pre-shipment and post shipment credits against export order/ L/C and working capital finance are delegated to the different levels of the sanctioning authority.

Unfortunately, some PCBs do not have delegation of business power. As a result, loan-sanctioning power is centralized to the Board of Directors of these banks, which does not conform to the BB's BRPD circular # 16/03 dated July 24, 2003.

BRPD circular No. 16/03 of BB(ST). In addition, loan sanctioning power of the banks should be decentralized for the SMEs as they usually need small project loans amounting Tk. 10 million ot Tk. 20 million.

2. Specifically for Shrimp growers, sanctioning authority should be delegated to the branches at field level.

Issue: Rigidity of Collateral Security in export financing

1. In the event of export failure/ stock-lots[38], garment sector SMEs are compelled to suspend/close their production. This is because they do not get further bank finance due to non-receipt of export proceeds, rigidity of collateral security, etc. In case of one-two stock-lot(s), they borrow money from informal moneylenders at a rate of 11% interest per month including 1% per month paid to the broker. BKMEA (Bangladesh Knitwear Manufacturing Exporters Association) reported that about 200 knitwear garments of this category regularly borrow money from the moneylenders as they fail to get additional bank finance.

2. According to the Delegation of Business Power of commercial banks, no project finance is allowed without collateral security. Shrimp exporters claim that 85% of the freezing capacity remains unutilized for want of finance. Processing bank loans is a lengthy procedure which has a cost to the exporters. Any attempt to expedite the process also has a cost in the form of 'speed money' and other forms of hidden costs as well.

Recommendations

Short Term

1. Delegation of business power should be appropriately amended so that banks extend finance against genuine export L/C or export order as per existing practice without insisting on collateral security. Industries with large workforce but small capital may be allowed to get finance from Equity Entrepreneurship Fund (EEF).

2. Shrimp growers should be declared as deemed exporters and also be allowed bank finance without collateral security since shrimp growers are of very small means.

3. Processing of bank loans has to be completed within a stipulated time mutually agreed by the bank and exporters.

[38] Stock-lot: Failure of the exporter to make shipment of the manufactured goods (stock –lot) in which case his banker makes payment of import bills for the value of raw materials imported under Back –to –Back L/C creating forced loan. Such goods are sold at a distressed price.

Issue: Banks' customer response cycles

Response time means the time spent from the date of loan application submitted by the borrowers to the date of disbursement of the applied loan[39]. The response time varies from bank to bank, size type and nature of the loan applied for. An industrial term loan proposal needs a long time for sanction by the financing banks while a working capital loan proposal needs a shorter period of time (generally 35 days). Again a loan proposal of a company or a group requires more time than that of an individual or a proprietorship concern due to simplicity of processing.[40] If this industrial loan is related to an export product, then, clearly its growth is bound to be constrained by this lengthy response cycle.

Discussions with bank officials reveal that most of the banks do not maintain the response time schedule for disposing a loan proposal. Some banks have introduced a "Top Sheet" or "Movement Sheet" to monitor the time taken in each of the steps to ensure speedy disposal. Two out of the three foreign banks did not provide the relevant information in this regard.

Recommendations

<u>*Short Term*</u>

1. Measures should be taken to reduce the customer response cycles of financing banks. There has to be a regular monitoring mechanism in place to oversee this cycle.

2. The decentralization of authority of NCBs is a must to reduce the total length of time needed to get financial services.

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39 The time taken at different levels of the sanctioning authority varies.

40 Loan sanctioning procedure of any bank is governed by the "Business Delegation Power" of the banks. This procedure begins from the very field level of the banks. Generally exporters apply to the branch for extending credit support. The branch then prepares a proposal in printed format and collects all other necessary papers and documents from the applicant. In many cases, sanctioning power is concentrated at the head office. Branches in that case forward that proposal to the head office. Head Office collects Credit Information Bureau's report prepared by the Central Bank and for lending analysis. These two steps need about fifteen days (see Annex --).

***Issue: Foreign Exchange Retention quota for Exporters**[41]*

1. Exporters are entitled to retain10% to 50% foreign exchange of their repatriated export proceeds in the FC account, which is termed as retention quota. The export retention quota for ICT exporters has been increased from 40% to 50%. Most exporters in this sector are not happy with the 50% retention quota and they demand 100% retention quota. However, the concerned officials of Bangladesh Bank revealed that the use of retention quota by ICT exporters is only 18% to 25% during the current year.
2. According to exporters of leather goods, retention quota cannot be used to import spare parts for machineries and 35 % duty has to be paid on import of spare parts.

Recommendations

Short Term

1. The demand for further enhancement of the retention quota by the exporters need to be examined more thoroughly before making any decision in this regard. In any case, there cannot be a blanket of enhancing quota for all the exporters as many of them have not been able to utilize even half of the quota provided to them. But certainly, better performers should get higher quota and if needed more than 50%.
2. Leather goods exporters, however, should be allowed to utilize their retention quota to import spare parts duty free.

Issue: International Credit Card

The financing commercial banks are permitted to issue international credit cards in favour of exporters against F/C account under Foreign Exchange Retention Quota which can be utilized for business travel only. Software developers, however, spoke of the requirement for upgrading software, ordering technical books, booking conferences, paying for vendors certification or business partner's affiliation fees etc. for which online payment by International Credit Card is the normal mode of payment. The standard alternative is to pay using a US$

[41] Use of foreign exchange under retention quota is limited to bonafide business purpose as under:

- Business visits abroad.
- Participation in exports fairs and seminars.
- Establishment and maintenance offices abroad.
- Import of raw materials.
- Import of machineries and spares

denominated cheque drawn on a USA bank. But this is not possible under current foreign exchange regulations. Very limited foreign currency exposure is involved – the typical purchases are less than US $1000 and most purchases are in the US$ 500 range.

Recommendations

Short Term

The use of the International Credit Cards should be widened as per recommendation of the Project Coordination and Development Unit (PCDU) report, which is as under:

1. Establishing a list of items and services that can be purchased online under pilot scheme in consultation with BASIS.
2. Approving companies in the software industry that have genuine need to purchase the approved items online.
3. Issuing a supplementary credit card for online purchase in foreign currency.
4. Setting a limit on the credit card equivalent to 3 months online spending.
5. Requiring the cardholder to produce documentation to validate the online purchases as part of the normal payment of outstanding balance. Failure to produce such documentation would result in the card to be withdrawn.

Issue: Delay in disposal of Duty Draw Back Claim

1. An exporter of manufactured products is entitled to draw back the value of the customs duties, sales tax, etc. already paid on the importation of raw materials used in the production/ manufacture of the export products.
2. There is, however, inordinate delay in receiving duty drawback. Claims submitted in year 2000 have not as yet been settled. The required documents are sought from exporters in several phases, which is time consuming.

Recommendations

Short Term

1. There should be specific time frame for settling the duty draw back claims.
2. The queries/documents should be requested at a time to avoid unnecessary time loss.

Issue: Cash Subsidy

1. There is unusual delay in payment/reimbursement of cash subsidy (CS) by BB (takes 1-2 years) due to inadequate budget allocation by the GOB and the lengthy procedure followed by the BB.

2. CBs provide loan against cash subsidy claim and charge interest @ 9% for first three months and @ 14% for subsequent periods which incurs a fairly high cost for the exporters.

3. The leather and pharmaceutical industries do not get any cash subsidy. The value addition of leather and pharmaceutical industries is 85% and 50% respectively. Garments industries with lower value addition of 20% to 25% have been receiving cash subsidy. It was reported by the pharmaceutical companies that Indian pharmaceutical exporters are getting 40% CS.

4. Until recently, export had to be made against L/C to get CS [42] . But fruits and vegetables are exported without L/C as the importers prefer to import under Cash Against Delivery (CAD) or against advance payment by Telegraphic Transfer (TT) to avoid the time lag involved in receiving export documents for release of goods. As such, the exporters of perishable goods are not entitled to receive CS. BB has recently waived the condition[43] · However, the exporters are not aware of the withdrawal of restriction by BB.

Recommendations

Short Term

1. Interest for finance against cash subsidy should be charged at the rate applicable for export finance (at flat rate over the period).
2. Considering the high value addition in the export of leather and leather products and pharmaceuticals, GOB should extend a reasonable percentage of cash subsidies for both the sectors.

Medium Term

3. GOB should allocate adequate budget for cash subsidy on the basis of past export volume and projected export. There should be a specific time frame for settling the cash subsidy claims.

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[42] Bangladesh Bank, *FE Circular No. 24*, 12th December 2002.
[43] Bangladesh Bank, *Circular Letter No. AFEPD 291/Krishi Ponno/Niti/2003-401,* 15th April 2003.

4. The government may consider making arrangements with foreign airlines to operate cargo flights and encourage private airlines to introduce cargo flights for vegetable exporters. The government may further provide Cash subsidy on airfreight instead of value of export. For instance, national/foreign airlines may be subsidised to introduce cargo flights for the exporters.

5. Decision taken by Bangladesh Bank should be promptly disseminated to the stakeholders involved in simple language. They should be posted on BB website and appropriately highlighted.

Issue: High rate of interest for export finance

High rate of interest is a major issue raised by exporters from all sectors. The commercial banks are not in a position to lower their lending rate mainly due to high cost of non-performing assets and high deposit rate. In order to allow some relief, export financing is being allowed at a concessional rate of interest from Export Development Fund (EDF)[44]. The rate of interest on EDF is LIBOR (which is around 1.2%) plus 3.5% including their spread of 2.5%.

Recommendations

Short Term

1. Bangladesh Bank should continue to put its weight behind management reform in NCBs to improve their efficiency. If this happens, the cost of banking operation will come down leading to lower cost of fund and hence, lower interest rates. It should also continue to put pressure on PCBs to further reduce interest rate as they are not saddled with high level of non-performing assets.

2. *Reduce interest rate on export finance to a single digit.*

Medium Term

3. Bangladesh Bank should widen the size of existing EDF of US $ 30.00 million and make export finance through banks. Commercial Banks should be allowed to borrow fund from international sources at LIBOR like EDF and NBFIs should be

44 Export Development Fund (EDF) of US 30 million has been created jointly by the IDA and the GOB for financing imports of raw materials and spare parts of export oriented manufacturers in order to diversify export and to promote and encourage non-traditional and higher value added export. The fund is to be utilized by the commercial banks for financing their exporters to the maximum of 70% of the export L/C at an interest rate of 1% above LIBOR. BB will provide a spread of 3.5% to the financing commercial banks on their advances to the new non-traditional exporters and a spread of 2.5% on all other advances rediscounted with EDF.

encouraged to extend support to the exporters. For this purpose, Bangladesh Bank and Board of Investment should simplify the existing procedure of approval.

Issue: Higher rate of interest for project finance

There is no scope for providing Project Finance to an export oriented organization at concessional rate of interest because according to BB regulations, "Export Credit" does not cover project finance for export credit. Large enterprises are entitled to get project loan at concessional rate of interest if Bangladesh Bank recommends but SMEs are not entitled to such facilities. Interest rates on project finance of some commercial banks are given below:

Task Force of GOB formed to Eradicate Different Problems and Hindrances in Export Business decided in their 28th meeting held on June 3, 2002 that commercial banks must provide export credit at 7% interest rate.

Recommendations

Short Term

Recently Bangladesh Bank has made concessional interest rate for following items mandatory and for others a band of 7% to 10%:

Table 9 : Interest rates for project finance of different banks

Name of the Bank	Rate for SMEs	Rate for Large
Enterprises IFIC Bank Ltd.	14%	15%
Islami Bank Ltd.	14.50	14.50
Prime Bank Ltd	15	15
UCBL	12	14
NCCBL	12	12
AIBL	15	12
NCCBL	15	15
Mercantile Bank Ltd.	12.5	12.5

This is preferential system of interest rate should be waived and a standard concessional rate of interest should be declared.

Table 10 : Concessional interest rate

	Commodities	Revised interest rate
1	Ready made garments	7%
2	Frozen food.	7%
3	Agro-based industry	7%
4	Leather shoes and Leather products	7%
5	Potato	8%

Issue: equity entrepreneurship fund

BB has introduced EEF in order to support risky new projects; especially software and food/agro based processing industries. Bangladesh Bank intended to introduce venture capital through EEF although there were some limitations. EEF has so far sanctioned Tk. 840 million for the two sectors and BB has earmarked Tk. 3 billion for the fiscal year 2002-2003.

Recommendations

Short-Term

Bangladesh Bank should continue to simplify procedures related to disbursement of EEF which has already started picking up. Given necessary policy support and regular monitoring, EEF may emerge as a major funding source for risk bearing techno based export. EEF should also be made available to other risky export sectors and not restricted only to software and agro-based industries.

Issue: Export Promotion Fund of EPB

Many exporters of ICT and handicraft sector informed that they are not aware of EPB's scheme for financing from its Export Promotion Fund.[45]

Recommendations

Short Term

EPB should arrange presentation for the members of the trade associations of the ICT and handicraft. EPB and Janata Bank should jointly publicize detailed procedure of export finance through Export Promotion Fund. The relevant information should also be made available electronically.

Issue: Export Credit Guarantee Insurance

GOB has introduced an Export Credit Guarantee Insurance (ECGI) to deal with credit risk associated with export trade. Administration of the scheme has been entrusted to Sadharan Bima Corporation (SBC), which has created a separate department known as Export Credit Guarantee Department (ECGD) to deal with

45 EPB and Janata Bank signed a MOU to extend financial support to ICT and handicraft exporters. Initially, EPB placed a fund of Tk. 50 million for this purpose. The fund has now increased to about Tk. 80 million. After the evaluation of the Technical Committee, EPB sanctions credit facility and Bhaban Branch of Janata Bank disburses the loan. From the inception of the scheme, two ICT companies have been financed against export order.

export credit insurance.[46] However, being a public commercial organization, Sadharan Bima Corporation is not perceived as the right institution to run such promotional schemes and besides, the department has no trained manpower to sell the products. SBC itself has advised MoC that unless the government makes its ECGD a separate corporation and diversifies the schemes, the schemes themselves would be at stake. Asian Development Bank (ADB) has also recommended that making ECGD an independent corporation is the only option for its survival. The Bank also added that export credit schemes are run by separate corporations in countries like India, Sri Lanka, Malaysia, South Korea, Hong Kong and Australia. In India, the Export Credit Guarantee Corporation is an autonomous company with 100% share being held by the government

Recommendations

Medium Term

As suggested by Asian Development Bank (ADB), the ECGD should be made an autonomous company so that it suits the need of the larger companies, SMEs and lending institutions. The SBC and Jiban Bima Corporation could be partners to its capital.

Issue: Lending rate

On the basis of current lending rates band prescribed by BB[47] each CB determines its lending rate depending upon the cost of fund. The lending rates are still high compared to neighboring countries like Pakistan and Thailand[48].

46 When it started on January 1, 1978, the Export Credit Guarantee Scheme Department (ECGD) had three schemes to offer. Since then the services remained the same, making it difficult for the ECGD to adjust to new realities.

47 Present deposit and lending rate of CBs in Bangladesh

CBs	Deposit Rate Lowest	Lending Rate Highest	Minimum	Maximum
NCBs	4.5%	7.25%	5%	15.15%
PCBs	4.75%	11.25%	8%	19.00%
FCBs	4.75%	11%	7%	19.00%

Average lending rate 12.8%

48 It is pertinent to mention here that the Task Force formed for immediate elimination of the problems and hindrances in export business in a meeting recommended for reduction in interest rate on export credit to 7%. Bangladesh Bank vide their BRPD circular revised interest rate for commodities like Ready Made Garments; Frozen Food; Agro-Based Industry; Leather Shoes and Leather Products; and Potato.

The Private Commercial Banks (PCBs) being newer generation banks have to offer higher rate of interest to attract deposits. Higher cost of fund in the NCBs may be attributed to the following facts:

a) The high incidence of non-performing loans of the banks pushes up the cost of bank financing.

b) About 30% of the total employees of the NCBs are directly or indirectly involved in trade union activities. They do no work at all or put in negligible working hours. 30% manpower of the NCBs is virtually surplus, and hence impacts negatively on their profit position.

c) NCBs conduct government transactions free of cost employing huge human and financial resources like collecting different types of utility bills, payment of "Distressed Women Allowance", providing pension to government servants and the Army. This too has a cost that has to be ultimately borne by borrowers.

d) National Savings Certificates offer artificially high interest rates and drive up the costs of funding.

Recommendations

Short Term

1. The GOB enacted a law, Artha Rin Adalat Ain 2003 to recover the bad loans (including non-performing loan to the exporters). A machinery may be set up to closely monitor the effectiveness of the law in loan recovery and suggest necessary improvements.

2. Minimum commission @ 2.5% should be paid to the NCBs to compensate the operational cost for government transactions.

3. The concerned ministry should place funds with the NCBs beforehand to meet the government obligations against army pension bills, food procurement bills and so on. Alternatively, the govt. should pay the cost of fund on the amount involved by the NCBs.

4. BB realizes penal interest on the debit balances in the accounts of the commercial banks. BB should also pay interest on the credit balances of such accounts so as to improve the financial position of the CBs.

Issue: Time and Cost of Recovery

Bangladeshi banks are burdened with huge amount of non-performing loans (25%). Non-performing loans are one of the major causes of high cost of recovery. Cost of recovery is not worked out by any of the banks/FIs interviewed and they do not have any procedure for calculation of the cost of recovery. However, for the purpose of this paper, a procedure has been devised to calculate the cost of recovery using the formula:

$$C= [\{(NL+RL) xALR\}+\{(NL+RL) xABR\}+\{IW+AF+LF\}/TLAx100]$$ [49]

But these factors are not disclosed in the annual report of Banks and FIs and the relevant statistics are not available even in the central bank[50]

Recommendations

<u>Medium Term</u>

Bangladesh Bank should make it mandatory for banks and FIs to disclose the cost of recovery of non-performing loan and advances in order to make it public how much the good borrowers are paying for the non-compliance of the bad

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49 Where:

C	=	Cost of recovery
NL	=	Total non performing loan
RL	=	Rescheduled and Blocked loan
ALR	=	Average lending rate
ABR	=	Average borrowing rate
IW	=	Amount of Interest waived
AF	=	Fees and commission paid to recovery agent
LF	=	Legal expenses for recovery
TLA	=	Amount of outstanding Loan and advances

This formula has been devised by Mohammad Abu Taher, financial analyst in Al-Arafa Islami Bank.

50 The authors identified the following components of cost of recovery and devised the above formula to calculate the cost of recovery.

- Loss of income due to non-performing assets: Banks lose income, which would have been generated from its non-performing loans and advances.
- Cost of non-performing assets: Banks have to pay for the depositors' fund, which yields no return in case the loans become non-performing.
- Amount of interest waiver: Very often banks waive interest to recover the principal loan. Banks also have to waive interest on Government directive.
- Loss for rescheduled loan: Banks incur loss when rescheduled loans are transferred to interest free blocked account.
- Operational Cost of recovery
- Amount of fees and commission paid to the recovery agents.

borrowers. These statistics should also be included in the Resume of Financial Institutions published by the Ministry of Finance and in the annual report of BB.

Issue: Schedule of charges on banking services

Most exporters interviewed (both large and SMEs), claimed that the prevailing charges on banking services are high and that they should be lowered for growth of the export sector. Such a decision has been taken by the banks on March 2003. Following the decision, Bangladesh Bank has provided a comparative list of charges to the banks for necessary actions.[51] From the available schedule of charges of different NCBs and PCBs, it has been observed that banks are yet to rationalize their charges. The FCBs however, have not provided any information on this issue. And also, *the banks charge very high service charge that increases the cost of doing business. For example, while DHL charges Taka 350 for a document delivery, banks would charge Taka 1,500. While Society for World-wide International Financial Telecommunication (SWIFT) costs Taka 50 for a money transfer to a bank, the bank charges Taka 3,000 for the same.*

Recommendations

Short Term

1. Commercial Banks should rationalize schedule of charges especially for the exporters as per decision taken by the Bankers on March 11, 2003.

2. Reduce bank charge: remittance charge, postage, courier (DHL), etc.

Issue: Lack of correspondent banking arrangement

In the absence of banking relationship with several countries including Russia, Ukraine, Afghanistan etc., export transaction with these countries are time consuming and risky.

Recommendations

Short Term

Bangladeshi commercial banks should establish correspondent banking relationships with foreign banks abroad, where such arrangements are absent. Bangladesh Bank may extend necessary assistance in this regard.

Issue: Consortium Finance

Bangladesh Bank has advised for syndication of any single credit facility equivalent to 50% and above of total capital (paid up capital plus reserves) of a

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51 BB's letter No. BRPD(P)661/29/2003/1059 date: March 11, 2003

particular bank.[52] But entrepreneurs, specially exporters do no feel comfortable in Consortium Finance arrangements as the system is complicated and time consuming.

Recommendations

Long Term

A government sponsored "Exim Bank" should be established to co-ordinate the services of the financing commercial banks, syndication of term loans and to cater the Imports/Exports need of the country.

Issue: Delay in repatriation and payment of export proceeds

Repatriation of export proceeds through most of the banks takes a long time. TT takes at least 7 days on an average. This adversely affects the cash flow. The delay is mainly due to bureaucratic bottleneck in the system and the absence of direct correspondent banking relations of the paying banks with the remitting banks.

Recommendations

Short Term

Bangladesh Bank should ensure speedy inward remittance of export proceeds through close monitoring. It is mentionable that recent steps taken by Bangladesh Bank in monitoring private foreign remittances from NRBs has produced very good results.

6.1.2 NBFIs related impediments

Issue: Complicated procedure for getting fund from International sources

NBFIs borrow fund from the local commercial banks at the rate of 11%-13%[53] and lend to exporters at the rate of 15%-18%.[54]

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52 BB's BRPD circular No. 08 date: 18/03/2003

53 Rates quoted here were as on the day of interviewing

54 There are 19 non-bank financial institutions in operation in Bangladesh. Amongst them, five have been interviewed during the field survey. The NBFIs are extending term finance for installation of capital machinery and construction of factory building. They do not provide working capital finance. NBFIs usually raise fund by taking loan from local commercial banks and in a few cases from foreign agencies. Field survey shows that the NBFIs are extending financial support to all the potential sectors like Textile and RMG, food and allied products, agro based industries, leather, ICT etc. The NBFIs provide service at the doorsteps of the investors; their officials going to the potential borrower for appraisal and evaluation. Borrowers are rarely required to visit NBFIs officials.

The exporters usually utilize the high cost fund of NBFIs for procurement of capital machineries, which increases their cost of production. NBFIs also borrow funds from international sources at LIBOR plus 3%. For availing of international funds, NBFIs need to obtain permission from Board of Investment (BOI) and BB. This is a lengthy and complicated procedure·

Recommendations

Short Term

BB should extend necessary guidelines and assistance to NBFIs to reduce their lending rates in order to provide lending to the SMEs at a lower rate. With this end in view, BB and BOI should simplify the existing system of approving borrowing by the NBFI from the foreign sources. Besides, NBFIs should also have access to local sources of financing.

6.1.3 Some other major sector-specific issues

Issue: Bonded Warehouse operating hours for jewellery

The gold imported through L/C (direct import) is stored in the bonded locker under joint custody of the manufacturer and the Customs authority. The Customs authority opens the bonded locker at 9 A.M. when workers are allowed to take the gold out and start work under the supervision of Customs authority. At 5 P.M., the stock of gold is stored again under joint custody.

Because the artisans are paid on a piece rate basis, they often require to work till late hours for completion of the task assigned to them. Besides, during shipment time, the exporters need to keep the factory open even for 24 hours to complete the export order.

Recommendations

Short Term

The Customs authority should accommodate flexible working hours for the jewellery artisans as in the case of the garment industry. It may be mentioned here that the garments industry, which also operates under bonded warehouse, is not subject to rigid 9.00 A.M - 5.00 P.M working hour.

Issue: Central Bonded Warehouse for RMG exporters

Representatives from BGMEA demanded for setting up of a central bonded warehouse. They claimed that this would reduce the lead-time and make the RMG *sector more competitive in the international market, but they did not give any mechanism for setting up and working of a central bonded warehouse. The proposal however, received criticism from representatives of the BTMA as each individual RMG exporter is enjoying bonded warehouse facilities and the central bonded warehouse will only import material when there is a bulk order from a number of exporters. Under such a system, the RMG exporters will place order to the central bonded warehouse to import fabrics against their Master L/C or export order. But it will not be profitable for the central bonded warehouse to import fabric/yarn/accessories for any single RMG exporter. This system may increase the lead-time rather than reducing it.*

Recommendations

Short Term

An in-depth cost-benefit analysis needs to be conducted on central bonded warehouse and how it will impact the volume of export, lead time, international competitiveness of RMG exporters in Bangladesh and the local textile industries.

Issue: Value addition by the customs authority

Under the existing rule, there has to be a 10% value addition on the exportable items of ornament whereas the actual value addition does not exceed 8%. The fixed value addition of 10% inflates price of the Bangladeshi ornaments. Recently the exporters' association made a representation for reduction of the value addition to 8%. The authorities have agreed to the proposal although but there is no Statutory Regulatory Order (SRO) as yet.

Recommendations

Short Term

Value addition should be reduced to 8% to make Bangladeshi jewellery more competitive in the international market. Furthermore, it is also recommended that the government should grant cash incentive of 50% on value addition to enhance competitiveness of the industry.

Issue : Financial support for setting up backward linkage industries

In the post MFA context, there is an urgent need for establishing backward linkage industries as Bangladesh will face stiff competition in the global market from 2005, when present trade protections/barriers will be abolished. There is apparently a conflict between the yarn/cloth producers with the garments manufacturers. Garments manufacturers are supporting the open market mechanism for importing/procuring yarn rather than for setting backward linkage industries. On the other hand the yarn and cloth producers are lobbying for setting up backward linkage industries.

Recommendations

Short Term

The banks may give financial support to the entrepreneurs of good track record coming forward to set up backward linkage industries.

Medium Term

An in-depth study on setting up of backward linkage industries may be undertaken. The garment industry will prefer to purchase raw materials from other countries if our backward linkage industries fail to offer quality products at an internationally competitive price. Therefore, the conflict between the two groups of exporters should be resolved immediately so that Bangladesh can cope with post MFA situation.

Issue: Valuation of Software

BASIS and its members observed that there is no standard mechanism or norms for valuation of software in Bangladesh, which deprives them from borrowing from financial institutions.

Recommendations

Short Term

Software valuation mechanism may be developed and finalized on the basis of:

(a) the recommendations of Bangladesh Bank's Committee and comments of CBs in this report.

(b) Software valuation mechanisms which already exist in Sonali Bank, Janata Bank and EPB.

Issue: Repeated financing of software

Software products can be sold several times after customisation. It is well recognized that ICT finance is quite different from financing RMG or vegetables for instance. But the financing banks do not consider this special feature of the industry for repeated financing, particularly to the SMEs.

Recommendations

Commercial banks should extend finance for customisation of software against irrevocable work/export order even if the software was financed previously. Bangladesh Bank should issue clear guidelines to the financing banks. Besides, it should also monitor regularly whether these guidelines are followed by the banks or not.

I***ssue: High interest rate on outstanding loans***

Eid Advance is allowed during Qurbani which is adjustable within the investment cycle of 270 days. Almost every tannery[55] has to sell out the cycle closing stock at a forced sale value to avail the next Eid advance which results in trade loss. The leather industries are allowed Export Cash Credit –ECC(Hypothecation), ECC (Pledge) and ECC (qurbani) facilities at 9% rate of interest for a period of 270 days. However, after expiry of credit line, interest is charged @ 14%.

Recommendations

<u>*Short Term*</u>

The value of carried over stock and the current year's finance taken together should be considered as Eid advance. Financing banks should charge interest @ 4% and Bangladesh Bank should provide them refinance @ 2%.

Issue : Restriction on remittance of registration fees in FCY

Cost of registration for each pharmaceutical product in different countries varies from US$10,000 to US$50,000. In Russia, each product registration costs US$50,000. It is extremely difficult to obtain this foreign currency through official channels before export begins. Moreover, remittance of registration fee in FCY is cumbersome and lengthy. A typical pharmaceutical firm has to spend between US $6000 and US $10,000 per month to maintain a marketing office abroad. But Bangladesh Bank allows remittance of only US $2,500 per month for this purpose.

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[55] The country's leather industry has been passing through a bad patch for the last two consecutive fiscal years as export earnings from the sector dropped by a quarter from its peak in 2000-01.Bangladesh has 206 tanneries, 83 of them are sick due to huge overdue bank loans. They have a total production of about 400 million square feet of wet blue, 300 million square feet crust leather and 130 million square feet finished leather per year. Bangladesh produces about 223.71 million square feet leather including 117.54 million square feet crust leather for export and 106.17 million square feet various type of finished leather for export and local consumption *(source: Bangladesh Tanners Association)*.

Recommendations

<u>*Short Term*</u>

Remittance of foreign currency for registration of products to the importing countries should be simplified and rationalized for which Bangladesh Bank/EPB should:

I. Prepare a list of exporters and their items of export.

II. Prepare a list of the importing countries and the amount of registration fees required by them.

III. Set a time frame for settling the remittance procedure.

Bangladesh Bank should accord permission for remittance of registration of items and maintenance of office on the basis of the above information/export performance within the set time frame.

Issue: Fraudulent use of Export Form (EXP) for agro-based products

There is a wide gap between the value of export proceeds realised and actual value of export. This is due to a large quantity of export being made against fake EXP. Interview with the financing bank reveals that their weakness in the controlling system has many loopholes to make fraudulent use of EXP, resulting in drainage of foreign exchange. In a meeting of the commercial banks, Bangladesh Bank and exporters of fruits & vegetables, it was decided to take corrective steps to stop fraudulent use of EXP. Accordingly, Bangladesh Bank issued a circular instructing the financing banks to implement the steps stipulated in the circular.[56]

Recommendations

<u>Short Term</u>

Bangladesh Bank should monitor and follow up the implementation of the decision taken in the meeting of the concerned parties involved in export of vegetables, which was subsequently circulated by BB to the CBs.

Issue: Local L/C for components

Bi-cycle composition requires various types of small parts, which are imported/procured under bonded warehouse facility. The exporters assemble the parts under the brand name of the parent concern. Customs insist upon opening of L/C for procurement of components from their allied concerns providing forward linkage. Each allied concern is a limited company and they partially procure

56 Bangladesh Bank, *Foreign Exchange Policy Department Letter No. 500A/2002-3093*.

components locally and partially through import from abroad. When the allied units supply components from the bonded warehouse, Customs Authority insists for L/C from the parent company. The problems associated with opening L/C are:

- Additional bank charge for opening six L/Cs.
- Preparation of 6 sets of export documents by specialised staff. Such L/C requires signing of a minimum of 21 papers for the opening bank and others institutions concerned.

Recommendations

Customs authority may allow delivery of parts and components manufactured/imported/ procured by the allied concerns if the customs officer in the bonded warehouse of the parent company ensures full utilization of the components delivered by the allied concerns. Under the proposed system, non-export and non-payment of duty will disqualify the parent/ manufacturing company to get subsequent delivery.

6.2 Issues related to other sources of finance

This study also identifies other sources of finance available for exporters. Some of the major issues and recommendations are discussed below:

Issue: Factoring Service

Factoring is a device of transforming non-performing or inactive assets into productive assets by selling book-debts to a company that specializes in book-debt collection and administration. Since Bangladesh is a developing country, there is good potential of launching such factoring services. However, there is no baseline information on factoring services in Bangladesh. There are no factoring companies or banks for taking over non-performing assets of the commercial banks.

Recommendations

<u>Short Term</u>

The following steps could be considered to introduce factoring services in our country:

1. BB may conduct a comprehensive study taking into account the various aspects of factoring services such as scope, procedure, organization, legal issues, funding, pricing, accounting, credit rating and managerial issues.
2. BB should facilitate establishment of Factoring Companies/Banks for taking

over non-performing assets of the banks and providing services to the business enterprises through collection of book-debts (receivables).

Issue: Counter -Trade

Bangladesh has undertaken different initiatives to start counter trade with different countries. The objective of starting counter-trade in Bangladesh is to reduce trade deficit and to reduce pressure on foreign currency reserve.

In case of counter-trade, both the countries have to maintain non-convertible US Dollar account. In every three months, accounts of both the countries will be settled.

Recommendations

The committee on counter-trade should make its recommendations public immediately so that GOB can start negotiating with potential partners like India, Philippines and others.

Issue: Stock Exchanges

Dhaka Stock Exchange and Chittagong Stock Exchange are non-profit organizations. They work as intermediaries between investors and companies. They help the companies to raise capital through initial public offering. Since the stock exchanges are not lending or borrowing institutions, DSE and CSE do not have any provision to maintain liquidity.

Recommendations

Short Term

Although the stock exchanges do not have any scope to extend special help to the exporters, they can certainly attract good companies to list with them to help raise fund from the shareholders.

Issue: EPB's service delivery

Many exporters and trade association complained that they face serious problems in getting timely delivery of the Certificate of Origin from the EPB for which sometimes there is delay in submission of export document to banks. They also complained that the officials of EPB take speed money for issuing certificates.

Recommendations

<u>*Short Term*</u>

With regards to complaint on delay in issuing Certificate of Origin, EPB should set a time frame for the issuance of the certificates and depute a senior executive to make regular monitoring. The complaint of taking "speed money" should be investigated into and appropriate action should be taken.

Issue: Venture Capital

Equity capital in young and risky business is known as venture capital.[57] BB has already introduced EEF in order to support the risky new projects. Grameen Bank has already started venture capital financing despite some limitations and Basic Bank and VANIK have taken some initiatives but equity capital financing has not started as yet. Bangladesh Bank is currently working on Credit Bridge and stand-by facilities

Recommendations

<u>Short Term</u>

1. Bangladesh Bank should accelerate the process.
2. SRO should be issued for withdrawal of Stamp duty on conveyance.
3. Introduce Secondary Bond Market.
4. SRO for VAT on Special Purpose Vehicle which has been issued should be disseminated to potential investors.

7. Conclusions

There is general consensus in the government, the banking sector, and the market that trade facilitation has a positive bearing on economic growth and on development in general. It is central to generating employment, promoting investment, upgrading technology, diversifying and strengthening the industrial base, developing infrastructure and aiding closer international economic linkage. There is therefore, a shared commitment of all stakeholders to ensuring a level playing field for trade, specially export. This is reflected in the extensive spread

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57 Specialist venture capital firms, wealthy individuals, and specialist firms and investment institutions such as pension funds provide it. The venture capitalist earns his/her return primarily in the form of capital gain. The main attributes of venture capital are equity participation, long-term investment, and participation of venture capitalist in management.

of services that are geared to export promotion. This study provides a broad overview of this spread. The study goes on to identify the deficiencies that characterize the existing portfolio of banking and export financing services. The study shows that these issues that affect efficiency range from structural problems (banks and FIs) to policy incongruities to lack of proper dissemination of information as well as the lack of financial discipline as part of the prevailing corporate culture.

The paper recommends specific remedies, and where necessary, also addresses the contributing factors behind such inefficiencies.

Paradigms in trade continue to evolve and it is essential to look beyond current trends and parameters for continuously upgrading the efficiency and effectiveness of export financing. Arrangements such as counter trade would be attractive to smaller economies due to its potential to reduce foreign currency dependency. One other issue that would have to be examined in a broad frame is the question of regional cumulation.

As mentioned before, there is a duality in export financing that stems from the competing claims of effective export facilitation on one hand and financial discipline on the other. The efficiency and effectiveness of financial institutions rest on how responsive and sensitive they are to the needs of exporters. The FIs have to restructure themselves more vigorously to face up to the challenge of MFA phase out. The efficacy of response of FIs again, is affected by the financial responsibility shown by exporters. This critical linkage would provide an important direction for manipulating both short-term and long-term variables to enhance the efficiency and effectiveness of banks and financial institutions. This linkage could perhaps, present a major challenge for policy makers to identify a Pareto optimal level which is firm on regulations and flexible on facilitating increased and diversified export.

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