

EXECUTIVE SUMMARY

Development Challenges

Bangladesh has made significant progress in improving social conditions, particularly in the fields of health, education and population. At the same time, it has achieved a certain degree of macroeconomic stability. However, Bangladesh remains one of the poorest countries in the world with a per capita income of approximately \$337 in 1998 and nearly one half of the population living below the poverty line.

Poverty reduction is the central thrust of the development agenda of the Government and all the major funding agencies in Bangladesh, including the Bank. Despite efforts by the Government, external funding agencies, and the world's most active nongovernment organizations (NGOs) and microcredit movement, the pace of poverty reduction has been very slow. Even this slow pace may not be sustainable as the possibility of reversal remains high. Any bad harvest or sudden flooding, such as the one that happened recently, can easily reverse the trend.

Slow economic growth is one of the primary reasons for the stagnation of poverty reduction. The economy has suffered from low annual gross domestic product growth of 4 percent for more than a decade. This was caused by weakness of public policies and institutions, poor governance, severe bottlenecks in infrastructure and finance, and slow progress in private sector development. This growth rate could only marginally match the population growth rate and some income growth of the nonpoor. Bangladesh needs an annual growth rate of at least 6 to 7 percent to make a substantial impact on poverty. Furthermore, rising inequality has reduced the impact of poverty reduction. It is estimated that one fifth to one third of the potential poverty reduction resulting from growth may have been lost because of higher inequality. Slow poverty reduction has also resulted from the low level of human development and the poor environment.

Lessons Learned

Compared with its operations in the 1970s and 1980s, the Bank's assistance to Bangladesh in the 1990s has been more relevant to the strategic objective of poverty reduction and more effective in terms of project implementation. More emphasis has been placed on structural reforms, capacity building, and institutional development. Partnerships with the Government, NGOs, and civil society have also been strengthened.

Nevertheless, one of the major problems has been the coverage of too many sectors and subsectors: Bank operations have so far reached almost 30 sectors/subsectors in Bangladesh. This has tended to weaken the impact of Bank interventions. Given limited resources, this approach has resulted in the Bank having once-only interventions or a very long break between two interventions in a sector or subsector. Such projects usually encounter more problems since the reform and institutional changes proposed are often not sustainable as the Bank loses leverage quickly after leaving the sector. More importantly, this approach makes it difficult to discern a strong logical and strategic pattern for systematic reforms and institutional buildup, as any meaningful reform in Bangladesh needs a long-term and continuing effort by both the Government and the funding agency.

New Strategy

Consistent with the Government's development strategy and Bank's Medium-Term Strategic Framework, the Bank's overall strategic objective in Bangladesh will be poverty reduction. This will be achieved by promoting faster economic growth, creating better development opportunities for the poor, improving human development, and protecting the environment. The Bank's operational priorities will cover the following four areas.

Promoting faster private sector-led economic growth. One of the core strategies for supporting poverty reduction is to promote private sector-led economic growth. The Bank will assist the Government to speed up policy reform and create a level playing field conducive to private sector development. The Bank will focus on providing assistance to improve infrastructure and the financial system, which are the main constraints for private sector development. Furthermore, the Bank will support private sector development from its private and public sector operations. The Bank will also provide assistance to promote subregional cooperation.

Creating better development opportunities for the poor. The Bank will assist the Government to invest, and encourage the private sector to participate, in rural development, including rural roads, small irrigation projects, flood protection, microfinance, and crop/agro business credit. In the urban area, the Bank's intervention will focus on the development of small and secondary towns. It is expected that these activities will have a positive impact on the poor and income distribution.

Improving human development. The Bank's operational priority in the social sector is mainly in areas that can increase the productivity of the poor including primary health, and primary, secondary, and nonformal education. As in the past, special efforts will be made to increase equitable access of women and disadvantaged people to social services.

Improving and protecting the environment. The Bank's operational thrust under its environment program over the medium term will be to address environmental concerns in all Bank projects. Capacity building for environmental planning, management, legislation, and regulation will be emphasized. Particular attention will be placed on improving the urban environment and addressing poverty-related environmental issues.

New Approach

The key features of this new country operational strategy are its sharper focus and emphasis on long-term involvement. Past experience has shown that the prospects for

reducing poverty and development in the four priority areas will not improve significantly unless structural reforms are deepened and governance is strengthened. Such reforms are not a one-time effort, but a series of interventions undertaken on a long-term, coherent basis. Therefore, to promote sustainable policy and institutional changes, the Bank should consider providing successive interventions to a sector or subsector over a longer time horizon than the current strategy period of three to five years. Accordingly, the policy and institutional reforms as well as physical investment in the sector and subsector can be divided into several phases and be tackled by each project. This requires that Bank operations be focused on fewer sectors than is currently the case with the very wide range of interventions.

Based on medium-term resource projections, it is proposed that the Bank's future involvement be reduced from 30 to at most 15 subsectors. These subsectors should have the following characteristics: (i) there is substantial scope for policy and institutional reforms in the areas of involvement and clear signs of the Government's firm commitment to these reforms; (ii) the Bank has comparative advantages in the area; (iii) the Bank has played or will play an important role, preferably the leading role, in the area; (iv) the Bank's involvement will play a critical catalytic role in bringing private sector financing or cofinancing; and (v) there is a clear division of labor with other funding agencies.

To address the governance issue, the Bank will assist the Government in developing core administration capacity at both the central and local levels and in undertaking anticorruption efforts. The Bank will also help to strengthen the Government's development partnership with NGOs, the private sector, and other civil society.

Risks and Measures to Address Them

Political factors constitute the main risks for the successful implementation of the proposed country operational strategy. As the general election comes closer, political unrest is expected to heat up. The Government may face some difficulties in pursuing politically sensitive reforms and institutional changes that could be

controversial. The pace of some ongoing reforms could also slow down. To minimize these risks, the Bank's approach during this period could (i) incorporate this risk in project design and move politically sensitive components of the reforms to the next phase of sector intervention if it is possible; (ii) stand firm on project covenants when timely implementation is absolutely important and any delay could jeopardize the entire reform program; (iii) use the opportunity to do more sector studies and prepare for the opportunity of the new round of reforms after the election; and (iv) assist civil society to support the Government's reform efforts.

While the current East and Southeast Asian financial crisis has not yet had any significant negative impact on the Bangladesh economy, the country is still very vulnerable to the old type of crises caused mainly by the weak economic fundamentals including a large nonperforming portfolio in the banking sector, low foreign reserves, and poor fiscal revenue collection. The country could also be affected if the major countries in the region experience financial crisis. The Bank could help the Government to strengthen macroeconomic monitoring and supervision capacity, particularly in the areas of managing statistics of macroeconomic indicators, capital markets, and balance of payments. The Bank could also assist the Government to actively participate in regional cooperation and coordination of macroeconomic policy with neighboring countries to minimize contagion effects.

Based on the Bank's new country classification, Bangladesh is classified as a class B country with access to the Asian Development Fund and limited amounts of ordinary capital

resources (OCR) lending. Although the country is below the per capita gross national product cutoff, its debt repayment capacity could allow limited borrowing from OCR. Some access to OCR could boost resource flows to the sectors that have strong revenue and foreign exchange generation or substitution capacity such as power, gas, ports, and certain areas in finance and industries. However, the Bank should be extremely cautious not to jeopardize the country's debt payment capacity. A special assessment should be made for each OCR loan, and the Bank should monitor the country's debt payment capacity periodically. OCR lending should be suspended if the debt service ratio increases sharply or any other debt indicator deteriorates substantially.

As the Bank shifts its role from a project financing institution to a broad-based development institution and the Bank operations increasingly involve core policy reforms and institutional changes, the project failure rate in terms of traditional standards could increase. The Bank should put less emphasis on traditional evaluation indicators such as annual lending level, disbursement, loan delivery, economic and financial internal rate of return, etc. and put more emphasis on overall development impact, performance of policy reforms, and institutional changes. To maintain project quality and strengthen the enforcement of reforms, the Bank should implement a more flexible exit policy to slow down the project process or even temporarily walk away, if necessary, from projects that show slow progress of reforms. The Bank should also be prepared to provide more staff time and efforts for sector study, and project preparation and administration.

I. BACKGROUND

1. Bangladesh is one of the poorest countries in the world with a per capita income of approximately \$337 in 1998. High population density, poor resource management, and numerous natural disasters coupled with frequent political turmoil have affected the economic and social development of the country over the past two decades. Economic growth has remained low and poverty is prevalent among both rural and urban households. The country is ranked 147th of 174 countries in the 1998 Human Development Report.

2. In the 1970s and 1980s, the Bangladesh economy was dominated by the public sector and depended heavily on foreign aid. Economic policy was more favorable to State-owned enterprises (SOEs) and tariff and nontariff barriers were high. While there were several attempts to address those macroeconomic imbalances, reform processes were frequently interrupted by political disturbances.

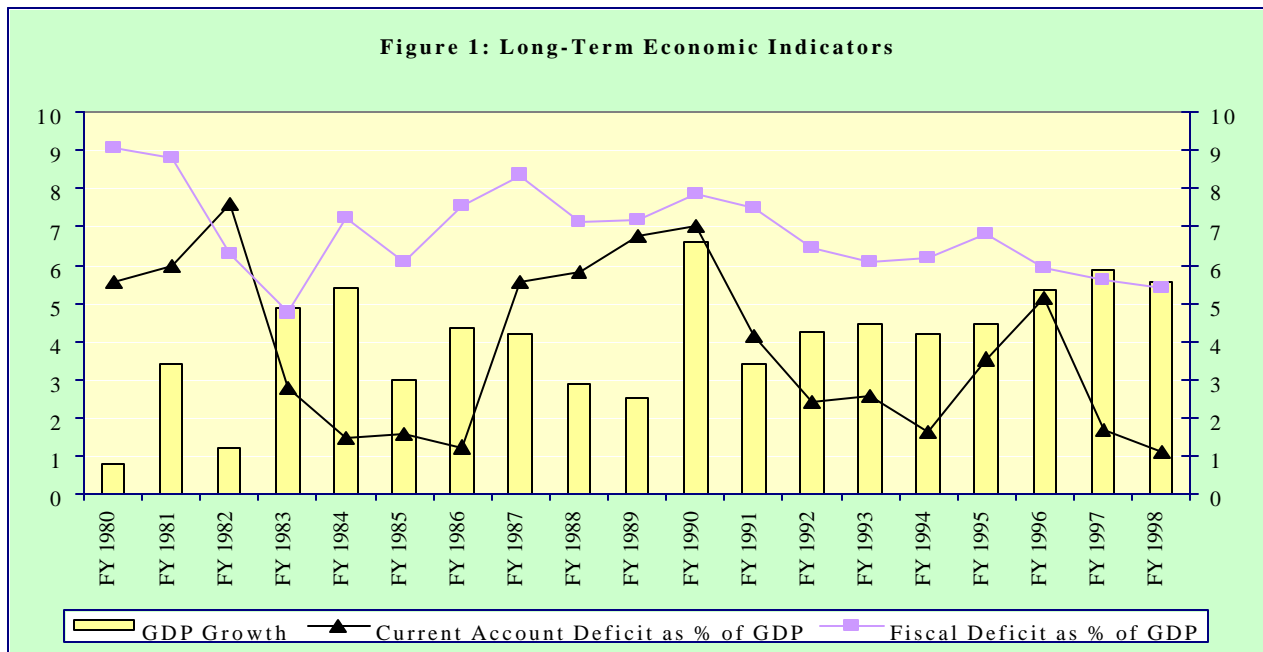
3. Since the early 1990s, the country has been endeavoring to carry out a comprehensive set of structural reforms aimed at liberalizing the foreign trade and exchange rate regimes, restructuring the industry sector, strengthening fiscal and monetary management, encouraging private sector investment, and privatizing SOEs. As a result, a degree of macroeconomic stability has been achieved, and the country has made some improvements in the area of social development (Figure 1). Significant progress has also been made in the country's social conditions. Enrollment in primary and secondary education increased substantially, especially for girls. Improvement is also notable in the reduction of the population growth rate and total fertility rate, and increase in the contraceptive prevalence rate.

4. Bangladesh's primary challenges will continue to be progressive reduction of poverty incidence and improvement of living conditions. To achieve these,

there is a need to accelerate gross domestic product (GDP) growth, and Bank can play an important role in helping the enhance the provision of social services and make them more accessible to the poor and disadvantaged segments of the population. As in the past, development partners such as the Bank can play an important role in helping the country to achieve its long-term development goals.

5. Since the previous country operational strategy for Bangladesh was approved by the Board in 1993, the country's political and economic environment has undergone considerable change. Economic reform and deregulation in the early 1990s led to a more stable macroeconomic environment compared with that in the 1970s and 1980s. However, this sound development was interrupted in 1994/95 by mounting inflationary pressures and deteriorating fiscal and current account balances. The reversal in economic trends was brought about partly by prolonged political unrest during the period and partly by the slower implementation of structural reforms.

6. With the return of political stability in 1996, the economy bounced back to a more favorable path. GDP growth rate improved substantially reaching 5.4 percent in FY1997 and 5.2 percent in FY1998, much higher than the average growth rates in the first half of the 1990s. More prudent macroeconomic management, together with generally better aggregate supply conditions, particularly in foodgrains, resulted in an improved fiscal and external account situation. Fiscal reforms broadened the coverage of the value-added tax. Meanwhile, the Government's current expenditure was largely under control. As a result, the country was able to increase its financial share of the annual development program from almost nil in FY1990 to over 45 percent in FY1997. There was also significant progress in opening up the infrastructure and energy sectors to private investment in recent years.



7. The impact of the recent turbulence in the East and Southeast Asian financial markets on the Bangladesh economy has so far been limited. Nonconvertibility of the capital account and the virtual absence of foreign portfolio investments has largely insulated the economy from external attack. The relatively low current account deficit and light external debt burden have also protected the economy from the crisis in other markets.

8. In spite of these improvements, macroeconomic stability is still fragile. Over the past two years the fiscal deficit remained as high as 5 percent of GDP, and foreign exchange reserves were persistently below three months of imports. The pace of structural reforms remained slow in many areas critical for growth and private investor development. Supply shortages were felt in almost all key infrastructure sectors. Despite the Government's efforts to attract foreign investment, the achievements so far have been limited. There is an increasing sense of frustration that many reform actions, which could lead Bangladesh into a much higher growth path, are not being taken because of opposition from powerful vested interests. Corruption, delays in taking action against bank defaulters, little progress in privatization, and stagnant public administration reform all contribute to the general sense of disappointment and pessimism.

9. Recently, Bangladesh was affected by a devastating flood. The continuous and heavy monsoon rains in and outside the country and tidal surge in the Bay of Bengal caused excessive flooding across 51 of the 64 districts. The duration of this flood has surpassed all previous records, including that of 1988.

10. The extensive flood destabilized macroeconomic performance, which had fared well over the past years. The GDP growth rate for FY1999 is estimated at only 4.8 percent from the 5-6 percent range of the past three years. The flood outcome will further strain the balance of payments situation, and the current account deficit remained as high as 2.1 percent of GDP during FY1999. Flood-induced expenditure, i.e., additional foodgrain imports and post-flood rehabilitation spending, and shortfalls in current revenue collection due to the disruption of economic activities are expected to lead to budget deficits by 1-1.5 percentage of GDP.

II. DEVELOPMENT ISSUES AND OUTLOOK

A. Slow Progress in Poverty Reduction

11. Poverty reduction is the central thrust of the development agenda of the Government,

nongovernment organizations (NGOs), and all several decades of effort, poverty has declined substantially in both rural and urban areas. However, compared with other countries, the pace of progress in reducing poverty has remained very slow.

12. A recent household expenditure survey supported by the Bank reveals that absolute poverty, measured by the basic dietary requirement of 2,122 calories intake per day, was reduced from 55.7 percent of the population in FY1986 to 47.5 percent in FY1996. Hard-core poverty, measured by 1,805 calories intake per day, dropped from 26.9 percent in 1985/86 to 25.1 percent in FY1996¹ (Table 1).

This improvement is mainly attributable to the improved availability of foodgrains and widespread antipoverty programs organized by the Government, NGOs, and external funding agencies. However, the improvements slowed down in the early 1990s reflecting the slow pace of economic growth and increased inequality. The rate of absolute poverty has remained virtually unchanged from FY1992 to FY1996, although some improvement was recorded among the hard-core poor. Urban poverty, in fact, deteriorated partly because of substantial rural-to-urban migration—which is one of the highest rates in the world.

Table 1: Incidence of Poverty

Survey Year ^b	Number and Percent Of Population Below the Poverty Line Indicator ^a					
	National		Rural		Urban	
	Number (millions)	Percent of Population	Number (millions)	Percent of Population	Number (millions)	Percent of Population
Poverty Line-1: Absolute Poverty						
1996	55.3	47.5	45.7	47.1	9.6	49.7
1992	51.6	47.5	44.8	47.6	6.8	46.7
1989	49.7	47.8	43.4	47.8	6.3	47.6
1986	55.3	55.7	47.4	54.7	7.9	62.6
1984	58.4	62.6	51.1	61.9	7.3	67.7
Poverty Line-2: Hard-Core Poverty						
1996	29.1	25.1	23.9	24.6	5.2	27.3
1992	30.4	28.0	26.6	28.3	3.8	26.3
1989	29.5	28.4	26.0	28.6	3.5	26.4
1986	26.7	26.9	22.8	26.3	3.9	30.7
1984	34.3	36.8	30.2	36.7	4.8	37.1

^a The Poverty line for absolute and hard-core poverty in 1983/1984 and 1985/1986 were estimated based on 2,200 and 1,800 kilo calories respectively. Figures for earlier years are based on Bangladesh Bureau of Statistics. 1992. *Household Expenditure Survey 1991/92*. Dhaka.

^b Indicates the year in which the survey was completed.

13. The household expenditure survey also reveals that rising inequality has reduced the impact of poverty reduction. Between FY1984 and FY1992, the Gini coefficient for income distribution remained in the range of 0.36-0.39. However, it rose from 0.388 in FY1992 to 0.432 in FY1996. It is estimated that one fifth to one third of the potential poverty reduction resulting from growth may have been lost

because of higher inequality.

14. In the long run, the challenge of poverty is indeed enormous. Despite all the efforts during the past decade by the Government, external funding agencies, and the world's most active NGOs, the incidence of national poverty has declined by only 8 percentage points since FY1986. This implies an annual rate of poverty reduction of less than

¹ The Bangladesh Bureau of Statistics (BBS) published another set of poverty data based on the cost of basic needs method in the 1996 household expenditure survey. This set of data shows that the poverty level is much lower in urban areas than in the rural areas. The upper poverty incidence in national, rural, and urban areas is 53.1, 56.7, and 35 percent. The lower poverty incidence in national, rural, and urban areas is 35.6, 39.8, and 14.3 percent.

1 percent. Even this slow pace may not be sustainable, as the possibility of reversal remains high. Any bad harvest or sudden flooding, such as the most recent, can easily subvert the trend.

15. Slow economic growth and rising income inequality are the primary reasons for the slow progress in poverty reduction. Slow poverty reduction has also been the result of the low level of human development and the poor environment.

B. Slow Economic Growth

16. The economy has suffered from a low GDP growth rate of 4 percent for a decade. Only in the past three years has the rate increased to above 5 percent. The slow growth is only marginally

matching population growth and income growth of the nonpoor. It has had little benefit for the poor and hard-core poor. Many studies show that to make a substantial impact on poverty, Bangladesh needs growth rate of at least 7 percent.

17. Recent debate on the puzzle of the success of microcredit but limited overall impact of the microfinance program on the incidence of poverty reveals that even in the case of Bangladesh, where NGOs and microcredit are the most vibrant in the world, direct poverty intervention efforts will not necessarily have a significant impact on poverty reduction without increased economic growth¹ (Box 1). In other words, this confirms that fast economic growth with equality is a necessary condition for any significant poverty reduction in the country.

Box 1: Limited Overall Poverty Impact of the Microcredit Program in Bangladesh

The central puzzle of the empirical findings of the poverty program in Bangladesh is the mismatch between the success of microcredit and its relatively limited overall impact on poverty reduction. Thanks to many nongovernment organizations and the Government's poverty reduction programs, by the end of 1997 microcredit had reached about 8 million households or about half the rural poor households. The combined volume of microcredit of Grameen Bank and BRAC alone has exceeded the aggregate rural lending in the country. Almost all evaluations of microcredit schemes have found that the programs are indeed poverty reducing as measured by various methodologies.

Furthermore, the expansion of NGO programs in rural areas was accompanied by favorable shifts in public spending. One estimate was that the aggregate allocation of budgetary resources, which have either a direct or indirect bearing on rural poverty, had gone up substantially since the early 1980s from 30 to 50 percent by 1994/1995.

Despite all of the effort, however, the statistics show that the pace of poverty reduction at the macro level was minimal. From the late 1980s and mid-1990s, when the microcredit program and other poverty reduction programs became increasingly dominant, rural poverty as a percentage of the rural population remained unchanged and even increased slightly in absolute terms. There seems to be an inconsistency between the increased inputs that went into the programs and the unsatisfactory outcome of actual poverty reduction.

¹ One explanation of this puzzle is that since the rural poor population increases by about 1 million a year, this implies that rural poverty declined by about 0.8 million annually during the past few years. This figure alone is a big achievement for the microcredit program. Some scholars also argue that the social impacts of microcredit are more significant than the impact of income. In fact, all of the social indicators of the country in the past five to ten years have improved significantly. In this respect, the microcredit program has had a significant impact on the poor.

18. Slow economic growth is caused mainly by weaknesses in macroeconomic management, a low savings and investment rate, infrastructure bottlenecks, and slow progress in private sector development.

19. Weaknesses in Macroeconomic Management.

Strong economic growth depends on sound macroeconomic management and faster pace of reforms. In the fiscal area, raising Bangladesh's low tax and nontax revenue collection through better coverage and administration is the top priority of fiscal management. The ratio of fiscal revenue to GDP is one of the lowest among Asian countries. Given the current declining trend in the availability of foreign aid, it will be more important for the country to mobilize domestic resources. To keep the fiscal deficit at a manageable level, the ratio of revenue to GDP needs to be increased by half a percent per year as occurred in the early 1990s. On the monetary front, the challenge is to implement policy that does not support excess demand pressures and maintains inflation at a low level.

20. In spite of being considerably downsized during the past decade, SOEs still play an important role in the economy. In FY1997, total direct losses by SOEs are estimated to exceed Tk12 billion (about 1 percent of GDP). The persistent SOE losses were accommodated by borrowing from national commercial banks. This resulted in the crowding out of private borrowing and created huge bad loans in the banking system. It is estimated that the cost to maintain one job in an SOE per year is 15 to 17 times the average wage of a worker in a private garment factory. In 1993, a comprehensive privatization policy was adopted. However, by June 1998, fewer than 20 out of more than 200 SOEs had actually been privatized.

21. Low Savings and Investment Rate. Another key challenge facing the country is how to mobilize more domestic resources for development. The domestic savings and investment rate in Bangladesh is one of the lowest among developing countries.¹ Growth requires substantial increases in saving and investment, which in turn depend on the timely implementation of comprehensive financial sector reforms. The financial system in Bangladesh is characterized by inefficiency, poor quality of intermediation, and lack of accountability. A large

proportion of the portfolio of commercial banks is classified as nonperforming. Supervision and regulation by the Central Bank are lax, particularly in enforcement. The high loan defaults increase the costs of banking and penalize private investors. Furthermore, private enterprises have difficulty finding long-term financing resources. Commercial banks, which have to confront the problem of bad loans, have largely stopped their long-term lending. Development finance institutions, mostly owned by the Government, are also facing serious financial problems. Their new lending has been virtually frozen for many years.

22. Infrastructure Bottlenecks. The shortage of infrastructure is another major bottleneck for fast economic growth and poverty reduction. Supply shortages have been felt in almost all key infrastructure subsectors. For instance, per capita consumption of electric power in the country is extremely low with power available only to 15 percent of the total population. The energy sector has suffered considerably from low efficiency and huge system losses.

23. In the transport sector, the underdeveloped and poorly integrated transport system is hampering private sector development and foreign investment. The port system is the most critical bottleneck. It is estimated that the cost of moving one container through a port in Bangladesh is about three times higher than that in Colombo and two times higher than in Bangkok. The capacity of the major ports is heavily constrained by berthing shortages, outdated equipment, and labor problems. The road network is generally in poor condition and does not satisfactorily meet present traffic requirements.

24. The Government recognizes that these problems cannot be solved by relying only on public investment and has taken concrete steps to involve the private sector. In 1993, the Government introduced a new petroleum policy to encourage private sector participation in gas exploration and production under production-sharing contracts. This policy has been generally successful and the flow of gas from the first round of contracts is expected shortly. The current gas shortages are expected to be overcome by 1999. At present the Government is negotiating contract awards under the second round of production-sharing contracts. In the power sector,

¹ A recent revision of the national account by Bangladesh Bureau of Statistics made an upward adjustment of savings and investment rates in Bangladesh. In FY1995 for example, the investment rate, gross national savings, and gross domestic savings rate are 21.4, 18.8, and 15.2, respectively, about 2-3 percentage points higher than the previous published data.

the private power generation policy was approved in October 1996. Power supply will be increased by 45 percent from the current installed capacity by the private sector through build-operate-own and build-operate-transfer arrangements over the next five years.

25. Slow Progress in Private Sector Development.

It has long been recognized that the private sector in Bangladesh has great potential to contribute to economic growth and poverty reduction. The Government has been pursuing policies in which the private sector the dominant role in the country's development efforts. The success of this policy is reflected in the sharp increase in the share of private sector investment in the economy, with private investment increasing from 5.8 percent of GDP in FY1991 to 10.9 percent in FY1997.

The impressive development of the ready-made garment industry in the past decade showed that with appropriate policy support, the private sector can make great contributions to the economy (Box 2).

26. While the country has made a good start on private sector development, there is still much room to reduce the bias against the private sector and improve incentives for the private sector participation development process. Currently, the expansion of private sector activities is adversely affected by the prevailing serious weaknesses of infrastructure particularly in ports and power. The private sector has also suffered considerably from the inadequacies of the banking system, development finance institutions, and the capital market.

Box 2: A Success Story – The Bangladesh Garments Industry

When the export-oriented garments industry made its debut in the early 1980s with only a few sewing machines, there was notable skepticism about its potential for success. This industry not only survived but also achieved more than 20 percent growth annually, reaching \$3.8 billion or 73 percent of total export earnings during FY1998. About 3,000 export-oriented garments factories are now providing job opportunities to over 1.5 million workers, 85 percent are women.

The success of the garments industry is a result of the favorable international and domestic business environment. Many buyers were attracted to Bangladesh not only by its low labor cost, but also by its favorable situation under the Multi-Fibre Agreement. Internally, the most important factors were the external financing through back-to-back letters of credit and provision of special bonded warehouses to access imports at international prices. In addition, the Government left the sector unregulated.

The boom in garments has also helped the development of other related industries. Presently, about 80 percent of accessories like buttons, elastic, collar bands, price tickets, zippers, clips, etc. are locally manufactured. There has also been some expansion of the capacity of the local dyeing, finishing, and textile mills. Locally produced handloom fabrics like Grameen check are used in the garments industry. Knitted and hosiery garments already have a strong history — or position because of accumulated experience in knit fabrics.

However, the development of the garment industry faces a number of challenges. The major problem is that with the gradual phasing out of the Multi-Fibre Agreement, Bangladesh will face tough international competition. Weakness in infrastructure is another major constraint. Power supply, air and sea port facilities, and other infrastructure are inadequate. Cheap labor will not be enough to compete in aggressive international markets. Establishment of backward linkages, diversification of product lines, development of infrastructure, and continued policy support are critically important for the future growth and sustainability of the country's garment industry.

27. Limited Inflows of Foreign Direct Investment. The long-term development prospects depend on the scale of foreign capital inflows, both official and private. Bangladesh has one of the most liberal trade and foreign payment regimes and provides the most favorable incentives to attract foreign investment in South Asia. Despite those efforts, the actual achievements have been very limited because of poor infrastructure, high transaction costs, and political uncertainties. There are now considerable prospects for attracting foreign direct investments (FDI). Several large-scale foreign investment projects are currently under negotiation in the power and gas subsectors. How this potential can be realized will depend on the improvement of the country's overall investment climate. In addition, these investments may not directly generate foreign exchange reserves at least in the short term. Unless the country can attract a large amount of export-oriented FDI or develop gas export schemes, the medium-term outlook for the balance of payments could worsen rather than improve.

C. Weak Governance

28. Poor governance and weak institutions are the most important development constraints. The Government's performance in providing key public services, such as law and order, judicial service, human resource development, rural infrastructure, and poverty reduction, is poor. Project failures, cost overruns and severe completion delays are common. The Government's inadequate capacity and ability to establish an effective enabling framework is undermining private sector development.

29. Meanwhile, the Government is involved in too many commercial activities that are often done better by the private sector. The public sector accounts for over a quarter of GDP, more than two thirds of industrial production and one fifth of the employees in the formal sector. SOEs have a dominant, and in many cases, monopoly role in utilities and key manufactures and inputs.

30. The poor public service reflects deep-rooted organizational and institutional problems including lack of transparency, weak monitoring and accountability, and monopolistic power of the government agencies. In the past, numerous attempts have been made to improve public administration, but the impacts are limited. There was a lack of a strong political commitment and strong leadership to champion the reforms. In addition, the reforms have not been fully appreciated and supported by the civil

servants who are responsible for implementing them. Finally, the reform design was often too comprehensive and did not have a realistic time frame for implementation.

D. Slow Progress in Social Development

31. Despite impressive gains over the past decade, human development in Bangladesh remains one of the lowest in the developing world. This low level of human development is constraining the graduation of the poor from poverty.

32. **Education.** Significant progress has been made in both primary and secondary education, especially with the substantial increase in the enrollment of girls. The Government has also considerably increased the allocation of public expenditure to education. However, the quality of education at all levels remains low and dropout rates remain high. About 15 percent of the 6-10 year age group, with the majority coming from the poorest communities, do not enter primary schools. Teachers are poorly trained, and teaching and learning materials are in short supply. The quality of education is becoming a more pressing issue. Institutional capacity to prepare, implement, and monitor programs and projects is weak at all levels.

33. **Population and Health.** During the 1990s, some progress has been made in controlling population growth and improving the health conditions of the people. The population growth rate has declined to 1.8 percent, the lowest rate of countries at a similar development level. Some improvements in the fertility and contraceptive prevalence rates has also been observed. The infant mortality rate declined from 92 to 78 per 1,000 live births from 1991 to 1996. Access to sanitary latrines increased from 9 percent in 1991 to 35.3 percent in 1996.

34. Despite these achievements, the level of health service remains inadequate: 60 percent of the population lack access to basic health, over 90 percent of children are malnourished. The maternal mortality rate at 449 per 1 million live births is one of the highest in the world. Government-provided health services play a minor role; only less than a quarter of the population uses these services.

35. To address these problems, the Government approved the Health and Population Sector Strategy last year, and an implementation plan was developed. It prescribes a work program for the

Ministry of Health and Family Welfare for the next five years and provides a comprehensive basis for investment by development partners led by the World Bank.

36. **Gender.** The Government has adopted policies and programs to narrow the gender gap, with the support for many development partners. As a result, some inequalities have been reduced, notably in education and health, as illustrated by rising school enrolment rate and declining fertility rates. Substantial progress has also been made in widening women's horizons through successful NGO-assisted microcredit schemes, and increased female participation in the labor force through self-employment or in garment manufacturing. However, social indicators show that women in Bangladesh are still much worse off than men. More attention should be paid to increasing women's rights and their role as active participants and agents in development.

E. Environment and Poverty

37. In Bangladesh, poverty and environmental degradation are closely linked. High population growth coupled with widespread poverty and nonsustainable production practices have brought about increasing pressures on the natural resource base. On one side, poverty acts as a catalyst to many forms of pollution and natural resource degradation. Poor people who often are landless and lack secure property rights increasingly rely and often overexploit common property resources such as land, forests, water resources, and fisheries. In addition, the poor, in their struggle for immediate survival, focus on the present more than on the future, and therefore have low willingness and ability to pay for environmental protection including water and soil conservation. The poor are also the main victims of environmental degradation, as they tend to live in areas more prone to environment-related disasters such as flooding and cyclones, or close to heavily polluting factories, dumps, and hazardous waste sites. Malnutrition and poor general health make them more vulnerable to infectious diseases and other health problems caused by poor sanitation, water and air pollution, and lack of solid waste management. In this context, while formulating and implementing policies and designing technical assistance (TA) and investment programs, it is important to recognize that the poor are also a key part of the solution to environmental degradation and not only a part of the problem.

38. New policies and a legal framework were formulated to deal with the situation. In August 1997, the country was provided with the required framework of rules and bylaws for the effective implementation of the 1995 Environment Protection Act. However, the authority to enforce the act, which was given to the Ministry of Environment and Forests, needs to be more effectively used. Two factors will now play a major role in environmental management in the future: (i) the degree of environmental commitment and ownership at the highest institutional and political levels; and (ii) the extent to which external assistance is streamlined and coordinated to effectively assist the country in achieving its main objectives.

F. Development Potential and Outlook

39. Economic growth during the past three years broke the 4 percent level that persisted over the last decade, although this rate is still insufficient for addressing the problems of poverty and development. The challenge for the Government is to accelerate economic growth while maintaining external and internal balance.

40. In the short term, the Government has to undertake a big effort on flood rehabilitation and reconstruction. The impact of the 1998 flood, which is one of the worst in the country's history, could be far-reaching and prolonged. GDP growth, the fiscal deficit, and inflation, as well as the balance of payments are expected to be adversely affected. The vulnerable population in the affected areas having lost their crops and personal assets are now homeless and face acute unemployment. It is expected that the poor will struggle for some time to recoup their losses. Many people who over the years crossed over the poverty line have been thrust back into poverty. The Government will need substantial resources over the next one or two years to recover from this devastating flood and to get its future growth plan back on track. The rehabilitation of damaged infrastructure will require huge amounts of external assistance.

41. In the medium term, the main task is to speed up the pace of economic reform and institutional development. The macroeconomic imbalances need to be corrected by keeping the fiscal deficit at a manageable level and pursuing appropriate monetary management to keep inflation under control. Tax coverage, administration, and

compliance need to be improved. Implementation of the annual development program has to be prioritized with emphasis on externally assisted projects, while pruning nonpriority locally funded projects. Structural reforms to remove distortions and tariff adjustments need to be put in place to attract private investment in these sectors.

42. Given the increasing scarcity of concessional assistance, domestic resource mobilization will become even more important. For this, financial sector reforms, both in the banking sector and capital markets, need to be accelerated. There should also be more intense effort to attract foreign investment.

43. The gas subsector is poised to make a major contribution to the development of Bangladesh (Box 3). There are real prospects that the gas reserves may become the driving force in the economic

development of the country by closing the energy supply demand gap and by providing additional foreign exchange earnings. They also offer a unique opportunity for attracting FDI thus freeing scarce concessional and public sector funds for investment in the social sectors and others that cannot attract funds. However, the foreign exchange required to service foreign investment in gas and power could create pressure on the foreign currency reserves of the country. Such investment will begin to repatriate foreign exchange as soon as projects go into production. Even the initial investment will not generate foreign exchange, as a large proportion of the investment will go to importation of equipment. To reduce this pressure and maximize the economic benefit of the gas reserves, the Government needs to put a gas utilization policy and plan in place to enable the gas producers to sell their gas and make a reasonable return on their investment.

Box 3: The Gas Subsector – Looking Up

The gas subsector is poised to open up immense economic opportunities for Bangladesh over the coming years. The optimism about discovering more gas reserves led to widespread interest in exploration activities across the country.

The share of natural gas of commercial energy consumed in the country increased from 35 percent in 1980 to about 70 percent in 1998. In 1993, the Government introduced a new petroleum policy to encourage private sector participation in petroleum exploration and production under production-sharing contracts. This policy has been generally successful, and the flow of gas from the first round of contracts has commenced. The current gas shortages are expected to be overcome by 1999.

Recent developments provoked cautious optimism that increased quantities of gas could become available for domestic consumption as well as for export. The optimism stems in part from the favorable exploration results obtained by international companies that participated in the first-round bids. The second-round gas exploration and production bids now under way are attracting significant global interest. However, in the short term, there are some concerns that the foreign exchange required to service the private sector investment could strain the balance-of-payments position of the country. This, along with the need to maximize the economic benefits of gas reserves, requires that the Government put in place policies on gas utilization and expansion of the gas market, including the export of gas.

44. Another potential area in which Bangladesh has a comparative advantage is its low cost of labor. Used properly, cheap labor could be the treasure of the national economy. An international comparison shows that labor costs in Bangladesh are probably among the lowest in Asia. For example, the annual wage rate for making shirts in Bangladesh is only one half that in India and Sri Lanka, one quarter that in Pakistan, and even substantially lower than that in Viet Nam. The problem is that this cheap labor has not been matched

by adequate capital investment. Promotion of private investment in labor-intensive industries is therefore vital for a more efficient labor market and reduced poverty. The development of several export processing zones, including those targeted for specific investors from Japan and the Republic of Korea could bring in sizeable FDI. To promote such investments, the Government needs to establish a more favorable environment by speeding up major reforms.

45. With economic reforms and institutional changes touching more and more on the core issues, the Government must find mechanisms to mobilize public support and social consensus. This will require the Government to invest more efforts to gain broad acceptance of their policies by ensuring a more transparent policymaking process and by encouraging greater participation of civil society in the reform process.

G. Key Elements of the Government's Development Strategy

46. In the recently approved Fifth Five-Year Plan, the main thrust of the Government's medium-term development strategy is to reduce poverty through accelerated economic growth and to improve the standard of living of citizens by raising their level of income and ensuring an adequate supply of basic needs.

47. To achieve this, the Government's development agenda emphasizes the following:

- (i) generation of substantial employment opportunities by channeling greater resources to the rural economy and promoting labor-intensive production for export;
- (ii) attainment of food production beyond the self-sufficiency level;
- (iii) development of infrastructure and other services needed to promote private sector-led growth;
- (iv) development of effective local government institutions and vesting in them the power and responsibilities for the formulation and implementation of local-level development projects;
- (v) human resources development with emphasis on compulsory primary education and vocational training;
- (vi) protection and preservation of the environment by strengthening regulatory institutions and optimum exploitation of natural resources for sustainable development; and

- (vii) closing the gender gap by giving priority to women's education and training and income-raising employment generation.

48. The most striking feature of the Fifth Plan is its very high development targets. The major targets, for instance, include an average annual GDP growth rate of 7 percent. The investment rate is targeted to increase from the current 18.2 percent to 25.1 percent of GDP in FY2002, while the national savings rate is expected to grow from the current 13 percent to 17.8 percent by FY2002. The proportion of the population living below the poverty line is targeted to decline from the current 47.5 percent to 30 percent in FY2002. Although the major development targets of the FFYP are very ambitious compared with the country's previous performance records, they are critical to pursue if Bangladesh is to achieve a major breakthrough in economic growth and poverty reduction.

49. To reduce poverty and promote economic growth, the Fifth Plan particularly emphasizes the role of the private sector in the country's development. It is projected that during the plan period, the private sector will be the main engine of growth. The share of private sector investment will increase from 44 percent in the Fourth Five-Year Plan (1990 to 1995) period to 56 percent of total investment in the Fifth Plan period. The Government will take steps to (i) provide a stable macro environment for the efficient operation of the private sector, including financial reforms and legal and administrative reforms; (ii) continue to attract private investments in infrastructure, particularly in the energy, telecommunications, and port subsectors; (iii) speed up the privatization process; (iv) encourage FDI, particularly in export-oriented industries and high-technology and agro-based industries; and (v) strengthen the role of various chambers of commerce to develop partnerships between the Government and private sector.

50. While increased reliance on the market for resource allocation is the main characteristic of the Fifth Plan, it recognizes that because of market failures, there is a need for direct Government intervention in the area of poverty reduction.

51. The creation of employment opportunities is identified as the basic element in a poverty reduction program. Rural development has been

accorded priority, to increase production in both the farm and nonfarm sectors, generate self-employment opportunities, and develop human resources mainly through the dissemination of technology, training, and market information, and promotional activities. Particular attention is given to the development of the hard-core rural poor and depressed rural areas.

52. To link the rural poor with basic social services, allocation to social sectors will be adequately increased. Program coverage will be increased through the expansion of existing successful projects and launching of new projects in education, health, family planning, and social services. The rural poor will be given better access to resources, especially to microcredit, which is critically important and has high poverty reduction potential.

53. At the sector level, development objectives consist of the following: In agriculture, the main thrust is to achieve food production levels beyond that of self-sufficiency and to increase noncrop food products. Reduction of poverty through rural development is particularly emphasized and includes the creation of self-employment opportunities for the poor, the development of rural infrastructure, and the provision of rural credit facilities. In industry, the optimum utilization of indigenous resources, promotion of employment, and export-led industrialization are emphasized. In the energy sector, the focus is on private sector participation, including that of foreign investment. To achieve an 8-9 percent annual growth in the transport sector, development efforts will concentrate on five main corridors. In education, the objectives are a 75 percent literacy rate and bringing all children aged 5-11 years under the formal educational system. In public health, the main goal is to increase the coverage of primary health care services to achieve Health for All by the year 2000.

54. Another new development, which could have a major impact on Bank operations in Bangladesh in the next few years, is the emerging subregional economic cooperation by South Asian countries. With the recent greater openness to external trade and inflow of foreign capital, the political leadership in these countries has become more appreciative of the mutual benefits that can be derived from regional economic cooperation. This has prompted the governments of many South Asian countries to explore pragmatic ways of expanding cooperation.

III. DEVELOPMENT ASSISTANCE EXPERIENCE AND OUTLOOK

A. Existing Strategy

55. As the second largest multilateral funding source to Bangladesh, the Bank provided almost one fifth of the country's total foreign aid. The Bank has been involved in most major sectors, with agriculture, energy, transport, and social infrastructure receiving the bulk of support.

56. Since the 1990s, the Bank's operational strategy has given more emphasis to poverty reduction and social services through equitable and sustainable growth. The last country operational strategy, formulated in 1993, identified poverty reduction as the long-term objective. Over the medium term, the Bank's strategic priorities included:

- (i) promoting a faster rate of economic growth through greater market orientation, increased domestic resource mobilization, accelerated human development, and improved physical infrastructure;
- (ii) enhancing poverty reduction through employment generation and improved basic social services and infrastructure; and
- (iii) improving and protecting the environment, by addressing the physical and human consequences of poverty as well as natural resource management.

B. Impact Assessment of Bank Operations

57. Compared with its operations in the 1970s and 1980s, the Bank's assistance to Bangladesh over the past five years or so has been more relevant to the strategic objective and more effective in terms of project implementation, placing more emphasis on structural reforms, capacity building, and institutional development. Partnerships with the stakeholders, NGOs, and civil society have also been strengthened.

58. **Recently completed projects have better performance.** As of 30 June 1999, the Bank had provided 134 loans, including private sector loans, amounting to \$5.88 billion. The Bank also provided 242 TA for \$145.5 million projects to Bangladesh. To date 43 projects/programs have been postevaluated, with 35 percent considered generally successful, 56 percent partly successful, and 9 percent unsuccessful (Table 2). While the success ratio is

comparatively low, more recently completed projects have had a higher success ratio than those processed in the early years (Table 3). The recently completed surveys on the Bank's project preparatory TAs in the agriculture sector show that those approved in the later 1980s and early 1990s had substantially improved, in terms of addressing customers' needs, improving project design, and enhancing capacity of the agencies concerned.

Table 2: Summary of Postevaluation Results

Location	Number of Projects	Generally Successful (%)	Partly Successful (%)	Unsuccessful (%)
Bankwide	521	57.2	31.3	11.1
Group A Countries ^a	225	47.6	36.9	15.1
South Asia	160	49.4	36.9	13.8
Bangladesh	44	36.4	54.5	9.1

^a Group A countries are those developing member countries where the upper limit of Bank funding for projects is 80 percent.

Table 3: Summary of Postevaluation Results for Bangladesh by Year

Year of Approval	Generally Successful	Partly Successful	Unsuccessful
1970s	26.1	56.5	17.4
1980s	50.0	50.0	00.0

59. **The Bank's operations have become more relevant to the country operational strategy.** Projects on human development have had the strongest impact on poverty, followed by investments in physical infrastructure such as road and electricity. The role of new high-yielding varieties of crops come first and other interventions in agriculture next (Box 4). Since the late 1980s and early 1990s, Bank assistance has shifted in this direction along the line of the strategic objective of poverty reduction identified in the previous strategy.

While lending to traditional areas such as industry, irrigation, fertilizer, and fisheries declined, the lending to areas with higher poverty impact such as rural electrification, rural road and market development, and education increased considerably (Table 4). From 1990, the Bank also increased its role in providing direct assistance to the poor by providing microcredit support.¹ In the past five years, 48 percent of the Bank's lending was for projects with poverty reduction as the first or second objective.

¹ Loan BAN 1067: *Rural Women Employment Creation*, for \$8 million, approved on 13 December 1990. Loan BAN 1213: *Rural Poor Cooperative*, for \$28.9 million, approved on 17 December 1992. Loan BAN 1524: *Participatory Livestock*, for \$19.7 million, approved on 19 June 1997. Loan BAN 1634: *Rural Livelihood*, for \$42.6 million, approved on 29 September 1998.

Box 4: Impact of Rural Infrastructure on the Poor

According to a study by Ahmed and Hossain, based on data on the most- and least-developed villages in Bangladesh, the provision of good infrastructure could result in the average household income rising by 33 percent. Specifically, income from agriculture increased by 24 percent, from livestock and fisheries by 78 percent, and daily wages by almost 100 percent. Income from business and industries, however, rose by only 17 percent. The distribution of the increases revealed that the functionally landless and small farmers gained a larger share of the increase from crops, wages, and livestock and fisheries, while the large landowners captured the smaller increase in business and industries. Another recent study indicated that, on average, the incomes of households in villages with good roads and electricity are around 13 percent higher than those of their counterparts in villages with underdeveloped infrastructure.

Ahmed, Raisuddin, and Mahabub Hossain. 1990. Developmental Impact of Rural Infrastructure in Bangladesh, Research Report No. 83. International Food Policy Research Institute, Washington, DC.

Table 4: Sectoral Distribution of Bank Lending

Sector	1973-1997		1973-1977		1978-1987		1988-1997	
	Loan Amount	%	Loan Amount	%	Loan Amount	%	Loan Amount	%
Agriculture	1971.9	37.1	122.7	44.6	924.3	48.2	925.0	29.6
Energy	1069.7	20.1	55.0	20.0	558.4	29.1	456.4	14.6
Social Infrastructure	896.5	16.8	0.0	0.0	114.0	5.9	782.5	25.0
Transport and Communications	965.1	18.1	44.8	16.3	241.5	12.6	678.8	21.7
Industry and Finance	418.6	7.9	52.6	19.1	79.5	4.1	286.5	9.2
Total	5,321.8	100.0	275.0	100.0	1,917.7	100.0	3,129.1	100.0

60. **Bank operations, particularly program lending, have made a significant contribution to policy reform in many key areas.** Although it is difficult to segregate the impact of Bank operations from those of other external funding agencies, in many areas the Bank's active involvement has helped improve the policy environment over the years. Several program loans played a key role in policy reform. In the agriculture sector, the Bank has made a significant impact in reshaping the policy environment through the Foodcrops Development Program loan¹ and the Agricultural Inputs Program loan.² The programs have helped to increase

foodgrain production through greater market orientation in agriculture, including expansion of minor irrigation and private sector involvement in fertilizer distribution. In the energy sector, the Bank assisted the Government to restructure the power and gas subsectors from being Government-dominated to Government-regulated by rationalizing tariffs, unbundling the monolithic structure of the public sector, and promoting private sector participation. As a result, it is expected that the current supply shortage in both gas and electricity will be largely eliminated in the next two to three years.

¹ Loan BAN 1045: *Foodcrops Development Program* for \$125 million, approved on 6 November 1990.

² Loan BAN830: *Agricultural Inputs Program*, for \$51.7 million, approved on 7 April 1987.

61. In the railway sector, the Bank's program loan helped to implement major reform of Bangladesh Railways by improving its financial status, closing uneconomic operations, reducing staff numbers by one third, and commercializing part of its operations. In the capital market, the Bank has focused on strengthening market regulation and supervision, restructuring the State-owned Investment Cooperation of Bangladesh, as well as liberalizing private sector participation in merchant banks and other investment facilities. In education, the Bank's operational impact on primary and secondary education has been significant. With Bank assistance the Government has increased equitable access to education, improved the quality and efficiency of primary education, and restructured the secondary education system. The Bank has also played a catalytic role in institutionalizing nonformal education as an integral part of the basic education system. The Bank's involvement contributed to increased enrollment and completion rates of primary education, and encouraged the Government to make a substantial increase in the resource allocation to education.

62. **The Bank has increasingly emphasized governance and institutional development issues in recent projects.** In almost all newly approved loan and TA projects, institutional development and capacity building have become important component. In the infrastructure sector, extensive work has been made on commercializing parts of its operations, increasing private sector participation, and establishing independent regulators. In the urban sector, governance has been addressed through strengthening municipal management and secondary town development. In the area of rural development, the Bank has provided assistance for the institutional strengthening of the Local Government Engineering Department. The impact can be seen in the design of roads and bridges, an increased focus on operation and maintenance, and community participation in design and implementation.

63. The Bank has also provided assistance in key areas through its advisory TA to enhance the Government's capacity in administration and macroeconomic management. Among these TAs are (i) for public administration training strategy with the primary aim of establishing a contemporary approach to training senior civil servants; (ii) for the Bangladesh Bureau of Statistics to improve the macroeconomic monitoring system including revising the national accounts and conducting the recent household expenditure survey; (iii) for the land area

administration to significantly increase transparency and reduce the scope for corruption; and (iv) for the Ministry of Finance to develop a policy evaluation system to assess the impact of various policy reforms.

C. Lessons Learned from Past Experience

64. Despite the progress achieved, there are many areas to be addressed. A summary of the major lessons learned follows.

65. **First, Bank operations have covered too many sectors and subsectors.** So far Bank operations have reached almost every sector and more than 30 subsectors. Given the Bank's limited resources, this approach has greatly reduced the strength of its intervention. It has resulted in many one-time interventions or a very long break between two interventions in a sector or subsector. Such projects usually encounter more problems as the reform and institutional changes proposed by the projects are often not sustainable; the Bank loses leverage quickly after leaving the sector. This diversified approach also caused the Bank to be involved in many nonpriority areas or to play a less important role in the key sectors. For example, of the 30 subsectors where the Bank has been involved, the Bank can only be considered the lead agency in five or six. More importantly, with this widespread approach it is particularly difficult to discern a strong logical and strategic pattern for systematic reform and institutional buildup, as any meaningful reform in Bangladesh needs a long-term effort by both the Government and the external funding agencies.

66. **Second, economic and sector analyses and the long-term framework have been inadequate.** One of the general lessons that has been learned from operations in Bangladesh is that maximum impact occurs in those sectors where the Bank has detailed knowledge of the sector and retains continuous presence. Policy intervention should not be a one-time global effort. There should be a series of planned interventions on a long-term and coherent basis. The success of reform of the power subsector is partly because the Bank made long-term efforts for more than 20 years and provided nine projects. The interventions included a temporary withdrawal from involvement in the subsectors when the Government did not fulfill its commitments. Such efforts have paid back, and the policy environment of the power subsector has

changed significantly. However, such a successful approach has yet to become the dominant modality of Bank operations in Bangladesh.

67. **Third, there is a need for a closer linkage between investment and policy changes.** The policy environment has had a significant impact on the Bank's project performance. In the railway operations, for example, the Bank closely linked investment and policy reform measures together (Box 5). In recent years, the policy content of Bank operation has been strengthened through program lending and policy dialogue. However, policy components of project loans are still weak. For example, in many cases emphasis is more on project-related policy than on sector policy. Meanwhile, there

have been inadequate efforts to monitor and follow up on whether the covenants of the loan agreements are met.

68. **Fourth, governance needs to be further strengthened.** It is critical to pursue a realistic and rigorous assessment of the institutional environment and the capability of the executing agencies to implement and maintain projects. Those projects considered as unsuccessful usually underestimated the importance and complexity of bringing about institutional change and capacity enhancement. Bank operations are generally still weak in this area. Complex project designs with multiple components and weak institutional capabilities are usually the main reasons for project failure.

Box 5: Case Study: Bangladesh Railway

Bangladesh Railway (BR), one of the oldest and largest State-owned enterprises, has suffered from low efficiency and high operational losses and become a major burden for public finance.

The Bank has a long history in assisting BR. In the early years, however, the Bank's projects focused on physical rehabilitation with less attention to policy and institutional reforms. The results, of course, were very disappointing. Learning from this experience, since the early 1990s it has shifted its operational focus toward policy reforms and institutional strengthening. One program loan followed by a heavily policy-based project loan was provided to the sector in the past five years.

This policy-based approach has proved successful. The achievements include (i) downsizing of the staff complement by 17,000 or 30 percent, the largest public sector retrenchment undertaken in the country so far; (ii) decreasing the working ratio (expenses to revenue ratio) from 1.4 in 1995 to less than one in 1998; (iii) privatizing intercity ticketing services using build-operate-transfer concept; (iv) privatizing telecommunications services, (v) preparing BR to become an independent corporation, (vi) introducing a specific contractual and transparent arrangement for social passenger services; and (vii) introducing commercial policies and a new tariff structure for freight pricing.

The Bank has also assisted the Government in developing a multimodal transport strategy, including a plan for subregional links between Bangladesh, India, and Nepal. Based on this strategy, the Bank has extended support to the rail link on Jamuna Bridge, which was opened in June 1998. This key subregional project is an important component of the trans-Asian road and rail networks.

Recent successful operations in the railway subsector can be attributed to several key elements: (i) the Bank's assistance addressed key reforms and institutional development; (ii) before and during project implementation, the Bank did its homework with extensive sector analyses and studies, (iii) the reform program was realistic and was carried out step-by-step; (iv) the program emphasized up-front reform actions; (v) the Bank provided long-term, continued, and back-to-back assistance; and (v) Bank staff involvement in policy dialogue and performance-related actions was ongoing and persistent.

69. **Fifth, stakeholder ownership and participation are vital for success.** The Bank's past experience strongly indicates that stakeholder participation and ownership of the Government,

NGOs, civil society, as well as beneficiaries, are crucial for project success. The Bank cannot impose policy and investment if the country is unwilling. While the Bank has greatly enhanced the

approach in project design and implementation, this has yet to become standard practice in every project. Broader participation of society, including the private sector and civil society, should be mobilized. There are still other areas where the Bank can increasingly collaborate with NGOs and the private sector to implement public programs. More innovative approaches to bring the private sector and civil society into the development process may be needed.

70. Finally, more frequent, focused, and proactive supervision are needed during project implementation. This is particularly important for multicomponent projects and projects experiencing initial delays. The Bank's operational problems are including (i) serious start-up delays, especially in land acquisition, recruitment of consultants, and participating NGOs; and in timely establishment of project offices; (ii) serious and avoidable delays in procurement, particularly the preparation of bid evaluation reports and Government approval of contract awards; (iii) high turnover and inadequate training of key project staff; and (iv) excessive red tape and weak ownership of projects. Recently, a special arrangement was discussed with the Government to allow the Bank to directly recruit consultants for loan projects. The Bank also needs to develop a mechanism to ensure continuous administrative and budgetary support for the operation and maintenance of completed projects.

D. Aid Activities, Aid Coordination, and Cofinancing Potential

71. External assistance has played a vital role in the development of Bangladesh. The country has received assistance from almost 40 bilateral and multilateral funding sources and several private organizations. In addition to the Bank, the major multilateral funding bodies include the World Bank, the European Community, and the United Nations system. Major bilateral aid sources include Canada, Japan, Germany, United Kingdom, and the United States.

72. In spite of the substantial amount of external assistance received, given its large population, per capita aid was only \$12.5 in 1998. This is one of the lowest in the world among the low-income developing countries.

73. In recent years, the Government has made significant efforts to mobilize domestic resources for development finance. The share of capital account investment in the annual development program

steadily increased from nil in FY1990 to over 45 percent in FY1998. Total external assistance (on a disbursement basis) in FY1998 amounted to about \$1.34 billion, compared with about \$1.5 billion the previous year. However, domestic resource mobilization still lags behind the increased investment requirements of the economy. A high level of external assistance will therefore continue to be essential to support the rate of growth needed to reduce poverty.

74. With poverty reduction as the overriding common objective, the funding agencies share the same broad understanding regarding the development strategy for Bangladesh. There is close coordination between both multilateral and bilateral funding agencies, which confer annually at aid group meetings (recently renamed as the Bangladesh Development Forum). More frequently coordination of external funding agencies is through the sectoral local consultative groups in Dhaka. The Bangladesh Resident Mission coordinates the Bank's activities with other external funding agencies. The Bank is the lead agency in the power, urban development, railway, capital market, secondary education and nonformal education sectors/subsectors and oversees project implementation performance. The World Bank coordinates the subgroups on primary education, population and health, agriculture, water supply and sanitation (with the United Nations Development Programme) and private sector development (with the United States Agency for International Development).

75. Cofinancing is an essential part of the Bank's operational program. Cofinancing has been successfully mobilized recently for projects in forestry, power, livestock, education, and primary health, and railway project. In the past nine years (1990-1998) the leverage ratio of Bangladesh is 75.8 percent (amount of cofinancing/total lendings compared with 42.2 percent Bankwide). While opportunities for commercial cofinancing are limited due to country risk perceptions, these will be explored in conjunction with the Bank's efforts to encourage private sector participation in infrastructure.

76. The World Bank's overriding objective in Bangladesh is to help the country reduce poverty by promoting rapid, job-creating economic growth and interventions that directly assist the poor. Its recently approved country assistance strategy further identified that institutional development is a

core strategic goal for improving the development effectiveness of the World Bank Group in Bangladesh. While its program is fairly diversified in many sectors, since the early 1990s, there have been important changes in the pattern of its lending. Agriculture lost its prominence, the energy sector's share fell sharply, and social infrastructure accounted for a smaller proportion. But the transport sector surged notably. Industry and finance continued to receive sizable portions mainly because of two large sector adjustment programs: the Jute Sector Adjustment Credit and Second Industrial Sector Adjustment Credit.

77. With the recent restructuring of the World Bank, its resident office has been greatly strengthened. Depending on the implementation of the reform agenda, its country assistance strategy assumes that base-case lending for FY2000 will increase to an average of \$600 million-650 million per year compared with actual annual lending to Bangladesh, which amounted to \$250 million during FY1995-FY1997. In addition, changes in loan processing and approval procedures of the World Bank could sharply reduce processing time in Bangladesh. The Bank coordinates closely with the World Bank in almost all key areas and has established regular reviews to ensure coordination in both headquarters and resident missions. Both institutions jointly prepared the economic update for the last Aid Consortium Meeting.

78. The International Monetary Fund (IMF) plays a leading role in monitoring the short-term macroeconomic situation and provides support for macroeconomic stabilization and structural reform. IMF is now processing the Enhanced Structural Adjustment Facility for Bangladesh. Bank staff have participated in IMF Article IV missions every year and in the recent structural adjustment facility mission. The Bank has also closely coordinated with IMF in the areas of statistics, fiscal management, and sector policy issues with macroeconomic concerns. The priority of the United Nations Development Programme is poverty reduction through community empowerment, nonformal employment generation, women in development, improved environmental management, and improved public management. The other United Nations agencies also share the same goals, but work in their various areas. Japan is the largest of the bilateral sources of external aid to Bangladesh. The major objective of Japan's official development assistance is to promote sound economic development in the country. In recent years, the priority areas of assistance are infrastructure and rural development. The Bank has many projects cofinanced

with Japan mainly in the areas of infrastructure.

IV. THE BANK'S FUTURE ROLE AND OPERATIONAL STRATEGY IN BANGLADESH

A. Overall Strategic and Medium-Term Priorities

79. While the broad objectives and guidelines provided by the 1993 country operational strategy are still relevant to Bank operations, an adjustment is needed. This should take into account the important structural changes in the Bangladesh economy since 1993, as well as the changing development priorities outlined in the Government's Fifth Five-Year Plan. The strategy also needs to be revised in line with the Bank's strategic movement to develop itself as a broad-based development institution. The Bank will attempt to weave into this strategy its implementation experiences and draw on lessons learned from its recent operational activities. It will also try to sharpen the sector focus to have a more distinct impact on Bank operations. Finally, the emerging constraints on Asian Development Fund resources and the new status of Bangladesh in Bank lending should be considered.

80. Consistent with the Government's development strategy and Bank's Medium-Term Strategic Framework, the Bank's overall strategic objective in Bangladesh will be poverty reduction (Box 6). This will be achieved through the promotion of faster economic growth, creation of better development opportunities for the poor, improvement of human development, and environmental protection. The Bank's operational priorities will cover the following four areas:

- (i) **Promoting faster private sector-led economic growth.** The core strategy for supporting poverty reduction is to promote private sector-led economic growth. The Bank will assist the Government to speed up policy reform and create a level playing field conducive to private sector development. The Bank will focus on providing assistance to improve infrastructure and financial systems, which are the main constraints for private sector development. Furthermore, the Bank will support private sector development in its public sector operations and provide assistance to promote subregional cooperation.

- (ii) **Creating better development opportunities for the poor.** The Bank will assist the Government to invest, and encourage community and private sector participation in rural development including rural infrastructure and credit. In the urban area, the Bank's intervention will focus on small and secondary town development. It is expected that all these activities will have a direct impact on the poor.
- (iii) **Improving human development.** The Bank's operational priority in the social sector is mainly in the areas that can increase the productivity of the poor including, primary health, and primary secondary, and nonformal education. As in the past, special efforts will be made to increase equitable access of women to social services.
- (iv) **Improving and protecting the environment.** The Bank's operational thrust under its environment program over the medium term will be to address environmental concerns in all Bank projects, and institution building in the planning, management, legislation, and regulation capacity of the Government. Particular attention will be placed on urban environmental improvement and poverty-related environmental issues.

Box 6: Country Operational Strategy

OVERALL STRATEGIC OBJECTIVE

Poverty Reduction

MEDIUM-TERM PRIORITIES

Promote Faster Private Sector-Led Economic Growth

Create Better Development Opportunities for the Poor

Improve Human Development

Protect Environment

OPERATIONAL INSTRUMENTS

Emphasize Policy Reforms and Institutional Development

Enhance Participatory Approaches in Project Design and Implementation

Encourage Private-Public Sector Cooperation

Catalyze Additional Resources

Promote Subregional Cooperation

OPERATIONAL APPROACH

Sharper Sector Focus

Long-term Involvement

B. Poverty Reduction

81. Reducing poverty remains the central development challenge in Bangladesh. However, past experience has shown that direct interventions like the microcredit program, considered as the best in the world, is not enough to have a significant effect. Bangladesh's prospects for reducing poverty will not improve substantially unless more rapid economic growth is achieved, structural reforms are deepened, institutional development is strengthened, the private sector is stimulated, and human resource development is accelerated.

82. Therefore, Bank operations to reduce poverty must be broad based focusing on the following priority areas:

- (i) promoting labor-intensive economic growth, in particular, growth projects led by the private sector that generate employment;
- (ii) promoting rural and urban development, including rural roads, small irrigation projects, crop/agro business credit, microfinance, and small and secondary towns development, which have a direct impact on the poor and improve on income distribution;
- (iii) supporting investments in social services including basic health, education, family planning, and investments that can increase the productivity of the poor;
- (iv) supporting reform measures to foster a more equitable distribution of income and assets;
- (v) supporting activities that could strengthen the Government's monitoring and evaluation capacity of poverty reduction activities and assisting the Government in developing the institutional capacity to reduce poverty.

C. Strengthening Policy and Institutional Focus

83. The Bank's ability to assist the Government in reducing poverty and promoting fast economic growth will depend greatly on the policy reforms and institutional capacity of the Government. As the Bank is moving from mainly a project-financing bank to a

broad-based development institution, it will realign its role to ensure a more effective and efficient realization of its strategic development objectives. Therefore, the objectives of Bank lending in Bangladesh will go beyond just resource transfers and will put more weight on policy changes, capacity building, and institutional development. The Bank will provide assistance only to sectors and projects that have substantial policy reform and institutional development components that have the firm commitment of the Government.

84. This approach will imply some changes in the Bank's operational practice in Bangladesh:

- (i) **Sector and Subsector Level of Intervention.** Given the limited resource and comparative advantage of the Bank, its policy interventions have been mainly at the sector and subsector level.
- (ii) **Long-Term Involvement.** Reform and institutional improvement are not a one-shot effort, but a series of interventions undertaken on a long-term and coherent basis. The Bank will provide a loan only to the sector where a comprehensive sector study has been completed and a clear road map of the Bank's long-term involvement has been identified. The Bank should totally avoid an occasional or one-time type of project.
- (iii) **Principle of Gradualism.** The Bank recognizes that the goals of policy and institutional reform in Bangladesh can only be achieved gradually, step-by-step. Therefore, the Bank supports a pragmatic pace of reform. The reforms, as well as the Bank's involvement in the sector, should be unbundled with several coherent components consistent with the long-term framework and accomplished through a succession of projects.
- (iv) **Ownership and Commitment.** The success of policy reforms and institutional change relies fully on strong ownership and commitment from the Government. The extent and pace of change cannot and should not be dictated by the Bank. In other

words, the Bank will not invest in a new project where the commitment to reforms is weak. The Bank should slow down project processing, and if necessary, walk away temporarily from a sector where the public agency is not ready or does not implement the policy component agreed upon.

D. Promotion of Private Sector Development

85. Private sector development is particularly important in the context of Bangladesh. It is given special emphasis in the recently published draft of the new Fifth Five-Year Plan. In view of these adjustments in the Government's strategy, the Bank will strengthen its operations to promote private sector development in Bangladesh. The Bank should increase its support to private sector development in its public sector operations following these principles:

- (i) The priority of the Bank operation and policy dialogue is to help the Government create a level playing field conducive to private sector development.
- (ii) One of the key areas to help the private sector is to establish a well-functioning financial and capital market. The Bank's involvement will be through policy and regulatory reforms such as the recent Capital Market Development Program loan. The Bank will also support selective investments to help create and build the necessary institutions and schemes to fill gaps in the market. Where feasible, the Bank should consider more innovative ways through funds or credit facilities from its private sector window.
- (iii) In the area of infrastructure development, the Bank will strengthen its operations and catalytic role in supporting build-operate-transfer projects in power, ports, gas, and telecommunications.
- (iv) The Bank should identify more public sector projects that could pave the way for private investments in these infrastructure sectors.
- (v) Bank assistance in the area of SOE privatization has had unsatisfactory results. The Bank had to cancel the second tranche of the Second Industrial Program

loan in early 1990s. At present, there is not enough political will or public support for a large-scale privatization program. The Bank will continue to provide technical assistance to strengthen the Government's privatization effort. The Bank will revive lending operations in this area if political commitment strengthens considerably in the future.

- (vi) Given the decline in official development resources, more innovative ways to mobilize additional funds to the private sector, such as credit guarantees, need to be explored.

E. Key Features of the Bank's Future Operations

86. Given the Bank's resource and staff limitations, and to maximize the development impact of its assistance program, it is important that its operations concentrate on fewer sectors than the present very wide range of interventions. One of the major lessons learned is that a less concentrated approach greatly reduces the strength of the Bank's intervention, making it difficult to pursue systematic policy reforms and institutional development.

87. The reformulated strategy will thus consist of a sharper focus of Bank operations. The selection of sectors or subsectors will be based on the following principles:

- (i) Selection should be consistent with the overall operational strategy of the Bank and medium-term priority; more particularly, the activities in the sector should have a strong impact on poverty reduction and/or private sector development.
- (ii) There are substantial policy and institutional components accompanying sectoral initiatives, and clear signs of the Government's firm commitment to these reforms.
- (iii) The Bank has a comparative advantage in the area, and has done or will soon conduct a comprehensive sector study and a systematic long-term reform and investment program.

- (iv) The Bank has played or will play an important role, preferably the leading role, in the area.
- (v) The Bank's involvement could play a critical catalytic role in bringing in private sector financing or cofinancing.
- (vi) There is a clear division of labor with the other external funding agencies.

F. Performance Based Lending

88. The Bank will place increasing emphasis on a sound policy environment in its developing member countries. The Bank's ADF allocation for a country will reflect that country's performance in terms of the efforts made by the Government to strengthen policies and institutions. Since 1990, Bangladesh has received about one fifth of the Bank's total ADF resources. It is expected that this share will be maintained subject to satisfactory performance. Additional ADF resources could be provided if the performance of the country warrants a higher lending level. Within the country, performance-based resource allocation has been mainly operationalized through the selection of subsectors for Bank involvement. Many subsectors were dropped from Bank operations due to unsatisfactory performance. Meanwhile, Bangladesh has been reclassified from being an ADF-only country to one with access to ADF plus a limited amount of ordinary capital resources (OCR). Given resource projections based on current information, it is expected that the Bank could provide about four loans a year to Bangladesh in the medium term. To maintain the momentum of reforms and institutional change, the Bank should revisit the subsector, on average, every three to four years. Therefore, the Bank can at most support 15 subsectors, compared with its past involvement in around 30 subsectors.

G. Priority Areas of Bank Assistance

89. Based on the sector selection criteria and analyses of the previous chapters, Bank operational priority over the next 5-10 years will be focused on four areas and 15 subsectors. In the agriculture and rural development area, the Bank will focus on crop/agrobusiness credit and microfinance subsectors because of their strong impact on poverty. The Bank will continue to finance a series of projects to develop rural infrastructure, small irrigation, and flood protection where the Bank's past experience has been very positive and has a strong visible impact on poverty and rural development. As the leading

aid agency in the energy sector, the Bank will assist the Government in restructuring the power and gas subsectors from being Government dominated to Government regulated. Given its strong impact on economic growth as well as the firm commitment of the Government to pursue policy reforms, the Bank will remain active in the energy sector. In the financial sector, the Bank will focus on capital market development due to its strong impact on private sector development and economic growth, as well as the division of labor among the Bank, IMF, and the World Bank. In the transportation sector – given its crucial role in promoting more rapid economic growth, its strong impact on poverty, the comparative advantage that the Bank has developed in the past decades – the Bank's operation will be mainly on railways and roads, especially for those projects facilitating regional cooperation. The Bank's involvement in the ports subsector will be subject to the commitment of the Government to pursue important policy reforms. In the social sector, the Bank's operation will cover basic and secondary education as well as urban primary health due to their strong impact on the poor and division of labor among donor agencies. The Bank will also give special attention to governance and the environment, including direct lending to these areas.

90. The selection of these 15 subsectors is well balanced in terms of the Bank's main goal: poverty reduction, as well as medium-term priorities including economic growth, rural and urban development, private sector promotion, and social and environmental development. In future, a project that has a strong foreign exchange generation capacity will be gradually supported mainly by OCR funding. The ADF resource will be used mainly for projects with poverty reduction, social, and environmental concerns. It is recognized that 15 subsectors is still a relatively large number. Accordingly, further efforts will be taken to reduce this number based on the criteria for the Bank's involvement.

91. One of the newer strategic areas in which the Bank will operate in the near future is subregional cooperation. There are many opportunities for South Asian countries to accelerate regional economic cooperation. Since mid-1996, the Bank has been working toward encouraging regional cooperation in South Asia with efforts to support cooperation among Bangladesh, Bhutan, India, and Nepal. At this stage, Bank operations will focus on infrastructure development, particularly for regional road and rail linkages as well as regional

power-sharing arrangements.

92. It should also be pointed out that the Government's commitment to reforms and institutional change is a precondition for the Bank to maintain its assistance in the sector. This commitment, in our view, is still rather weak particularly in the areas of ports and parts of water resource management. The Bank will closely monitor the reform progress in those areas and provide TA, if necessary, before processing an investment project.

V. INSTRUMENTS OF BANK SUPPORT AND OPERATIONAL IMPLICATIONS

A. Project Lending

93. **OCR Lending.** Bangladesh is classified under the Bank's new country classification as a class

B1 country with access to ADF with limited amounts of OCR lending. Although the country is below the per capita gross national product cutoff, its debt repayment capacity could allow limited borrowing from OCR. Some assessment of OCR could boost resource flows to areas that have a strong revenue and foreign exchange generation or substitution capacity such as power, gas, telecommunications, and certain areas in finance and industries. Meanwhile it may not have a significant negative impact on the country's debt service ratio (Table 5). However, the Bank should be cautious not to jeopardize the country's debt payment capacity and a special assessment should be made on the OCR lendings. The Bank should also monitor the country's debt payment capacity periodically. OCR lending should be stopped if the debt service ratio increases sharply or any other debt indicator deteriorates substantially.

Table 5: Increase of the Debt Service Ratio¹ with Additional OCR Borrowing²

Year	Annual \$50 million OCR Borrowing (%)	Annual \$100 million OCR Borrowing (%)
2000	0.13	0.24
2005	0.40	0.79
2010	0.60	1.21
2015	0.57	1.13
2020	0.40	0.81
2025	0.29	0.58
2030	0.21	0.41

OCR=ordinary capital resources.

¹ Debt payment is (principal + interest/total exports of goods and services)

² Assumptions: (i) 7% growth annually of exports of goods and services.

(ii) Terms of OCR: grace period, 5 years; 15 years of maturity; interest charge, 6.76 percent annually.

94. **Lending Modality.** Reflecting the Bank's strategic priorities, the Bank will continue to perform its role in terms of resource transfer and retain its position as a leading partner in policy dialogue activities to further reform the structure of the economy, and improve the capacity and efficiency of the Government. The sector development program modality, which combines physical investment, policy reform, and capacity building, will be used more frequently and will gradually become the

preferred modality for the Bank's lending to Bangladesh.

95. **Guarantee Facility.** While Bangladesh so far has not accessed the Bank's guarantee facility, the possibility of using this facility in the future should be actively explored. In particular, the guarantee modality could be considered to support private sector involvement in infrastructure development and capital market development.

B. Technical Assistance

96. To support the Bank's operational strategy, the Bank will continue to provide TA to the Government for project preparation and project supervision, and advisory TA for policy and institutional development.

97. The quality of a project preparatory TA is directly related to the success of a project and the policy associated with the project. The operational focus of project preparatory TAs will mainly be in the 15 selected subsectors. The Bank should make strong efforts to strengthen project preparatory TA design and supervision. Since more emphasis will be placed on policy reform and governance aspects of a project, these TAs should also play an increasing role in identifying and proposing ways to solve structural and institutional problems on a long-term basis.

98. The thrust of the Bank's advisory TAs should be on macroeconomic and general institutional development issues that are not covered by the Bank's lending program. Advisory TAs could play a more active role in the nontraditional areas of the Bank's operations such as macroeconomic management, judicial reform, banking and financial sector development, administrative reform, foreign investment promotion, and civil society development.

C. Economic and Sector Work for Country Strategy

99. The economic and sector work programs are particularly important in the new strategy period. The Bank will only invest in a sector in which a comprehensive study and long-term policy and investment road map will be required for each subsector that the Bank is involved in. Within two years, a new set of long-term Bank operational strategies outlining where the Bank plans to invest is expected to be completed. Appendix 2 provides a detailed description of the economic and sector work program for the Bank's long-term subsector operational strategy study. The new studies will make a comprehensive reassessment of the Bank's sector strategy, priorities, and policy; institutional development; and investment agenda for several consecutive projects over the next 10 years. The focus of the studies will be on updating the Bank's understanding of the current issues in the sector and identifying the most effective areas for intervention.

100. After the completion of the Bank's subsectoral long-term operational strategy, the Bank could

consider initiating a comprehensive country assistance impact assessment in Bangladesh in 2002 to 2003 to have a systematic review of Bank's operational impact during the past ten years or so. The country impact assessment is designed to evaluate the relevance and efficacy of the Bank's assistance. This study will also provide an initial assessment on the long-term focus approach identified by this country operational strategy study. This study will be set as a foundation for the next round of country operational strategy review, which is expected to be completed in 2004.

D. Environmental Dimension of the Strategy

101. High population growth, along with widespread poverty and nonsustainable productive practices, has caused serious natural resource degradation and environmental pollution in Bangladesh. Pollution levels may further increase as urbanization and industrialization accelerate. Bangladesh's environment is seriously threatened by deforestation, declining soil productivity and land degradation, biodiversity loss, and water and air pollution in urban areas.

- (i) Improving and protecting the environment remains one of the main thrusts of the Bank's country operational strategy to achieve the central objective of poverty reduction. In this context, taking into account the National Environmental Management Plan and its ongoing prioritization exercise, as well as past Bank experience, the Bank's operational thrust under its environment program (Appendix 3) over the medium term will be on: institution building to develop the capacity for environmental planning and management including policy reform, legislation and regulation strengthening, and pollution monitoring and control;
- (ii) formulation/implementation of an appropriate coastal sustainable development strategy including participatory measures and additional income opportunities; paying special attention to identifying environmental protection and

enhancement components of infrastructure projects;

- (iii) urban environmental improvement including sanitation, drainage, water and air pollution control, solid waste management, and others; and
- (iv) increasing the environmental orientation and sustainability of Bank operations including investment lending, TAs, and other policy support and capacity-building programs.

E. Gender Dimension of the Strategy

102. Women in Bangladesh face multiple constraints. The patrilineal system has given high value to sons, who receive preferential treatment and better access to nutrition, health care, and education. Gender disparities persist in many areas, such as adult literacy, school dropout, and life expectancy.

103. Integration of gender issues in the Bank's policy dialogue with the Government includes women's rights, women's role as active participants and agents in development, and their role as actors with a specific agenda for development. A gender-focused approach seeks to redress gender inequity by facilitating strategic, broad-based, multifaceted solutions to gender inequality.

104. The Bank's gender strategy for Bangladesh (Appendix 4) will encompass the following elements: (i) assist in policy support, capacity building, and awareness raising; (ii) facilitate gender analysis of proposed projects; and (iii) assist in implementing commitments made at the United Nations' Fourth World Conference on Women. The Government's National Action Plan for Women (approved in September 1997) spells out specific objectives and activities of 13 ministries and divisions to implement the Beijing Platform for Action. The strategy takes a holistic approach to addressing key constraints systematically, at the policy, institution, and sector/program and project levels.

105. The Bank will assist the Government's main aim in its Fifth Five-Year Plan — integration of women's development into the macro-framework and reduction of gender disparities in all sectors. The Government gives high priority to gender analysis, training, and sensitization of key personnel in the public and private sectors. In particular, emphasis

will be placed on capacity building, gender awareness and sensitivity, particularly on violence against women, and monitoring functions to ensure that the quantifiable, time-bound targets set under the National Action Plan will be achieved.

106. Second, at the local level, the Bank will promote women's participation in planning, designing, and implementing programs and projects. Conscious efforts will be made to include women in stakeholder consultation on an equal footing with men. At the same time, empowerment at the grassroots level will be promoted by supporting programs for raising public awareness of women's legal rights and benefits and support services.

107. Third, at the project level, the Bank will continue to support increasing women's access to resources and services, especially among the poor and disadvantaged. In particular, as the major thrust of the Fifth Five-Year Plan will be on developing women's skills and productivity, investment in the social infrastructure sector will incorporate affirmative actions for women. At the same time, the Bank will support women's employment, so that the skills and abilities will not be wasted. Bank assistance will strengthen the linkage between human development, poverty reduction, and economic growth.

F. Cofinancing and Aid Coordination

108. Given the declining availability of concessional resources, the Bank will continue its efforts to mobilize additional resources and strengthen coordination of the funding agencies for Bangladesh. The goal will be for true additionally, so that funds obtained are not part of what is already earmarked for the country by other external funding agencies. This can be achieved by creating opportunities to facilitate investment in new areas and introducing innovative approaches. Greater attention will be paid to obtain financing from export-import finance agencies in appropriate subsectors such as oil, gas, power, and telecommunications.

109. Although commercial cofinancing in Bangladesh has been further constrained by the negative impacts of the financial crisis in East and Southeast Asia on the emerging markets, there is still room for commercial cofinancing. Recent developments in the gas subsector and the

opening up of the power subsector are promising and have attracted the attention of international investors. Some opportunities may also be available in the capital, insurance, and long-term credit markets. The Bank will increase its efforts to seek private financing through cofinancing or by encouraging FDI through loan and equity operations from the Bank's private sector window. The Bank will also explore the possibility of using credit enhancement and guarantee facilities in some key infrastructure areas.

G. The Role of NGOs and Civil Society

110. The partnership between the Bank, NGOs, and civil society can be further strengthened. The involvement of NGOs and stakeholders should start at the stage of project design and the project preparatory TA level. Currently, in the Bank operations in Bangladesh, the role of NGOs has been limited to acting as subcontractors in the implementation of project components. Some new modalities need to be developed for the Bank to assist and involve NGOs and civil society on a broad basis. The Bangladesh Resident Mission should play a more active role in the consultations on general and specific sector and project issues with NGOs and civil society.

H. Governance

111. Considerable efforts should be made to redefine the role, size, and functions of the Government. Bangladesh's governance problems include (i) poor public sector management particularly for fiscal issues and SOEs; (ii) the lack of accountability and responsiveness of public institutions; and (iii) an overly centralized administration system. Administrative reforms are urgently needed to achieve greater efficiency and transparency in public sector management. Reform of the clogged judicial system is also necessary to ensure a quick and transparent resolution of disputes.

112. There is an urgent need to make the reform process more extensive by proceeding with major restructuring efforts. These efforts will transform the Government from being solely responsible for growth to being a catalyst or facilitator for private sector-led growth. There is considerable scope for further reforms in the legislative and regulatory framework for infrastructure to allow greater private sector participation. Addressing the governance problem could also improve the quality of Bank projects, as most project implementation problems in the past were of this nature. These problems include lengthy loan processing procedures, inadequate and delayed release of budgetary counterpart funds,

delays in contract awards, and lack of beneficiary participation in project design and execution.

113. In the past, the Bank's intervention in the governance area has been mainly indirect through policy dialogue and through the capacity-building components of projects. The Bank will gradually move from this indirect approach to providing direct lending assistance to the governance issues. The forthcoming Reform in Land Administration Project is the first attempt. The Bank will provide more assistance from its lending and TA programs in the future.

114. The Bank's strategy and operational approach will focus on (i) helping the Government to develop core administrative capacity including the identification of national priorities, establishment of realistic policies, and effectively implementing these policies; (ii) supporting Government efforts for public enterprise reform and changing its role from that of being solely responsible for growth to that of a catalyst or facilitator for private sector-led growth; (iii) supporting Government reforms to strengthen the legal framework; (iv) assisting in the Government's anticorruption efforts; and (v) strengthening the Government's development partnership with NGOs and the private sector where possible.

115. Following the Bank's recently approved anticorruption policy, Bank operations in Bangladesh in this area will focus on (i) supporting an accountable and transparent public administration, and strengthening the Government's capability to monitor public expenditure particularly key institutions; and (ii) ensuring that the Bank's projects and staff adhere to the highest ethical standards. The Bank will also coordinate with other external funding agencies to help the Government develop an explicit anticorruption program.

I. Risk Factors and Measures to Address Them

116. Political risk is still the main risk for the successful implementation of the proposed operational strategy. As the general election comes closer, political unrest is expected to heat up. The Government may face some difficulties to pursue politically sensitive reforms and institutional changes, which could be controversial. The speed of some ongoing reforms

could also be slowed. To minimize those impacts, the Bank's approach during this period could be (i) to incorporate this political risk in the project design and move politically sensitive components of the reforms to the next phase of sector intervention if possible; (ii) to stand firm on project covenants for which timely implementation is absolutely important and any delay could jeopardize the entire reform; (iii) to use the opportunity to do more sector studies and prepare for the opportunity of the new round of reforms after the election; (iv) to de-politicize the reform agenda by obtaining the wide support of stakeholders including the private sector, NGOs, civil society, and others.

117. While the current East and Southeast Asian financial crisis has had no significant negative impact on the Bangladesh economy so far, the country is still very vulnerable to the old type of crises caused mainly by the weak economic fundamentals including the large nonperforming portfolio in the banking sector, low foreign reserves, and poor fiscal revenue collection. The country could also be affected if a major regional country such as India experiences any major financial crisis. The Bank could help the Government to strengthen macroeconomic monitoring and supervision capacity. If there is a need, the Bank could cooperate with IMF and the World Bank to develop an early warning system for any potential crisis. The Bank could also assist the Government to participate actively in regional cooperation and coordination in macroeconomic policy with neighboring countries to minimize contagion effects.

118. When the Bank shifts its role from a project financing institution to a broad-based development institution, and when its operations involve more core policy reforms and institutional changes, the project failure rate as assessed using traditional standards could increase. The Bank should put less emphasis on traditional evaluation indicators such as annual lending level, disbursement, loan delivery, economic and financial internal rates of return, etc., and put more emphasis on overall development impact,

performance of policy reforms, and institutional changes. To maintain project quality and strengthen the enforcement of the reforms, the Bank should implement a more flexible exit policy for untenable projects and walk away from line ministries that show slow progress with reforms. The Bank should also be prepared to provide more staff time and effort for sector study, and project preparation and administration.

J. Performance Monitoring

119. **Annual COSS Implementation Review and Assessment.** While the country operational strategy identified the overall objective and medium- to long-term priorities of Bank operations in Bangladesh, it needs to be fully incorporated in the annual country assistance program exercise and closely monitored to ensure that the strategy is implemented. A special section on implementation review and assessment should be included in the annual country assistance plan exercises.¹ This section will include (i) whether the operations program in the past year reflect the strategic reorientation of the country strategy; (ii) the impacts on the four strategic priority areas; (iii) policy and institutional achievements in the Bank's operational areas; and (iv) lessons learned and measures for improvement.

120. **A Well-developed Bank Long-term Subsector Operational Strategy.** As discussed in paras. 99-100, a new set of long-term subsector Bank operational strategies will be completed in the next two years. Monitoring in subsector level will be based on the sector policy, institutional development, and investment agenda identified in the Bank's long-term subsector operational strategy.

121. Program Department should lead this annual monitoring exercise with close cooperation with project departments, SPO and PEO.

¹ In the current format of Country Assistance Plan, the section I: Country Performance Assessment largely discusses the general performance of the country. It is suggested that this discussion could be included in the Country Economic Review. The CAP mainly discusses Bank's operational performance impacts.

SECTOR STRATEGY

A. Agriculture and Rural Development

1. The agriculture sector plays a vital role in the country's economy; contributing one third to the total gross domestic product engaging two thirds of the domestic labor force. Its performance impact is not merely on the country's food security, but also on poverty reduction and overall economic growth. There has been a rapid progress in food production, especially rice in the last decade, but the country now faces the major challenges of achieving and sustaining high growth rates in the agriculture sector. Future growth in the sector would depend on both intensification and diversification because of the binding land constraint. The country's fifth five-year plan document emphasizes moving beyond self-sufficiency to improving value of output and income levels of farmers with greater private sector participation especially in agroprocessing and agribusiness.

2. Among the major constraints inhibiting agricultural growth in the country are: (i) lack of effective rural financial services for a majority of small and marginal farmers, (ii) lack of marketing support and high postharvest losses, (iii) lack of high quality planting materials, (iv) weak rural development and extension support, and (v) large unexploited irrigation potential and its suboptimal utilization. Most can be addressed through policy and institutional reform and entry of the private sector.

3. In recent years, the Government has moved away from integrated rural development approaches to rural infrastructure development, mainly rural roads, bridges, and rural markets. The Bank supports this approach because of the simplicity of implementation and its strong visible impact on growth and poverty (see Box 4). The Bank will continue to finance a series of projects to develop rural infrastructure, small irrigation works, and flood protection. These include measures to strengthen the institutional capacity of the main Government agencies and local government in these areas. The Bank will also support microfinance and crop/agrobusiness credit because of their strong

impact on poverty and private sector development, as well as the opportunities they provide for working with NGOs.

1. Crop/Agrobusiness Credit

4. Intensification and diversification of agriculture will increase the demand for capital and investments in supporting markets (input and output markets, agroprocessing, etc.). Therefore, integral to any effort to improve the situation would be access to financial services, be it for investments in agriculture production or to expand NGO and private sector entry.

5. The Bank's strategy would be identifying opportunities and means for greater NGO and private sector participation in the agriculture sector, creating an enabling environment, and exploring options and modalities for provision of financial services to the farming and agrobusiness community. The Bank operations will address (i) encouragement of private sector and NGO participation in crop/agrobusiness credit; (ii) establishment of a suitable crop/agrobusiness credit delivery system and regulation and supervision system.

2. Rural Infrastructure

7. The Bank's strategy in the rural infrastructure subsector includes upgrading and maintaining rural roads and bridges, enhancing the flow of services and investment in the rural market, as well as providing the rural poor with the means to engage in income-earning activities. In line with the Government's policy for rural development, the Bank's future operations need to focus on several areas including (i) community participation in infrastructure development; (ii) coordination of complementary road and water transport activities; (iii) establishing and funding a sustainable maintenance system; (iv) increasing the role of the private sector in infrastructure development; (v) instituting viable operation

and maintenance systems for improved infrastructure; and (vi) continued institutional strengthening.

3. Water Resource Development

7. The water sector is of fundamental importance to agriculture both in terms of irrigation needs and reducing risks from flooding and drainage congestion. The National Water Policy developed by the Government recently provides guides for water resource development and management in the medium term. In the past, the Bank provided assistance to address both large- and small-scale irrigation as well as flood control projects. While the small-scale water resource development project performed well with active involvement with beneficiaries, the Bank's experience in large-scale water management area is not very satisfactory.

8. In the short run, the Bank will focus mainly on small-scale water resource management and flood protection. Its operational strategies are to support effective rehabilitation and to upgrade small-scale water resource infrastructure by enhancing participatory processes, improving financial efficiency, and helping the poor while at the same time not disturbing underlying natural processes. The Bank's investment will also address flood protection facilities. In the areas of medium and large-scale water resource management, the Bank's current focus is to support institutional reform initiatives to improve resource management and service delivery. Major investments in this area, however, will be contingent upon demonstrated success in implementation of the reform program and strengthened capacity of the Bangladesh Water Development Board. Recently, the Government approved the National Water Policy, which addresses many important issues including quality of operation and maintenance, cost recovery, community and beneficiary involvement, and participation of the private sector. The Bangladesh Water Development Board is also undertaking significant structural reforms. Given the importance of large-scale water resource management in the country and recent progress in the subsector, the Bank's role and involvement in this area will be reviewed in 1999 and revised as necessary.

4. Microfinance

Microfinance has become one of the most effective means for direct poverty intervention in Bangladesh and many parts of the developing world. However, despite rapid development over the past decade, there is still a large proportion of rural poor and almost all of the urban poor who have not been reached by any microcredit. Meanwhile, there microfinance program such as lack of creditable resources and poor sustainability capability.

10. The Bank's focus in this subsector will be on (i) assisting NGOs and Government in supporting microcredit institutions to convert them to formal financial institutions; (ii) helping the Government and Bangladesh Bank to develop a regulatory and supervisory framework on these upgraded institutions; and (iii) assisting NGOs to expand microcredit activities to help the urban poor.

11. In recent years, the livestock subsector has played an important role in providing food, cash income, employment opportunities, and security to the rural poor in Bangladesh. Over 90 percent of poor rural households raise poultry as an important source of cash income and food. Because of their minimum requirement for land and feed, beef, dairy, and goat projects have also played an important role in helping the poor. Currently, lack of quality feeds and lack of access to credit have constrained the expansion of all livestock activities, as have problems with animal diseases. The weaknesses of Government policies and institutions have also undermined the fast growth of the subsector.

12. The Bank's involvement in livestock will be through providing microfinance and policy support. The Bank's operational focus in the subsector will be to (i) support the Department of Livestock Service in reorienting its policy and approach to the delivery of services to the poor; (ii) develop the capabilities of Government agencies concerned, NGOs, and local communities to plan, research, and manage livestock development

activities; (iii) provide additional credit and financial resources via NGOs and others to the poor; and (iv) develop mechanisms for the sustainability of NGO activities in the area.

B. Energy

13. Shortage of energy has long been the major constraint to fast economic growth and poverty reduction in Bangladesh. Power is available to only 15 percent of the population, and the sector has suffered considerably from low efficiency and are many constraints to further expansion of a huge system losses. As the leading aid agency in the energy sector, the Bank assisted the Government in restructuring the power and gas subsectors from being Government dominated to Government regulated by rationalizing tariffs, unbundling the monolithic structure of the public sector, and promoting private sector participation. Given its strong impact on economic growth and poverty reduction, as well as the firm commitment of the Government in pursuing policy reforms in the area, the Bank will remain active in the sector. However, with the participation of the private sector in recent years, the energy supply of both gas and power has improved considerably. The Bank's operational focus, therefore, needs to be adjusted accordingly. Given the high return of the sector, the Bank will gradually convert this sector to ordinary capital resource (OCR) lending.

14. The shortage of power has become one of the most important bottlenecks to economic development. Per capita consumption of electric power is extremely low compared with its neighbors. Operational performance has deteriorated with high system losses and poor revenue collections. In view of this poor performance, the Government, with assistance from funding agencies, formulated comprehensive reforms in 1994. The Government has also taken concrete steps to involve the private sector. A potential power source has been created to add 1,400 megawatts (MW) of capacity over the next five years on a build-operate-own basis with the private sector. This is 45 percent of the current installed capacity. Functional restructuring of the sector is also under way. Tariff setting is being

adjusted periodically, and a statutory regulatory authority will be established soon.

15. The Bank's medium-term operational focus in the power subsector will be to (i) expand and upgrade the distribution capacity of the system particularly to the rural areas; (ii) continue to support the Government's reform measures, including unbundling the subsector into generation, transmission, and distribution companies, and establishing an independent regulatory authority; (iii) support and participate in private sector investment in generation and distribution; (iv) gradually convert Bank assistance from the Asian Development Fund (ADF) to OCR; and (v) promote regional cooperation.

16. Natural gas is an important resource for economic development. The share of natural gas in commercial energy consumed has grown from 35 percent in 1980 to about 70 percent in 1998. In 1993, the Government introduced a new petroleum policy to encourage private sector participation in gas exploration and production under production-sharing contracts. This policy has been generally successful, and the flow of gas from the first round of contracts is expected shortly. The current gas shortages are expected to be overcome by the end of 1998. There are real prospects that the gas reserves may become the driving force in the economic development of the country by closing the energy supply-demand gap and by providing substantial foreign exchange earnings.

17. Given the increasing inflow of private sector capital in the gas area, the Bank should gradually shift the focus from direct investment to mainly supporting policy and institutional reforms. The Bank's operational focus in the gas will be on (i) creating an enabling environment for private investment in the sector, including the creating a regulatory framework, increasing in efficiency of the public sector corporations, and rationalizing prices; (ii) reducing system losses and improving

efficiency; (iii) assisting the Government to develop a gas utilization policy to maximize the economic benefit of gas reserves; and (iv) promoting regional cooperation whenever an opportunity arises.

C. Capital Market

18. Sustainability of the growth of the economy at rates sufficient to reduce poverty depends to a large extent on the ability of the financial system to mobilize and efficiently allocate domestic resources and attract foreign investments. However, at the moment, a largely inefficient banking system and the nascent capital market make it hard to channel whatever scarce domestic savings are available in the economy into productive investments.

19. To assist Bangladesh in developing its capital market, the Bank in 1997 approved the Capital Market Development Program loan.¹ The reforms under the program aim to (i) strengthen market regulation and supervision; (ii) develop capital market infrastructure; (iii) modernize capital market support facilities, including automation of stock exchanges and establishment of an automated central depository; (iv) develop institutional sources of medium- to long-term funds to increase demand for securities; and (v) improve policy coordination. Considering the strong impact of financial markets on private sector development and economic growth as well as the division of labor among the Bank, IMF, and the World Bank, the Bank will continue to operate in this area as the leading aid agency.

20. The Bank will continue to focus its activities mainly on stock markets, insurance, and pensions. The objective of the Bank's strategy in this subsector will be to develop an efficient and transparent capital market to facilitate efficient resource mobilization and allocation necessary to attain sustainable industrial development and economic growth. This objective will be achieved through a combination of policy reforms, capacity-building efforts, and investments in close coordination with other funding source aimed at relieving existing bottlenecks in the sector, and promotion of competition and a level playing field.

21. More specifically, the Bank will continue to address capacity-building needs in the finance sector, including strengthening the existing regulatory authorities, i.e., Bangladesh Bank, Securities and Exchange Commission, Privatization Board, Board of Investments, etc., and establish autonomous regulatory authorities for the insurance sector and pension and provident funds. Further assistance will also be focused on the development of capital market institutions including possible equity participation in merchant banking, asset management, and central depository system.

22. In the insurance sector the focus will be on the (i) introduction of a new insurance act and prudential regulations, (ii) establishment of a level playing field that will allow more private sector participation in the insurance sector including exploring the possibility of participation of foreign companies; (iii) liberalization of insurance premium pricing; and (iv) restructuring and privatizing Jiban Bima Corporation and Sadharan Bima Corporation. In the area of pension and provident funds the focus will be on (i) enactment of revisions to the Trust Act and Provident Fund Act and rules; (ii) extension of the social security system to private sector employees; and (iii) introduction of prudential regulations and further liberalization of investment rules.

23. The Bank will assist the Government in the development of long-term financial market. Currently, there is an acute lack of financial institutions geared to provide a meaningful amount of long term financing to private sector. The Bank will explore the possibility of enhancing the capacity of the well performed financial institutions or developing new institutional vehicles in this area through an equity investment in a joint venture with local and international partners. Also, credit enhancement in the form of guarantees can be provided. These investments will further contribute to institutional deepening in the finance sector. Furthermore, the Bank will assist in the development of the domestic Government and corporate bond market.

¹ Loan No. 1580-BAN: *Bangladesh Capital Market Development Program Loan*, for \$80 million, approved on 20 November 1997.

D. Transportation

24. Road traffic is the most important transport mode accounting for about 60 percent of freight and 75 percent of passenger traffic, followed by inland waterways (32 percent and 13 percent) and railways (7 percent and 12 percent). During the last two decades, the prime modal shift was away from railways to roads. The principal port is Chittagong, which is the lifeline of the country's trade. The arterial corridor is from Chittagong through Dhaka (Bangladesh's main industrial base) up to the Northwest region. Demand for both passenger and freight traffic has been steadily increasing at 10 percent per annum since the mid-1970s, but is expected to increase with the shift to a market-based economy and the completion of the Jamuna Bridge, which will possibly attract freight from India and Nepal. Given the crucial role of the transportation sector in promoting faster economic growth, its impact on poverty (para. 59), as well as the comparative advantage that the Bank has developed in the past decades, the Bank's operation in this sector will focus on railways, roads, and waterways, with emphasis on promoting subregional cooperation.

1. Railways

24. The Bank has a long-standing involvement in the rail subsector with three projects and one program loan. The Bank's strategy for railways emphasizes commercialization and restructuring of Bangladesh Railway (BR) into an autonomous entity to improve sector efficiency. Some progress has been made under the ongoing program loan in spinning off some railway services to the private sector, increasing railway profitability, and consolidating the physical network. The medium-term objective is to put BR on sound financial footing: restructured, fully commercialized, and separated from the Government for corporatization. Under the strategy, priority is given to improving BR's freight business, financial performance, and administrative efficiency.

25. The Bank's intervention in the medium term will be concentrated in the areas of supporting major railway links to neighboring

countries, and supporting policy and institutional reforms in the railway subsector. It includes (i) further organizational restructuring and commercialization of BR aimed at separating it from the Government and transforming it into a more autonomous commercial entity before corporatization; (ii) establishing clear boundaries and distributing appropriate powers and authority to the Government, Bangladesh Railway Authority, and BR's management; (iii) adopting appropriate legislation and other measures required to make the reforms permanent and irreversible; (iv) strengthening the marketing and personnel departments; (v) corporatizing BR; (vi) focusing on freight traffic and restructuring freight tariffs as a means to improve BR's financial performance; (vii) rationalizing BR's resources including staff and assets to improve productivity; (viii) encouraging private sector involvement and private financing in selected areas; (ix) supporting the development of a core railway network for the major volume of traffic; (x) gradually downsizing and abandoning underutilized branch lines to reduce the need for subsidization supporting regional cooperation on railway issues.

2. Roads

27. The Bank has been involved in completing two of the five main road transport arteries in Bangladesh. Looking beyond those five corridors, the Bank could increasingly involve in subregional road links with neighboring countries and on policy and pricing issues. In the longer term, support of private sector operations is also an essential future Bank perspective.

28. To implement the strategy, the Bank could (i) support investment in sections of the major corridors especially those with regional implication; (ii) invest in internal road network particularly those with strong poverty impact; (iii) study institutional, legal, and regulatory measures to improve cross-border traffic flows on rail, road, and inland water; and (iv) investigate policy and

institutional changes for private sector mobilization of transport investments.

3. Ports

29. The ports subsector will be assisted through the proposed Port Efficiency and Access Improvement Project. The project will enhance the efficiency in the port subsector by providing essential equipment, improving access roads, and facilitating containerization infrastructure. It will also initiate policy dialogue for a regulatory framework conducive to commercialization and private sector participation, enhancing the autonomy and accountability of port authorities, and improving relations between port workers, port employees, and port management. Further investment will depend on the success of the project, and on continued political commitment of the Government to the reform process.

30. The Bank's future involvement in the port subsector will be subject to commitment by the Government to policy reforms and the progress of the Port Efficiency and Access Improvement Project. Its focus in the subsector will be on (i) support for sector reforms and efficiency improvements in the port subsector, (ii) encouragement of private sector participation in port development and management, (iii) skills training and human resource development, and (iv) environmental management and protection.

E. Urban Development

32. The key sector concerns in the area of urban development are poor living conditions and environmental degradation, weak institutional policy and regulatory frameworks for urban development planning and management, inadequate revenue generation and expenditure allocation policies and mechanisms, and antiquated and inefficient land administration systems and procedures. The continued productivity of urban areas is contingent upon the availability of urban infrastructure and services. However, the growth of urban areas in Bangladesh has consistently been faster than the growth of infrastructure and services. Most urban areas have no underground drainage system and suffer from

waterlogging problems. Road systems are insufficient with no regular and routine maintenance program being undertaken. Public facilities including markets, public health, solid waste management, and basic services for the urban poor do not meet the demands of the communities.

33. Bank assistance is mainly to secondary towns. The operational focus is on (i) improving decentralization and strengthening the local government's capacity to deliver quality services in a sustainable manner; (ii) ensuring sustainability in the delivery of urban services through strengthening urban management capacity, particularly improving financial revenue generation; (iii) supporting community and private sector involvement in urban services; (iv) improving the living conditions of the urban poor; and (v) addressing urban environmental issues.

F. Social Infrastructure

34. Bank assistance to social infrastructure has increased gradually during the past decades. From 1973 to 1987, lending was only 6 percent of total Bank lending to the country. This rose to 25 percent from 1988 to 1997.

35. In spite of the considerable efforts made by the Government and funding agencies, human development inadequacies remain the principal impediment to poverty reduction and social advancement. Social infrastructure should thus be a principal area of the Bank's program. The Bank's long-term operational focus will be on secondary and basic education as well as urban primary health, given their strong impact on poverty reduction and considering the division of labor among the donor agencies. The effectiveness of service delivery and the availability of funds are the most critical issues in human development. The Bank's policy focus in this area is to support more community involvement and private sector participation in service delivery. Efforts should also be made to address institutional capacities for sustained growth.

1. Education

37. The Bank is one of the major funding agencies for education. To date, Bank assistance has covered primary, secondary, and nonformal and distance education, as well as vocational/skills training. Apart from being a lead agency in secondary education, the Bank has also played a major role in assisting the Government in enhancing the accessibility and quality of basic education.

37. While the Government has made substantial progress in making basic education more accessible, its goal of eradicating illiteracy by 2006 will require continued support from funding agencies, including the Bank. The Primary Education Development Plan (1997-2002) of the Government identified several priorities. For instance, the current student-teacher ratio of 70 to 1 needs to be reduced to a more manageable and internationally acceptable level of about 40 to 1. The quality of education is expected to become a more pressing issue as additional new schools are built. This issue also needs to be addressed at several fronts given its multidimensional nature. Access to secondary schools remains poor with only about 34 percent of secondary school-aged children attending. Secondary schools are inadequately managed, have limited facilities, and offer a low standard of education that does not prepare graduates for higher education or employment. In addition, the success in achieving higher completion rates in primary education is now exerting pressure on the country's secondary school system. To help address this issue, the Bank is helping the Government to prepare a secondary education development program (1999-2004), which will serve as the basis for the Bank's strategic involvement in secondary education.

38. The Bank's operational strategy for education aims to (i) increase equitable access to basic education, particularly for girls and disadvantaged children; (ii) improve education quality and system efficiency, particularly in teacher training; (iii) strengthen the institutional and management capacity to deliver basic and secondary education; and (iv) support decentralization and community involvement in

education. The Bank's future involvement will focus on basic education, which includes primary, nonformal, and secondary education.

2. Urban Primary Health

39. The vast majority of the country's population continues to suffer from poor health even if Bangladesh has made some remarkable progress in improving its health and fertility indicators since its independence. Poverty-related infectious diseases have remained the major causes of death.

40. Bank operational experience has shown that the complexity and variety of health issues in Bangladesh will require that the Bank adopt innovative approaches that can be tested on a pilot basis initially and replicated later with improvements. These pilot projects would be more focused and more manageable than large-scale programs that are designed within the administrative framework of the Ministry of Health. In order to improve coordination with the Government and other donors, the Bank should formally participate in Health and Population Sector Program in the future.

41. The Bank's operational focus in the health sector is in the area of urban primary health, mainly in the small and secondary towns. The sector strategy aims to (i) support the Government policy for decentralization of health services, communicable disease control, and reproductive health; (ii) develop public-private partnerships for primary health services and supply of drugs; (iii) enhance privatization of primary health services to vulnerable groups in a more effective manner; and (iv) develop alternative health care financing schemes, including a social insurance system for providing affordable medical care and protection for old age.

G. Regional Cooperation

42. One of the newer strategic areas in which the Bank will operate in the near future is in the field of subregional cooperation.

There are plenty of opportunities for South Asian countries to accelerate regional economic cooperation. The Bank has extensive operational experience in South Asia and enjoys an excellent relationship with all the countries in that region. It also has considerable experience in regional cooperation through its support for the Greater Mekong Subregion and other such groupings. Since mid-1996, the Bank has been working toward encouraging regional cooperation in South Asia. Efforts have focused on cooperation between Bangladesh, Bhutan, India, and Nepal.

43. The Bank's strategy and operational approach will adhere to the following principles:

- (i) It will focus on selected projects and sectors rather than attempt to establish any global framework or institutions for cooperation. The Bank's role should be as a provider of expertise and background facilitator, that is, to be an honest broker rather than a leader of the cooperation.

- (ii) Initially, relatively small projects that have self-evident benefits could be chosen; those that can be developed from ongoing national programs are also preferred.

- (iii) An important element of Bank assistance will be the dissemination of information as well as extensive consultations for consensus building, not only within governments but also in wider civil society.

44. The Bank's operational focus will be concentrated on infrastructure, particularly for regional road and rail linkages. In the future, the Bank will support road and railway projects only if the project and program are a part of the regional network and support regional cooperation efforts. The Bank will play a leading role in regional power-sharing arrangements. If the opportunity is available, it is ready to support regional cooperation in gas and other subsectors.

ECONOMIC AND SECTOR WORK PROGRAM FOR COUNTRY STRATEGY

The main task of the economic and sector work for Bangladesh in 1999 and 2000 is to develop a set of Bank long-term operational strategies in each subsector selected by the country operational strategy. The focus of the studies will be on updating the Bank's understanding of the current issues of the subsector and identifying the most effective areas for intervention. The new set of the studies will make a

comprehensive reassessment of the constraints and lessons learned from the Bank's past operations in the subsector. They will also identify the Bank's subsector strategy and priorities. Support to policy reforms, institutional development, and investments under several consecutive projects in the next 5 to 10 years will also be identified by the studies, details of which are presented below:

Economic and Sector Work Program

No.	Title	Description	Year of Initiation
1	Bank's long term operational strategy in private sector development	Assess the constraints to private sector development in Bangladesh, formulate Bank's long term strategy, and design phased interventions to promote private sector development.	1999
2	Bank's long term operational strategy in Governance	Examine governance issues in Bangladesh; formulate Bank's long term operational strategy, and design interventions to promote good governance.	1999
3	Bank's long term operational strategy in Environment	Discuss environment issues in Bangladesh, formulate Bank's long term operational strategy, and design phased TA and lending program to help address environmental issues.	1999
4	Capital Inflow and Risk Management in Bangladesh	Conduct risk management in the context of capital flows to Bangladesh. The major policy concerns arising from the recent East Asian Crisis and probable balance of payment impact of significant FDI flows will be assessed.	1999
5	Bank's Long Term Operational Strategy for Advisory Assistance for Macroeconomic Analysis and Data Management	Review advisory technical assistance requirements for macroeconomic analysis and data management, and lessons learnt from the Bank operations in this area. The study will also identify and recommend areas of Bank's involvement over the longer term for macroeconomic analysis and data management.	1999

Economic and Sector Work Program (cont'd.)

No.	Title	Description	Year of Initiation
6	Bank's long term operational strategy in capital market	Assess capital market constraints to private sector development; define the Bank's long-term strategy, and design-phased interventions to promote capital market development.	1999
7	Bank's long term operational strategy in road transportation	Review the Bank's past experience in the sector and government's development focus; identify Bank's long term strategic approach and design phased intervention in the roads, railway and waterways subsectors with emphasis on promoting subregional cooperation.	1999
9	Bank's long term operational strategy in urban development	Assess Bank's operational experience in the sector and identify the most effective way for intervention. Three or more phases will be designed.	1999
10	Bank's Long Term Operational Strategy for water resource management	The study will review the recent progress of reforms in the sector and assess institutional capacity of Bangladesh Water Development Board. The study will recommend whether the Bank should continue to be involved in the large-scale water resource management area.	1999
11	Bank's long term operational strategy in crop/agro-business credit	Review the Bank's past experience in the sector and government's development focus; identify Bank's long term strategic approach and design phased intervention in the area; identify ways to promote NGO and private sector participation in the development of crop/agrobusiness credit system.	2000
12	Bank's long term operational strategy in energy	Assess Bank's operational experience in the sector and identify the most effective way for intervention. Three or more phases will be designed.	2000
13	Bank's long-term Operational Strategy in urban primary health	Discuss sector issues in secondary towns primary health and formulate Bank's long term assistance program which includes policy reforms, institutional development and investments.	2000
14	Bank's long-term operational strategy in basic education	Review past experience and current constraints of the sector and identify the Bank 's long term strategy and interventions in both primary and non-formal education; particular attention should be given to improvements in quality and system efficiency.	2000

ENVIRONMENT STRATEGY*

1. High population growth, along with widespread poverty and nonsustainable productive practices, has caused serious natural resource degradation and environmental pollution in the country. Pollution levels may further increase as urbanization and industrialization accelerate. Bangladesh's environment is seriously threatened by deforestation, declining soil productivity and land degradation, biodiversity loss, and water and air pollution in urban areas.

2. The Bank's environmental lending to the country has mainly focused on (i) sustainable management of natural resources; (ii) urban environmental improvement and urban infrastructure; and (iii) water resource management, flood control, and protection.

3. Improving and protecting the environment remains one of the main thrusts of the Bank's country operational strategy to achieve the central objective of poverty reduction. In this context, taking into account the National Environmental Management Plan and its ongoing prioritization exercise, as well as past Bank experience, the Bank's strategic priorities in the environment sector will focus on the following areas:

- (i) All Bank operations will have to be more environmentally oriented and systematically incorporate crucial environmental dimensions. Particular attention will be given to environmental problems closely linked to poverty perpetuation processes.
- (ii) Major efforts, through innovative approaches involving local communities and the private sector, will focus on strengthening Government capacity to adopt new coherent policies, and to effectively enforce compliance with existing environmental regulations. Institutional gaps and failures will warrant special focus on a better definition of roles and responsibilities,

intrasectoral and intersectoral coordination, and incorporation of environmental concerns into sectoral policymaking, and investment plans.

- (iii) Forestry and biodiversity. The Bank has three ongoing projects (Coastal Greenbelt, the Forestry Sector, and Sundarbans Biodiversity Conservation). Major issues currently addressed relate mainly to the legal and institutional reorganization needed to effectively implement the new forest policy. As present capabilities of the Forestry Department are inadequate, it may not be appropriate to add more interventions in the forestry sector until the ongoing policy reform process is consolidated and shows concrete positive results. Based on comprehensive reviews to be conducted within the Bank's three ongoing projects, further directions of Bank operation in the area will be developed during the next revision of the country operational strategy.
- (iv) Urban environmental management. There is a strong need to substantially improve urban governance for environmental services. As a part of the Bank's urban development strategy, the focus will be mainly on secondary town environmental management. Enhancing private sector involvement by providing a conducive regulatory framework and promoting the provision of urban services by private operators could go a long way in addressing environmental needs in a financially sustainable way. Similarly, other programs could be aimed at increasing efficiency/effectiveness of public administration, and supporting greater community and nongovernment organization participation.

* This section is prepared by Daniele Ponzi, Economist (Environment), Programs Department (West).

GENDER STRATEGY¹

A. Key Issues and Constraints

1. Women in Bangladesh face multiple constraints. The patrilineal system has given high value to sons, who receive preferential treatment and better access to nutrition, health care, and education. Gender disparities persist in many areas, such as adult literacy, school dropout, and life expectancy.

2. About 36 percent of women in Bangladesh are economically active (crude activity rate, age 10 years and over, 1995/1996). Because of their low levels of educational attainment and lack of skills, a large majority of the female workforce are unpaid family workers. While nearly 90 percent of women are employed in agriculture, the female labor force is growing at a faster rate than that of males in the industry sector, particularly for low-skilled jobs. The growth of the urban female labor force has raised concerns such as male-female wage disparities, limited upward mobility, poor working conditions, security, housing, and legal/regulatory issues.

3. In the agriculture and informal sectors, women are forced to accept low-paying jobs due to poverty and landlessness. There is a strong correlation between poverty and gender inequality. These households headed by women earn 40 percent less than households headed by men. Differential wage rates exist for women and men. Women generally have little access to or control over productive resources including land and formal credit because of prevailing religious and cultural beliefs and practices. Women's entrepreneurial activities are limited as the social norms restricting women's mobility make it difficult for them to have access to training, market information, and interactions with wholesalers and other entrepreneurs.

the development process, as stipulated in the Bank's policy on gender and development.² Strategic emphasis is widened to include women's rights, women's role as active participants and agents in development, and their role as actors with a specific agenda for development. A gender-focused approach seeks to redress gender inequity through facilitating strategic, broad-based, multifaceted solutions to gender inequality. In line with the above Bank policy, the gender strategy for Bangladesh will encompass the following elements: (i) assist in policy support, capacity building, and awareness raising particularly on violence against women; (ii) facilitate gender analysis of proposed projects; and (iii) assist in the implementation of commitments made at the United Nations Fourth World Conference on Women and the subsequent Government's National Action Plan (NAP) for Women.

C. Bank Assistance and Operations

5. The main thrust of Bank assistance is to support the NAP, which stipulates specific objectives and activities of 13 ministries and divisions. The NAP focuses on institutionalization and implementation of the sectoral gender-accounting system by setting up time-bound and quantitative targets to achieve gender parity. Bank assistance will be provided through (i) policy dialogue, (ii) incorporation in the Bank's sector strategies and operational programs, and (iii) at project level through loans and technical assistance (TA).

6. Macro-level policy dialogue encompasses the review of public resource allocation to promote gender equality, while working directly

¹ This section was prepared by Yuriko Uehara, Social Development Specialist, Programs Department (West).

² R74-98: *The Bank's Policy on Gender and Development*, 11 June.

with the focal points in line ministries on the sectoral issues. The relevant chapters of the NAP have been circulated to the project divisions concerned. The Bank will ensure the implementation of the NAP in all sectors where the Bank is involved and that Bank loans and TAs contribute to achieve quantifiable, time-bound targets set under the NAP.

7. The absolute majority of women are employed in the agriculture sector. Of all the household assets, the most important for women is land, especially homesteads wherein they carry out economic as well as household activities. The lack of rights to hold homesteads and/or land places women in a very insecure position, especially in the event of crises (widowhood, separation, and abandonment) and can deprive them of the benefits of development assistance. The Bank will address this issue encompassing land titling, inheritance rights, and user rights through policy dialogue and project level interventions (loans and TAs), especially in rural development.

8. The Bank will continue to support increasing women's access to resources and services, especially among the poor and disadvantaged. In particular, as the major thrust of the Fifth Five-Year Plan is developing women's skills and productivity, the Bank will promote women's employment and income generation to reduce poverty. Poor rural women need to be organized and involved as stakeholders to receive lasting benefits from resources they help to create. Investment in the social infrastructure sector will incorporate affirmative actions for women with specific attention to reduce locational and class disparities. The Bank will ensure the participation of tribal women in development.

9. In the urban sector, supportive infrastructure and services for women workers in the formal sector, such as working women's hostels, childcare facilities, and training programs, are urgently needed. These could be considered in the context of developing a strategy to address the urban poor and supporting community and private sector involvement.

BANGLADESH
COUNTRY PERFORMANCE INDICATORS

Item	FY1994	FY1995	FY1996	FY1997	FY1998	FY1999 ^d
ECONOMIC INDICATORS						
A. Income and Growth^a						
1. GDP per Capita (dollars, current)	285.0	314.0	330.0	333.0	337.0	350.4
2. GDP Growth (% , in constant prices 89/90)	3.8	5.8	4.6	5.4	5.2	4.8
Agriculture	-0.8	-0.6	3.4	6.1	3.0	3.5
Industry	6.1	10.0	6.6	5.6	8.3	4.0
Services	4.4	7.0	4.2	4.8	4.6	6.0
B. Savings and Investment (current market prices)						
	(percent of GDP)					
1. Gross Domestic Investment	18.6	19.8	20.4	20.3	20.4	20.5
2. Gross National Saving ^b	19.4	19.3	18.1	19.9	19.8	19.0
C. Money and Inflation						
	(annual percent change)					
1. Consumer Prices (annual average) ^c	3.3	8.9	6.6	2.6	7.0	9.0
2. Broad Money (M2)	15.4	16.0	8.2	10.8	10.1	12.0
D. Government Finance						
	(percent of GDP)					
1. Total Revenue	9.1	9.4	9.4	9.7	9.7	9.0
2. Total Expenditure	13.9	14.7	14.3	14.2	14.0	14.3
3. Overall Surplus/Deficit (-)	-4.8	-5.3	-4.9	-4.5	-4.3	-5.3
E. Balance of Payments						
1. Merchandise Trade Balance (% of GDP)	-4.9	-6.3	-7.6	-6.8	-5.7	-5.9
2. Current Account Balance (% of GDP)	-0.3	-1.8	-3.2	-1.3	-0.6	-2.1
3. Export (\$) growth (annual percent change)	6.3	37.1	11.8	14.0	16.8	2.7
4. Import (\$) growth (annual percent change)	2.9	39.2	17.9	4.1	5.1	6.0
F. External Payments Indicators						
1. International Reserves (billion dollars, end of period)	2,770.4	3,085.1	2,037.4	1,718.6	1,750.7	1,522.0
- months of imports	8.2	6.3	3.6	2.9	2.8	2.3
2. External Debt Service (% of exports of goods & services)	11.6	10.3	12.1	11.4	n.a.	n.a.
3. External Debt (% of GDP)	43.5	39.3	39.1	38.5	n.a.	n.a.
Memorandum Items:						
GDP (current prices, billion Taka)	1,342.4	1,512.1	1,648.4	1,765.4	1,938.3	2,187.0
GNP (current prices, billion Taka)	1,384.7	1,558.6	1,698.0	1,810.6	1,989.2	n.a.
Exchange Rate (Taka per dollar, annual average)	40.0	40.2	40.9	42.7	46.3	48.5
Population (million)	117.7	119.9	122.1	124.3	126.5	128.7

^a The Government set up an independent Task Force in May 1996 to review the National Accounts. It appears that the accounts were flawed by inadequate coverage, outdated coefficients and methodological weaknesses. On the basis of the recommendations of the Task Force and advice of experts at home and abroad, the accounts have been rebased on the constant prices on FY1989/90. These new series have been adopted for use by the International Monetary Fund and the World Bank. The Government is reviewing them prior to official approval.

^b Gross national saving = GDP at current market prices less consumption plus net factor income from abroad plus net private transfers from abroad.

^c At FY1985/86 = 100, consumer price index, National.

^d Provisional estimate.

Note : Fiscal year for Bangladesh is from 1 July to 30 June, e.g., FY1997/98 figures cover the dates 1 July 1997 to 30 June 1998.

Sources: *Bangladesh Annual Economic Update 1997*.

Economic Indicators, Office of Resident Representative, IMF, 8 June 1998.

Bangladesh Bureau of Statistics.

Ministry of Finance, Economic and Relations Division, "Memorandum for Bangladesh Development Forum 1999-2000".

**BANGLADESH
COUNTRY PERFORMANCE INDICATORS**

	1985	1990	Latest Year
POPULATION INDICATORS			
Total Population (millions)	97.50	109.60	128.70(1998-99)
Annual Population Growth Rate (% change)	2.07	1.95	1.80(1998-99)
SOCIAL INDICATORS			
Total Fertility Rate (births per woman)	4.70	4.30	3.40(1997)
Maternal Mortality Rate (per hundred thousand live births)	-	-	449.00(1994)
Infant Mortality Rate (below 1 year; per '000 live births)	112.00	92.00	78.00(1996)
Life Expectancy at Birth (years)	55.00	56.00	58.00(1996)
Female	56.00	55.70	58.10(1996)
Male	55.00	56.50	57.60(1996)
Adult Literacy (%)	33.00	35.30	47.30(1996)
Female	18.00	25.80	38.10(1996)
Primary School Enrollment (% of school age population)	63.00	76.00	95.00(1996)
Female	43.80	70.00	94.00(1996)
Secondary School Enrollment (% of school age population)	17.00	19.00	38.00(1994)
Female	10.00	14.00	-
Child Malnutrition (% of under age 5)	-	64.20	-
Population Below Poverty Line (%)	-	47.50	47.50(1995-96)
Income Ratio of Highest 20% to Lowest 20% ^a	-	4.03	-
Population with Access to Safe Water (%) ^b	-	80.00	-
Population with Access to Sanitation (%) ^c	-	63.00	-
Public Education Expenditure as % of GNP ^d	1.77	1.80	2.30(1995)
Public Health Expenditure as % of GDP	0.67	0.90	1.25(1995-96)
Human Development Index	0.32	0.19 ^e	0.37(1995)
Human Development Ranking	108.00	147.00	147.00(1995)
ENVIRONMENTAL INDICATORS			
Forestry			
Forest Area (thousand sq km)	-	-	10.00(1993)
Extent of Forest and Woodland (% of total land area)	9.54(1980)	11.30(1990)	13.20(1993)
Annual deforestation (sq. km.)	-	-	88.0(1990-95)
Annual deforestation (average % change)	-	-	0.80(1990-95)
Biodiversity			
National Protected Areas (%)	-	0.70(1990)	0.80(1997)
Land Use			
Per Capita Crop Land (ha)	0.10(1983)	0.08(1990)	0.07(1994)
Cropland (% of land area)	70.00	-	67.00(1994)
Permanent Pasture (% of land area)	5.00	-	5.00(1994)
Water Pollution			
Emissions of organic water pollutants(kg/day)	66,700.00	-	171,00.00(1993)
Global Environmental Problems			
CO ₂ emissions (total metric tons)	7.60	-	20.90(1993)
(per capita metric tons)	0.10	0.15 (1982)	0.20(1993)
Energy Efficiency of Emissions			
Per Capita Commercial Energy Consumption (Giga joules)	-	3.00(73-93)	3.50(1995)
Traditional fuel use (% of total energy use)	67.80	-	49.90(1995)
GDP per unit of energy use (1987\$ per kg oil equivalent)	4.50	-	3.00(1995)

^a Refers to expenditure ratio.

^b Percent of households with either tap or tube well water source.

^c Refers to % of households.

^d Percent of GDP for FY1984/85 and FY1989/90.

^e Human Development Index and Rank may not be comparable in different years since statistical administration and research bodies seek to update or improve their estimates using new sources of data such as censuses and surveys as indicated in the *Human Development Report 1997* of UNDP.

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