ACE Anti-Corruption Evidence
Making Anti-Corruption Real

Working Paper 003

Anti-Corruption in Bangladesh: A political settlements analysis

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Executive Summary

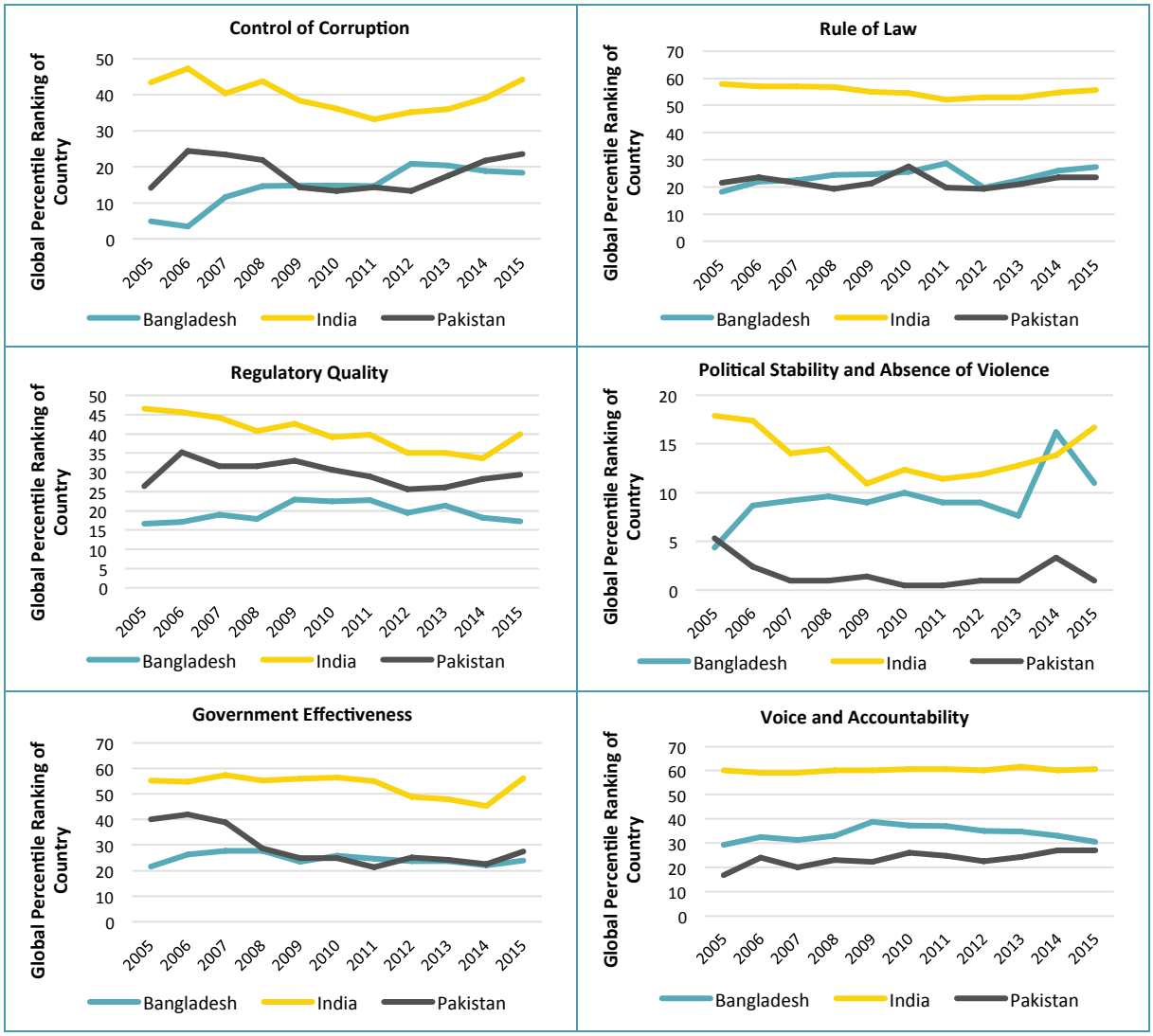
Bangladesh has some of the worst governance and anti-corruption scores in the world, and in South Asia it is behind India and Pakistan on most governance indicators. Yet, since 1980 it has made moderate to good progress on different indicators of economic and social development, prompting some to talk of the 'Bangladesh paradox'. An analysis of its economic growth drivers and its evolving political settlement helps to explain the paradox and to identify the vulnerabilities of its contemporary position. Economic growth has been driven largely by the emergence of a single globally competitive sector, a growing inflow of remittances, stable growth in agriculture, and effective NGOs making the most of Official Development Assistance (ODA) inflows. The most important of these has been the growth of the labour-intensive garments and textiles sector, as a result of a lucky combination of events in the late 1970s and governance initiatives that enabled the country to learn this technology at a critical time. The subsequent emergence of 'competitive clientelism' in the 1990s created the political and policy stability for private investments to drive growth in this and a small number of other sectors, even if it was at the cost of high levels of corruption. This pattern of growth is unlikely to continue without limit as rapid productivity growth has to be achieved and political stability has also been challenged by the re-emergence of single-party rule after the controversial 2014 elections. The current governance arrangements are inadequate for meeting these challenges.

Anti-corruption and governance initiatives in Bangladesh have to be located in the context of these opportunities and challenges. Anti-corruption strategies in Bangladesh have largely been of the systemic type, attacking corruption in general, with policies to promote transparency, investigate corruption and impose legal penalties through prosecution. When Bangladesh acceded to UNCAC in 2007, it already had in place most of the formal legislation to be potentially compliant with UNCAC requirements. The problem has been that Bangladesh, like many other developing countries, has informal processes and power relationships that prevent the implementation of these laws. A direct investigative attack on allegations of high-level corruption in the current political settlement, as in the Padma Bridge case, is likely to have little effect and may even be counterproductive. Our analysis supports an incremental and sector-specific approach to anti-corruption, to create coalitions of interests that can support the solution of specific developmental problems. If systemic improvements in governance and anti-corruption are unlikely in the short to medium term, alternative anti-corruption strategies have to be devised to sustain social development and inclusive growth. The paper develops an analysis of economic drivers and political settlements to identify a range of sectoral issues where an incremental and sector-specific anti-corruption approach can lead to feasible and effective anti-corruption strategies in line with the Anti-Corruption Evidence programme (ACE)approach.

1. Introduction

Bangladesh is at the lower end of the list of South Asian countries on all major governance indicators. As Figure 1 shows, Bangladesh had the worst scores in South Asia on WGI indicators for the *control of corruption*, *regulatory quality* and *government effectiveness*, with scores considerably lower than India, and even lower than Pakistan, which has suffered from severe political instability in recent years. On the indicators for *rule of law*, *political stability*, and *voice and accountability* Bangladesh scores lower than India but just above Pakistan. Its low score on the *control of corruption* is an important reason why its governance is perceived to be constraining its ability to sustain its success in growth and poverty reduction in the future. While there have been modest improvements in Bangladesh's corruption ranking since 2005, it is still in the bottom 20 percent of countries, a status that, apart from anything else, severely constrains its business climate and signals potentially serious problems of rent capture and resource wastage affecting its development.

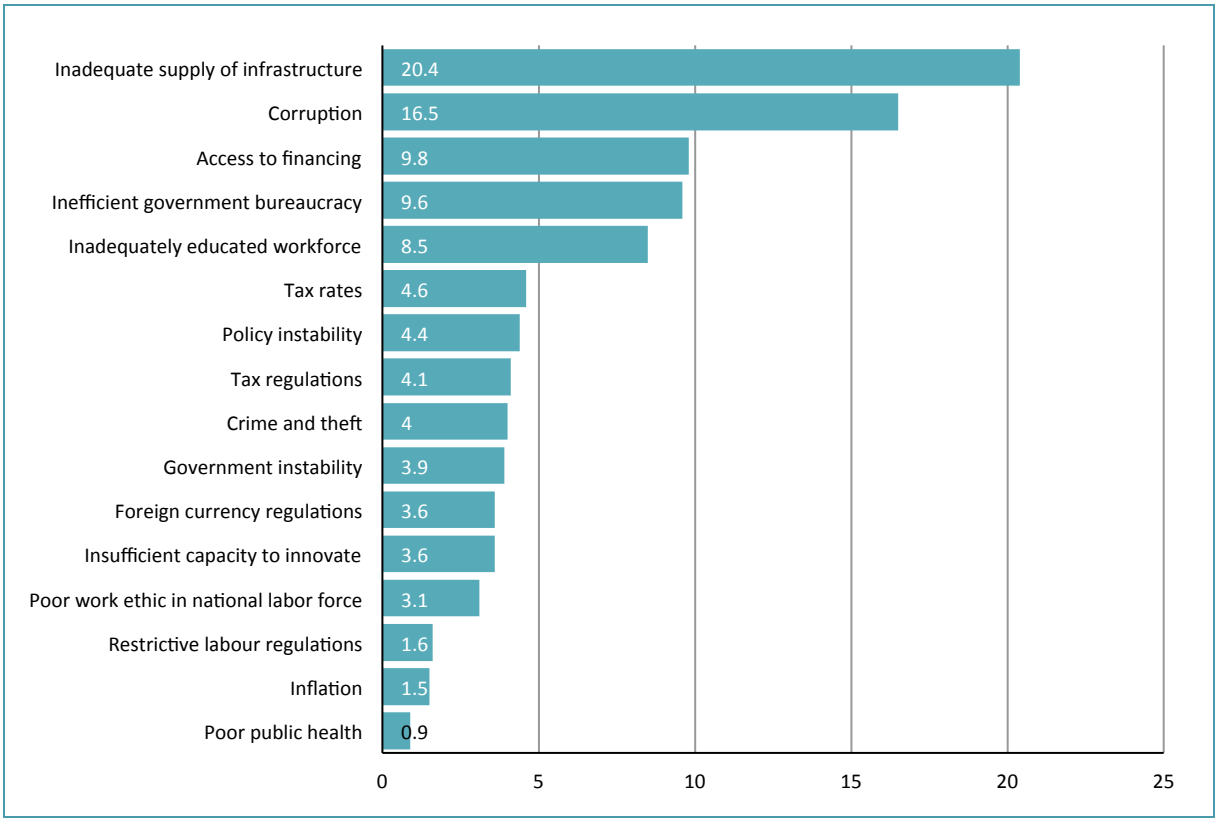
Figure 1: Bangladesh Governance Rankings 2005-15



Source: World Governance Indicators 2016

The business sector in Bangladesh has consistently ranked corruption as one of its top three concerns. Figure 2 shows that in 2016 executives surveyed in the World Economic Forum's Executive Opinion Survey ranked corruption as the second most constraining factor for doing business in Bangladesh. Some of the other important factors identified by these executives as constraints include inadequate infrastructure, bureaucratic inefficiency and poor workforce skills. The persistence of these constraints is also linked to the pervasiveness of corruption as corruption makes infrastructure and power supplies, bureaucratic capabilities and skills development more difficult to address. The overall impact of corruption on business is therefore likely to be very significant.

Figure 2: Most Problematic Factors for Doing Business in Bangladesh 2016



Source: Executive Opinion Survey (World Economic Forum 2016: 110). The numbers are weighted scores of each factor.

At the same time, the Bangladesh economy has been growing at between 5 and 7 percent per annum since the 1990s, despite weak governance, high levels of corruption and political instability. Moreover, growth has been driven by productive sectors rather than natural resource extraction, with private investments in manufacturing playing an important role in driving growth. This combination of relatively good developmental outcomes in a context of poor governance has led to a discussion of a 'Bangladesh paradox' (World Bank 2007; Mahmud, et al. 2008). Our political settlements approach helps to explain the paradox, and also to show why the combination of growth with poor governance is not likely to be sustainable over time. Growth since the 1990s was underpinned by the competitiveness of a small number of low-technology sectors like garments and textiles, while a *competitive clientelist political system* provided political stability at the cost of high levels of political

corruption. The competitive clientelist political settlement also delivered a predictable longer-term political environment, in a context where some sectors were already globally competitive. Investors could credibly believe that while parties in power changed regularly, there would be no significant policy changes because both parties expected to come back to power and had no interest in harming growth.

Changes in the political settlement in Bangladesh after 2008 have undermined this political system. Constitutional and administrative changes reduced the chances of opposition parties winning an election and dramatically increased political uncertainty. As the return to power of the opposition through elections became less and less plausible, the future strategies of excluded groups have become more uncertain. After a spurt of violence involving the mainstream political opposition around the 2014 elections that the opposition boycotted, mass political violence declined as a result of severe policing. But there have been worrying signs of an increase in extremist violence finding political space, particularly after the killings at the Holey Artisan bakery in Gulshan in the summer of 2016 and other acts of sporadic violence. At the same time, official violence directed not just at extremists but also at opposition parties in the form of arrests and harassment, disappearances and deaths in mysterious circumstances have also increased. Through all of this, economic growth appears to have been sustained, even though there are questions about the accuracy of official growth figures. Even if growth has not been as high after 2014 as the official figures suggest, it has certainly not collapsed.

The public expectation is that employment opportunities will continue to grow and wages will continue to rise. These expectations create an imperative to achieve higher productivity growth in existing economic sectors and accelerated job creation in new sectors beyond garments and textiles. The political tensions and the space for extremism can be magnified if the shrinkage in the political space is combined with a serious economic setback. These economic imperatives provide both compulsions and opportunities for (at least) some incremental governance improvements provided the government does not perceive every governance improvement as a threat to its political interests. This is an area where the ACE programme can contribute, by providing evidence-based ways of thinking about feasible and effective anti-corruption and governance strategies to support sectoral growth strategies.

Governance can affect growth (and development) by affecting the investment share or the economic and social productivity of investments, or both. If poor governance affects either or both, there will be negative effects on economic and social development. Failures of governance have affected the investment share in Bangladesh whenever political conflicts have resulted in reduced private investments as a result of political uncertainty. This happened during the rule of General Ershad and has emerged once again after after the abolition of the caretaker system for organising elections in 2011. Other governance failures and in particular corruption have also affected the productivity of investments by restricting the government's capacity to provide high quality power and infrastructure at a reasonable price, to effectively regulate industries, deliver quality health and education or promote the development of new sectors with targeted support and skills training.

In Section 2 we see that economic growth in Bangladesh since the 1980s has been driven by a combination of very fortunate factors that include the emergence of the garments and textile industry as a globally competitive export sector, the steady growth of remittances, steady if low growth in agriculture and a political environment with a supply of innovative NGOs that ensured that foreign aid had a positive effect on poverty reduction. However, all of these factors are contingent and sustaining growth requires increasing the investment share, developing new competitive sectors, improving health, education and skills and overcoming serious limitations in infrastructure. Thus, governance weaknesses have in the past affected *both* the investment share and the productivity of investments and of public expenditures. Corruption of different types is involved in all these processes, and therefore constitutes a serious threat to the sustainability of growth in Bangladesh.

Section 3 looks at how political conflicts and governance capabilities have changed over time in terms of our political settlements framework. This allows us to track how governance challenges have changed, as have opportunities for intervention in different areas. This analysis shows that the major acceleration in Bangladesh's growth happened in the democratic period of 'competitive clientelism' as this political arrangement was relatively inclusive and the competing parties represented similar constituencies in terms of economic interests. As a result, the circulation of the two major parties in power created political stability and sustained high rates of investment. This political settlement began to change after the failure of the 2006-8 emergency that attempted to radically reform the corrupt clientelist politics that had characterised democratic politics from 1990 to 2006. The result of the failure was that the party that won the 2008 elections found it possible to restrict the political space and moved in the direction of 'vulnerable authoritarianism' in the terminology of the political settlements classifications in my 2010 paper (Khan 2010). Even though the forms of democracy have been maintained, the 2014 election was uncontested and subsequent elections have been heavily influenced by administrative interference. This is arguably an unstable political arrangement in Bangladesh, given the distribution of the potential organisational power of social networks, even if the dominance of one party is maintained for a while through effective restrictions on opposition activities and an unprecedented politicisation of the administration. This unusual context is the backdrop for assessing opportunities and challenges for governance and anti-corruption interventions.

Section 4 looks at the background of anti-corruption laws and agencies in Bangladesh. Bangladesh acceded to the United Nations Conventions against Corruption (UNCAC) in 2007 and it has in place almost all the requisite formal laws. However, enforcement has been very poor, in line with our expectation that systemic anti-corruption will work poorly in developing countries, particularly those characterised by competitive clientelism or vulnerable authoritarianism (Khan et al. 2017). We outline some of the evidence of major corruption scandals and the responses to them in recent years, which suggest that a frontal or systemic attack on corruption is unlikely to be effective. This is generally true in developing countries, but is particularly true in Bangladesh today where, unlike Tanzania or Nigeria, the other focus countries of the ACE programme, anti-corruption is not even a political priority for the government in power. In this context we argue that an incremental approach to anti-corruption is the only feasible way forward, and this is in line with our approach to anti-corruption in adverse contexts (Khan et al. 2017).

We conclude in Section 5 by identifying strategic opportunities for anti-corruption work in Bangladesh using our incremental intervention approach. Our analysis of growth in Bangladesh and of growth challenges helps us to identify priority sectors where improved resource allocation outcomes could have a big impact. This, together with an analysis of the challenges posed by characteristics of the political settlement, leads us to select some feasible areas for incremental anti-corruption work. These are areas where the ruling coalition is unlikely to perceive incremental anti-corruption as a threat to its interests. As our anti-corruption strategy is not based on enforcing rules across all powerful organizations from above, but rather on trying to change institutions and policies to create incentives for some powerful stakeholders to behave in more productive ways in specific sectors, the government may even see the benefits of improving developmental outcomes in these ways in critical sectors. These are the likely areas where feasible and high-impact anti-corruption strategies are most likely to be developed.

2. Major sectors and drivers of growth in Bangladesh

Table 1 shows that all three large South Asian countries experienced growth accelerations in the 1980s, though this happened for somewhat different reasons. In Bangladesh, the acceleration was linked to the rapid growth of the export-oriented garments and textiles sector, together with moderate growth in agriculture, a growing flow of remittances from Bangladeshi workers in the Middle East and elsewhere, and in the early years, significant flows of foreign assistance that contributed to poverty reduction as a result of the role of innovative NGOs. Growth in Bangladesh continued to accelerate over the next three decades, overtaking Pakistan in the 2000s. In a dramatic reversal of fortune, Pakistan, which had the highest growth in South Asia up to the 1980s, became the slowest growing region in the 1990s. Apart from the regional conflicts that affected Pakistan from the 1990s onwards, this reversal of fortune had a lot to do with Bangladesh's relative success in a few export-oriented manufacturing sectors.

Table 1: Growth in South Asia 1960-2015

	Bangladesh	India	Pakistan
		GDP Growth Rates	
1960-80	2.4	3.5	5.9
1980-90	4.0	5.6	6.3
1990-00	4.7	5.6	3.9
2000-05	5.1	6.7	5.0
2005-10	6.1	6.7	3.4
2010-15	6.3	6.7	4.0
		Per Capita GDP Growth Rates	
1960-80	-0.3	1.2	3.1
1980-90	1.3	3.2	2.9
1990-00	2.5	3.6	1.4
2000-05	3.3	5.0	2.8
2005-10	4.8	6.5	1.3
2010-15	5.1	5.4	1.8

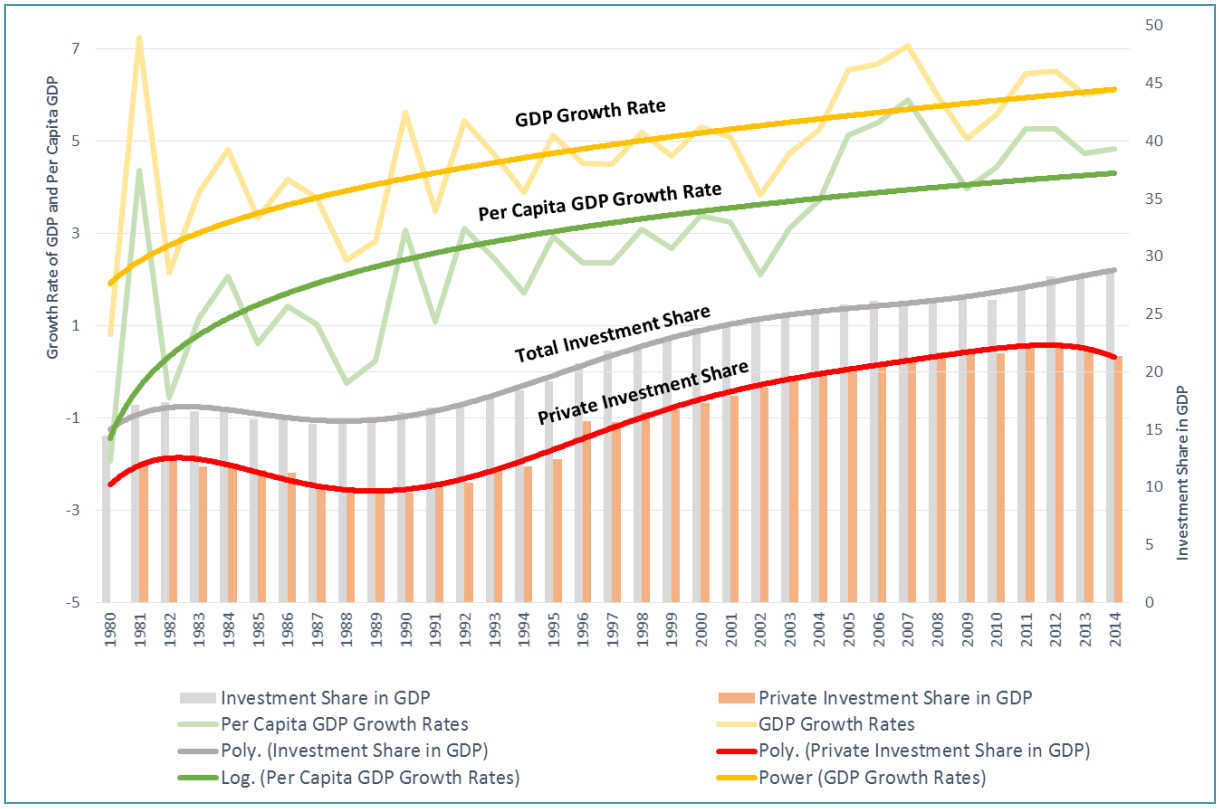
Source: World Bank. World Development Indicators. http://data.worldbank.org/data-catalog/world-development-indicators (accessed February 2017) and Handbook of Statistics on Pakistan Economy, 2015.

2.1. Governance effects on the investment share

Figure 3 shows that the growth acceleration in Bangladesh since the early 1980s was associated with an increase in the aggregate investment share, and particularly an increase in the *private* investment share. Private investments grew as the nationalizations of the early 1970s were reversed and new competitive sectors emerged. The productivity of private sector investments was greatly helped by organisational learning in key manufacturing

sectors, particularly in garments and textiles. This helped to sustain private investment by making it profitable to invest. However, the first phase of the private sector take-off was short-lived. The private investment share *declined* between 1982 and 1989. The crisis was driven mainly by the growing and increasingly violent opposition to the autocratic rule of General Ershad, which damaged the investment climate and investor expectations. As soon as Ershad stepped down in 1990, and a democratic process was restored, private investment immediately picked up as political instability ended.

Figure 3: Investment and the growth acceleration from the 1980s



Source: Based on World Bank (2015a). Does not include the reduced estimate for GDP growth in 2015.

Trend lines: For the total and private investment shares, polynomial curves describe the trend. For the GDP growth rate a power trendline is used to summarize the acceleration and flattening out, while for per capita GDP a logarithmic trend is fitted because of occasional negative values.

The democratic period from 1990 to 2006 saw a steady increase in the private investment share, demonstrating that the two-party competitive clientelism at least had the merit of creating stable investor expectations of political stability. Political stability was achieved at the cost of high levels of political corruption, because all powerful coalitions had a chance of sequentially accessing political rents. The system hit a crisis in 2006 over the organisation of elections and a two-year emergency government failed to resolve it. The private investment share reached a peak in 2009 and then once again flattened out exactly at the time when the continuation of political stability through competitive clientelism was no longer assured. Political uncertainty increased further in 2011 when the ruling party abolished the interim government system which had ensured elections were reasonably free and fair. The private investment share began to immediately decline after 2012. The evidence suggests that even with other aspects of weak governance, if political stability can be sustained in Bangladesh

through a democratic process, private investment remains buoyant. However, significant improvements in the private investment share in the long-run are also likely to require steps to improve the productivity of investments.

The World Bank has argued that the aggregate investment share in Bangladesh has to rise by at least another five percent of GDP from the 28 percent reached in 2015 if growth is to be sustained (World Bank 2015b: 15). The acceleration in the growth rate has also flattened out, with growth rates appearing to stabilize at around the 6 percent level, well before reaching the 8-10 percent levels required to sustain rapid poverty reduction. There is some question about the accuracy of the growth figures provided by the Bangladesh government, which show that economic growth has continued to rise after 2012 despite declining private investments. The World Bank (2015b: 11) has argued that the 2015 growth figure for Bangladesh is likely to be an overestimate given the political disruptions that happened in the earlier part of the year, and the official growth rates of close to 7 percent for 2016 and 2017 are also likely to be overestimates, particularly given the slowdown in private investments. The available data on investments and growth taken together suggest that growth is likely to have held up at around the 6 percent level, but that this rate is unsustainable unless private investments and the productivity of investments begin to rapidly improve.

2.2. Governance effects on productivity

The effects of poor governance on the productivity of investments in Bangladesh is more complex. According to the *Doing Business* surveys of the World Bank, Bangladesh's ranking declined from 122 (out of 183) in 2012 to 174 (out of 189) in 2016. In terms of the ease of getting electricity for a business venture, Bangladesh declined from 182 out of 183 countries in 2012 to the bottom position of 189 out of 189 countries in 2016 (World Bank 2012: 81, 2016: 187). Beyond these obstacles, the government has limited capacity to efficiently address critical market failures constraining the development of new sectors, such as managing effective incentive schemes for investments in new sectors, providing support for technology acquisition, ensuring effective regulation and providing critical public services including health, education, skills delivery, infrastructure, power generation and so on. One of the critical failures of governance affecting the productivity of private investments has been the low capacity of the government to achieve efficient outcomes in each of these areas. These shortcomings are indirectly captured in the WGI indicators reported in Figure 1, but they are directly visible in the poor quality and high cost of infrastructure and power supplies, the poor quality of education and skills, the poor quality and coverage of the health system and so on.

The effects of governance on the efficiency of investments (their productivity) and on the investment share are interdependent. If the efficiency of investments is low, profitability will be low and the investment share will eventually start to decline. Equally, if the investment share is too low, productivity and productivity growth will be low. As a result, the effects of poor governance on these two drivers of growth are often difficult to distinguish. Nevertheless, it can be useful to make a conceptual distinction for identifying policy priorities and to assess the implications of different types of failures of governance.

2.3. Garments and textiles driving export growth

Despite its governance problems, Bangladesh achieved an acceleration in growth from the 1980s. Governance was just 'good enough' in a few critical areas, and Bangladesh was lucky to benefit from a number of global opportunities. Its growth has been driven by a combination of four factors referred to earlier. First, there has been the rapid growth of the export-oriented garments and textiles industry that directly created upwards of four million jobs, and indirectly many times that number in transportation, services, packaging and so on. The garments and textiles sector now accounts for around 80 percent of Bangladesh's export earnings, and while the sector remains at the lower value end of the global supply chain, in terms of total exports, Bangladesh has consistently been in the top two or three garment-exporting countries in the last ten years.

The strong growth in exports continued despite the global slowdown of 2008-09 because the cheaper garments and textiles that Bangladesh produced benefited from expenditure switching, as consumers in advanced countries confronted austerity. More recently, merchandise exports have faltered, partly because of political uncertainties of 2012-13 referred to earlier and because not enough effort has been put into diversifying the manufacturing sector, upgrading technologies and improving productivity. By 2017 garments exports were stagnating or declining, with growth switching to India, Vietnam and other countries as Bangladesh suffered from stagnant productivity and inefficient ports and infrastructure that hindered exports. Merchandise exports also remain heavily dependent on one sector - garments and textiles - making the country particularly vulnerable to demand switches in that sector.

On the whole, despite some of the more advanced garments producers moving up the value chain through backward linkages and producing higher-valued garments, the Bangladesh garment industry continues to operate at the lower end of the global value chain. Wage rates in the industry are also known to be one of the lowest internationally and the lowest amongst its regional South Asian competitors (Ahmed and Hossain 2006: Figure 4). Wages and conditions in the garments industry have therefore become a growing source of friction between management and workers. After the Rana Plaza building collapse in 2013 in which more than 1000 garments workers died, there has been growing pressure on the industry to improve the quality of its building infrastructure and to raise productivity to enable higher wages. International inspection and certification agreements like *Accord* and *Alliance* involving global buyers have considerably improved the situation in building safety and infrastructure since then. However, while moving up the value chain into higher value-added products and raising productivity in existing lines are critically important challenges for Bangladesh, progress in these areas has been slow.

2.4. Remittances

A second driver of inclusive growth has been a steady growth of remittances as millions of relatively low-skilled Bangladeshi workers found employment in the Middle East and South East Asia where, paradoxically, low-skilled and low-wage workers were often in short supply.

Workers from poor backgrounds have families that are dependent on their remittances, so a very large percentage of their earnings are remitted. This sustained demand in rural areas, supporting education and allowing construction activities that improved living standards. Remittances from unskilled Bangladeshi workers in the Middle East and South East Asia are unlikely to keep growing and may even fall, as the demand for unskilled labour may shrink over the next few years if oil prices and the global economy remain weak.

Remittances reached a peak of about ten percent of GDP around 2008 and has stagnated at that level since then, with some reductions in recent years. Apart from the possible slowing down in the demand for workers in the Middle East and South East Asia, there is also evidence of significant rent extraction from potential migrants from Bangladesh by unscrupulous manpower export businesses, operating in close collusion with political patrons and overseas labour importers. The extraction of large charges and bribes from potential migrants contributes to capping numbers, and diverts resources from the poor into the pockets of powerful labour-export intermediaries.

2.5. Agriculture

A third driver of growth has been agriculture where there has been a steady improvement in yields through the spread of 'green revolution' technologies. Population pressure on the land was reduced as a result of the departure of large numbers of underemployed farm workers to manufacturing and to overseas job markets. This alone contributed to raising labour productivity on the land. As Table 2 shows, agricultural growth rates in Bangladesh have been steady and have been higher than other South Asian countries in the last fifteen years. But sustaining this may be difficult as agriculture suffers from a number of structural constraints. Despite outmigration from agriculture, farm sizes are shrinking under population pressure as land becomes subdivided through inheritance. Shrinking farm sizes makes it more difficult for farmers to mobilise investments, and mechanisation and irrigation become technically more difficult. Some of these obstacles can be overcome using collective solutions to pool resources and to share investments in machines and irrigation networks, but these become progressively more difficult as farm sizes keep falling. Moreover, there are signs that greater fertilizer and pesticide use cannot keep raising yields, and the water table is also dropping (Titumir 2013).

Table 2: Comparative growth in agriculture in South Asia

	1980-1990	1990-2000	2000-2010	2010-2015
Bangladesh	2.2	3.6	4.4	4.0
India	4.4	2.9	2.4	3.4
Pakistan	4.3	4.4	3.2	2.3

Source: World Bank. World Development Indicators. http://data.worldbank.org/data-catalog/world-development-indicators (accessed February 2017)

Table 3: Land fragmentation in Bangladesh 1984-1997

Size of holdings (acres)	1983-4 Census		1996-7 Census	
	Frequency (%)	Owned Area (%)	Frequency (%)	Owned Area (%)
Small (0.05-2.5)	75.4	18.2	83.1	26.2
Medium (2.5-7.5)	19.9	56.2	14.3	56.3
Large (7.5-)	4.7	25.6	2.6	17.5

Source: World Bank (2000: Tables 1.5 and 1.6).

The agricultural sector in Bangladesh is characterised by tiny farms and significant surplus labour. Table 3 shows that land sizes are small and getting smaller over time, as a result of population growth and the division of land through inheritance. In the 1997 census, farms over 7.5 acres in size accounted for only 2.6 percent of farms and 17.5 percent of the total arable land. The figures describe an important constraint on raising agricultural productivity. Small farm sizes not only constrain basic mechanization, the small farmers themselves typically do not have access to sufficient capital to develop new farming methods and technologies.

Moves towards land consolidation through the land market face considerable resistance, as risk averse small farmers are generally unwilling to sell land at market prices. An additional problem for policy-makers is that yields on micro-farms can appear to be higher than yields on slightly larger farms. This has several causes but the main one is that larger farms face a relative disadvantage in terms of supervising very labour-intensive farming technologies. In contrast, smaller farms can use family labour to supervise higher labour inputs per unit of land. Large farms can achieve higher yields only when they cross a minimum threshold of size that allows mechanisation and other technologies that require less intensive labour use and supervision. The extreme fragmentation of land in Bangladesh means that small increases in size (from micro to small) can actually appear to be *lowering yields*. A simplistic interpretation of this inverse size-productivity relationship can lead to misleading policy conclusions that support the growth of even smaller farms as a good thing. The emergence of smaller farms may appear to raise yields in the very short run, but they are unviable in the longer run when growth depends on raising labour productivity using mechanisation and new technologies (Khan 2004; Titumir 2013).

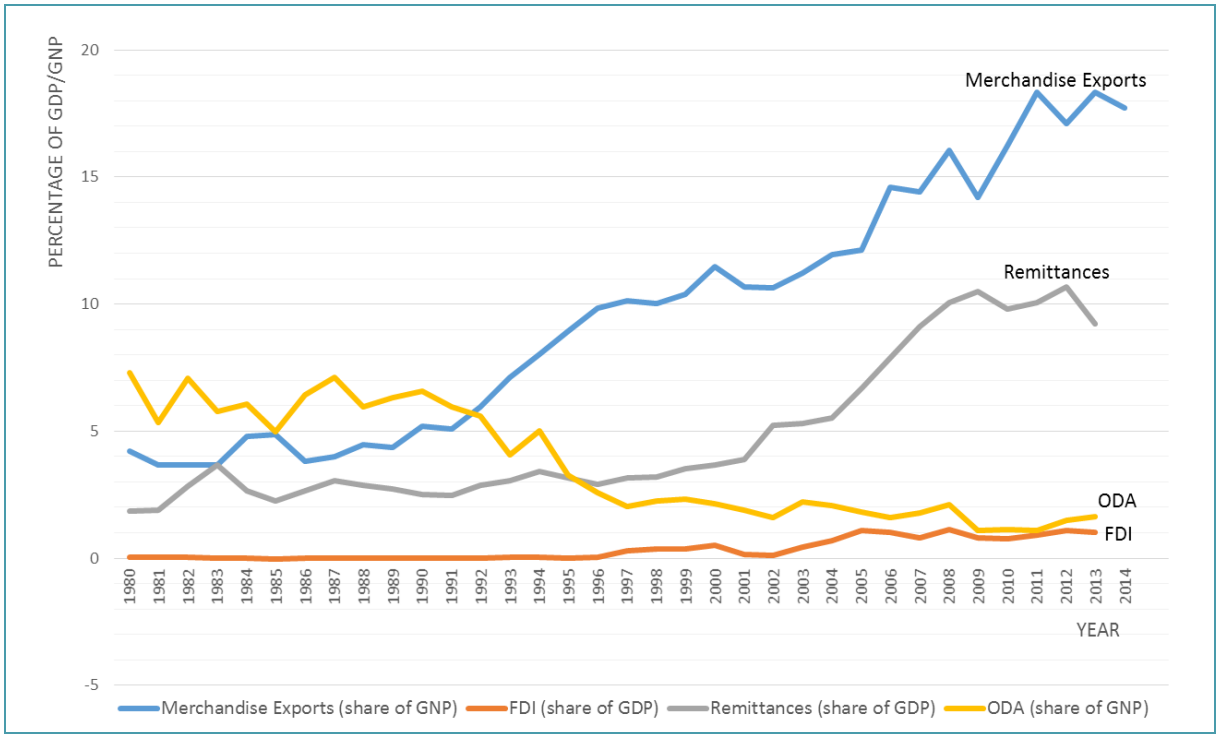
Despite these constraints, Bangladeshi agriculture has achieved long-run growth rates of around three percent per annum that are comparable to neighbouring countries. This has been achieved through the spread of green revolution technologies of high-yielding seed varieties, combined with steady increases in fertilizer and pesticide use. These technologies are neutral to scale up to a point and Bangladesh's small land sizes did not constrain the adoption of these technologies. The shorter crop cycles of high-yielding varieties of rice also allowed the country to move from single to double cropping, and in many areas to triple cropping. The growth that was unleashed through the increase in cropping intensity is likely to be exhausted over the next ten years, and the limits to fertilizer and pesticide use have already been reached. There are still growth opportunities through shifting to higher value crops like vegetables and fruits in some areas, and much still-unexploited potential for developing pisciculture. Given the fragmentation of land, the role of cooperatives and other

forms of collective or pooled farming or fishing will be very important. Governance and corruption affect the development of these collective farming models and ACE will be looking at these issues as well.

2.6. Overseas Development Assistance

Finally, until the 1990s Bangladesh also received significant inflows of overseas development assistance (ODA) and it was lucky that the country's fragmented power structure ensured that aid could not be captured or wasted by a narrow elite at the top (Khan 2014). The war of independence that led to liberation in 1971 resulted in the emergence of charismatic individuals committed to development, like Sir Fazle Hasan Abed who set up BRAC, and Nobel Laureate Mohammad Yunus who set up Grameen Bank. The presence of a large number of locally-owned NGOs that had committed leaderships with relatively high capabilities *and* who were engaged in competition with each other for development resources ensured many innovations in aid delivery. As a result, aid in useful forms reached a much broader segment of the population than is typical in many other developing countries at similar levels of development. Bangladesh was therefore able to achieve better results in areas like maternity health and primary education, and this in turn sustained inclusive growth, and prevented political instability running out of control.

Figure 4: Sources of foreign exchange



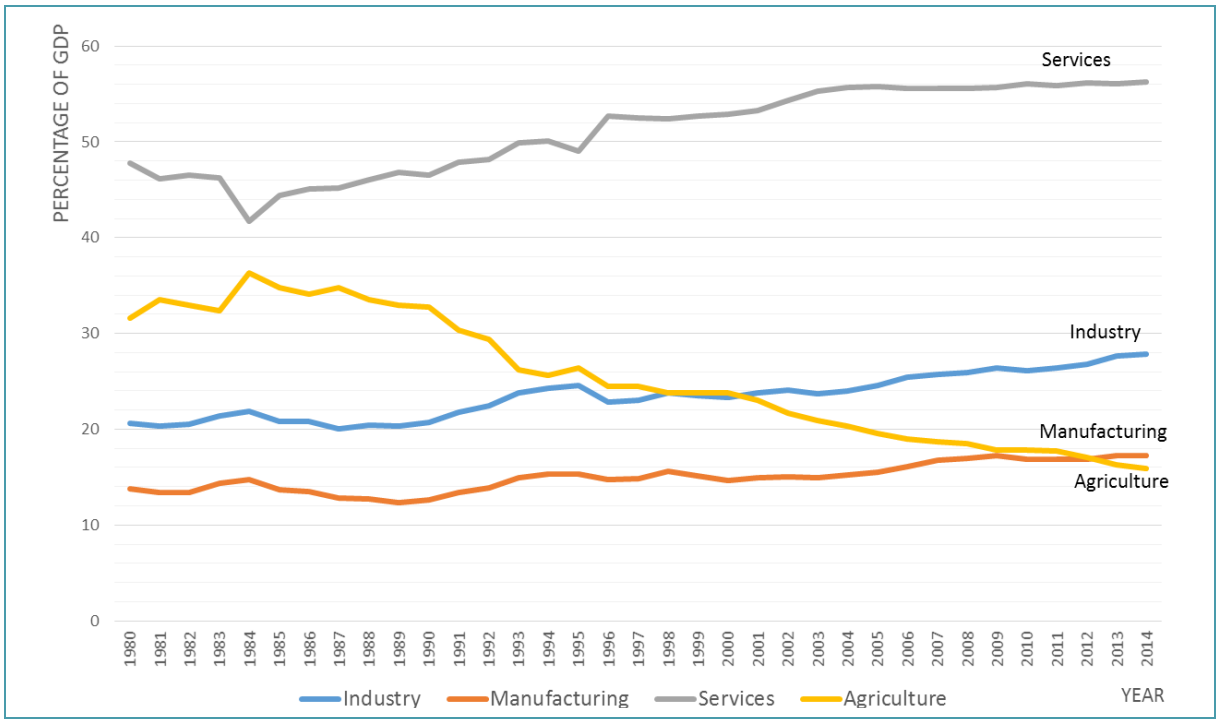
DEPSource: Based on data in World Bank (2015a).

Figure 4 shows the huge transformation of the economy driven by these processes. Even in 1980, overseas development assistance (ODA) was the main source of foreign exchange, at around 7 percent of GDP. By the early 1990s merchandise exports overtook ODA and by the mid-1990s, so did remittances. By 2013 ODA commitments had declined to around 2 percent

of GDP, largely as a result of the growth in GDP, while merchandise exports grew to contribute close to 18 percent of GDP, and remittances another 10 percent. Foreign direct investment (FDI) also increased since the early 1980s, but is still negligible compared to other South Asian countries at around 1 percent of GDP.

There has also been steady growth in the services sector, however, it has not been a driver of growth. The service sector is dualistic, with some modern services like banking and finance, modern hospitals and so on that add high value per person, and a broad range of very low-productivity activities that absorbs millions of individuals with no jobs in manufacturing or agriculture who are forced to eke out a living in low-wage service activities. These include very low value-adding household services, low technology transportation, peddling street food, and so on. Bangladesh cannot rapidly increase the high value-adding services sector because, unlike India, its education system produces fewer of the high-human capital graduates that are required in the upper segments of the service sector. Therefore, a rapid growth of per capita incomes in Bangladesh is unlikely to be driven by the service sector in a significant way.

Figure 5: Growing shares of industry and manufacturing



Source: Based on data in World Bank (2015a).

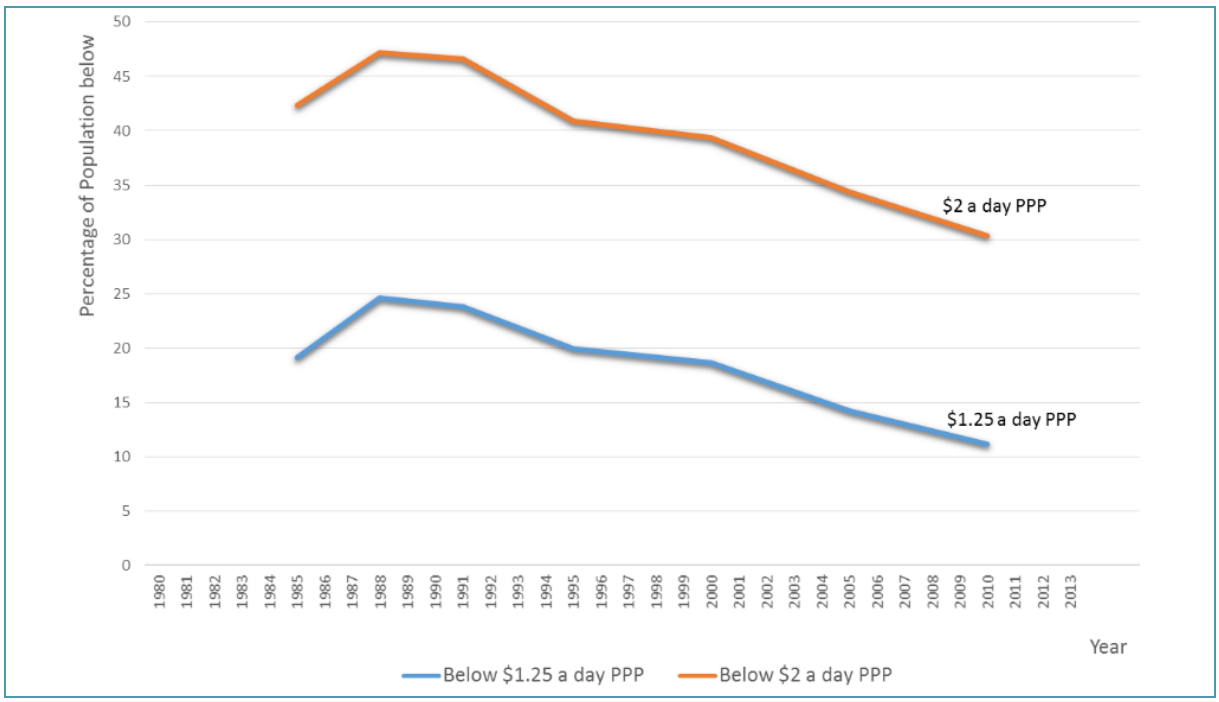
The rapid growth of industry and manufacturing has meant that the structure of GDP has changed significantly over this period. Figure 5 shows that agriculture was overtaken by industry in the late 1990s and by manufacturing on its own in 2012. Currently, the share of manufacturing at around 18 percent of GDP is comparable to India, but it is concentrated in lower-technology and labour-intensive sectors. However, even though the share of agriculture in GDP dropped to 18 percent by 2010, its share in total employment only declined to around 47 percent of the labour force. This reflects the low productivity of labour in agriculture and an insufficiently rapid creation of jobs outside agriculture (Jolliffe, et al. 2013: 57).

2.7. Poverty reduction and the role of manufacturing

The performance of agriculture and manufacturing is important for making sense of the decline in poverty that Bangladesh achieved since 1980. Figure 6 shows that a rapid decline in the headcount measure of absolute poverty was achieved from the late 1980s onwards. The percentage of the population living below two dollars a day declined from more than 45 percent in 1988 to 30 percent by 2010. As in many other countries, the available data also show that there was a worsening in the distribution of incomes over the same period of time but, nevertheless, the decline in absolute poverty was an important achievement (World Bank 2015a).

As Bangladesh does not have significant income redistribution programmes, the improvements in absolute poverty reduction were primarily achieved through economic growth. The relationship between agricultural and manufacturing growth and the reduction in absolute poverty is complex and different studies have highlighted somewhat different mechanisms through which this happened. However, as there are significant policy implications for governance reforms and the prioritization of sectors, we will look at this evidence carefully.

Figure 6: Reduction in absolute poverty



Source: Based on data in World Bank (2015a).

The World Bank has provided a detailed analysis of the drivers of poverty reduction between 2000 and 2010 (Jolliffe, et al. 2013). The analysis uses a decomposition method to attribute the overall poverty reduction to different factors. The most important explanation for the improvement in consumption levels of the poor was the growth of labour income from wage growth, particularly in the agricultural sector. According to the decomposition, 47 percent of the poverty reduction can be attributed to increased labour income on farms, another 17

percent to increased incomes in other sectors, and 25 percent to demographic changes that increased the proportion of the population in work. Only 11 percent of the reduction is attributed to international remittances (Jolliffe, et al. 2013: 53). The study is right in its identification of returns from employment as the most significant contributor to poverty reduction. However, the overall decomposition can be misleading if wrongly interpreted. It suggests that only 3 percent of the poverty reduction was due to intersectoral transfers of labour from agriculture to other sectors. This is because this estimate looks only at the wage differences between agriculture and other sectors when labour moves, and ignores the huge indirect effects of intersectoral labour transfers on agricultural incomes.

The fact that wages in labour-intensive manufacturing were only slightly higher than in agriculture means that if we look at the wage increase as the main benefit of labour moving from agriculture to industry, there was only a 3 percent improvement in incomes. However, workers leaving agriculture indirectly improved incomes in the agricultural sector and this too needs to be accounted for. The share of total employment in agriculture declined from 51 to 47 percent over the decade, and this was exactly balanced by an increase in the share of labour in industry from 14 to 18 percent. With a labour force of around 70 million in 2010, this roughly translates into at least five million new jobs being created over the decade in industry. More significantly, it translates into more than 8 percent of the agricultural workforce leaving the sector over a decade.

What would have happened to agriculture and agricultural incomes if industrial growth had not absorbed millions of underemployed workers from agriculture in aggregate? The impact on agricultural wages and poverty in this counterfactual is difficult to estimate accurately, but the impact is likely to have been massive. If the 8 percent or more of the agricultural workforce that left over this period had remained in a state of unemployment or under-employment in agriculture, the impact on agricultural wage growth may well have been very severe. This is because productivity improvements in agriculture have not been labour-using, and a large pool of underemployed labour would have depressed wage growth even with the improvements in yields and productivity that were achieved. This is likely to have effectively prevented much or all of the improvements in the consumption of the poor that were observed in agriculture.

Indeed, the fact that industrial wages did not rise much despite the massive growth in employment suggests that there were many underemployed workers in agriculture in line with the model of Sir Arthur Lewis (1954). The only way that wages can actually rise in agriculture in these contexts is through the gradual absorption of surplus labour in gainful employment elsewhere. In Bangladesh that has been happening through labour transfers to the industrial sector, in the way that Lewis predicted, ultimately helping to raise agricultural wages. The methodology of the Bank study does not provide a satisfactory estimate of the full impact of intersectoral labour transfers on poverty reduction, taking into account both the direct and indirect effects. But background studies to the report have recognised the possibly much greater contribution of manufacturing to poverty reduction in line with the Lewis model (Jolliffe, et al. 2013: 71).

The policy implications of this re-evaluation are very significant: inclusive growth greatly benefited from the rapid growth of employment in manufacturing which allowed wages and incomes to rise from very low levels in agriculture, as well as offering slightly higher wages in manufacturing. Agriculture remains the biggest employer of labour but at a much lower average productivity than manufacturing or services. If poverty reduction is to continue, the country must continue to create millions of new jobs in labour-intensive manufacturing. Even though the impact of manufacturing employment on poverty reduction is underestimated in the Bank study, the authors make robust policy recommendations for supporting inclusive growth. Investments, particularly in skills, are identified as important for supporting job creation. We could add to this the importance of policies supporting the creation of new organisational capabilities within firms in manufacturing, improving the supply of power for manufacturing expansion and other policies that support the emergence of greater numbers of competitive firms in manufacturing. The Bank study also recommends better targeting of safety nets and a continuation of support for family planning, and these are obviously sensible recommendations based on an analysis of the data on growth and poverty (Jolliffe, et al. 2013: xxx-xxxii).

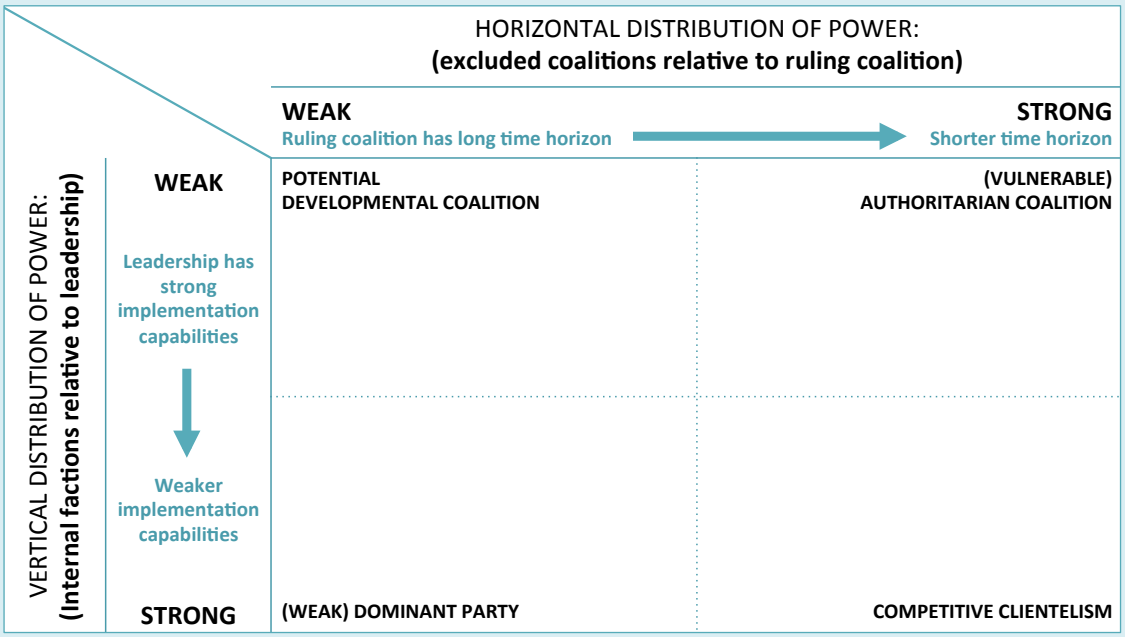
Despite its successes in manufacturing, huge challenges remain for Bangladesh given its low per capita income, the shortage of skills, and its steadily rising population. While its population growth rate has declined, Bangladesh still added 19 million people to its population between 2000 and 2010. This rate of increase is likely to continue for some time, with the UN estimating that Bangladesh will add another *21 million people* between 2010 to 2020 (Jolliffe, et al. 2013: 60). Services and agriculture are likely to continue to grow but given the constraints of creating high wage jobs in services and the constraints on an acceleration of agricultural growth, it is likely that only rapid manufacturing growth based on labour-intensive technologies can create millions of new jobs with the promise of wage growth.

3. Political settlements and political corruption in Bangladesh

The political settlements framework looks at the distribution of power across political and economic organisations in a society (and its evolution over time) in order to understand the types of policies that emerge, and even more importantly, how effectively policies are implemented or distorted by the organisations that are affected by them (Khan 2010, 2012, 2013b). The configuration of political power has important implications for understanding the capabilities of a ruling coalition in implementing policies, as this depends on the degree of control the leadership has over the ruling political organisation. It can also determine the time horizon and commitment to development of a ruling coalition, because that can depend on its confidence or vulnerability relative to other organisations that are currently excluded. This section will discuss how the configuration of political power has evolved in Bangladesh in recent decades using a simple classification of types of political configuration summarised in Box 1.

Box 1: The Political Settlements Analysis (PSA)

The distribution of organisational power in a society (its political settlement) is an important determinant of the policies and institutions that emerge and how effectively they can be implemented. The distribution of power affects implementation because it identifies the organisations that are likely to capture rents, if necessary by distorting formal policies. The distribution of power *across* political organisations and *within* the ruling coalition are both important. The capabilities of economic organisations and of the bureaucracy (including the military) are also important components of the overall configuration of power. However, the configuration of *political* power is particularly important and we use the framework in Khan (2010) to describe this aspect of the political settlement as shown below.



The configuration of power in the top left hand corner of the diagram describes *potential developmental coalitions* where the ruling coalition faces weak opposition from excluded groups and the leadership has effective power over their own organisations. This combination results in long time horizons, as the ruling coalition is not vulnerable and significant implementation capabilities as its lower levels can be disciplined by higher levels. These coalitions may appear to be authoritarian but rarely have to use violence. In principle, they could also be elected to power.

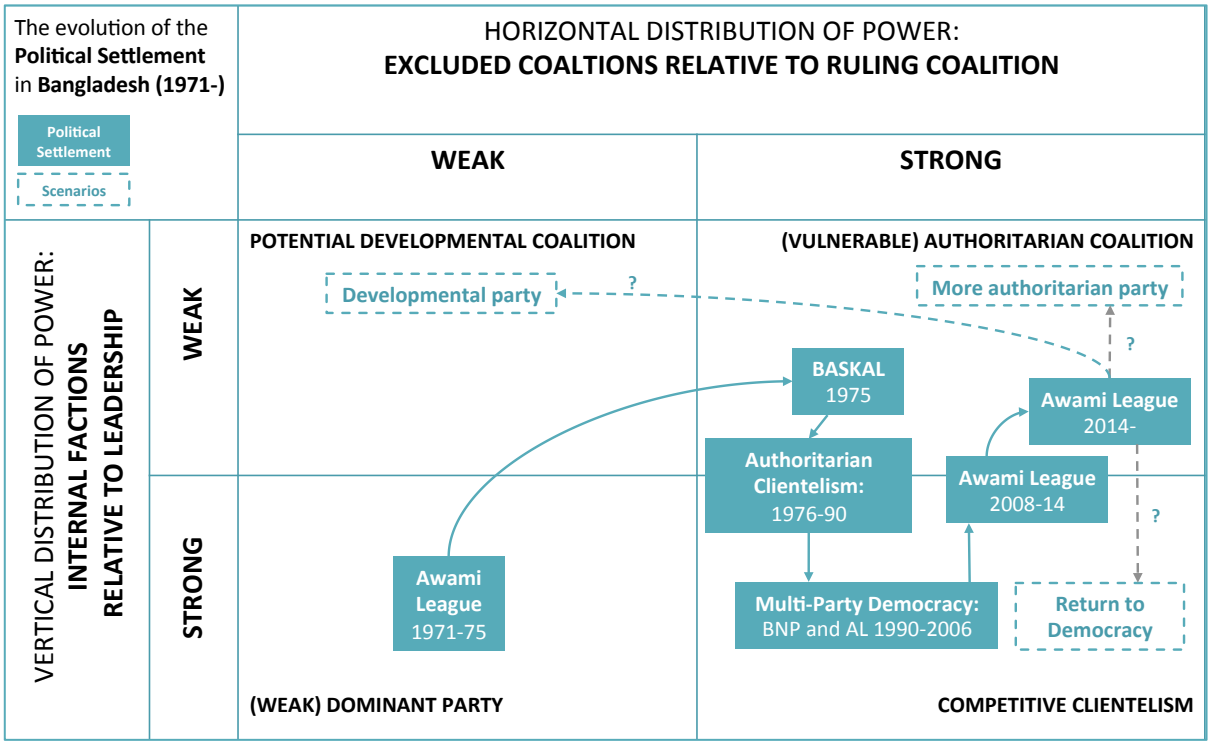
As excluded organisations become more powerful, the ruling coalition may have to use more repression or violence to stay in power. We then have the emergence of *vulnerable authoritarian coalitions* as we move towards the top right. These coalitions have a shorter time horizon and the leadership engages in more unproductive rent capture even if their control over their followers remains strong.

However, these ruling coalitions tend to lose control over lower levels because it is difficult to control lower levels if powerful excluded organisations offer them better deals. Parts of the ruling coalition can begin to leave and build new organisations or join the opposition hoping to get better deals. As multiple parties emerge, each party has weaker control over their organisation because disaffected members can leave. We are then in the bottom right hand corner described as *competitive clientelism*. This configuration of power typically supports democratic competition in developing countries. Democracy can be more stable and less repressive than a vulnerable authoritarian coalition if organisational power has actually become fragmented, but democratic parties also have short time horizons and weak implementation capacities. If the competing parties can work out 'live and let live' arrangements of replacing each other in power, institutional and policy stability may emerge with good development outcomes in some contexts.

Finally, a configuration of power where a large political organisation faces limited opposition can result in a *weak dominant party* in the bottom left hand corner. Such a ruling coalition may have limited implementation capability because by including almost everyone the leadership pays the price of not being able to impose discipline on their own organisation. These ideal types are simplifications and many examples lie on the boundaries of these configurations: for instance dominant parties with strong organisations can be close to being developmental coalitions, developmental coalitions that face growing resistance can become vulnerable authoritarianisms and so on (Khan 2010).

The configuration of political power in the political settlement of Bangladesh can be usefully divided into four phases that are closely associated with changes in governance characteristics that affected economic performance (Khan 2013a). The trajectory of the political settlement since 1971 is summarised in Figure 7 using the classification in Box 1. We summarise this trajectory below and then discuss the phases in greater detail, with particular emphasis on the latest period, to draw out the likely implications for opportunities and challenges for governance and anti-corruption reforms.

Figure 7: The evolution of the political settlement in Bangladesh 1971–2017



Source: Author

The turbulent first phase from 1971 to 1975 immediately after the independence of the country was one of a dominant party becoming a vulnerable authoritarianism. This period included an attempt at socialist planning based on nationalising the entire modern manufacturing sector. The ruling Awami League had campaigned for Bengali rights and later for independence under the charismatic leadership of Sheikh Mujibur Rahman. The party was initially inclusive of almost all major political forces in the country, and therefore the ruling coalition was located in the bottom left of the diagram. Despite Mujib's enormous personal popularity, his party failed to manage internal political competition in a democratic way. Its attempt to create a one-party state (the Workers and Peasants Awami League or BAKSAL) as a way of imposing discipline on its supporters created a *vulnerable authoritarianism* that was very unpopular and did not last. The period ended with the assassination of the President by disgruntled junior army officers.

The second phase, from 1975 to 1990, saw a managed return to multi-party politics under parties led by ex-military rulers. This was a hybrid period ,with characteristics of both *vulnerable authoritarianism* and *competitive clientelism*. We have described this hybrid elsewhere as authoritarian clientelism (Khan 2013a), located somewhere between the two boxes on the right hand side in Box 1. Ex-military rulers were in power, but they formed political parties and opened up the political space to enable multi-party politics to begin again. This period combined multi-party democracy with some authoritarian limits on the extent of political competition that was allowed. The overthrow of General Ershad in 1990 brought in a period of democratic competition without restrictions on the political activities of the opposition, a distribution of power that we describe as *competitive clientelism*.

The years of *competitive clientelism* from 1990 to 2006 were, in hindsight, a halcyon period for Bangladesh. The admittedly shaky political institutions of democracy were in equilibrium with the competitive clientelist distribution of power. As a result, all powerful political factions had a reasonable chance of getting to power and accessing political rents. This in turn created investor confidence in the long-term stability of the political system. Much of the growth acceleration in Bangladesh happened in this phase of open multi-party competitive democracy. The economic interventions that allowed capability development in garments had already happened in the late 1970s. Now a period of political predictability led to sustained improvements in private investment. This was the period in which the term 'Bangladesh paradox' was born. High levels of corruption and apparently weak governance coexisted with high levels of private investment, export growth and accelerating growth rates. The democratic phase came to an end in 2006, as a result of a failure by the two major parties to institutionalise credible electoral rules. There followed a two-year interregnum of a military-backed Emergency Government that ended with elections that brought in a new Awami League government.

The fourth phase, which began in 2008 with the election of a new Awami League government, has seen an evolution of the political settlement away from *competitive clientelism* towards an effective one-party system. The underlying changes in the distribution of organisational power are still fluid at the time of writing (2017) and the following analysis therefore outlines a number of possible scenarios for the future. On the basis of the available information, the emerging one-party system in Bangladesh is not a move back towards a dominant party in terms of Box 1, because a true dominant party is based on a ruling coalition that includes all major political networks and organisations. Rather, the emergence of the new one-party system is more accurately a move towards a *vulnerable authoritarianism*, where a ruling coalition stays in power by enforcing electoral rules of its own choice and restricting the organisational freedoms of the opposition.

The current transitional stage can be described as 'authoritarian clientelism', which is a stage between *competitive clientelism* and *vulnerable authoritarianism*. The ruling coalition uses organisational restrictions on the opposition, but is itself not very consolidated and disciplined and some opposition activity takes place. As a result, this configuration is not stable and is likely to evolve further in a number of possible ways, depending on mobilisations and counter-mobilisations by different forces. In the first scenario, the ruling coalition can move further northwards in box 1 by consolidating its own discipline to further limit the scope of opposition activities. Some political activities of the ruling party, in terms of attempting to establish control over the state administration and restricting the activities of the opposition, suggest that they may want to move in this direction. But there are questions about the sustainability of this strategy, given the relatively short life span in Bangladesh of previous coalitions that used similar strategies to stay in power.

In a second scenario, the political settlement could revert back towards competitive clientelism and a multi-party democracy, either as a result of an effective challenge by excluded groups or as a result of divisions within the ruling party or some combination of both. This would be strongly resisted by sections of the ruling party as they may be fearful of reprisals by opposition parties if they are voted out of power, as the opposition has faced

repression for some time. Nevertheless, this scenario is likely to materialise sooner or later as an institutional equilibrium in politics is only likely in Bangladesh if all groups have a reasonable chance of getting to power through competitive politics.

Finally, the least likely scenario is that the ruling Awami League becomes simultaneously much more inclusive (thereby reducing external opposition and the need for repression) and more disciplined (making it capable of implementing developmental policies). In this scenario the Awami League becomes more like a developmental party like Malaysia's Barisan National in the 1970s. While this is a trajectory that some party ideologues are promoting as a possibility, the configuration of power within and outside the party makes this the least likely scenario.

3.1. From dominant party to vulnerable authoritarianism: Awami League 1971 to 1975

The Awami League government that was elected in what was East Pakistan in 1970 was enormously popular and was initially an example of an elected dominant party. A significant number of the powerful groups and factions in the country were under the Awami League umbrella at that time, united in their determination to get a fair deal for Bengalis. When the West Pakistani elites refused to accept the results of the 1970 election and East Pakistan split to become Bangladesh, even more groups joined the Awami League. It was a classic example of a weak dominant party because it included so many groups that it faced little opposition from outside, but its very size and complexity meant that the leadership had limited control over the organisation. From the beginning, tensions began to rise over the distribution of resources and opportunities, and some groups began to leave the party and set up counter parties from 1972.

The years immediately after 1971 were economically difficult because of the disruption and destruction caused by the war. The limited industrial capabilities that had developed in modern industry were mostly in West Pakistani-owned firms, including many jute mills in East Pakistan. When the West Pakistanis left in 1971, the nationalisation of these assets was perhaps necessary given the absence of Bengali entrepreneurs who could have taken over and run these companies. But the government went beyond necessity by also nationalising the assets of Bengali capitalists.

What ensued was a period of unconstrained asset and resource grabbing by party members (Islam 1979: 225-6). This was a version of political corruption, but on a bigger scale than is normal in developing countries, where informal resources have to be found by political leaders for their organisers and supporters. In the aftermath of independence there were very high pent-up demands of organisers who had led the movement. Some of the asset capture could also be described as 'primitive accumulation' in the sense that individuals with political power were accumulating assets through these means. Primitive accumulation can sometimes have positive outcomes if it results in the emergence of productive capitalists, but this takes time and needs additional conditions. However, the immediate impact of the corruption and primitive accumulation was to exacerbate the destruction of the war.

Productivity in manufacturing collapsed to an average of less than 50 percent of the level reached in 1970, and real wages in manufacturing to around 60 percent of their 1969/70 level (World Bank 1978: Vol. II Annex I.6 p. 173, 1984: Vol. II Table 9.12 p. 118).

In 1974 Bangladesh suffered from a serious famine that took place without any significant decline in aggregate food availability (Sen 1983). The causes were largely state failure in managing distribution and ensuring purchasing power in a context of hoarding and smuggling. More than a million people died in the famine, dissipating broad support for the party (Sen 1983: 134-41; Karim 2005: 335-40). Growth collapsed to -0.1 percent over the period, partly caused by the ravages of the war, but partly also compounded by policy choices and rent management failures of the government.

The response of the regime to the growing economic and political crisis was to announce the formation of a one-party state and to ban all other political parties and organisations. This attempted transition to a *vulnerable authoritarianism* did not prove sustainable. The Awami League was renamed the Peasants and Workers Awami League (BAKSAL). Paradoxically, the attempt was not to *exclude* opposition networks but rather to force them to join an *inclusive* party. But forced inclusion does not create an inclusive party: it was soon clear that the move triggered strong resistance that would have required repression to sustain. Forced inclusion excludes many organisations from competing for rents on their own terms and has to be enforced by administrative restrictions and suppression, a characteristic of *vulnerable authoritarianism*. For existing Awami Leaguers the implication was also a dilution of their control over rents, as well as reduced bargaining power with the leadership, as they would no longer have a credible threat of leaving the party (Khan 2013a). To be sustainable, the leadership would have to impose greater discipline on the party and this too was resisted, making the move towards vulnerable authoritarianism in Figure 7 particularly difficult. Senior members of the party and state publicly voiced approval for the new arrangements, but their subsequent actions in instantly supporting the post-Awami League regimes reveal that many were deeply dissatisfied. The regime did not last long after the introduction of BAKSAL, as Mujib was assassinated in August 1975.

3.2. Authoritarian clientelism and the gradual return to democracy 1975 to 1990

More turbulence followed the assassination of Mujib, with coups and counter-coups, till Major-General Ziaur (Zia) Rahman became chief martial law administrator in 1976, and President in 1977. Under him, multi-party democracy was gradually restored and he set up the Bangladesh Nationalist Party (BNP) in 1978. By allowing the mobilisation of other parties, including the Awami League and Islamist parties, Zia was able to reduce the resistance and violence coming from excluded organisations. The party he built was based on absorbing factions from all sides and this meant his capacity to discipline the new party was not very high. Zia himself had a reputation for integrity, but the BNP was a typical clientelist party, like the Awami League, and rent distribution based on political corruption was essential for maintaining the organisation. A form of *competitive clientelism* was emerging but it was initially constrained by the strong rule of Zia, which ensured that while factions could mobilise

and compete with or join the BNP, their realistic chance of displacing the leader was small. This is why we describe this transitional phase as *authoritarian clientelism* in Figure 7.

While Zia's new party was weak as an organisation for policy implementation, his personal charisma and control over the administration allowed him to push through some critical policy innovations. Nationalisation and the 'socialist' planning that had been introduced under the Awami League began to be reversed. In particular, he oversaw and enabled the Desh-Daewoo partnership that brought the modern garments and textile industry to Bangladesh. Its entry was based on enabling a new type of industrial policy that passed on some of the 'quota rents' created for Bangladesh by the MFA to a foreign technology provider, Daewoo, to induce them to transfer organisational and technical capabilities to a Bangladeshi-owned firm, Desh (Rhee 1990; Khan 2013b, 2015). Once Desh had acquired these capabilities, it did not stop its managers from migrating and setting up their own firms, allowing rapid growth through imitation and clustering. Desh did not resist imitation because it saw the advantages of clustering that attracted a steady stream of orders and buyers.

Zia was a popular war hero, but he too was assassinated in 1981 by dissidents within the army. His successor, General Ershad was much less popular. He was also personally corrupt, popularly reputed to take a 10 percent cut on all projects. During his rule, opposition political parties consolidated their power and demanded that he step down so that they would have a real chance of winning. This was the beginning of the realisation in Bangladesh (a realisation shared by both the Awami League and the BNP at the time) that it was virtually impossible to defeat a sitting government in an election, while it controls the administration. The incumbent does not have to stuff ballot boxes (though that occasionally happens). There are many different infractions including policing delays in particular areas, and obstructions and intimidation of some voters that collectively mean it is very difficult to oust an incumbent in elections, a problem that remains to this day. Ershad's refusal to stand down resulted in political violence and instability that led to the decline in private investment that we discussed in Section 2. The fall of his regime brought about the innovation of a 'Caretaker Government' an electoral arrangement that set up a neutral administration to organise the elections and hand power over to the winner. The next fifteen years saw repeated transfers of power in elections as a result of this innovation becoming institutionalised in 1996.

3.3. Competitive clientelism and democracy 1990 to 2006: growth and the Bangladesh paradox

The transition to democracy in Bangladesh brought about political peace because the configuration of power between and across political organisations was reflected in political institutions that gave all powerful groups a realistic chance of getting to power and accessing rents. Excluded organisations were strong, but as they perceived they had a chance of getting back to power through elections, other forms of competition such as the use of violence remained *relatively* limited. However, limited does not mean absent. There were frequent episodes of violent confrontations between the two major parties: the BNP and the Awami League. Nevertheless, the elections were sufficiently well managed by the Caretaker

System of conducting elections, formally introduced through the 13th Amendment to the Constitution in 1996. Nevertheless, political parties had short time horizons and the competitive political structure meant that leaders found it hard to discipline their organisations and could only keep them together with generous internal rent allocations. Political corruption was paradoxically even higher than under the egregious Ershad, to the surprise of many democracy campaigners who had hoped that democracy would result in a reduction of corruption. The real advantage of democracy was in achieving stability and reducing the conflicts between competing coalitions of factions. Private investments shot up, beyond the levels that could be achieved by the authoritarian Ershad regime, largely because of a more predictable long-term strategy through which the private sector could protect its interests by doing deals with the two main parties.

The high growth during the democratic period in Bangladesh can be attributed to a combination of three factors. First, greater *political stability* was beneficial for supporting investments in sectors that were already competitive. This would not, however, have been sufficient without a second critical factor: the *prior existence of a number of competitive sectors*, both in industry and agriculture. These sectors included garments and a few others, like basic pharmaceuticals. Stability without competitiveness would not have worked. In addition, there were a number of sectors with simple technologies where organisational learning was not difficult. These included sectors like poultry, shrimp and fish farming, and food products. Businesses entering these types of sectors could expect to rapidly establish the local political and bureaucratic connections necessary for doing business. Finally, *political competition created a perception of safety from excessive rent extraction*. If a government was becoming too extractive, businesses could threaten to switch support to the opposition. Perhaps for this reason, both major political parties continued to be business-friendly, and both had a live-and-let-live attitude to businesses, regardless of the parties they supported. Businesses closely associated with the current ruling party were likely to be somewhat more privileged, but other businesses were not destroyed and could wait for a change in government to get better opportunities.

On the other hand, there were serious problems of governance during this period. The close links between business and politics were often problematic. Many entrepreneurs began to stand for and win elections with party tickets and many became party financiers. By the late 1990s, the majority of parliamentarians described themselves as businessmen or women. As we would expect in these contexts of informality and personalised relationships, the businessmen in politics did not represent collective business interests, but rather their own interests in capturing rents. The greater participation of businesses in politics therefore did not result in better public goods for the private sector, better regulation, or developmental policies or rules-based governance. Instead, it resulted in greater competition for rents between the parties based on increased investments in rent-seeking, and a consequent worsening of some developmental outcomes.

This political context described above did not support the credibility of long-term contracting, particularly between governments and domestic investors. Foreign investors were somewhat better off because their investments were often protected by sovereign guarantees, for instance in the power sector. There were only two major private sector

investments in power generation between 1990 and 2006, and both were by foreign companies. The Haripur and Meghnaghat 1 power plants became operational in 2001 and 2002 respectively, with significant World Bank funding or World Bank Partial Risk Guarantees. Both investments were led by the US company AES (Allied Energy Systems) and contracted to sell electricity at very competitive prices in plants that are still operational. Both were later owned and operated by the Malaysian company Pendekar Energy. No further private investments of any significance were forthcoming over the next six years, resulting in growing power shortages[1].

Political stability also began to fray towards the end of the period as the competition between the two parties became more fraught. During the last BNP government there was a grenade attack in August 2004 on a rally attended by the leader of the opposition Awami League causing the deaths of 24 people. In 2005 the Awami League's ex-Minister of Finance was assassinated. The investigations into these incidents by the BNP were not sufficiently robust and did not satisfy the Awami League. The failure of politics in Bangladesh was that the live-and-let-live principles on which the formal and informal rules for rent allocation were based could not be sustained.

On most measures of governance quality, Bangladesh fared poorly or even retrogressed during the democratic period. Corruption was high and generally increasing, there was creeping politicisation of the administration that got worse with every successive government and the formal institutionalisation of rules proved to be difficult. Political violence also crept up gradually. Ultimately, the failure to institutionalise and follow the critically important electoral rules of the caretaker system led to the emergency of 11 January 2007. The political settlements analysis therefore provides an explanation for the 'Bangladesh paradox' but also suggests why the paradox could not last forever. The economic challenges for Bangladesh going into the future remain: how to develop new sectors and to increase productivity and diversification, and how to encourage long-term investments (Khan 2013a). Even if *competitive clientelism* had continued, the challenge of addressing some of the governance failures affecting productivity growth would have emerged.

3.4. Return to single-party rule: towards a new vulnerable authoritarianism 2008–?

After the two-year Emergency that followed the breakdown of elections in 2006, elections in 2008 brought the Awami League back to power. The Emergency was a period of lost opportunities, because policy-makers during this period attempted to introduce 'good governance' and eliminate corruption in general. Instead, a more politically astute approach would have focused on implementable reforms that addressed some of the most damaging

[1] Some commentators have jumped from the observation that a few businesses did make long-term investments (and were thus able to deal with both parties) to the erroneous conclusion that contract enforcement in general was not a problem constraining long-term investments (Hassan 2013: 23-4). The negligible scale of private domestic investments in the power sector over this period falsifies this claim.

types of corruption. The collapse of the Emergency period reforms and the return to democracy could have marked a return to *competitive clientelism*, but it soon became clear that the new ruling party, the Awami League, was intent on changing the rules of the game to ensure the opposition could not win the next election. Its strategy included reducing the organisational freedoms of opposition parties and changing the electoral laws by abolishing the Caretaker System in 2011, through the Fifteenth Amendment to the Constitution. This significantly reduced the credibility of elections and unleashed serious conflicts and uncertainty. The 2008 Awami League was therefore already positioning itself to take on the opposition using administrative and policing methods: for this reason in Figure 7 we locate it as moving towards *vulnerable authoritarianism*.

Despite intense and violent opposition and a boycott of the elections by the opposition BNP, the government moved ahead with the 2014 elections. The 2014 Awami League government was effectively an unelected government, as more than half the seats in parliament were uncontested and no election was held in these seats. In the rest, the competing candidates were all members of the Awami League or its close allies. The 2014 Awami League government therefore began life with a low level of legitimacy. The suppression of the opposition has been quite systematic and has raised questions about the sustainability of these political arrangements. We have already seen in Section 2 the dampening effects of political uncertainty on private investments.

The single-party rule that has emerged at all levels of administration in the country probably does not reflect a real change in the latent power of underlying political networks in the country. It is more plausibly the result of an effective deployment of administrative power and political strategies of delegitimising and blocking the activities of the opposition. This has been effective for a while, but its long-term sustainability must be questionable. The post-2014 Awami League is therefore not a dominant party like the 1971 Awami League, and is more accurately described as a *vulnerable authoritarianism*. While it clearly enjoys the support of its core constituency, its stay in power has depended on not allowing elections under the only set of rules that have actually worked in changing governments in Bangladesh. The interesting question is how this new configuration of power is likely to evolve in the near future.

In Figure 7 we suggested three possible alternative scenarios over the next five years. The first is a consolidation of the current strategy of the ruling party. If the Awami League intends to stay in power by continuing to reject demands for a neutral administration to organise elections, it will have to become more effective and disciplined in dealing with concerted opposition over time. The success of this strategy will depend on the emergence of a more 'authoritarian' party. Such a party will still be vulnerable because it will have to continuously confront opposition, perhaps from new sources. There are signs of growing internal conflicts within the Awami League and the party is unlikely to remain sufficiently disciplined to make this scenario viable in the longer term. Newspaper reports suggest sustained and growing violence, often lethal, between competing factions of the ruling party over contracts and positions. Imposing discipline on such a party may not be easy. But if the party is internally divided, its capacity to take on and resist growing opposition may be compromised.

Moreover, in an unexpected challenge to its strategy of politicising the administration, the judicial branch struck down the Sixteenth Amendment to the constitution (which allowed parliament to impeach judges deemed to be 'incapable' using a two-thirds majority) passed by the Awami League in September 2014. As the Awami League and its allies control parliament after the uncontested 2014 elections, this would have institutionalised party control over the judiciary. The High Court declared the amendment illegal in May 2016, and a government appeal to the Supreme Court was defeated in July 2017. This has opened up a new front in the government's attempts to establish control over the administration. Immediately after the verdict, the government made clear that it disagrees with the Supreme Court and will attempt to by-pass the verdict. If it does, this too will be a point of conflict with uncertain long-term consequences. Finally, if the uncertainty continues and investor confidence suffers much more, economics will kick in to make the scenario unsustainable. The long-term sustainability of the first scenario is therefore questionable given these economic, political and administrative constraints. Nevertheless, the political determination of the ruling party to go in this direction suggests that there is at least a 50 percent probability that some variant of this scenario will persist in the medium term.

The second scenario is a return to democracy of a competitive clientelist variety. This is likely to be a more sustainable outcome over time, but the transition has become increasingly difficult and an immediate transition does not appear very likely. A necessary condition would be the emergence of credible election arrangements, such that the winner of the election was perceived to actually have more popular support and therefore legitimacy as the winner. This is unlikely to happen without popular mobilisation for a change in electoral rules back towards something like the caretaker system. But such a mobilisation is difficult in the presence of significant political control over the police and other parts of the administration, even though some aspects of political control are fraying. While some form of *competitive clientelism* is likely to bring about the best feasible conditions for long-term stability and private sector investments in the context of Bangladesh, the political strategy of the ruling party currently gives this scenario no more than a 40 percent chance of materialising in the medium term.

A third scenario is that the Awami League becomes a developmental party. This would be a desirable outcome, but is the least likely one given that this would require the ruling party to become not only more disciplined but also more inclusive, to reduce the necessity of using administrative mechanisms for limiting opposition. Achieving greater inclusion through a voluntary process is very difficult in the Bangladeshi context as the history of BAKSAL in 1975 shows. The political networks that are against the Awami League have deep ideological differences with it and, in addition, many have experienced harsh repression in the recent past which they are unlikely to forget. In the current context of Bangladesh it is hard to imagine a viable strategy through which the Awami League could absorb enough of the opposition to allow it to stay in power without administrative limits on political activity or even repression. While some Awami League supporters have been promoting the construction of a developmental party that provides 'development first and democracy later', the realistic possibility of such an outcome materialising in the configuration of power in Bangladesh is not more than 5 percent.

Other alternatives like a military coup are not likely in the current political situation. The army appears to be content to stay out of the political fray and that is in any case a desirable outcome for political development in Bangladesh. However, given that legitimate elections appear to be unlikely in the near future, one of a large number of unpredictable black swan events cannot be ruled out in this uncertain political context, even though they appear to have low probability or feasibility at the moment.

The economic and political outcomes that we observe in contemporary Bangladesh are therefore consistent with a direction of travel towards a *vulnerable authoritarianism*. In some respects, governance capabilities appear to have declined relative to the democratic period. The impunity and politicisation of law-enforcement officers appears to have increased. There appears to be higher levels of corruption in banking and other sectors that are not satisfactorily investigated despite repeated media exposures of large scale scams. There is a creeping growth in political violence and the growing politicisation of all branches of government (Transparency International Bangladesh 2014). If the government eventually wins its battle with the judiciary over the Sixteenth Amendment, it will be able to politicise the judiciary to an unprecedented extent. The possible exception to this story of poor development outcomes is an increase in investments in power generation and infrastructure, discussed below, even though some of these investments are relatively inefficient ones. Despite these areas of relative success, the general impression is one of governance facing substantial implementation and enforcement problems. This is consistent with short time horizons of investors and politicians, and inadequate levels of control by the political leadership over their party organisation.

The weak disciplining of big business is one example of the problem. A number of big business houses have had significant problems with servicing large loans. These problems can occasionally emerge without any cronyism, and restructuring and rescheduling of large loans is sometimes necessary. However, a distinctive characteristic of developmental states is that occasional loan restructuring and other forms of assistance are combined with the imposition of conditions that the investor has to meet to ensure that the requisite improvements in productivity and competitiveness are achieved. Otherwise the rescheduling of loans is likely to require further rescheduling in the future, at a higher cost in terms of lost resources. While small borrowers face very hard conditions when they request rescheduling, large politically connected business houses in Bangladesh are often given very easy rescheduling terms that are unlikely to result in productive outcomes.

In 2014, one of the largest politically connected business groups, Beximco, asked for almost US$ 700 million of non-performing loans to be rescheduled. A restructuring of US$ 130 million was almost immediately agreed by Sonali Bank, followed by US$ 240 million rescheduling by Janata Bank. Not only that, Beximco was granted a two year repayment holiday and it would *then* enjoy an interest rate two to three percent *lower* than the market rate (*Daily Star 15 December 2014: Tk. 1.849cr Beximco Loans Rescheduled*). Beximco was not alone in getting sweet deals that more productive smaller companies could not hope for. Nine of the biggest business groups with similar political connections asked for loan rescheduling amounting to US$ 1.8 billion. Here was an opportunity that an aspiring developmental party may have seized on to impose conditions for greater productivity and competitiveness over time.

Instead, the poor performers were only requested to meet their restructured repayments. These examples are consistent with the more pessimistic scenario of the emergence of a *vulnerable authoritarianism* with short time horizons and low enforcement capacities, rather than an emerging *developmental coalition* of the East Asian type.

Not surprisingly, asset owners appear to be increasingly concerned about the safety of their assets in such a context. There are worrying trends of accelerating capital flight to safe havens abroad. Recorded deposits of Bangladeshis in Swiss banks were reported to have doubled in two years, from 258 million dollars in 2012 to 550 million dollars in 2014 (*Daily Star 21 June 2015: Eyes Abroad*). If we had figures for flight to all havens, including unrecorded flows, the capital flight is likely to be several billions of dollars since 2012. The Global Financial Integrity Report of 2015 suggests that illicit capital flight from Bangladesh increased from US$ 5.4 billion in 2010, to US$ 7.2 billion in 2012 and US$ 9,666 million in 2013 (Kar and Spanjers 2015: Appendix Table 3). The absolute numbers in the report are estimates based on specific methodologies, but all the evidence points to a significant *growth* in illicit flows from Bangladesh over this period.

The Bangladesh Bank has also expressed concern at the unusually high figures for machinery imports in 2015, in a context of suppressed private investment overall. The Governor of the Bank raised the possibility that machinery imports were being over-invoiced to illegally transfer capital out of the country (*The Guardian Bangladesh 26 May 2015: Capital Machinery Imports: BB checking banks' BoE to unearth capital flight*). The many dimensions of this evidence suggests that the private investment slowdown may be more than a temporary blip, and may reflect a more persistent problem of confidence leading to the withdrawal of capital from the country. The dynamics of business-government relations and private sector investments will be important to track in the future. Business confidence could return if it became clear that the opposition was temporarily not in a condition to pose any challenge to its exclusion, but this too could be reversed once excluded groups began to mobilise in new ways.

Two areas that appear to be an exception to the general story of poor resource management are electricity generation and some infrastructure investments. Investments in infrastructure have significantly increased but cost inflation has also been very high, so that the real increase has been much lower than the nominal increase. The story in the power sector is only marginally better. After 2009 there has been a rapid growth in generation capacity but a large part of the increase has come from the commissioning of peaking power plants also known as quick rental plants. The unit cost of generating electricity is considerably higher in these smaller plants (up to five to six times higher per MW compared to larger plants), partly because they use more expensive fuels like furnace oil. There were often no bidding processes through which the contracts were allocated, and no transparency. The high costs of these power generation projects were passed on to the exchequer, because power was being distributed to consumers at a much lower price. Parliament also passed a law indemnifying the granting of these contracts from prosecution (Shah 2014: 6). The legal status of this indemnity is questionable once the government changes, but it does suggest that because the contracts were more than usually attractive and were often allocated without bidding, the indemnity was required to protect investors

and the government from challenges in court during the lifetime of this government. These lucrative contracts did attract investments by both Bangladeshi and foreign firms and began to make an impact on the very severe energy shortage in the country. However, the social cost of generating power in very expensive ways has been rising. Currently, around half a billion to one billion dollars (depending on the price of imported fuels) have to be transferred every year from the government's budget to the Bangladesh Power Development Board to pay for these expensive power supply contracts. It is clear that this route to expanding power supplies is not very sustainable.

However, some efficient investments have also taken place in bigger power projects like Meghnaghat 2 and Bibiyana, led by companies like Summit Power. Meghnaghat 2 became operational in late 2015. The credibility of complex long-term international contracts was crucial to the success of these bigger ventures, as was the capacity of the promoters to raise capital relatively cheaply in international capital markets. In Meghnaghat 2, for example, the turbines come from the American company GE, the plant was constructed by a Chinese company, the management and operation will be in the hands of a South Korean company for a period of several years, while the Bangladeshi sponsor, Summit, organised the finances from domestic and international sources and will eventually take over the operation. Contracts for the supply of gas and fuel and for the purchase of the power produced are with Bangladeshi public sector organisations. The capability of companies like Summit to raise money in international markets for long-term power projects has depended on their size and asset base, and their close connections to the government. There are very few Bangladeshi companies with this mix of characteristics and this has constrained efficient investment in these complex long-run projects. They also require a level of credibility of complex contracts, as many different parties have to feel assured about their liabilities, rights and responsibilities under plausible contingencies. If the Bangladesh government moves too much in the direction of a *vulnerable authoritarian* regime, this too may damage the credibility of private sector contracting in areas like power where the country has to do even better in the future.

4. History and evidence of anti-corruption measures in Bangladesh

Like many developing countries, Bangladesh has extensive formal legislation supporting anti-corruption, but is deficient in the interpretation, application and implementation of these laws. These laws, and the associated enforcement agencies, are geared to attacking corruption in general, which we have described as systemic anti-corruption based on the enforcement of a rule of law from above (Khan et al. 2017: 12). The problem is that a general or systemic attack on corruption based on 'vertical enforcement' is implausible in a context where many of the most powerful organisations in the country are engaged in rule-violating behaviour or in informal contracting on a daily basis. In these contexts, the 'horizontal' support by powerful organisations for the enforcement of *general* rule of law is weak. If anti-corruption laws are enforced from above in such a context, they are at best likely to be applied selectively to individuals and organisations currently out of favour with the ruling coalition. This type of enforcement is not likely to do much for the achievement of a general rule of law, and this is indeed what we see across developing countries, with Bangladesh no exception. In contrast, the ACE approach looks for opportunities in particular sectors, where policies can be feasibly changed to create incentives for some of the powerful players within these sectors to behave productively and thereby reduce unproductive rent capture. If we can identify such opportunities, there may be sufficient horizontal support at the sectoral level for the enforcement of rules for effective anti-corruption that achieves better developmental outcomes. In this section we list some of the limitations of systemic anti-corruption initiatives in Bangladesh, and the implications for our alternative anti-corruption strategies.

Bangladesh acceded to UNCAC (the United Nations Convention against Corruption) in 2007 during the tenure of the Emergency Caretaker Government that was committed to anti-corruption. At that time, the Government of Bangladesh commissioned a study to identify possible gaps in existing laws and capacities that would need to be addressed to bring Bangladesh in line with requirements of the Convention (GOB 2008). This study concluded that in terms of the legal regime, Bangladesh was already largely compatible with the standards and principles of UNCAC (GOB 2008: 9). Of course, this refers to the formal aspects of the law and not its actual application in practice. The latter depends on enforcement capabilities, and how powerful interests use informal procedures to modify or subvert the application of formal laws. The fact that the formal structure of laws is largely aligned with UNCAC, and that considerable investments in capacity building for better enforcement have not had significant effects, suggests that a focus on vertical enforcement is insufficient for making a significant impact on corruption.

The comprehensive legal regime in place in Bangladesh includes an anti-corruption law (the Prevention of Corruption Act, 1947) and the Anti-Corruption Commission Act, 2004, that created an independent anti-corruption body. Furthermore, a comprehensive procurement regime exists with the Public Procurement Regulations, 2003 and the Public Procurement Act, 2006. The regulatory regime that serves to promote public sector integrity, and governs

issues of public sector recruitment, hiring, retention, promotion and retirement, consists of the Bangladesh Civil Service Rules, 1981, the Bangladesh Civil Service Recruitment (Age Qualification and Examination for Direct Recruitment) Rules, 1982, the Public Service Commission Ordinance, 1977, and guidelines for public sector training such as the Public Administration Training Policy (PATP), 2003. Furthermore, institutions such as the constitutionally sanctioned Office of the Comptroller and Auditor General (CAG) and the Central Procurement Technical Unit (CPTU) are additional mechanisms to ensure greater transparency and accountability in public procurement and public finance.

The study commissioned by the Emergency Government, referred to above, recognised that implementation was weak, but did not give an indication of how seriously weak and in which sectors and activities. For instance, it says that in procurement, the rules are applied 'inconsistently' across government, and implementation is hampered by 'inadequate resources' in concerned agencies (GOB 2008: 10). This is a serious understatement of the scale of the problem. In the World Bank's Enterprise Survey of 2013, 49 percent of firms in Bangladesh expected to 'give gifts' to secure a government contract, compared to 46 percent in South Asia and 29 percent globally[2]. Public procurements are a serious problem across developing countries, because they are closely linked to governments' patronage and rent-sharing strategies, making procurements a particularly difficult area in which to develop a feasible sectoral anti-corruption strategy. In Bangladesh, the close links between the government, politically connected contractors and more recently the army, in infrastructure construction and contracting are well known. In our analysis, this makes it hard to find feasible and effective anti-corruption strategies in this sector using our methodology. It is not surprising that systemic anti-corruption enforcement strategies have delivered few results in public procurements in Bangladesh. While procurements and contracts in construction projects involve powerful coalitions and allocations of some of these rents on political grounds to maintain the regime, procurements in other areas may offer greater opportunities for incremental improvement. There may be opportunities for incremental improvements in the procurements of medicines, for instance, where a variety of productive interests are involved, rents are not generally allocated by the government to powerful players to sustain the regime, and the quality and price of drugs have an impact on the delivery of health services that directly affect voter perceptions.

Another area where laws already appear to be in compliance with UNCAC requirements is in the recruitment and promotion of public officials (GOB 2008: 10). Once again, the report argues that implementation is weak and capacity improvements are necessary. However, this is another area of systemic politicisation and corruption, involving political patronage and strategies of regime reproduction. The 'political' nature of the corruption in recruitment and promotion means that anti-corruption strategies are again likely to face implementation problems that go beyond the technical capacity of enforcement agencies. The recruitment and promotion of bureaucrats has become progressively more politicised and closely linked to political strategies of regime maintenance of whichever party is in power. Here too, not only have systemic anti-corruption strategies failed to make any significant impact, in our

[2] World Enterprise Survey http://www.enterprisesurveys.org/data/exploreeconomies/2013/bangladesh

assessment incremental and sector-specific strategies are also likely to make little headway. It would be difficult to find coalitions of bureaucrats and politicians, at any level, who have both the power and the interest to want to implement formal rules for the selection and promotion of civil servants as laid out in the legislation.

Both construction procurements and public service appointments and promotions are examples of areas of corruption where the changes in the political settlement in the direction of a single-party regime have made addressing these issues even less feasible. Given the threats it faces from a potentially powerful but administratively excluded opposition, the ruling party is even more concerned to ensure that civil service appointments are limited to people it can politically trust. Similarly, the allocation of large government construction contracts is an important way of creating coalitions of the powerful to support the ruling party in administrative and other ways. The political settlements analysis therefore tells us that these types of corruption are likely to be much less feasible to address right now.

The Anti-Corruption Commission (ACC) has not been able to achieve systemic anti-corruption improvements for these reasons, because some important types of corruption are quite intractable given the political settlement. The ACC has carried out a lot of activities, but individuals and organisations that are currently powerful do not end up being prosecuted, though very occasionally some may be investigated. In 2015 the ACC had 3509 ongoing investigations, out of which it submitted charge sheets for 389 cases (ACC 2015: 26). The cases then go to court and the outcome depends on further uncertainties as courts are also subject to political pressure and corruption. Sometimes large scams that very probably involved some politically powerful individuals are indeed investigated by the ACC, and some offenders do end up in court. An example was a scam at the publicly owned Basic Bank, where the equivalent of US$ 450 million was stolen as a result of collusion between borrowers and bank officials. In this case the investigation resulted in arrests and prosecutions, though it remains to be seen what the courts decide in terms of convictions or punishments (ACC 2015: 30-31). Actual recovery of any stolen money is extremely unlikely on the basis of past experience.

When corruption allegations have included individuals connected with the government there have always been forceful denials. Direct allegations or requests for action by the international community have had limited effects, or have been entirely counterproductive. An example of this was the Padma Bridge affair. A World Bank-led consortium had agreed to fund a $3 billion bridge that would improve connectivity with southern Bangladesh and deliver significant development benefits. Shortly before the project was to begin, an unconnected investigation in Canada revealed documents that suggested that a Canadian company, SNC-Lavalin, had been planning to bribe ministers in Bangladesh to get a $50 million dollar engineering contract. SNC-Lavalin documents referred to a Bangladeshi minister, an ex-minister and other senior bureaucrats and political figures. The World Bank insisted that the minister should be included in a full investigation, and though the government eventually agreed to an investigation by the Anti-Corruption Commission (ACC), the government insisted that the minister would not be included. The ACC did investigate a number of lower-level individuals but they were all eventually acquitted. The World Bank

eventually withdrew from the project in January 2013, in the absence of a satisfactory investigation. Far from encouraging the government to take anti-corruption more seriously, the government eventually found more expensive financing from Chinese and other sources to construct the bridge. The cost of construction was also inflated several times in the absence of any credible external monitoring of contracting and costs. Even if the bridge is eventually built, Bangladeshi citizens will have paid a heavy price in terms of the overall project cost and the interest charges. Regardless of the truth of the allegations, this exercise in anti-corruption did nothing to reduce corruption, and may even have strengthened the government in future allegations, because it has shown that criticism could be resisted and that the Bank and other development partners would return to participate in other projects.

While the ACC has not made any significant dent on systemic corruption, it is engaged in a number of activities that are potentially useful from the alternative perspective of incremental and sector-focused anti-corruption strategies. The ACC organises public hearings at district and sub-district level in remote parts of Bangladesh, where members of the public are invited to question officials of a number of ministries (so far Land, Health and Power) on issues of corruption, delays in delivery, poor quality of services and so on. These events are useful not only for raising awareness and putting some pressure on public officials, but potentially also for generating evidence about the types of corruption that are of concern to people and the feasibility of addressing them. One of the commissioners of the ACC is interested in working with the ACE programme, and has invited us to use the public hearings as a forum to collect evidence for our research. We are exploring a partnership with the ACC in one of our health sector programmes, to use their public hearings for this purpose.

The weakness of governance and the prevalence of corruption has also affected development on a number of other fronts in recent years. A spate of industrial accidents, including the tragic Rana Plaza collapse in 2013 where more than a thousand people died, highlighted the direct effects of regulatory corruption on lives and indirectly on export markets and jobs. This accident, like others in the industrial sector, was largely due to failures of regulation and widespread corruption in the granting of building licenses and other certification. Subsequently, some progress in credible certification has been achieved through the Accord and Alliance processes. The regulation of building and labour codes is one area where an incremental sector-based anti-corruption strategy for improved regulatory compliance has potential. This is an example of a sectoral problem where the interests of powerful players in the garments and textiles industry, and potentially of other export-oriented industries, are aligned with the achievement of better health and safety outcomes, because their export incomes depend on it. Closer attention to the design of regulatory institutions and certification processes should result in feasible reductions in corruption, with very positive developmental impacts, and this is therefore an example of an area where the ACE programme will focus.

There have been a number of major financial-sector scandals in recent years, with the loss of large sums of money that will have to be ultimately borne by the taxpayer. We have already referred to the Basic Bank scandal. In the Hallmark scam in 2012, involving the state-owned Sonali Bank, collusion between borrowers and bank managers led to the disappearance of

almost half a billion dollars that were never recovered. A very small branch of the state-owned Sonali Bank, located in a central Dhaka hotel, provided illegal loans to a group of companies including Hallmark that amounted to US$ 460 million between 2010 and 2012. The loans were letters of credit provided to fake suppliers to these companies, which were encashed against fake documents showing the supplies had been provided. The loans hugely exceeded what the bank could lend to single clients, collateral documents were missing, and the loans also exceeded what the tiny hotel branch was authorised to lend. It was clear that the branch manager could not have done this on his own without the sanction of higher political authorities (Sabet and Ishtiaque 2013). Although this fraud was six times bigger than the next biggest fraud that had happened till then (involving the Oriental Bank in 2007), the Finance Minister initially dismissed the case as one involving an insignificant amount of money. Pressure from various quarters eventually led to the arrest of a few people, but almost no money was recovered and the deeper political links were not uncovered. The growing scale of bank frauds in recent years suggests that fraudsters, colluding with bureaucratic or political insiders, clearly feel that they can now get away with fraud on a very large scale. This could be because the chances of another political party coming to power and trying to trace the money are now much lower, and this had been an important factor constraining large-scale corruption in the past.

Bangladesh is at a critical point in its governance and developmental evolution. It faces significant challenges in diversifying its economy and maintaining its growth rate in a context of a global slowdown and its own growing population. A broad-based productive economy, that could have supported systemic anti-corruption and improvements in other governance indicators, with an effective demand for the enforcement of a rule of law that it could pay for through taxes, has not yet developed. Powerful organisations are therefore still largely outside the productive sector, and they do not have a significant interest in the enforcement of a rule of law. Anti-corruption efforts that are based on vertical enforcement are therefore weak, despite a robust civil society and a relatively active media. Moreover, international pressure against systemic corruption is strongly resisted by ruling parties, as political corruption is an important part of the process through which they stay in power. This is common to all developing countries with systemic political corruption, but the resistance to investigation is greater in the context of political governments that have a legitimacy deficit and feel vulnerable. In this context, supporting the diversification of the economy and sustaining inclusive growth requires a more nuanced approach to anti-corruption. We should seek sectoral opportunities for feasible governance improvements that can reduce corruption in the form of unproductive rent and resource capture, without immediately taking on the most sensitive types of political corruption.

5. Strategic opportunities for anti-corruption in Bangladesh

The political settlements analysis in Section 3 suggests that not only is systemic anti-corruption unlikely to deliver significant results in Bangladesh, the strident reaction of a vulnerable government to charges of corruption can result in significant setbacks for development partners who try to address corruption through vertical enforcement, investigation and prosecution. This is not to say that development partners like the World Bank should ignore the possibility of corruption in major projects. For instance, it may have been necessary to quietly withdraw from the Padma Bridge project, if there was a doubt about a conspiracy that could not be adequately investigated. But we should not have a high expectation that demands for a thorough and impartial investigation in these areas will actually be carried out. Our political settlements analysis suggests that implementable anti-corruption activities should have a low profile, and be based on an outcome-oriented and incremental set of policy proposals. The emphasis should not exclusively be on prosecution and punishment, but rather on finding policy combinations that create incentives for stakeholders in particular sectors or activities to behave in more productive ways. If horizontal support for anti-corruption cannot be found at a systemic level for a general rule of law, we should look for horizontal support for very specific anti-corruption efforts that align development outcomes with the interests of powerful sectoral stakeholders.

Our alternative approach to anti-corruption looks for feasible and high-impact anti-corruption opportunities in areas where changes in policies and interventions may be potentially supported by some powerful players, who see the enforcement of specific policies as being in their own interest. Clearly these opportunities have to be carefully sought out. We make a distinction between different types of corruption and we focus on the types that are most likely to be relevant for our approach.

Some corruption is driven by red tape and bureaucratic delays. We call these types of corruption **market restriction-driven corruption**. The causes of this type of corruption are often quite feasible to address through the simplification of procedures. For instance, the World Bank is already doing good work in Bangladesh and elsewhere on this front, through its Doing Business surveys and reforms linked to that. However, reducing this type of corruption often does not have a huge impact on development outcomes. A more serious type of corruption is when corruption distorts the implementation of important state policies, for instance through the capture of resources in health, education, the financing of skills and technology acquisition and so on. We call this **policy-distorting corruption,** and we argue that if some of this can be feasibly addressed, the impact on development can be significant. Not only do these types of corruption have a high impact on outcomes, the presence of potentially productive players in these activities create opportunities for the type of anti-corruption strategies that ACE investigates. Another important type of corruption in developing countries involves patronage and rent distribution by political parties and we call this **political corruption**. Political corruption can often interface with policy-distorting corruption if politicians capture policy resources and allocate these to

clients. This can make policy-distorting corruption difficult to address, but the problem is not equally severe in every sector or activity. This is why addressing corruption in areas like the Padma bridge procurements is so difficult: policy-distorting corruption may be too sensitive to address when senior ministers are involved. Political corruption is much more difficult to address, and attempting to tackle this brings anti-corruption into conflict with political leaderships. This is one reason why systemic anti-corruption strategies typically fail. Finally, there is **predatory corruption**, and this happens when individual politicians or bureaucrats steal public resources for themselves, or extort from others. This too is often difficult to address because when it happens on any significant scale, it is an indication that the state has lost control over itself (Khan et al. 2017). If predatory corruption has become significant, it can only be addressed with very significant changes in the organisation of the political settlement and the institutions of the state. In our assessment, while there is a danger that Bangladesh may be moving in that direction, predatory corruption is still not the primary type of corruption that the country faces.

Combining our analysis in Section 2 of the drivers of growth in Bangladesh (and therefore the policy priorities for sustaining inclusive growth) with our analysis in Section 3 of the political settlement and its evolution, we outline the types of sectoral anti-corruption opportunities that are important to explore as part of our portfolio of incremental anti-corruption strategies. Inclusive growth in Bangladesh requires policies supporting *manufacturing employment growth,* as well as supportive productive strategies in agriculture and services. This suggests a number of areas of anti-corruption that may be both feasible and have high impact, our two conditions for identifying effective anti-corruption strategies (Khan et al. 2017). In productive sectors, we look for policy-distorting corruption where the corruption is not closely connected with high-level political interests and regime strategies for staying in power. In these areas, there may be productive interests who may be induced to support more productive strategies in their own interest, with judicious changes in policies, incentives or the organisation of appropriate collective action.

In our scoping studies we looked for such opportunities, keeping our analyses of economic challenges and political settlements in mind. In consultation with DFID, other development partners, our country research partners, and using our own knowledge of the country and of past research, we have identified a series of evidence-based research projects that will aim to identify feasible and high-impact anti-corruption opportunities. We have taken care to include projects in a number of significant sectors of development activity: public goods and infrastructure, productive sectors and skills, health and health delivery and governance agencies and media. The opportunities in each of these categories were not identical in our three study countries (Bangladesh, Nigeria and Tanzania). Here we report the types of sectoral anti-corruption opportunities that we want to study in the case of Bangladesh, as well as the cross-country studies. Each of our projects is expected to generate evidence about feasible anti-corruption strategies that are likely to fall into one of four types of anti-corruption strategies. These strategies and the projects which we believe will generate evidence of feasible anti-corruption under each, are summarized in Figure 8 and explained in more detail in Khan et al. (2017). Figure 8 also lists more than ten sectoral projects that we have planned for Bangladesh over the life of the ACE programme.

Figure 8: Sectoral anti-corruption research projects in Bangladesh

ACE Sectors / ACE Strategies	Public goods & infrastructures	Productive sectors & skills	Health & health care delivery	Governance agencies	Media
1. Aligning incentives	**Power** (BNT)	**Business Groups** (BNT) **Skills** (BNT) **Fishery Co-operatives** (B)	**Health providers** (BNT)		
2. Designing for differences		**Regulation in Garments** (B) **Secondary Education** (BNT)			
3. Building coalitions	**Climate Change** (B)		**Health Social Accountability** (BNT)	**National Board of Revenue (NBR) and Electronics Industry** (B)	**Media** (BNT)
4. Resolving rights	**Land** (BNT)				

Notes:

1. Aligning incentives
Here, the focus of the anti-corruption strategy is to change the relative returns to activities in different parts of a connected production process or value chain, to create support for specific anti-corruption initiatives.

2. Designing for differences
Here the focus of the anti-corruption strategy is to address differences in the interests and capabilities of different types of organisations to enable the potentially compliant to comply, and selecting appropriate strategies for dealing with others.

3. Building coalitions
The primary focus of these strategies is to organise groups to engage in effective collective action to support the enforcement of particular aspects of an anti-corruption strategy.

4. Resolving rights
Some corruption problems emerge because there are overlapping or contested rights and the only resolution available to the contesting parties may be to engage in corruption as a way of resolving disputes.

See Khan et al. (2017) for more details on each of these strategies.

(B): projects that only cover Bangladesh, (BNT): cross-country projects that cover Bangladesh, Nigeria and Tanzania.

Source: Author

Under public goods and infrastructure we have identified three areas for evidence-based investigation of anti-corruption opportunities. The power generation sector is crucially important for inclusive growth. This sector involves very large rents with significant policy-distorting corruption. As we described earlier, generation capacity has increased significantly since 2009, but many of the new generation companies are high cost peaking power plants that were not designed to support base load. However, there are now vested interests that seek to sustain and expand what was initially an emergency measure. The companies at play are also typically politically connected. It may therefore appear to be an area where effective and incremental anti-corruption may by unlikely given the significant political involvement. This assessment is not wrong, but it is also a sector where there is considerable

opportunity for making money in productive ways. Our scoping analysis suggests that with a feasible change in financing instruments (hence re-aligning incentives), some productive players may begin to support better enforcement of procurement and other rules that reduce unproductive rent capture. Anti-corruption strategies are not always guaranteed to work, but if our research suggests that this is a plausible outcome, it would provide evidence for development partners and industry insiders to lobby for changes in the requisite policy combinations.

Corruption in climate change investments has been very significant in Bangladesh and has resulted in a virtual termination of support for this sector by development partners. Our project looks at the evidence supporting smaller, localised projects, aligned with the interests of local stakeholders as a corruption-reducing strategy. In the public goods category, we also look at the registration of land rights. Here our scoping study suggested that digitisation and transparency may indeed help to reduce some types of corruption, but do not address a very important source of corruption: the problem of conflicts between competing land-right documents where each may be partially legitimate. Here our anti-corruption research explores the significance of this driver of corruption, and the evidence supporting the possibility of conflict-resolution strategies as a way of mitigating this type of corruption.

We have a number of important projects under productive sectors and skills. The study on business groups is a historical political economy study that compares the rise of big business houses across our three countries. Companies like Beximco or Summit in Bangladesh, or Bakhresa in Tanzania, or Dangote in Nigeria have grown through a combination of political connections and their own capability development and enterprise. They differ amongst themselves in their capabilities and efficiency. Moreover, there are many other politically connected companies that are considerably less productive. The question for this research will be to explore the conditions under which business-government relationships have had positive or negative effects on the development of enterprise and productivity in our three countries. This evidence will be important for designing sectoral anti-corruption strategies involving businesses as partners.

The skills programme is also comparative across our three countries and addresses a critically important sector. Huge budgets are allocated to skills development in these countries but much of it is wasted. Unskilled trainers are often appointed and collusion or design failures result in large numbers of trainees not being employable. We will work with our consortium partner Palladium, who run the (DFID-supported) Sudokkho programme in Bangladesh, and other successful skills providers like UCEP, to see how mismatches between trainees and employers, and particularly poor capabilities of employers, can create incentives for damaging types of corruption in training programmes. The hypothesis is that if employers do not have the capabilities to achieve higher productivity and profits once they get more skilled workers, they are unwilling to pay for the training either directly or in higher wages. This creates incentives for training providers to provide poor training and to engage in corruption to get outcome-linked payments released. To enable skills providers to meet their performance targets without corruption, policy may have to combine skills training for workers with capability development investments for employers. Our project on secondary

education will begin at a later stage in the life of the ACE programme, and will look at some of the causes of the massive resource leakages that result in very poor outcomes in secondary education in Bangladesh.

Our garments sector research will look at regulatory failures that lead to catastrophes like the Rana Plaza collapse. Here too, the evidence of Accord and Alliance show that policy changes can result in support for compliance from industry. Our research will look at the evidence of how differences in the capabilities and capitalisation of firms can result in different compliance strategies. Effective policy combinations for improving regulatory compliance have to address the distinct problems of different types of firms.

The fishing cooperatives research will look at why cooperatives of poor fishermen suffer from high levels of corruption, and achieve low increases in yields, compared to informal cooperatives of small landholders like the Daudkandi model innovated by the NGO Shisuk. We believe the evidence will show that the legal framework does not adequately recognise the capabilities of different types of fishing collectives, and corruption can be significantly reduced and yields enhanced with changes in the law on cooperatives. Given the low productive and entrepreneurial capabilities of poor fishermen, the design of collective organisations that does not create opportunities for capability development and enterprise, actually creates incentives for unproductive rent capture. The relative success of the Daudkandi (Shisuk) model is that its design allowed the rapid growth of entrepreneurial capabilities and investments, in contrast to the standard cooperative model. However, Bangladesh's current law does not support the organisation of collective farming using this type of enterprise model, as existing company law and cooperative law do not address the problems of capabilities and investments adequately.

Our project on how smuggling affects the prospects of the domestic electronics industry is a way of looking at the operations of the National Board of Revenue (NBR), which is known to often corruptly collude with taxpayers to collect lower taxes. In general, horizontal pressure on the NBR from powerful organizations to collect taxes is low given that these organizations do not yet benefit much from limited government expenditures on public goods. However, there are some areas like electronics smuggling where powerful domestic interests are hurt by the failure to collect duties. Evidence of the costs of this smuggling, and the sources of leakages, can provide ammunition to the electronics industry to organise its collective action to build coalitions and to put pressure on the NBR to properly collect customs duties on electronics imports. This can help to improve the enforcement of duty collection for electronics products as well as supporting the growth of the domestic electronics industry. Incremental improvements in tax collection aligned with domestic productive interests may provide a more sustainable strategy of improving the overall performance of governance agencies like the NBR.

Under health we have a number of projects on different aspects of health provision, pharmaceutical production and regulation and the procurement of medicines by health providers. In all these projects we will be looking for possibilities of improving outcomes by exploring and helping to justify the creation of incentives for some health sector providers or stakeholders to behave differently, in more productive ways.

Finally, we have a cross-country project on the media where we look at evidence of how the media reports corruption, the impact of this reporting and how the media could be incentivised to think about and report on incremental anti-corruption strategies, in ways that may help feasible policy implementation.

In all these projects, the ACE approach to evidence and analysis is to find possibilities of creating coalitions of interests at the sectoral level that have an interest in changing their behaviour in productive ways, with some interdependent policy and governance interventions. An anti-corruption coalition is most likely to be effective in contexts like Bangladesh if it does not seriously challenge the political settlement and, in particular, the core regime-survival interests of the ruling coalition. In the research questions we have chosen this condition is met, though in some cases unproductive interests in a sector may turn out to be closely connected with powerful political players. In some of these cases, feasible incremental changes may not be possible, and the task of the research is also to evaluate these risks before time and resources are wasted on policy formulation. Nevertheless, we believe that by selecting our research projects on an understanding of the political settlement and using a framework for identifying feasible anti-corruption strategies, we have maximised our chances of finding a number of feasible and high-impact anti-corruption opportunities in our countries. We have also deliberately focused on sectors in each country where the multiplier effects of better development outcomes are highest, in terms of supporting proven trajectories of inclusive growth and contributing to broad-based development. This is the best strategy for supporting progressively more ambitious anti-corruption strategies that should eventually lead to the possibility of implementing a society-wide vertical enforcement of a general rule of law.

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