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Evolution of Service Sector in Bangladesh: An Overview

Introduction

The service sector constitutes a significant share of gross domestic product (GDP) in most of the developing countries in South Asia, Africa and the Caribbean region since these countries have an important stake in the Doha Round of negotiation on services liberalisation. Among the many issues being negotiated “Domestic Regulation” has become very important for developing and least developed countries (LDCs) while undertaking liberalisation of their service sectors. The Doha Round points out national policy objectives to be a valid concern as long as these are not used to restrict trade. It strives to facilitate trade in services and yet focuses on achieving a level playing field between domestic and foreign service providers.

However, the stress is on regulatory measures which can be applied to limit anti-competitive practices that may arise from market dominance by a few firms (domestic as well as foreign). Moreover, regulation can enhance consumer welfare by ensuring quality and appropriateness of services in the midst of a wide range of providers under progressive liberalisation on services.

Importance of Service Sector

In the era of global economic integration, competitiveness plays a vital role in the success of international trade. In addition, the competitive environment of domestic markets facilitates higher economic growth and can help in reducing poverty. Competition in the services sector can therefore play a fundamental role in ensuring the competitiveness of an economy. Services are used intensively in the production of all goods, making up around 10-20 percent of production costs in both manufacturing and agriculture, and sometimes more (Sauvé, 2006)¹. Over the years, it has increasingly played an important role in economic activity and displayed more dynamism *vis-à-vis* other sectors. This has led to most countries seeking export markets for services.

Expansion of services offers room for increased foreign exchange earnings through exports and foreign direct investment (FDI) resulting from improved capacity and efficiency of the sector. Depending upon the pattern of growth, it further contributes towards national development by enhancing efficiency in sectors which are key sources of

national output and employment required to battle against poverty and illiteracy.

Service Sector and GDP

Over the past three decades, Bangladesh has evolved from a controlled economy to a market oriented economy through a wide range of policy reforms which include reforms in trade policy, industrial policy, monetary and fiscal policy, exchange rate policy, and promotion of foreign direct investment. Trade liberalisation has been one of the major policy reforms in Bangladesh. During the course of the overall trade liberalisation programme, the liberalisation of service sectors (especially telecom and financial sectors) also received much importance. Service sectors are increasingly becoming the core of Bangladesh economy. In the context of South Asia where growth rates in services sector has been fluctuating during the last two and a half decade, India and Bangladesh have been the exceptions with consistent growth.

For instance, the annual average growth in services has increased from 3.71 percent in 1981-90 to 4.48 percent in 1991-00 to 5.67 percent during 2001-05 for Bangladesh. The significant change in Bangladesh’s approach towards trade and investment liberalisation in services may be attributed partly to the growing importance of the services sector in the economy and its trade and investment flows in recent years.

Economic development inevitably triggers a structural change in the composition of output in favour of services. One of the striking features of the Bangladesh’s growth performance during the last decade has been the strength of the services sector. During this period, Bangladesh economy has been experiencing a significant structural change the role of agriculture has been declining and those of industry and services have been growing inconsistently.

Between 1980-81 and 2006-07, agriculture’s contribution to GDP declined from 33 percent to 21 percent, while that of industry increased from 17.3 percent to 29.8 percent. During the same

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Table 1: Share of Service Sector to GDP and Its Dynamics (at 1995-96 constant prices)

Contribution (% share in GDP)								
Sectors	1980-81	1985-86	1990-91	1995-96	2000-01	2004-05	2005-06	2006-07
Agriculture	33.07	31.15	29.23	25.68	25.03	22.27	21.84	21.11
Industry	17.31	19.13	21.04	24.87	26.20	28.31	29.03	29.77
Service	49.62	49.73	49.73	49.45	48.77	49.42	49.13	49.12
Total	100.00	100.00	100.00	100.00	100.00	100.00	100.00	100.00
Annual Average Growth Rate (%)								
Agriculture	3.31	3.31	2.23	3.10	3.14	2.21	4.94	3.18
Industry	5.13	6.72	4.57	6.98	7.45	8.28	9.74	9.51
Service	3.55	4.10	3.28	3.96	5.53	6.36	6.40	6.74
GDP Growth	3.74	3.34	3.24	4.47	5.41	5.93	6.63	6.51

Data Source: Bangladesh Economic Review (2007)

period, the services sector contributed around 50 percent of Bangladesh's GDP (see Table 1). This highlights the role of service sector as the driver behind accelerated growth.

Table 1 also indicates that since 2004-05, the overall GDP of the economy has been increasing at a rate over 6 percent, which has been facilitated by high growth in industry and services sectors. During 2001-05, services sector in Bangladesh grew, on average, at a rate of 5.67 percent per annum as against of 5.5 percent growth in overall GDP.

The rates of growth in some services sub-sectors have been higher than the growth in overall GDP growth rate in 2006-07. In terms of the share in GDP the major sub-sectors in services sector are 'wholesale and retail trade', 'transport, storage and communication', 'real estate, renting and business activity' and 'community, social and personal works', and their respective contributions to GDP in 2006-07 are 14.17 percent, 10.21 percent, 7.65 percent and 7.09 percent.

Among these services sub-sectors, 'whole sale and retail trade', and 'transport, storage and communications' grew at rates faster than that of the overall services sector, as in 2006-07, these two sub-sectors grew by 7.44 and 8.25 percent respectively while the services sector as a whole grew by 6.74 percent.

Another sub-sector where a high growth has been witnessed is the 'transport, storage and communication' sub-sector from where a major contribution to GDP comes and which shows linkages with production and external sectors. The transport head covers roads, railways, air transport, port and shipping services; but high growth in this sector is mainly because of strong growth posted by communications that comprises telecommunication, IT and postal services. Robust growth momentums in the communication sector as well as in the financial services have been triggered by liberalisation and reforms in these sectors.

For example, deregulation policy for the telecommunication sector and market driven reforms have created a huge demand for new products which have been instrumental in attracting new foreign investment in this sub-sector. With the entry of five foreign cellular operators namely, Telenor, Orascom, TM International, SingTel and Warid Telecom, competition in the cellular phone market has become tougher leading to improvement in service quality and further reduction in tariffs to the advantage of consumers. Inception of the state-owned cellular phone company, namely Teletalk, has further augmented this competitive environment. Finally, despite low contribution to GDP, 'education' and 'community, social and personal services' are also having high sectoral growth rates.

Box 1: Share of Service Sector in Employment

Service sector employment has also shown a rising tendency but its contribution to total employment is much lower than its contribution to country's GDP. Table 2 shows the sectoral composition of employment over the two decades. There was a sharp rise in employment share of the agricultural sector in the eighties from 58.8 percent in 1982-83 to 66.4 percent in 1989-90. Since then Bangladesh economy has been witnessing a declining trend in the employment share of agriculture. The share of agriculture in total employment reached to 51.7 percent in 2002-03, which signifies the increase of non-farm activities during that period. On the other hand, the share of the manufacturing sector in total employment increased from 11 percent in 1982-83 to 13 percent in 1989-90, however declined to 9.6 percent in 1995-96, which again rose to 13.7 percent in 2002-03. The employment share of the service sector has been somewhat unstable during the last two decades. It declined from 24.2 percent in 1982-83 to 16.2 percent in 1989-90. During the late 1990s and early 2000s, when liberalisation of some services sectors, like telecommunication and financial intermediaries, was one of the major policy reforms, the employment share of service sector grew substantially, which reached to 34.6 percent.

Table 2: Sectoral Composition of Employment

Year	Sectoral composition of employed workforce (%)		
	Agriculture	Manufacturing	Service
1982-83	58.8	11	24.2
1984-85	57.7	11.5	26
1989-90	66.4	13	16.2
1995-96	63.2	9.6	25
1999-00	62.1	10.3	23.5
2002-03	51.7	13.7	34.6

Source: WDI (2007)

Impact of Liberalisation

Different country experiences suggest that trade liberalisation alone cannot act for growth and development. Especially for the LDCs, lack of trade related infrastructure facilities and deficiency of knowledge on sectoral potentiality deprive them from gaining through greater openness. Following are some of the issues need to be taken into account:

- The problem of lack of infrastructure facilities is acute for Bangladesh, which involves poor transportation, port and customs, and storage facilities, along with power supply and communication system. The marketing and distribution facilities are far from satisfactory. Moreover, Bangladesh experienced problems of implementing WTO commitments, partly due to lack of know-how and institutional capacity. ‘WTO Cell’ under the Ministry of Commerce and ‘Bangladesh Foreign Trade Institute’ have been formed to improve the institutional and human capacity in trade negotiations. Despite these efforts, Bangladesh still lacks the capacity to manage the whole negotiation process.
- The complications relating to service trade negotiations call for policy makers to be able to assess the potential implications arising out of certain provisions. Furthermore taking effective participation in services trade may require enacting the necessary domestic regulations. For effective utilisation of all these requires technical assistance.
- Aid for Trade can be an effective instrument to provide technical assistance to Bangladesh in this regard to build the supply capacity for services sectors, to strengthen domestic services capacity, efficiency and competitiveness, to build institutional and human capacity, and to put up requisite infrastructure and new technologies. Technical assistance through the Integrated Framework could be provided to Bangladesh in this regard and it will help improve the institutional capacity of the country to participate actively in GATS negotiations, and will help implement commitments to

GATS. Moreover, technical assistance will be needed to assist in the undertaking of appropriate regulatory reforms and translating the services regulatory framework into GATS language.

- The Hong Kong Declaration emphasised on assisting LDCs to enable them to identify sectors and modes of supply that represent development priorities. However, there is no such initiative from the developed country members to consider the special priority sectors and LDC modes of supply. There also lacks LDC initiatives to prepare a negotiable ground for this. Bangladesh should identify the areas where technical assistance is required.

Service sector has the growing potential to be a driver of sustainable economic growth and significant poverty alleviation in Bangladesh. The growing trade in services has important implication for the productivity enhancement and economic growth. Services sector in Bangladesh is the largest sector, and it is the area where local firms have larger participation and are better able to compete, as compared with the manufacturing sector. Demand for many services is highly income-elastic, i.e. as people grow richer, their consumption of services such as tourism, education and health, expands more rapidly than their demand for manufactures and agricultural products.

As a result, the issue about trade liberalisation in services raises an important concern to the government as to what extent service trade liberalisation will be beneficial to achieve the national objectives such as economic growth, poverty alleviation, and inequality reduction.

GATS explicitly recognises the right of the members to regulate and initiate new regulation on the supply of services within their territories in order to meet national policy objectives. Bangladesh has liberalised important services sub-sectors unilaterally rather not using the right to liberalise under request-offer process of the GATS negotiations. Unilateral service trade liberalisation has been the hallmark of Bangladesh trade policy reforms. However, there are concerns among, negotiators, policy makers, and civil society that unilateral service trade liberalisation may not ensure persistent economic growth and poverty alleviation. Unilateral service trade liberalisation is one of the issues that have given rise to greater concern alike. Moreover, as service sector is the major stakeholder in our economy, decision about service trade liberalisation has greater implication for the economy.

The implication of service trade liberalisation to Bangladesh economy is still least explored. One of the few such studies by Raihan (2005) outlined negotiation strategies for Bangladesh in service trade liberalisation. The study identified the sectors with balance of payments surplus such as computer related services, telecommunication services and distribution services, as having export

interests, while the sectors with balance of payments deficit such as leasing services, transport services and construction services, as having import interests.

According to optimistic scenario of the study, liberalisation will bring efficiency, predictable environment for investment, and will create new opportunities for exporting services. And, according to pessimistic view of the study, liberalisation of all services sectors might jeopardise the macroeconomic stability of the economy through affecting the SMEs in transport sectors, construction sectors and distribution services.

A recent study done by Bhuyan *et al* (2007) reviewed the development of the services sector in Bangladesh focusing on the barriers, regulations and difficulties faced by the country. The study also assessed the potentials of the sectoral liberalisation and the associated position of the country's services sector *vis-à-vis* the rest of the south Asian countries. The study recommended cautious liberalisation for telecommunication sector, banking sector, retailing services, tourism services and health services. However, the study suggested protecting the insurance and transporting services.

Regulatory Framework²

In Bangladesh, the level of market concentration in the services and utility sector tends to be significantly higher than that of the manufacturing sector. These enterprises are often granted monopoly rights that they sometimes auction off to private concessionaires through long term revenue-sharing concessions.

Consequently, the market structure of most service industries can be described as monopolistic or oligopolystic. Grameen Phone, a telecommunication service provider, had an estimated market share of 63 percent at the year-end of 2006. Grameen Phone was the most profitable part of Telenor's global mobile network in the final quarter of 2006 that the Norwegian company reported, with subscribers in Bangladesh almost doubling during the year.

Communication: There is no specific rule for postal services under Modes 1, 2, and 4. In the case of postal service, the Government has the exclusive privilege of conveying by post, from one place to another, all letters. Therefore, under the existing law postal services under Mode 3 are not allowed.

Telecom: There is no explicit rule under Modes 1 and 2. Under Mode 3, any foreign company may seek to get license from BTRC to operate in the country. This is subject to meeting the terms and conditions set by BTRC. Though, there is no specific law about Mode 4, a foreign person may be allowed to provide services if s/he gets the work permit from the Board of Investment.

Transport: There is no regulatory barrier to trade under Mode 1 and anyone can avail transport service under Mode 2 subject to the compliance with the relevant rule of the respective department. A foreigner with valid passport and visa after obtaining work permit from the Board of Investment may engage trade under Mode 4 in compliance with all requirements applicable for a citizen of Bangladesh.

Banking: There is no specific law under Modes 1 and 2. Under Mode 3, any company, registered with the Register of Joint Stock Companies (RJSC), under the Companies Act, 1994, incorporated in Bangladesh or incorporated outside Bangladesh, can achieve the right to operate banking services in Bangladesh by obtaining license from Bangladesh Bank under Banking Companies Act, 1991, and by satisfying the following conditions as per the Bangladesh Bank guide lines.

Insurance: There is no specific regulation about the market access under modes 1 and 2. However, a Bangladeshi can buy the insurance services from the foreign providers when he is travelling or working abroad holding valid visa. There is no impediment to start insurance business obtaining licence from CCI and getting registration from RJSC under the mode 3. Any foreign citizen can involve in insurance services in Bangladesh under Mode 4 by getting a valid visa, and also a work permit from the Board of Investment.

Health: There is no specific rule regarding the Mode 1. In case of Mode 2, a valid visa holder can avail services from any hospitals or clinic paying specific services. Under Mode 3, a company, incorporated outside Bangladesh, may operate health services in Bangladesh subject to having a valid license from the Directorate General of Health Services under the Medical Practice and Private Clinics and Laboratories (Regulation) Ordinance, 1982. There is no specific rule regarding Mode 4. A foreign health professional needs permission from the Ministry of Health through Bangladesh Medical and Dental Council (BMDC). As per the BMDC rules, a foreign practitioner is given temporary permission up to 6 months to practice in Bangladesh.

Tourism: In Bangladesh's schedule of specific commitments, there are market access limitations under modes 1 and 2. But in the existing legislation, there are no specific rules and regulations under modes 1 and 2. However, any persons from a country which has diplomatic relation with Bangladesh may avail tourism services in Bangladesh as per the Visa Rules 2006. There is no specific legislation under Mode 3 for this sector. Existing legislation does not provide any rule governing Mode 4.

Box 2: Technical Assistance Required

Trade facilitation in the services sector requires technical assistance of different types at various levels. Technical assistance is needed for improving institutional and human capacities that can manage the negotiating process at different levels:

- developing infrastructure facilities which include transportation, port and customs and storage facilities along with power supply and communication systems;
- evolving marketing and distribution facilities that are presently far from pleasing;
- broadening the scope of Aid for Trade that can provide technical assistance while undertaking regulatory reforms and translating the services regulatory framework into GATS language; and
- enabling identification of sectors and modes of supply that represent development priorities.

Conclusions

Different country experiences suggest that trade liberalisation alone cannot result in growth and development. This is true especially in the case of LDCs where infrastructure facilities are not suitable and knowledge deficiencies regarding sectoral potentiality further deprive them of the gains through trade openness.

On the whole there are several issues concerning trade liberalisation and domestic regulation in the services sector which require immediate attention. Some of these are as follows:

- Although Bangladesh has made some significant gains from trade liberalisation, a rather slow and cautious approach is preferred by many stakeholders.

- There is a need to strengthen the capacity for domestic regulation, the underlying rules to strengthen the process of trade liberalisation in a number of services sectors.
- There is a need to actively involve all stakeholders (civil societies, private sector, etc.) at every stage of the decision making process from assessment studies to formulation to actual policy formulation. This could help build domestic support for trade liberalisation of domestic regulation.

Endnotes

- 1 The figure is 20-25 percent for ready-made garments in some countries (United Nations, 2005).
- 2 **Mode 1: Cross-border supply** covers services flows from the territory of one Member into the territory of another Member (e.g. banking or architectural services transmitted via telecommunications or mail).
Mode 2: Consumption abroad refers to situations where a service consumer (e.g. tourist or patient) moves into another Member's territory to obtain a service.
Mode 3: Commercial presence implies that a service supplier of one Member establishes a territorial presence, including through ownership or lease of premises, in another Member's territory to provide a service (e.g. domestic subsidiaries of foreign insurance companies or hotel chains).
Mode 4: Presence of natural persons consists of persons of one Member entering the territory of another Member to supply a service (e.g. accountants, doctors or teachers). The Annex on Movement of Natural Persons specifies, however, that Members remain free to operate measures regarding citizenship, residence or access to the employment market on a permanent basis.

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