



**Pozières
Consulting**

CASE STUDY



Bangladesh's RMGC Sector



Pozières Consulting Inc.

www.pozieresconsulting.com

info@pozieresconsulting.com



CASE STUDY: BANGLADESH'S RMG SECTOR

Brief:

Our client was a large European clothing importer/retailer who imported a large amount of Ready Made Garments (RMG) from Bangladesh. Having expanded in recent years, the company was involved in both the import/distribution and the high street retailing of their RMG's. Our client enjoyed a successful relationship with a core group of Bangladeshi factories and had been approached by the largest of these with a joint venture proposal. The proposal would allow our client to invest in and own a stake in the manufacturing process. On paper the financials looked promising but our client was aware that this was only half of the picture. Pozières Consulting was engaged to undertake due diligence on the Bangladeshi partners, on the factory and to provide an assessment of the political and security landscape in the context of their potential investment.

Our Methodology:

We undertook a number of qualitative research methods over the course of three months to create a detailed picture of the industry as a whole, the localized area of the factory and the potential partners themselves. We were able to conduct a comprehensive due diligence process without the potential partner being aware of the fact as well as carry out significant checks on conditions within the factory and conditions for the factory's workers. We were able to gain access to the small trade union movement, the local factory owners' network and speak with numerous officials and elites at a local and national level. We were also able to gain a number of critical business intelligence insights from our in-country contacts.

Context:

Our research was conducted at the beginning of 2015 as a protester blockade of the country's transport system was underway to mark the anniversary of the disputed 2014 parliamentary election the year before. The blockade, which was accompanied by violent clashes with the police and the deaths of more than 120 protesters, was organized by the Bangladesh Nationalist Party (BNP), Bangladesh's second largest political party. The BNP refused to take part in the 2014 elections and were accusing the ruling Awami League of wanting to transform Bangladesh into a dictatorship. Violent clashes between



supporters of the two parties was escalating across Bangladesh and the blockade threatened the stability of the country and of its' exports trade.

The continued polarisation between the governing and opposition parties became a key political risk for Bangladesh's economic outlook despite the year on year GDP growth exceeding 6%. Investor confidence in Bangladesh as a key production hub was also at risk and with the RMG sector making up 81% of Bangladesh's exports, any shift in this status as a garment hub would have huge and immediate ramifications for the country's economy.

Enormous systemic and structural weaknesses within Bangladesh's political institutions exacerbate any short term political instability and served to increase the political volatility at the time. An ineffective judiciary, a dictatorial executive and a culture of corruption that pervades every aspect of life in Bangladesh means that there are few institutional mechanisms to balance or rectify political instability. The pervasive nature of corruption and rent seeking also posed and would continue to pose a direct reputational and legal risk to international investors.

The lack of effective political institutions restricts the distribution of public goods and the ability to respond to disasters. Under these conditions Bangladesh has struggled to effectively address the serious problems of poverty in the country and would continue to struggle to deal with the huge risks associated with climate change for which Bangladesh is especially vulnerable.

Perhaps overshadowing even the recent political protests was the memory of the collapse of the Rana Plaza garment factory building in April 2013, which left over one thousand workers dead. The tragedy made headlines around the world and brought into focus the often perilous working conditions of garment workers in Bangladesh. Since the disaster the government had enacted laws to strengthen labour rights and safety standards however they have been poorly policed and rarely enforced. Corruption, threats from the exceptionally powerful textile lobby and a lack of resources for enforcement bodies has meant that little real progress had been made. Our own research indicated that union leaders often faced threats and intimidation, workers were often unaware of their rights, foreign companies were unaware of conditions and enforcement of standards were almost non-existent. As of 2015 there were just 18 qualified labour inspectors assigned to monitoring the nearly 5,000 garment factories in the Dhaka area alone.

Key Findings:

- The Bangladeshi partner was well funded and backed by a family with longstanding business relationships and links to the area;
- The Bangladeshi partner had strong links with a number of political elites but they were not overly exposed politically and posed little risks in the context of future regime changes;
- The Bangladeshi partner had a good reputation among business elites and foreign buyers;
- The factory was in fact a group of factories that were run in a centralized production line model but with a semi-autonomous management team for each individual factory;
- None of the factories met the minimum government standards nor did worker conditions.
- Investments had been made in computerized cutting machines but many other facilities were either run down or outdated;
- Dangerous chemicals which are banned but which are still commonplace in Bangladesh were still being used in the factories;
- There was sufficient room within the factories for expansion unlike in many similar factories;
- Union membership was banned and treatment of workers involved in organizing was harsh and swift. This poses a critical reputational and operational risk;
- Conditions for workers did not meet government standards we believe they fell well below the standards set out in the International Covenant on Civil and Political Rights (ICCPR), the International Covenant on Economic, Social, and Cultural Rights (ICESCR), and the Convention on the Rights of the Child (CRC) each of which Bangladesh is a signatory to;
- Government oversight was minimal and bribery almost certainly occurred at every level of the business; this is not pernicious rent seeking nor is it out of the ordinary however it poses several risks for international investors as business operators;
- There were few safety or business continuity procedures and nothing in place to deal with disasters relating to climate change or terrorism;
- There was a growing security concern in the areas around the factory linked to increasing Islamic extremism in the country;
- Infrastructure around the factory area was in exceptionally poor condition and there appeared little funding or government will power for improvements in the medium term;
- The area of the factory was exceptionally vulnerable to flooding, even in the context of the high country-wide flood risk rating;
- The community surrounding the factories were completely reliant on the RMG sector and any slowdown would have massive ramifications on the area and likely lead to



instability quickly; the poor relations between workers and management would likely exacerbate this instability.

Findings in Context:

- In the context of Bangladesh, the proposed partners are of a good standing and do not pose a large political exposure risk;
- While the regulation breaches within the factory are commonplace in Bangladesh, they pose a strong reputational risk for international investors especially if an accident were to occur. This reputational risk would obviously be much higher if the client was a business operator rather than just a buyer;
- The institutional corruption does not presently pose a significant risk to the client as a buyer but as an owner there would be direct risks and implications at a domestic level and in regard to EU and US anti-bribery legislation;
- The working conditions of workers mirror that of most factories in Bangladesh but would still pose a reputational risk as well as a potential source of future instability should be business or security environment change;
- Obtaining insurance and financing for the investment may be challenging given some of the above mentioned breaches;
- There is a medium term risk of increased terrorism interrupting business and therefore effective business continuity plans should be put in place for this;
- There is a high short, medium and long term risk of climate change related disasters affecting either the factory or the surrounding infrastructure which would suspend production and thus effective business continuity plans should be put in place for this;
- There is a medium term risk that even a slight slowdown in the RMG sector in Bangladesh will result in massive and widespread instability and even violence;
- Political instability at a national level will persist for many years to come and will continue to pose a significant risk on a number of levels including regulatory risk;
- Bangladesh is exceptionally prone to, and ill prepared to handle political and security shocks of which the risks are high.

While many of the risks associated with purchasing RMG's from Bangladesh can be minimised, taking ownership of, and making direct capital investments in an RMG manufacturer in Bangladesh makes this a much harder proposition. Risks such as workers' conditions, factory conditions, corruption, terrorism, and government interventions become direct business risks in the event that the client becomes an owner rather than a purchaser. From a political risk perspective, we would recommend



investigating potential direct investment in the Vietnamese RMG sector as an alternative or simply remaining a buyer.

Conclusion:

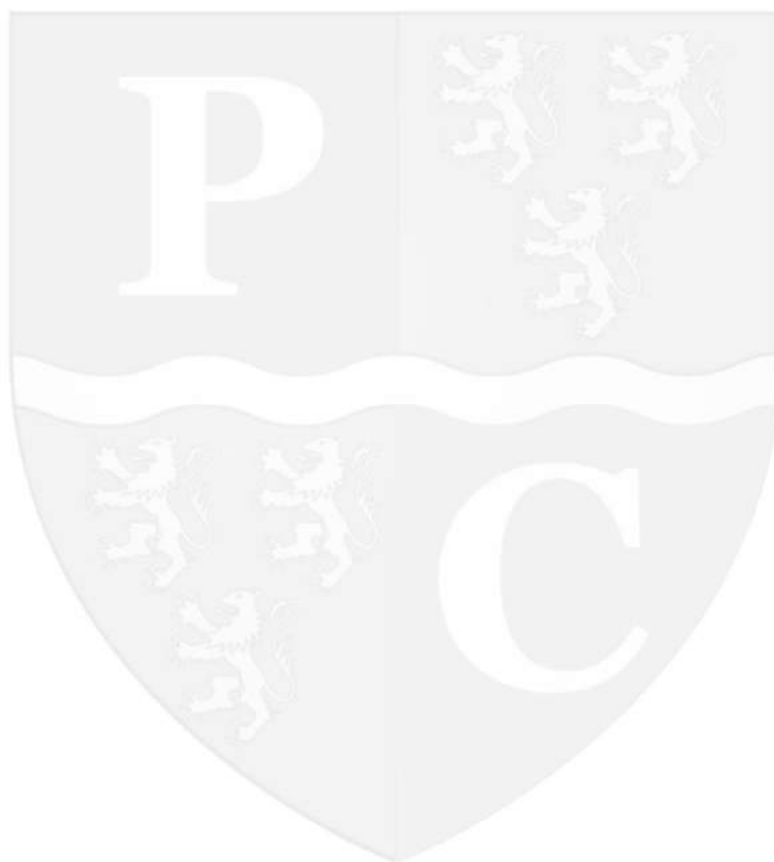
Often, even the most attractive financial proposal can have a number of hidden risks to consider. Our client had considered and measured the political and security risks associated with purchasing their RMG's from Bangladesh however moving from a purchaser to an owner/operator changes the nature of those risks hugely. Their Bangladeshi partner was not conducting business in a way that was any different to most of the factories in Bangladesh who provide RMG's most of the largest retailers in the world; their factory wasn't up to standard, but it wasn't inferior to the factory next door; the labour conditions mirrored most other Bangladeshi factories; the environmental impact of the factories was heavy, but no heavier than most; they were involved in corruption but in Bangladesh that's impossible to avoid; but ultimately context matters. Weak political institutions, the rising risk of climate change and terrorism, reputational risks and continued political instability in Bangladesh mean that the risks to on-going returns on large capital investment will be high for the foreseeable future.

Editor's Note:

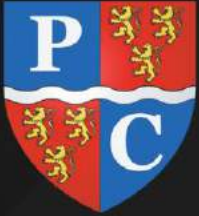
As a political risk consultancy it is our role to identify and contextualise political risks, translating them into effective business insights for our clients; we do not generally draw specific conclusions for our clients but arm them with insights that can be integrated into their wider decision making methodology. On this occasion however we were working with a longstanding client for whom we had a strong rapport and were feeding back information on an ad hoc basis rather than through a final report and thus we were able to provide stronger, more pointed recommendations than is often possible or appropriate.



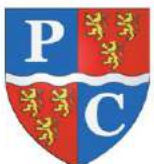
Pozières Consulting Inc is a Political Risk Advisory firm, providing bespoke analysis and business intelligence through our worldwide network of analysts and sources. We work with clients to identify, analyse and contextualise strategic Political Risks and turn them into tangible, actionable business insights. We utilise a combination of in-depth thematic research, innovative analytic tools and tailored business intelligence gathering to provide a bespoke service to clients. For comprehensive Political Risk advice and a confidential consultation, contact us at info@pozieresconsulting.com



Copyright © Pozières Consulting Inc 2015



Pozières Consulting



Pozières Consulting Inc.

www.pozieresconsulting.com

info@pozieresconsulting.com