BUSINESS REGULATION IN SOUTH ASIA and THE BELT AND ROAD INITIATIVE
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and THE BELT AND ROAD INITIATIVE
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### Acronyms and Abbreviations

<table>
<thead>
<tr>
<th>Acronym</th>
<th>Description</th>
</tr>
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<tbody>
<tr>
<td>ADB</td>
<td>Asian Development Bank</td>
</tr>
<tr>
<td>BOI</td>
<td>Board of Investment (Sri Lanka)</td>
</tr>
<tr>
<td>BPP</td>
<td>Benchmarking Public Procurement</td>
</tr>
<tr>
<td>BRI</td>
<td>Belt and Road Initiative</td>
</tr>
<tr>
<td>DB</td>
<td>Doing Business</td>
</tr>
<tr>
<td>DTF</td>
<td>Distance to Frontier</td>
</tr>
<tr>
<td>EPC</td>
<td>engineering, procurement, and construction</td>
</tr>
<tr>
<td>FDI</td>
<td>foreign direct investment</td>
</tr>
<tr>
<td>GCI</td>
<td>Global Competitiveness Index</td>
</tr>
<tr>
<td>GCR</td>
<td>Global Competitiveness Report</td>
</tr>
<tr>
<td>GDP</td>
<td>gross domestic product</td>
</tr>
<tr>
<td>GIRG</td>
<td>Global Indicators of Regulatory Governance</td>
</tr>
<tr>
<td>GPA</td>
<td>Agreement on Government Procurement (WTO)</td>
</tr>
<tr>
<td>GST</td>
<td>Goods and Services Tax</td>
</tr>
<tr>
<td>GVC</td>
<td>global value chain</td>
</tr>
<tr>
<td>ICT</td>
<td>information and communication technology</td>
</tr>
<tr>
<td>IIA</td>
<td>inward investment account</td>
</tr>
<tr>
<td>ITC</td>
<td>investment tax credit</td>
</tr>
<tr>
<td>LPI</td>
<td>Logistics Performance Index</td>
</tr>
<tr>
<td>MSME</td>
<td>micro, small, and medium enterprise</td>
</tr>
<tr>
<td>OSS</td>
<td>one-stop shop</td>
</tr>
<tr>
<td>PTA</td>
<td>preferential trade agreement</td>
</tr>
<tr>
<td>SAIDI</td>
<td>system average interruption duration index</td>
</tr>
<tr>
<td>SAIFI</td>
<td>system average interruption frequency index</td>
</tr>
<tr>
<td>SME</td>
<td>small and medium enterprise</td>
</tr>
<tr>
<td>WBES</td>
<td>World Bank Enterprise Surveys</td>
</tr>
<tr>
<td>WGI</td>
<td>World Governance Indicators</td>
</tr>
</tbody>
</table>
The Belt and Road Initiative (BRI), a large, multicountry initiative primarily concerned with infrastructure, was announced by the Chinese government in 2013 with the goal of connecting South-east Asia to Europe and the Middle East, with China as the fulcrum. The BRI now spans over 70 countries. It includes major infrastructure investment projects—roads, ports, and railways—aimed at improving connectivity along a number of transport corridors, as well as measures to promote trade and investment that will utilize this infrastructure.

A recent World Bank study has emphasized the need for BRI partner countries to undertake complementary reforms, including some pertaining to the business environment, to maximize gains from the initiative and to ensure that these gains are widely shared. Poor business and regulatory environments not only negatively impact business growth and development, they also result in missed opportunities for countries that could benefit from large multicountry initiatives like the Belt and Road.

According to a database maintained by the Centre for Strategic and International Studies, BRI projects appear to be underway in many South Asian countries: 101 in Pakistan, 31 in Bangladesh, 10 in Sri Lanka, 7 in Nepal, and one in Afghanistan. India opposes the BRI, but the marked involvement of other South Asian countries raises the question of whether business regulatory requirements in those countries hinder them from fully benefiting from BRI project spillovers.

World Bank Enterprise Survey data suggest that infrastructure (electricity/transport) is one of the biggest obstacles for South Asian firms. While the BRI aims to fill much of these countries’ infrastructure gaps, governments must simultaneously concentrate on regulatory and business environment issues to ensure that firms benefit from BRI-induced opportunities, including, among others, enhanced trade and investment, integration into value chains, job creation, skills development, government procurement, and public-private partnerships.

This study provides a comprehensive comparative analysis of the business environment in six South Asian countries—Afghanistan, Bangladesh, India, Nepal, Pakistan, and Sri Lanka—to examine whether business regulatory requirements in these countries hinder them from fully benefiting from BRI project spillovers. The analysis is based on available secondary data sources and responses to a structured questionnaire sent to selected private sector participants in each of these countries, eliciting information on the law, regulation, and practice in a wide range of thematic areas influencing the overall business and regulatory environment.

Survey respondents identified nine key themes as the most challenging for the private sector, including from the perspective of potential benefits from BRI-induced opportunities. The thematic areas are: (a) licensing/inspection requirements; (b) regulations and practices governing foreign investment; (c) access to resources such as land, credit, and electricity; (d) regulatory restrictions on the operation of foreign firms, such as local content requirements and currency repatriation; (e) regulatory governance and corruption/state capture; (f) predictability and quality of the regulatory framework, especially corporate taxation; (g) government procurement laws and practice; (h) effective dispute settlement/grievance mechanisms; and (i) trade and customs regulations. The identified thematic areas promote connectivity and regional integration and thus are particularly relevant from the BRI perspective. Improvements along different dimensions of these thematic areas would likely enable countries in the region to gain from BRI-induced opportunities.

1. While the World Bank Group considers Bhutan and Maldives to be part of the South Asia region, these countries are excluded from this analysis due to data collection constraints.
While the business regulatory environment in South Asia has improved over time and the six countries considered here have implemented nearly 68 reforms between 2016 and 2020, according to the World Bank’s Doing Business data, significant challenges remain. Some conditions continue to stifle the growth and development of private enterprise, preventing countries in the region from reaping the spillover benefits of large infrastructure projects like the BRI. In all the thematic areas covered in this study, systemic issues such as corruption, lack of transparency, and cumbersome, often discretionary bureaucratic procedures continue to affect firms throughout their full lifecycles.

Despite shortcomings, starting a business in South Asia is faster and cheaper than in the East Asia and Pacific region, according to the World Bank’s Doing Business database. Both similarities and differences in the ease of doing business appear across countries in South Asia when it comes to regulation and practices governing entry into markets. Licensing requirements are mostly sector specific, as are the mechanisms and criteria for allocation of licenses. The procedures for building projects in South Asia continue to be complicated and costly, however, involving licensing requirements from several different agencies that increase the opportunities for rent-seeking and corruption.

Access to resources—land, finance, and electricity—an important ingredient of the business climate, remains a challenge across the region. Access to land is particularly relevant for large-scale infrastructure projects and for those involving overland corridors such as the BRI. Land governance hampers the region’s competitiveness, however. In addition to poor-quality land administration, foreign land ownership is also restricted in places across South Asia. Similarly, access to finance is regarded as one of the biggest obstacles for the operation and growth of business in South Asian countries. Especially daunting are its negative effects on the productivity of smaller firms. Access to electricity also remains challenging in the South Asia region. While countries like India and Sri Lanka have shown progress in ensuring reliable supply and transparent tariffs, especially in their major cities, an inadequate electricity supply remains an issue in all countries covered, with considerable disparities in the rest of South Asia and even within these countries at the subnational level.

While the share of FDI in GDP is less than 2 percent, even in India and Sri Lanka, FDI policy is transparent and has been nondiscriminatory in most South Asian countries. India is a recent exception; there, rules governing FDI inflows from neighboring countries, especially China, were amended in April 2020 in the wake of the Covid-19 crisis. Even in sectors that do not restrict entry of foreign firms, however, FDI involves multiple administrative approvals from the domestic authorities concerned, and these, in some cases, use cumbersome procedures that impede foreign investors’ efforts.

Countries in the South Asian region place regulatory restrictions on the operation of foreign firms, including both local content requirements and restrictions on currency convertibility and repatriation. Local content requirements, either in law or in practice, are especially prevalent in public procurement. While hiring local labor and using local content is one way BRI-partner countries can ensure positive spillovers from this initiative, the quality of such domestic resources has a direct bearing on the viability and sustainability of such large infrastructure projects. Currency convertibility and repatriation are also highly regulated across countries in the region, although the nature and form of this regulation differs by country.

Different attributes of the World Bank’s World Governance Indicators for 2018 across countries in the region suggest that Sri Lanka and India are the best performers in South Asia, while Afghanistan is the worst regional performer. With the exception of Sri Lanka, corruption has been identified in various World Bank Enterprise Surveys as a major impediment to the operation and growth of businesses in South Asia, with Afghanistan and Bangladesh, in particular, being the worst performers in the region. Allegations of corruption in the award of BRI-contracts (see Ghossein et al. 2018) may be among the few negative spillovers of this initiative and suggest that countries in the region would do well to prevent vulnerability along this dimension.
Feedback received from survey respondents reveals that inefficiency and corruption in tax administration, both of which are likely to deter firms from participating in BRI projects, are another pervasive problem in the South Asian region. Close to 30 percent of firms in the World Bank Enterprise Surveys identify tax rates as a major constraint. Some countries, like India, have introduced a Goods and Services Tax (GST), replacing in July 2017 some 20 consumption taxes charged by the central government and states and doing away with the VAT. Others, like Sri Lanka, now have a system for national taxes to be paid online. Most of the region’s tax administration systems, however, remain inefficient and prone to bureaucratic discretion and corruption.

South Asian countries show considerable heterogeneity in performance on procurement practices and contracting with the government. While open tendering is the default method of procurement in these countries, they also resort to limited and selective tendering as well as direct procurement, depending on the value and type of good/service to be procured. Foreign participation in the procurement process is not prohibited, although de facto requirements may exist that local inputs and local labor be used, as well as a de jure preference for domestic suppliers, mostly taking the form of price preferences. Corruption has also been identified in various World Bank Enterprise Surveys as a major feature of the procurement process in countries across the region: 46.9 percent in Afghanistan, 48.9 percent in Bangladesh, 39.8 percent in India, 64.5 percent of firms in Nepal, 88.2 percent in Pakistan, and 29.8 percent in Sri Lanka are expected to pay bribes for securing government contracts.

Contract enforcement is poor across South Asian countries and among the slowest globally. Respondents point to lengthy and opaque dispute settlement practices across the countries covered in this study: it can take three to five years to resolve a commercial dispute. Feedback from respondents also noted that current grievance systems remain inadequate to address business needs.

Businesses in South Asian economies face a number of obstacles in exporting or importing goods and services, including tariffs, quotas, and a host of nontariff barriers that greatly increase costs or prevent trading altogether. According to World Bank Enterprise Surveys, 17 percent of South Asian firms consider trade regulations to be a major business constraint.

Feedback from respondents reveals that BRI firms in Nepal, Pakistan, and Sri Lanka may have received preferential treatment in meeting regulatory requirements. In Pakistan, these pertain to access to land, licensing and inspection, fiscal or nonfiscal incentives and state aid, currency repatriation, and public procurement. In Sri Lanka, BRI firms may have received preferential treatment in access to land, government procurement bidding, and FDI policy. In Nepal, preference seems to have been shown in the context of both taxation and trade.

Improving the business environment of South Asian countries will not only benefit these nations’ firms and boost their competitiveness, creating jobs and transforming economies, it will also enable the region to gainfully reap the benefits and spillovers from BRI projects and regional connectivity. A good strategy for improving competitiveness is to reduce transaction costs and strengthen institutions and property rights and to enable firms to compete domestically and globally by providing efficient infrastructure services, a smoother business environment, and more effective public services. Productivity growth can also be driven by moving resources from less productive to more productive firms within narrowly defined economic activities.
01. THE BELT AND ROAD INITIATIVE AND THE NEED FOR REGULATORY REFORM
The Belt and Road Initiative (BRI), a large, multicountry initiative primarily concerned with infrastructure, was announced by the Chinese government in 2013 with the goal of connecting South-east Asia to Europe and the Middle East, with China as the fulcrum. The BRI now spans over 70 countries and includes major infrastructure investment projects—roads, ports, railways—aiming to improve connectivity along a number of transport corridors, as well as measures to promote trade and investment that will utilize this infrastructure.

Regulatory factors not only determine firms' ability to integrate into regional and global value chains but also their ability to benefit from large multicountry regional connectivity projects like the BRI. A recent study by the World Bank suggests that, if fully implemented, BRI transport infrastructure can reduce travel times for economies along the affected transport corridors by up to 12 percent, reducing trade costs and increasing trade by an estimated 2.8 to 9.7 percent for corridor economies and 1.7 to 6.2 percent for the world. At the same time, the report emphasizes the need for BRI partner countries to undertake complementary reforms to maximize gains from the initiative and to ensure that these gains are widely shared.

Existing literature also shows the positive relationship between simpler business regulation and long-term economic growth. The significance of regulatory governance for economic development is also well-recognized in the private sector development literature. To maximize private sector development and job creation, policymakers must consider the factors in the regulatory environment that affect firms' full lifecycles, from entry to operation to international expansion and all the way to business exit.

Against this background, the present study provides a comprehensive, comparative analysis of the business environment in six South Asian countries—Afghanistan, Bangladesh, India, Nepal, Pakistan, Sri Lanka—to identify reform areas for firms to benefit from BRI-induced opportunities. The analysis draws on secondary sources.

2. The initiative prioritizes the Maritime Silk Road and six international “land corridors”: the new Eurasia land bridge; the China-Mongolia-Russia economic corridor; China-Central Asia-West Asia economic corridor; the China-Indochina Peninsula economic corridor; the China-Pakistan economic corridor; and the Bangladesh-China-India-Myanmar economic corridor. http://english.gov.cn/beltAndRoad/.
4. Using cross-country data, Djankov, McLiesh, and Ramalho (2006) find that simpler business regulations are associated with higher long-term growth. Eifert (2009) uses indicator-level data to show that better performance in business regulations indicators in general is linked to higher investment and growth. Divanbeigi and Ramalho (2015) show that, although small changes in the overall level of business regulations may have a negligible link to growth, moving from the lowest quartile of improvement in business regulations to the highest quartile is associated with a significant increase in annual per capita growth of around 0.8 percentage points. Their results also highlight the importance of sound entry and exit regulations and sound credit market regulations and court enforcement for growth.
5. A rapidly growing body of empirical and theoretical research shows that poor regulatory governance impedes economic development. Stern and Holder (1999) study twelve infrastructure industries in six developing Asian countries and find “structural liberalization” (i.e., opening of the industries to competition) to be an important catalyst for developing good practice regulation. Their findings show the “clarity of roles and objectives, autonomy, participation, accountability, transparency, decision-making and predictability of regulatory governance” (World Bank 2019b) to be significant determinants of industry performance, thereby also highlighting the importance of transparency for effective regulation. Similar conclusions have been reached by Andrés, Guasch, and Straub (2007), Stern and Cubbin (2005), Jacobzone et al. (2010), Cordova-Novion and Jacobzone (2011), Gutiérrez and Berg (2000), Gutiérrez (2003), Ros (2003), Cubbin and Stern (2006), Maiorano and Stern (2007), Andrés, Guasch, and Lopez Azumendi (2008), and Estache, Goicoechea, and Trujillo (2009).

In fact, Laffont (2005) was among the first to address regulatory governance in developing countries and emphasized the need for regulatory institutions and policies to be adapted to the requirements and stage of development of developing countries. Reviewing the empirical evidence on the impact of regulatory reform in developing countries, Kirkpatrick (2014) found a positive relationship between regulatory reform and improved economic performance, although he also emphasized the need to broaden the range of designs and methods for assessing the impact of regulatory reforms in developing countries.
data and feedback from respondents to a structured and standardized questionnaire sent out to selected private sector participants in each of these countries, eliciting information on the laws, regulation, and practice in a wide range of thematic areas that influence the overall business and regulatory environment.

Of these areas, survey respondents reported nine key themes as the most challenging for the private sector, and these have been organized in the report using the firm lifecycle structure. These thematic areas are (a) licensing/inspection requirements; (b) regulations and practices governing foreign investment; (c) access to resources such as land, credit, and electricity; (d) regulatory restrictions on the operation of foreign firms, such as local content requirements and currency repatriation; (e) regulatory governance and corruption/state capture; (f) predictability and quality of the regulatory framework, especially corporate taxation; (g) government procurement laws and practice; (h) effective dispute settlement/grievance mechanisms; and (i) trade and customs regulations.

The identified thematic areas are particularly relevant from a BRI-perspective as they promote connectivity and regional integration. Improvements along different dimensions of these thematic areas are likely to enable countries in the region to gain from BRI-induced opportunities. Bangladesh and Pakistan are already major BRI partner countries, while Sri Lanka has also witnessed considerable Chinese investment in the Hambantota port development. According to a database maintained by the Centre for Strategic and International Studies, BRI projects appear to be underway in many South Asian countries: 101 in Pakistan, 31 in Bangladesh, 10 in Sri Lanka, 7 in Nepal, and one in Afghanistan. While India is openly opposed to the BRI, the marked involvement of the other South Asian countries leads to the question of whether business regulatory requirements in these countries are hindering them from fully benefiting from BRI project spillovers.

World Bank Enterprise Surveys data suggest that infrastructure (electricity/transport) is one of the biggest obstacles for firms in South Asia. While the BRI aims to fill much of the infrastructure gaps in these countries, governments must simultaneously concentrate on regulatory and business environment issues to ensure that firms can benefit from BRI-induced opportunities. The latter include, among others, enhanced trade and investment, integration into value chains, job creation, skills development, government procurement, and public-private partnerships. Some of these gains can only be realized, however, with adequate regulatory reform.

To illustrate, by eliminating power shortages BRI investments in the power sector have the potential to strengthen firms’ productivity and competitiveness in all sectors, especially those facing strong potential demand. Nontransparent tariffs, however, can prevent firms from realizing this potential benefit. Similarly, BRI connectivity infrastructure has the potential to increase trade flows, which means opportunities for firms to participate more extensively and deeply in international trade. In some countries, however, this may remain only an opportunity until border management is modernized and reformed. Likewise, inordinate delays in resolving commercial disputes may impede BRI-related investment.

Another significant benefit of the BRI is its potential to generate local employment and develop local skills. This is particularly salient in South Asia, where the need to create jobs is well recognized. World Bank research shows that “South Asian countries will add 1.0 million to 1.2 million new entrants to the labor force every month for the next two decades and will contribute about 40 percent of the total new entrants to the global working-age (15–64) population.” This further underscores the need for countries in the region to leverage BRI-induced opportunities and its infrastructure creation potential by implementing effective regulatory and business environment reforms.

6. More than 70 respondents across the six countries have generously provided the input used for the analysis in this study. The choice of respondents was determined by their knowledge of both the thematic areas and the BRI, resulting in the relatively small number of respondents. That said, the quality of the feedback and the expertise of the respondents compensates for their number. The responses also serve to corroborate the range of secondary data from the various sources analyzed for this study.

02. AN OVERVIEW OF THE SOUTH ASIA REGION
The countries of the South Asian region demonstrate an eclectic mix of similarities and differences. While most of the region’s countries share a common history and some similarities in GDP and labor force sectoral composition (Table 1), clear and subtle differences can be seen in the countries’ business and regulatory environments, resulting in heterogeneous outcomes on the ground with implications for private sector participation in general and for foreign firms in particular.

Another similarity across these countries is the importance and role of small and medium enterprises (SMEs; see Box 1). SMEs are regarded as the backbone of economic development in South Asian countries, although the definition of what qualifies as an SME varies within the region. Nonetheless, the sheer number of SMEs in the region (see Figure 1) highlights the strategic importance of the sector in overall economic policy objectives. The SME sector plays a pivotal role in each country’s pursuit of inclusive economic growth, job creation, and poverty reduction. SMEs in the South Asia region make investments in plant and machinery and create value by producing both goods and services. More progressive SMEs

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**Table 1: Select indicators in six South Asian countries**

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Afghanistan</th>
<th>Bangladesh</th>
<th>India</th>
<th>Nepal</th>
<th>Pakistan</th>
<th>Sri Lanka</th>
</tr>
</thead>
<tbody>
<tr>
<td>Real GDP (USD bln, 2018)</td>
<td>21.0</td>
<td>194.1</td>
<td>2846.1</td>
<td>22.8</td>
<td>253.9</td>
<td>85.3</td>
</tr>
<tr>
<td>Share of agriculture in GDP (%)</td>
<td>20.5</td>
<td>13.1</td>
<td>14.5</td>
<td>25.0</td>
<td>22.6</td>
<td>7.9</td>
</tr>
<tr>
<td>Share of industry in GDP (%)</td>
<td>22.1</td>
<td>28.5</td>
<td>27.0</td>
<td>13.4</td>
<td>18.2</td>
<td>27.0</td>
</tr>
<tr>
<td>Share of services in GDP (%)</td>
<td>52.7</td>
<td>53.0</td>
<td>49.0</td>
<td>50.3</td>
<td>53.5</td>
<td>56.8</td>
</tr>
<tr>
<td>Real GDP per capita (USD, 2018)</td>
<td>563.8</td>
<td>1203.2</td>
<td>2104.2</td>
<td>1196.6</td>
<td>1196.6</td>
<td>3936.5</td>
</tr>
<tr>
<td>Labor force (mln, 2017)</td>
<td>14.1</td>
<td>68.4</td>
<td>509.9</td>
<td>16.3</td>
<td>73.9</td>
<td>8.7</td>
</tr>
<tr>
<td>Share of agriculture in employment (%)</td>
<td>38.6</td>
<td>40.2</td>
<td>43.9</td>
<td>70.1</td>
<td>41.7</td>
<td>25.9</td>
</tr>
<tr>
<td>Share of industry in employment (%)</td>
<td>17.6</td>
<td>20.5</td>
<td>24.7</td>
<td>13.0</td>
<td>23.6</td>
<td>28.3</td>
</tr>
<tr>
<td>Share of services in employment (%)</td>
<td>43.8</td>
<td>39.4</td>
<td>31.5</td>
<td>16.9</td>
<td>34.7</td>
<td>45.8</td>
</tr>
<tr>
<td>FDI inflow (% of GDP, 2017)</td>
<td>0.3</td>
<td>0.9</td>
<td>1.5</td>
<td>0.8</td>
<td>1.0</td>
<td>1.6</td>
</tr>
<tr>
<td>ICT penetration (% of population, 2017)</td>
<td>11.4</td>
<td>18.0</td>
<td>34.5</td>
<td>21.4</td>
<td>15.5</td>
<td>34.1</td>
</tr>
<tr>
<td>Exports of goods and services (% of GDP, 2018)*</td>
<td>5.9</td>
<td>14.8</td>
<td>19.7</td>
<td>8.8</td>
<td>8.5</td>
<td>22.8</td>
</tr>
<tr>
<td>Imports of goods and services (% of GDP, 2018)*</td>
<td>45.3</td>
<td>23.4</td>
<td>23.4</td>
<td>45.5</td>
<td>19.4</td>
<td>30.1</td>
</tr>
</tbody>
</table>

*Source: World Development Indicators.*

*Notes: * = 2017 for Afghanistan; ** = International Trade Centre Investment Map.*

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8. According to India’s MSME Development Act (2006), investments in plant and machinery should not exceed US$2.5 million for a manufacturing MSME, and US$1.5 million for service enterprises. According to the State Bank of Pakistan, SMEs employ up to 100 employees for trading establishments and less than 250 employees for manufacturing and service establishments, the annual turnover is less than Rs. 800 million. In Sri Lanka, an SME is defined as an enterprise with fewer than 50 employees and capital investment of less than Rs. 5 million.
innovate process and product technologies, pushing the technological frontier outward. The regions SME sectors serve the domestic markets, providing nontradable services, and smaller firms are increasingly involved in producing parts and components for regional and global value chains serving large producers locally or abroad. At the same time, the adverse effect of regulatory and business environment constraints identified in global databases like World Bank Enterprise Surveys, World Bank Doing Business, World Bank World Governance Indicators, and the World Economic Forum Global Competitiveness Index is particularly severe on SMEs in every country.

**Box 1: Stylized facts on SMEs in South Asia**

According to the 73rd Round of the National Sample Survey (NSS) in India, there were 63.4 million MSMEs in the country in 2015–16, while the share of MSMEs in GDP in 2016–2017 was 28.9 percent. Meanwhile, according to the Asian Development Bank (ADB; 2015), SMEs accounted for 42.4 percent of the country’s total exports by value in 2014. As per the 73rd Round of the NSS, the MSME sector created 111 million jobs (36 million in manufacturing, 38.7 million in distribution, and 36.2 million in Other Services, with 7,000 jobs in noncaptive electricity generation and transmission) in rural and urban areas across the country.

In Bangladesh, SMEs accounted for 90 percent of the private enterprises, with 7.2 million firms in 2013, and 99 percent, with 7.9 million firms if micro enterprises are included. The SME sector employs 70 to 80 percent of the nonagricultural workforce. In 2014, SMEs contributed 25 percent of the country’s GDP and 40 percent of manufacturing output (ADB 2015).

In Pakistan, SMEs constitute nearly 90 percent of all enterprises, employing 80 percent of the nonagricultural labor force, with a 40 percent share in annual GDP.

In Afghanistan, SMEs make up about 80 percent of Afghan businesses, half the country’s GDP, and employ more than one-third of the labor force.

Finally, in Sri Lanka, SMEs account for over 75 percent of all enterprises, provide 45 percent of employment, and contribute 52 percent to the country’s GDP.

In fact, World Bank Enterprise Surveys indicate that the importance of small firms in South Asia is greater than in comparator East Asian countries (Figure 1).

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9. SMEs in Developing Asia: New Approaches to Overcoming Market Failures,
10. The Doing Business Reports cover only the largest business cities in each country. The measure of performance on the topics covered may thus not be a true reflection for every country, especially in the case of large federal countries such as India.
11. Data availability constraints mean that some of the employment data presented in this section are dated and thus do not completely reflect the current situations in the sample countries.
Private sector feedback as well as existing data and literature show that a poor business environment in this region still stifles firms’ opportunities for growth and places them at a clear disadvantage vis-à-vis select comparators in other parts of the world. On average, countries in the region score poorly on major indices used globally to capture key aspects of competitiveness, such as the Global Competitiveness Index (GCI) published by the World Economic Forum and the World Bank’s Doing Business report (see Figure 2).

The varying performance of the countries is underpinned by various economy-wide constraints as well as by disparities in the reform impetus across the region. Notwithstanding changes over time in the Doing Business (DB) Index’s Distance to Frontier (DTF) scoring methodology, countries in the region, barring India, have demonstrated slow progress towards the frontier. Barriers to the entry and growth of firms can likely be found in policies entailing burdensome entry processes, licensing restrictions, labor regulations that increase the cost of hiring and firing, financial sector regulations that favor small enterprises, and inadequate bankruptcy laws that limit the ability of efficient firms to grow and enable inefficient ones
to survive. Taxes or labor costs that affect larger firms more than smaller ones reduce the larger firms’ return on investment. Impediments to accessing new market opportunities as well as to reaching foreign markets, both due to trade policy and high logistics costs, also impede expansion. These constraints are also likely to affect the ability of the region’s firms to benefit from BRI-induced opportunities.

Heterogeneity in the pace of business environment reform also emerges across the region. For example, over the past five years, India and Pakistan carried out 25 and 17 business regulatory reforms, respectively, while Nepal carried out 11 reforms, only 6 of which were positive and aimed at improving the business environment. In Sri Lanka, after a short-lived reform spurt in 2012–13, when eight DB reforms were carried out, momentum slowed during 2014–2017, with only five reforms (see Figure 3). The year 2018 saw some resumption in reform momentum, with four reforms, but it is too early to say whether this momentum will be sustained. More recently, in 2019, Pakistan and Nepal carried out six and four business environment reforms, respectively, according to Doing Business 2020. While India and Sri Lanka are the better performers in the region, all countries still lag well behind the OECD high-income average ranking of 30. Improvement in a country’s ranking on indices like Doing Business or the World Economic Forum’s Global Competitiveness Index generally indicates that a more business-friendly regulatory environment is being created.

Figure 3: Doing Business reform trends

Source: Doing Business 2020 database.
03. WHAT ARE SOME OF THE CONSTRAINTS FIRMS FACE IN SOUTH ASIA?
This section addresses the major constraints firms face in the nine key thematic areas reported by survey respondents as being the most challenging for the region’s private sector.

3.1 Business entry

3.1.1. Business registration and licensing requirements

Registration, licensing, and inspection requirements can be considerable impediments to the growth and operations of business. Research suggests that costly regulations undermine the creation and entry of new enterprises (Klapper, Laeven, and Rajan 2006), while simplified registration processes are associated with firm and job creation (Bruhn 2011). Simplifying registration formalities by eliminating requirements, such as obtaining a company seal, publishing company documents, or using notaries, and establishing one-stop shops (OSS) can go a long way toward facilitating business entry and registration. Evidence also exists on the correlation between simplified entry regulations and increased formalization of firms; see, for instance, Kaplan, Piedra, and Seira 2011; Monteiro and Assunção 2012. Establishing an OSS can simplify business registration by decreasing firms’ transaction costs. Branstetter et al. (2010) found that establishing an OSS for company registration resulted in a 17 percent increase in new firm registrations and created seven jobs per 100,000 inhabitants.

While clear differences in the ease of doing business exist across countries in South Asia, when it comes to regulation of practices governing entry into markets and obtaining operating licenses, several similarities appear. For instance, all countries in South Asia have eliminated the need to have a paid-in minimum capital requirement to set up a private limited liability company.15 Archaic requirements, like the use of a company stamp and notaries, still prevail in Bangladesh, India, Pakistan, and Nepal, however, and facilities for online business registration remain underdeveloped. In most cases, approvals are needed from several associated entities, and no OSS or consolidated online register is available that can accept and issue all licenses. This assessment is corroborated by feedback received from respondents (see Box 2).

Box 2: Licensing remains an important challenge in South Asia

SRI LANKA
“While certain licenses can now be obtained online, other licenses have to be manually obtained and may take time. There are bottlenecks at an administrative level at the Registrar of Companies.”

PAKISTAN
“Paperwork required to obtain licenses is extensive.”

BANGLADESH
“Issue of license restricted in transport sector, energy and infrastructure”.

Source: Feedback received from survey respondents.

Despite these shortcomings, starting a business in South Asia is faster and cheaper than in the East Asia and Pacific region. In South Asia, it takes on an average 15.4 days and costs 9.7 percent of the per capita income, whereas in East Asia and the Pacific, it take 25.7 days and 17.4 percent of the per capita income. A similar trend can be seen with respect to the time required to obtain an operating license.

Figure 4. Barriers to entry measures

![Figure 4: Barriers to entry measures](image)


Figure 4 shows two elements of barriers to entry: the time taken to obtain a license (taken from the World Bank Enterprise Surveys for the years 2013–2014) and the time to start a business (sourced from the World Bank Doing Business database 2020). At 33.5 days, the time taken to obtain a license is highest in Bangladesh and lowest in Nepal at 9.8 days, with India (17.8) and Sri Lanka (16.7) both above the South Asian average of 14.8 days and Pakistan (10.4) and Afghanistan (13.7) both below the average. Similarly, with 22.5 days, the longest time to start a business is in Nepal and the shortest in Afghanistan (8.5) and Sri Lanka (8). Bangladesh, India, and Pakistan all perform slightly behind the regional average of 15.4 days.

Reforming business licensing is often a starting point for improving the investment climate to leverage gains from the BRI, among other benefits. Complex licensing procedures may encourage firms to remain unregistered and operate in the grey economy, which in addition to impeding opportunities for joining the BRI-network, gives rise to difficulties later in accessing finance from formal financial institutions and constrains productivity and expansion. Across sectors, this can suppress new firm establishment and therefore the new job creation, dragging down overall economic growth (World Bank 2013a). According to the World Bank Enterprise Surveys, 17 percent of businesses in South Asia consider business licensing and permits to be a major constraint. Approximately 25 percent in Pakistan, 20 percent in Sri Lanka, and only 11 percent and 10 percent of businesses surveyed in India and Nepal, respectively, identify business licensing as a major constraint. At the same, governments in the region have been making efforts to reform licenses; for example, India has streamlined licensing and inspections at the subnational level for over 50 different licenses.

The business licensing sector is also tainted with perceived corrupt practices of public officials. As can be seen in Figure 5, 30 percent of South Asian firms expected to give gifts to get an operating license. In Bangladesh, as many as 58 percent of firms expected to give gifts, whereas in Sri Lanka and Nepal, only 12 and 19 percent, respectively, expected to do so.

16. South Asia average values used in this report are the authors’ own calculations based on the data for the six South Asia countries covered in this report: Afghanistan, Bangladesh, India, Nepal, Pakistan, and Sri Lanka.
In the South Asia region, licensing requirements are mostly sector specific, rather than blanket operational requirements. The licensing process and allocation criteria vary from one sector to another. Sector-specific restrictions may also apply on license issuance, such as in the energy sector in Pakistan (including restrictions on the ability of foreign service providers to sell/dispose of their licenses) and in the transport, energy, and infrastructure sectors in Afghanistan. In some other cases, licenses in certain sectors may only be issued to public sector entities, thereby restricting private participation in those sectors. For instance, in Sri Lanka, the license to transmit electricity is only issued to the Ceylon Electricity Board, while in the aviation industry, the license to carry on certain aeronautical services, such as operation and maintenance of aerodromes, aviation security, and so on, is issued only to Airport and Aviation Services (Sri Lanka) Limited, a state-owned enterprise.

Simplifying business licensing is about limiting licenses to those that are justifiable. The first step is to conduct a stocktaking of all required licenses and then to cut unnecessary licenses. Where licensing is not restricted, the process of obtaining a license should not impose an unnecessary burden on businesses. Good practices show that imposing a license or equivalent on a particular economic activity relates to its expected impact on the aim of protecting any of the following public interests: (1) the environment; (2) public health and safety; (3) limited natural resources; (4) national security; (5) financial activities; or (6) controlling undesirable practices. Risk matrices may be deployed to undertake a cost-benefit analysis of licensing in the region. Risk matrices are fundamental instruments used to classify establishments depending on their risk level and to adapt regulatory responses (e.g., inspections, licensing) on that basis. This allows for more effective and efficient use of resources, minimizes the administrative burden, and maximizes positive outcomes (World Bank 2013c).

Similar to excessive licensing requirements, inspections can result in substantial costs for the state and a burden for businesses. Issues surrounding inspections include vague requirements and uncertainty, insufficient coordination among agencies, persistent discretion, and inspections focused on discovering violations rather than enhancing compliance and extracting “compliance fees.” Moreover, the lack of a risk focus can subject low-risk businesses to inspections (Blanc 2012).
All regulatory requirements impose compliance costs on licensees and governments and should only be imposed if the benefits of doing so exceed these costs. To identify whether the benefits outweigh the costs, it is therefore necessary to consider the level of risk being addressed and whether the licensing requirements imposed are proportionate to that risk. Is the level of risk high enough to justify the requirement? Is the extent of the requirement in proportion to the existing risk? For instance, if the problem relates to a low-risk/low-impact activity, it may be appropriate to require only notification of commencement of operations rather than prior approval. Another method of applying the risk-based approach is through license duration; low-risk operations could be given longer-term licenses or licenses with no fixed term if no noncompliant behavior is demonstrated or found.

### 3.1.2. Construction Permitting

Once they have registered their property and secured their title, firms in South Asia also struggle to obtain construction permits. Reforms that regulate construction more efficiently and transparently can help reduce corruption and informality while encouraging construction companies to go through formal channels and ensuring compliance with important standards, such as those impacting safety or mitigating climate change. Good regulations, combined with sound enforcement mechanisms, ensure safety standards that protect the public while making the permitting process efficient, transparent, and affordable for both building authorities and the private professionals who use them. A recent study shows that long delays to obtain permits could lead to higher transaction costs and fewer transactions (Hamman 2014). The payoff for construction permitting reforms can be significant, yielding benefits for both the public and private sectors. Examining the impact of construction permit reforms on new income generation, one study in the United States (PricewaterhouseCoopers 2005) shows that a modest acceleration of the permitting process could increase construction spending by 5.7 percent and generate 16 percent more in property tax revenue over five years. It also shows that for every ten jobs directly related to a construction project, another eight jobs are created locally. These impacts yield not only additional income for the community, but additional investments and tax revenues for the government. Beyond economic returns and the pay-off of attracting more investment, the most important benefit of building permit reforms is to protect public safety.

**Figure 6. Time and steps required to obtain construction permits**

The procedures for building projects in South Asia continue to be complicated and costly, involving licensing requirements from several different agencies and thus increasing the opportunities for rent-seeking and corruption. These challenges in obtaining construction permits may not only hinder firms’ operations in general, they can also impede firms in the region from benefitting from BRI-induced opportunities. An analysis of World Bank Enterprise Survey data in Doing Business 2010 shows that the share of firms expecting to give gifts in exchange for construction approvals is correlated with the level of complexity and cost of dealing with construction permits (World Bank 2009).
While India and Sri Lanka have recently improved their permitting processes, the remaining countries in the region still have cumbersome and inefficient building permitting systems. For example, in the past three years India improved the process for obtaining a permit, making it faster and less expensive, by implementing an online system that has streamlined the process in the municipalities of New Delhi and Greater Mumbai and established strict time limits for preconstruction approvals. It also improved building quality control by introducing decennial liability and insurance.

Figure 6 shows the number of procedures required to obtain construction permits (sourced from the World Bank Doing Business 2020). India (15), Pakistan (17), and Bangladesh (16) are all above the regional average (14.3), while with 13, 13, and 12, Afghanistan, Sri Lanka, and Nepal, respectively, make the permitting process less burdensome than do their regional peers. While the discrepancy in the number of procedural steps is not considerable, it masks huge variations in the time taken to finalize the permitting process, ranging from a mere 86 days in Sri Lanka, making it among the fastest globally, all the way to 274 in Bangladesh (281 in Dhaka).

Construction permitting is another area where a risk-based approach could be considered. A growing consensus in the construction industry points to the need for supervisory bodies to consider the potential risks imposed by a building, rather than applying the same permitting and inspections standards to all buildings and edifices (Doing Business 2014). Risk-based inspections, as opposed to random, untargeted inspections, allow governments to allocate resources where they are most needed, without compromising worker and public safety. While only a handful of countries globally have risk-based inspections for construction mandated by law, none of the South Asian economies have such risk-based inspections.

### 3.1.3. Entry of foreign firms: Regulations and practices governing foreign investment

Foreign direct investment (FDI) is associated with numerous beneficial effects for host countries. It is the largest source of external finance in many developing countries, and as such it has the potential to drive significant growth. In addition to unlocking capital constraints, research shows that FDI facilitates technology transfers and promotes market competition, thus enhancing both firm-level and aggregate productivity and creating better-paying, stable jobs. FDI is most wanted in developing countries, as it is considered a stimulating engine for economic growth, complementing domestic investment (Jude and Silaghi 2009). FDI brings in additional technology and diversifies exports (Echandi, Krajcovíčová, and Qiang 2015), both key determinants of prosperity in any country dependent on the technical knowledge embedded in the goods and services it exports (Hausmann, Hwang, and Rodrik 2007). Most importantly, foreign investments have the potential to create jobs across a range of skill categories, including in mid- and high-skill occupations, which are of high relevance for South Asian countries.

Countries that demonstrate openness to foreign investment and international trade tend to be more productive and faster growing. Policymakers seek to attract FDI to create jobs, bring in cutting-edge knowledge and technology, connect to global value chains, and diversify and upgrade their economies’ production capabilities (Reyes 2017). An increase in FDI inflows increases growth of real output per capita (Calderón and Nguyen 2015), has a significant positive impact on income growth rates (Blomstrom, Lipsey, and Zejan 1992), and facilitates technology transfer (Borensztein, De Gregorio, and Lee 1995). Multinational firms have advantages in terms of productivity, scale, and market access that challenge incumbents as no other entrant can. Domestic firms, especially high-growth ones, are primary beneficiaries of FDI through two main channels: (1) contractual linkages between foreign and local firms that promote spillover of foreign firms’ knowledge and practices, leading to an upgrade in domestic suppliers’ technical and quality standards; and (2) the “demonstration effect,” allowing local firms to imitate foreign technologies or managerial practices through observation or by hiring workers trained by the foreign company.

Foreign firms also typically enter at a larger scale than do domestic start-ups and with significantly more positive growth prospects (World Bank 2019b). At the same time, they face barriers due to their foreignness, against which they typically evaluate returns from entry into a new market. Although a
country’s attractiveness as an investment destination is influenced by factors such as market size, macroeconomic fundamentals, business costs, commitment to liberalization, political stability, and infrastructure development, FDI policy also plays a critical role in positioning the market as a host country, hence attracting or deterring foreign investment, especially in infrastructure projects.

Given their value-addition in terms of jobs, tax revenue, and spillover, many countries have investment policies aimed in part at recruiting operations of large multinational enterprises. With FDI declining worldwide (from 5.3 percent of GDP in 2007 to 2.3 percent in 2017), developing countries—including those in South Asia—must compete for ever scarcer investments (see Figure 7). The situation will get even worse as global FDI flows are expected to fall from 5 to 15 percent due to the Covid-19 pandemic (UNCTAD 2020). Countries in the region would thus need to do even more to attract foreign investment.

Figure 7. Developing countries—including in South Asia—must compete for ever scarcer FDI

Foreign Direct Investment as a share of GDP, 2007 and 2017

Source: Authors’ calculations from World Development Indicators (2019).

The importance of country-specific reforms in facilitating private and foreign sector participation to realize gains from the BRI has been emphasized in a recent World Bank study (World Bank 2019a). The report notes that “to increase private sector participation in the BRI, participating countries will need to improve the investment climate and reduce the risks facing potential investors. Specific reforms include improving the regulatory environment and strengthening legal protection of investment through legal rules and their enforcement.”

In fact, computable general equilibrium (CGE) results underlying the key messages in the report suggest that the proposed BRI transport network could increase FDI flows to corridor economies in South Asia by 5.2 percent, with reductions in trading time estimated to have large effects, in particular, on low and lower-middle-income economies, with estimated FDI increases of 7.6 and 6.0 percent, respectively.

Meanwhile, as Table 2 shows, there are huge variations in FDI inflows in the region’s countries, both in absolute value and on a per capita basis, ranging in 2018 from a mere US$139 million (or US$3.7 per capita) in Afghanistan to a huge US$42.3 billion (US$31.3 per capita) in India. On a per capita basis, the value is the highest in Sri Lanka, at US$74.3. Even the top destinations in the region, however, are only able to attract less than 2 percent of their nominal GDP as inward investment.
In most South Asian countries, FDI policy is transparent and has been nondiscriminatory, with the recent exception of India, where rules governing FDI inflows from neighboring countries, especially China, were amended in April 2020 in the wake of the Covid-19 crisis, moving investments from the region to the government approval route. While prior approval from the government or government-approved bodies is needed for foreign investment in the sectors open for foreign investors, restrictions in certain sectors across countries in the region are mostly imposed on the grounds of national security. Despite the relative openness, South Asia’s intraregional and global ties remain relatively weak (World Bank 2016). In other sectors, limits are imposed on the amount of FDI allowed, except in the sectors where 100 percent FDI is permitted. Treatment of FDI within the region is heterogeneous. Nepal, for instance, has failed to attract substantial FDI inflows because of the high entry barriers and a long list of excluded industries, such as real estate businesses; others have recently been added to the banned list.

This assessment is also corroborated by the Heritage Foundation’s Index of Economic Freedom (2020), which seeks to understand the freedom of capital movement and the extent of the state’s supervision over it. According to the index, investment freedom in Afghanistan, Bangladesh, India, Nepal, and Sri Lanka, is considered repressed; Pakistan is considered the only country in the region with a moderately unfree investment environment (Figure 8).

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17. The Indian Ministry of Finance (DEA) released the notification under FEM (Non-debt Instruments) Rules (2019), with the following proviso:

Provided that an entity of a country, which shares a land border with India or the beneficial owner of an investment into India who is situated in or is a citizen of any such country, shall invest only with the Government approval:

Provided further that, a citizen of Pakistan or an entity incorporated in Pakistan shall invest only under the Government route, in sectors or activities other than defence, space, atomic energy and such other sectors or activities prohibited for foreign investment:

Provided also that in the event of the transfer of ownership of any existing or future FDI in an entity in India, directly or indirectly, resulting in the beneficial ownership falling within the restriction or purview of the above provisos, such subsequent change in beneficial ownership shall also require government approval.

18. Outright restrictions and prohibitions are not the only factor keeping FDI inflows low. Others include poor infrastructure (electricity, roads), insufficient guarantees of investor protection, and complicated processes for currency repatriation (World Bank 2016).
In fact, even in sectors that do not restrict entry of foreign firms, FDI involves multiple administrative approvals from the concerned domestic authorities, making it in some cases cumbersome for foreign investors. Moreover, as feedback from respondents suggests, foreign investors must periodically reapply for permits and approvals (see Box 3 for details).

**Box 3: Foreign investors must periodically reapply for permits and approvals in South Asia**

**AFGHANISTAN**
“Foreign investors need to reapply for approvals/permits every three years.”

**BANGLADESH**
“Depending on the category of the establishment, for liaison office/branch office foreign investors need to reapply for approvals/permits every two to three years.”

**NEPAL**
“High bureaucracy rates and discretion in issuing of licenses. There is a practice of imposing conditions while issuing the license for certain projects.”

**PAKISTAN**
“Foreign investors need to reapply for approvals/permits every three or five years.”

**SRI LANKA**
“Depending on the type of permit obtained, foreign investors need to reapply for approvals/permits every three to seven years.”

*Source: Feedback received from survey respondents.*

The time required to get FDI approvals also varies by country. For example, apart from the automatic route, FDI in India is also administered under the government route, wherein prior approval is required from the Government of India. Proposals for foreign investment under the government route are submitted online, using the Foreign Investment Facilitation Portal. The DPIIT (Department for Promotion of Industry and
Internal Trade) identifies the relevant ministry; the proposal is then circulated thereto, as well as to the Reserve Bank of India for comments from the perspective of the country's Foreign Exchange Management Act (FEMA). DPIIT and the Ministry of Home Affairs (if applicable) also provide comments. The proposal usually gets approved within eight to ten weeks.19

According to the WTO’s 2018 Trade Policy Review for Nepal, all applications for a Foreign Investment Approval Letter (FIAL) in Nepal are processed either by the Investment Board Nepal (IBN) or the Department of Industry (DOI) on the basis of fixed capital. The decision regarding the FIAL from the IBN must be made within 30 days from the application date (subject to extension), whereas decisions on industrial licenses, registrations, and duty drawbacks must be made within 30, 21, and 60 days, respectively.

In Bangladesh, the Bangladesh Investment Development Authority (BIDA) is responsible for screening, reviewing, and approving FDI in the country, except for FDI in Economic Zones. All foreign investors must obtain clearance certificates from the relevant authorities or, in certain cases, a “no objection” certificate. According to WTO’s 2019 Trade Policy Review for Bangladesh, the authorities indicated that the investment approvals are issued within one week.

All FDI applications in Sri Lanka must receive an approval from a government authority. There are two types of approval for FDI under the Board of Investment (BOI) Act: FDI without fiscal incentives, under Section 16, and FDI with incentives, administered under Section 17. To obtain investment approval, an investor applies to a One-Stop-Shop (OSS) under the BOI. Further, OSS receives the response from relevant authorities, including the Urban Development Authority (UDA), the Central Environment Authority (CEA), the Tourism Development Authority, and the Geological Survey and Mines Bureau, among others, within 20 working days (World Trade Organization 2016).

In Pakistan’s manufacturing and industrial sectors, foreign investors are permitted to hold 100 percent equity without the need to receive permission from the government. All sectors are open for FDI unless specifically prohibited. No Objection Certificates (NOC) are not required to locate the project anywhere in the country except in specific “negative areas.” To register a company in Pakistan for a nonmanufacturing project, the State Bank of Pakistan (SBP) must be notified.20

In Afghanistan, all foreign or local citizens may make investments in all sectors of the economy unless specifically prohibited. Any investment above US$3 million requires approval from the High Commission on Investment (HCI) (Article 4 of Private Investment Law).21

Governments in the region also review FDI policy on an ongoing basis, aiming to achieve further liberalized and simplified requirements. For instance, in 2019, the Indian government liberalized FDI in single-brand retail by diluting the stringent condition of local sourcing. It also allowed 100 percent FDI in commercial coal mining and in contract manufacturing through the automatic route, in a bid to attract global vendors seeking to diversify supply chains in wake of the US-China trade war. The government had already issued a notification allowing 100 percent FDI in insurance intermediaries.22 Similarly, the BOI in Sri Lanka established a Project Screening Committee to screen all investment applications jointly with cross functional departments to grant approval expeditiously. BOI also introduced a web portal by interconnecting all line agencies to streamline and fast track the investment approval process.23

Among other challenges constraining FDI in the region, one key issue facing IFC investments in Bangladesh has perennially been a long, complex approval process for foreign loans. Another major issue facing foreign investors has been arbitration and the relative refusal of governments in the region to abide by negotiated agreements. Addressing these challenges would facilitate FDI flows.

### 3.2 Access to resources

#### 3.2.1 Land

Access to land is an important ingredient of the business climate, as firms invariably need land to set up plants or factories. Two factors determine access to land: the quality of the land system (e.g., property registration and cadastral agencies), and land availability. A substantial literature links land registration and property rights to long-run macroeconomic performance. Efficient land administration systems and land policies provide a range of economic benefits. For example, using Russian firm-level survey data, Karas Pyle, and Schoors (2015) find that private land rights facilitate credit access and promote investment among large urban industrial enterprises.

Access to land is particularly relevant for large-scale infrastructure projects and those involving overland corridors, such as the Belt and Road Initiative. In fact, an overland "belt" to link China to Central and South Asia and onward to Europe, the Middle East, and parts of Africa will be unattainable should land be inaccessible. The direct channels between land availability and development are significant. Using evidence from the agricultural sector in Bangladesh, one of the most land-scarce countries in the world, Rahman and Rahman (2009) find that a 1 percent increase in land fragmentation reduces rice farm productivity by 0.05 percent. Concentrated ownership of key factor endowments (i.e., land, labor, and capital) and the adoption of technology are associated with improvements in technical efficiency. Niroula and Thapa (2005) argue that laws of inheritance, regressive taxation, and the underdevelopment of land markets have impeded land consolidation in South Asia.

Accessing land is a serious concern for industrial and manufacturing sectors. Bangladesh, for example, has struggled to attract FDI in several sectors. Samsung could not invest in Bangladesh because it could not find 250 acres for itself and its suppliers around Chittagong, leading the multinational company to withdraw a planned $1.25 billion investment with the potential to create 50,000 jobs; Samsung invested in Vietnam instead (World Bank 2017). While some industrial zoning may help firms grow sustainably (e.g., under greenbelt laws), inappropriate land-use regulations may exacerbate land scarcities and raise costs for businesses and consumers. One World Bank study found that building height restrictions in Bangalore imposed welfare costs that ranged from 3 to 6 percent (Bertaud and Brueckner 2004).

Land acquisition constraints have meant that most countries across the region have implemented some form of economic zones regime: 8 export processing zones (EPZs) and 88 economic zones (EZs) in Bangladesh; 3,381 industrial land clusters in India; 14 special economic zones (SEZs) in Nepal; 12 zones in Sri Lanka; and at least 4 EPZs and several planned zones in Pakistan. These zones address one major challenge relevant to manufacturing entities and also likely to pertain to BRI infrastructure projects: the need to look for land in areas outside metropolitan areas, with a preference for serviced industrial land.

Problems with land governance in South Asia also deter the region’s competitiveness. Findings on legislative land reforms in India’s states from 1958 to 1992 indicate an association with poverty reduction (Besley and Burges 2000), whereas evidence on the land formalization program in rural Benin finds that improved tenure security through demarcation leads to a shift toward long-term investment (Goldstein et al. 2018).

It turns out that most countries in the South Asian region are plagued by the same issues when it comes to the quality of the land administration system in the largest business city in each economy. For instance, in Afghanistan, Bangladesh, Nepal, Pakistan, and Sri Lanka, no electronic database allows checking for
encumbrances, and the majority of land plot maps are kept in paper format. Further, in all countries, information recorded by the immovable property registration agency and by the cadastral or mapping agency is kept in separate databases. Due to the lack of information-sharing among agencies and the absence of centralized databases, transactions such as conducting due diligence on property requires consulting multiple sources. These factors increase both procedural complexity and the risk of regulatory uncertainty since no options exist for cross-verification.

In South Asia, no separate mechanism exists for filing complaints about problems at the agencies in charge of immovable property registration. The system of immovable property registration is not subject to state or private guarantees, and no compensation mechanism is in place to cover losses incurred by parties who engaged in good faith in a property transaction based on erroneous information certified by the immovable property registry. Privately held land plots are neither formally registered at the immovable property registry nor mapped. It takes on average more than three years to obtain a decision for the court of first instance to resolve a dispute over property tenure rights.

Feedback from respondents corroborates these concerns as well as the slow pace of modernization of records in India; multiplicity of institutions in charge and lack of transparency in Sri Lanka; limited accessibility and reliability of land records, together with discretion in the bureaucracy, in Pakistan; and corruption in Afghanistan, Bangladesh, and Pakistan (see Box 4).

Box 4: Problems with access to land in South Asia

**INDIA**
“The quality of the land administration system in the country is unsatisfactory. There is no electronic database for checking encumbrances, or for recording boundaries, etc., for most of the States. Land disputes are time consuming and cumbersome and are also negatively impacted by the backlog faced by courts in India.”

**SRI LANKA**
“While Sri Lanka does possess an effective land administration system, it can be prone to delays and frauds.”

**NEPAL**
“Real Estate and Access to Land is a serious problem”; businesses find it “difficult to find out separate approval and requirements.”

**PAKISTAN**
“Land administrative offices are riddled with corruption and backlogs. The system is overly bureaucratic and poses significant hurdles to parties unfamiliar with dealings in Pakistan.”

**BANGLADESH**
“The quality of the land administration system in the country is ‘very bad.’”
“Businesses feel obliged to give payments like tips/gifts/bribes, etc., when registering land/real property.”
“Land records relating to title of the land are not available online. It is very difficult to obtain updated information regarding title and possession of land from land record office. Suits to resolve land disputes have to be instituted in the subordinate courts; sometimes these suits may take 20 to 25 years to be disposed of. While in theory, there is equality of access to property rights, in practice wealthy and influential sections of the society tend to grab and acquire the land of others with impunity.”
“Discretionary treatment by regulatory officials when it comes to allocation of land is a serious problem.”

**AFGHANISTAN**
“Long procedures and huge corruption stain the land administration system.”

Source: Feedback received from survey respondents.

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24. This is also true for Delhi and Mumbai, the largest cities in India. The situation is similar across major cities in the country.
This assessment is reflected in the performance of the countries in terms of the “quality of the land administration index” for the Doing Business 2020 report, as shown in Figure 9, which shows a performance below the regional average for four out of the six countries surveyed countries. While India and Pakistan perform better than their regional peers, Afghanistan is amongst the worst performers globally.

In addition to poor-quality land administration, restrictions are placed across South Asia on foreign ownership of land. For instance, while India has no restrictions on ownership of land that applies particularly foreign entities, the country’s FDI policy only allows foreign entities to lease buildings or structures over land but not barren land. In Sri Lanka, foreign entities cannot buy land unless their shareholding is less than 50 percent, although they are allowed to lease land up to a maximum of 99 years. Only nonresident Nepalese with identification cards can own or acquire land in Nepal; no other foreigners are allowed to do so. Firms owned by foreign investors (fully or partly) may purchase land only for the purposes of their business activities, such as to establish a factory or a hotel or to set up residences for their workers. Pakistan imposes restrictions on coastal and border land for reasons of national security that apply to all private companies, including foreign firms. In Bangladesh, according to feedback received from survey respondents, a foreign firm is required to have a local subsidiary to obtain ownership of land.

**3.2.2 Finance**

The role of access to finance in firm growth and private sector development is well documented in the literature. Ayyagari et al. (2016) investigated the effect of access to finance on job growth in 50,000 firms across 70 developing countries, finding that increased access to finance results in higher employment growth, especially among micro, small, and medium enterprises. Firms that are not credit constrained were found to experience faster growth than firms that were (Fowowe 2017). Evidence also suggests that financing constraints play an important role in explaining the “missing middle”—the failure of small enterprises in developing countries to grow into medium-size or large firms (T. Dinh et al. 2010).

Access to finance is essential to establish and operate a business efficiently. Strong legal rights of borrowers and lenders are crucial components that determine the effectiveness of the legal financial system and facilitate access to credit. For instance, Beck et al. (2000) find that economies with legal systems that more
effectively protect the rights of outside investors have greater financial development and economic growth than those that don’t. Research on the enactment of China’s 2007 property law, which increased creditors’ rights over the assets underlying their secured loans to private companies and increased protection granted to private companies against potential expropriation, shows that enactment of the law resulted in an increase in firm value (Berkowitz, Lin, and Ma 2015). Most recent research also associates credit infrastructure characterized by strong insolvency regimes with lower credit costs, increased access to finance, higher recovery rates, and better labor market outcomes (Neira 2017).

The transparency and availability of credit information is also an important determinant of the quality of the legal financial system. Sharing credit information among credit bureaus and registries can help tackle information asymmetries and improve confidence in the system, thereby contributing to improved access to credit. A study on the impact of credit reporting and identification systems on financial intermediation in 172 countries between 2000 and 2008 shows that implementation of an obligatory identification system has a positive effect on financial intermediation and financial access (Giannetti and Jentzsch 2013). Evidence also suggests that introducing collateral registries for movable assets increases smaller and younger firms’ access to financing (Love, Martinez-Peria, and Singh 2015).

A good-quality financial system is needed to efficiently administer access to finance for borrowers and guarantee protection for lenders. The World Bank’s CPIA financial sector rating and the Enterprise Surveys data show that economies in the South Asia region with stronger and more efficient financial systems see larger shares of investments financed by banks.

Access to finance is regarded as one of the biggest obstacles for the operation and growth of business in South Asian countries, however, as revealed by survey responses; existing data sources concur with this finding. The negative effects are especially daunting for smaller firms versus larger firms in terms of productivity. Larger firms tend to innovate more, particularly in process and organization, because they can more easily secure financing for risky projects and because of the potential for economies of scale in research and development investments (Del Mel, McKenzie, and Woodruff 2008). Ten years ago a World Bank Investment Climate Assessment argued that South Asian countries underperform comparator countries like China and Vietnam on many investment-climate measures, including access to finance. Similar results emerge from the most recent round of Enterprise Surveys, which show an average firm in South Asia consistently ranks financial constraints as more binding than does an average firm in comparator peers.

Figure 10 below shows two indicators of access to finance taken from the Enterprise Surveys assessment, based on the data for the year 2013/14: the share of firms with an existing credit line or bank loan and the share of firms that had recent applications rejected. Sri Lanka has over 40 percent of firms with a bank loan, the highest share in the region, followed by Nepal and Bangladesh, whereas Pakistan has the lowest share of firms with a line of credit, i.e., below 10 percent. Meanwhile, the region has the second highest percentage of firms where recent loan applications were rejected (15.2 percent, compared to 7.6 percent in East Asia and Pacific) and the rejections of loan applications appear to be correlated with the lack of credit lines in South Asian countries (see Figure 10). For example, Nepal and Sri Lanka, countries with the highest share of firms using loans, also have the lowest share of firms who reported rejection of the most recent application (below 10 percent), while Pakistan has the second largest share of reported rejections of loan applications. Receiving a rejection for a loan application may therefore hinder firms’ incentives to apply for a loan again. As a result, firms must rely largely on their own sources of finance, which may create financial constraints and hamper business operations, particularly in case of SMEs.

25. Data not available for Afghanistan.
Figure 10. South Asian economies with more rejected loan applications have fewer firms with an existing credit line

![Graph showing the relationship between the percent of firms whose recent loan application was rejected and the percent of firms with a bank loan/line of credit.]

Source: Enterprise Surveys (2013-14); author’s own calculations.

Figure 11. Access to Finance: Getting Credit

![Bar chart comparing access to finance across South Asia and selected countries.]

Source: Doing Business 2020 database.

The Doing Business 2020 report also shows a below par performance on aspects related to the depth of credit information and strength of legal rights (see Figure 11). Nepal and Afghanistan, followed by India, have relatively strong legal frameworks that protect the legal right of borrowers and lenders with respect to secured transactions. For example, Nepal and Afghanistan provide for unified legal frameworks for secured transactions that extend to the creation, publicity, and enforcement of functional equivalents to security interests in movable assets, whereas no unified central registry where security interests over different

26. For countries where data exist on both the credit bureau and the credit registry, the one with the higher coverage is considered.

27. The legal rights index measures the legal rights of borrowers and lenders with respect to secured transactions by focusing on whether certain features that facilitate lending exist within the applicable collateral and bankruptcy laws. The credit information index measures the coverage, scope, and accessibility of credit information available through credit reporting service providers such as credit bureaus or credit registries.
types of collateral are registered currently exists in other South Asia’s countries. In terms of depth of credit information, India and Pakistan, followed by Sri Lanka have the largest coverage, scope and accessibility.28

But difficulties accessing finance and financial institutions has negatively impacted countries in the region by holding back development of high-potential sectors such as ICT, R&D, and others (World Bank 2017). Access to finance is critical to the adoption of e-commerce or to promote R&D, among other opportunities. The region’s moderate achievements on many of these dimensions may hint at a lack of financing facilitation. Financing constraints are also likely to be a major impediment to the ability of the region’s firms to benefit from BRI-induced opportunities.

Another major challenge associated with regional access to finance is insolvency resolution. Regulatory frameworks are only just modernizing in the region, but these economies are not yet dealing with a huge stock of nonperforming loans (see for example Lee and Rosenkranz 2019).29 Modernizing insolvency resolution and practice will be critical to help stabilize the financial sector, strengthen banks, and release unproductive assets back to these countries’ economies.

### 3.2.3 Electricity

Extensive and efficient infrastructure is a necessity for flourishing trade and business development, and it plays a key role in economic development and competitiveness. Well-developed infrastructure bridges distances and helps national markets connect to global markets. High-quality, extensive infrastructure networks contribute to businesses in a number of ways. For instance, effective transport of goods, people, and services enables entrepreneurs to get their goods and services to destination markets in a secure and timely manner. A reliable supply of electricity, without interruptions and shortages, allows businesses and factories to work unimpeded. Extensive and reliable telecommunications networks allow for rapid, free-flowing information, increasing overall economic efficiency by helping economic players make decisions with all available relevant information. In contrast, poor infrastructure raises the cost of doing business.

Low-quality infrastructure poses significant constraints, especially in rural areas, due to bottlenecks and slow turnaround times, erratic and/or inadequate energy and water supplies, transport failures, and limited communication, all of which again weaken firms’ ability to become a part of the BRI-network.

An economy’s electricity supply is one of the main determinants of firm productivity (Escribano, Guasch, and Pena 2009). Existing work on Africa also finds that power disruptions have negative impacts on long-run GDP (Andersen and Dalgaard 2013) and on manufacturing productivity (Moyo 2013). Geginat and Ramalho (2015) demonstrate that simpler and cheaper electricity connection processes are associated with higher firm performance, especially in industries heavily dependent on electricity.

Yet access to electricity remains challenging in the South Asia region. In a 2006 Investment Climate Assessment, the World Bank argued that South Asian countries underperform comparators on many investment climate dimensions, including infrastructure and electricity supply.

In most countries surveyed, firms have identified access to electricity as among their biggest obstacles. Notably, Bangladesh and Afghanistan remain among the 30 countries with the lowest performance on the Doing Business Getting Electricity ranking. Utilities in both these countries do not calculate the system average interruption duration index (SAIDI) or System average interruption frequency index (SAIFI)—the Doing Business indices for average duration and frequency of electricity interruption—and score 0 points on reliability of supply and transparency of tariffs index. Further, obtaining a new electrical connection in these countries remains relatively expensive, with the cost amounting to over 1,700 percent of per capita income in Bangladesh and almost 2,500 percent of per capita income in Afghanistan, compared to less

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28. A credit bureau or registry in Afghanistan covers less than 5 percent of the adult population and hence the country was not scored.
than 30 percent of per capita income in India. Furthermore, in Afghanistan, Bangladesh, and Pakistan the process of obtaining electrical connection is very lengthy, taking around four months.

This said, countries like India and Sri Lanka have shown progress in ensuring reliable supply and transparent tariffs (made available online, with the possibility for digital payment in Sri Lanka), especially in the major cities in these countries. Inadequate electricity supply remains an issue in all countries covered, however, and there are considerable disparities in the rest of South Asia and even within these countries at the subnational level.\textsuperscript{30}

Firms in Sri Lanka find that access to electricity is considered less constraining than tax rate and access to finance, although the entire process of obtaining a new electrical connection is time-consuming, even in Colombo. For instance, upon submitting an application, private investors wait 25 days to receive on-site inspections and a price estimate from the Ceylon Electricity Board, the local public utility; it takes approximately 63 days for the utility to lay down the electrical cables and install the switchgears and equipment that allow electricity to flow.

Meanwhile, insufficient generation and defective infrastructure in power distribution are more significant obstacles to business activity in Nepal than in other countries. Electricity is considered the biggest and most detrimental obstacle to local business activity in Pakistan, with more than 75 electrical outages occurring in a typical month and an average duration of electrical outages of more than 16 hours, compared to 4.1 outages of 1.5 hours in Sri Lanka (see Table 3). Chronic issues affect the local distribution system, even as Lahore was found to be more efficient than Karachi in terms of obtaining a new electrical connection. Power outages are also a big constraint on the Afghan economy.

Unreliable electricity supply results in a significant proportion of firms in each country securing back-up sources of electricity by owning or sharing generators. Dependence on generators is observed across all countries in South Asia; it is most pronounced in Pakistan and Bangladesh, where over 60 percent of firms own or share a generator, and least pronounced in Sri Lanka, with 35 percent of firms using a generator (see Table 3). Self-generated electricity is usually more expensive than electricity from the grid, however, as it requires significant investments, thereby raising production costs (Foster and Steinbuks 2009). Given the high costs associated with owning and operating a generator, typically over US$10,000, such high levels of dependence on generator use for electricity supply in South Asia pose a significant challenge to businesses, as well as underlining the severity of electricity supply problems.

\textbf{Table 3: Indicators of electricity infrastructure in South Asia}

<table>
<thead>
<tr>
<th>Country</th>
<th>Year</th>
<th>Number of electrical outages in a typical month</th>
<th>Average total time of power outages per month (hours)</th>
<th>Value lost due to electrical outages (% of sales)</th>
<th>Firms owning or sharing a generator (%)</th>
<th>Electricity from a generator (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Afghanistan</td>
<td>2014</td>
<td>11.5</td>
<td>3.8</td>
<td>9.6</td>
<td>48</td>
<td>38.3</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>2013</td>
<td>64.5</td>
<td>1.2</td>
<td>5.5</td>
<td>62.8</td>
<td>26.1</td>
</tr>
<tr>
<td>India</td>
<td>2014</td>
<td>13.8</td>
<td>2</td>
<td>3.7</td>
<td>46.5</td>
<td>8.8</td>
</tr>
<tr>
<td>Nepal</td>
<td>2013</td>
<td>8.7</td>
<td>3.6</td>
<td>17</td>
<td>50.5</td>
<td>41.3</td>
</tr>
<tr>
<td>Pakistan</td>
<td>2013</td>
<td>75.2</td>
<td>16.9</td>
<td>33.8</td>
<td>65.4</td>
<td>41.4</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>2011</td>
<td>4.1</td>
<td>1.5</td>
<td>3</td>
<td>35.1</td>
<td>4.8</td>
</tr>
</tbody>
</table>

30. For instance, data from the 2014 World Bank Enterprise Survey for India show that Indian states highly affected by electrical outages include Arunachal Pradesh (85 hours per month), Assam (81 hours per month), and Jammu & Kashmir (76 hours per month). In contrast, some of the territories least affected by electrical outages are Gujarat (61 hours per month), Maharashtra (3 hours per month), and Chhattisgarh and Delhi (both at 4 hours per month).
3.3 Regulatory restrictions on the operation of foreign firms

3.3.1 Local content requirements

Local content and local labor requirements may boost the domestic economy and accentuate FDI spillovers, but these invariably impose additional costs on firms, thereby making host markets uncompetitive. The costs emanate from the poor quality of local content and the poor capacity of local labor and may also prevent firms from sourcing more advanced technology. For instance, experience with IBRD lending projects indicates that provisions that mandate at least 20 percent local content in public procurement lead to adverse outcomes in procurements intended to improve or upgrade technology levels, as newer technologies may not be available in the local market.

While hiring local labor and using local content is one way BRI-partner countries can ensure positive spillovers from this initiative, the quality of such domestic resources has a direct bearing on the viability and sustainability of such large infrastructure projects. It is thus in the best interests of the economies in the region to continue improving the quality of their resources.

Countries in the South Asian region have some form of local content requirements, either in law or in practice, especially in public procurement. In India, for instance, local content requirements have become significant in the wake of efforts to promote the “Make in India” campaign, as it has accompanied efforts to liberalize FDI in certain sectors. The requirements most famously delayed a major retail investment by Apple in 2016. A review by the European Center for International Political Economy (2018) found that India had the world’s highest number of local content requirements, approaching the number imposed by the rest of the world combined. In an attempt to protect Indian MSMEs from the economic downturn emanating from the Covid-19 crisis and to create assured demand for their goods and services, the government amended the General Financial Rules (GFR) in April 2020 to disallow global tender enquiries. Similarly, Article 7 of the Procurement Law in Afghanistan requires entities to prefer procurement of domestic products in accordance with bidding documents, provided that their value in comparison with foreign sources does not exceed the limits prescribed by the procurement rules of procedure.

Nepali law contains no provisions for local content requirements, except for the retail banking sector (where Nepal was allowed to continue with local content requirements for foreign investment under Nepal’s WTO accession commitments). To establish business in the country, however, local experts report that foreign investors in Nepal are encouraged to use locally produced inputs and to hire local staff.

Pakistan’s laws also contain no provisions setting forth local content requirements. Although foreign investors are not legally required to use locally produced inputs, they are encouraged to do so. Similarly, despite lack of explicit regulatory requirements to hire Pakistani nationals, either as laborers or as representatives on boards of directors, as per feedback received from local experts, foreign investors are implicitly encouraged to do so in order to establish business in the country.

Foreign investors in Sri Lanka are encouraged to use locally produced inputs. According to respondents’ feedback, for investors approved under the Board of Investment, certain goods set out in the negative list are required to be sourced in Sri Lanka. While the required proportion of local inputs to total inputs varies, according to some experts’ estimates “it may amount to 30 percent.” In addition, public tenders or open bids may have their own set of requirements. Foreign investors are also implicitly encouraged to hire local staff when establishing business in the country. Nonetheless, in an effort to reduce obstacles to FDI, the Sri Lankan authorities have recently taken steps such as simplifying and introducing online processing of business visas for foreign firms.

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Meanwhile, in Bangladesh, employment of foreign nationals in an industrial undertaking (as defined in the National Industry Policy 2016) shall not exceed a local to foreign ratio of 10 to 1 during the initial stage of the investment project, and 20 to 1 during the operational stage of the project. Similarly, foreign nationals in a commercial (branch, representative/liaison) office shall not exceed the ratio of 5 to 1 (including the top manager) during the initial stage, and 10 to 1 during the operational stage. Feedback from respondents corroborates that companies bidding on government procurement tenders are often informally encouraged to have a local partner and to produce or assemble a percentage of their products in country.

In Afghanistan, foreign investors are encouraged to use locally produced inputs and to hire local employees. Pursuant to Article 7 of the country’s Procurement Law, domestic firms and domestic products, Afghanistan-based foreign companies and foreign firms in a joint venture with local firms, all get explicit and well-defined preferences in matters of public procurement vis-à-vis all other foreign firms based outside Afghanistan. Also, while there is a preference for hiring local employees, and foreign investors are encouraged to hire local staff, no legal provisions allow employing foreign nationals.

### 3.3.2 Currency repatriation

The ease of converting and transferring currency is one of the critical and decisive factors for foreign investors to invest into a country. The ease of transferring capital into and out of a country ranked as the seventh (out of 19) most important factor impacting firms’ investment decisions (A.T. Kearney FDI Confidence Index 2019). According to the MIGA survey of senior executives from multinational enterprises investing in developing countries, 37 percent of respondents identified transfer and convertibility restrictions as of greatest concern to their companies when investing in emerging economies in the next twelve months period (MIGA 2014). Naturally then, these are also likely to major determinants in BRI-investors’ decisions to partner with the region’s countries.

Research suggests that capital control policies on FDI, inter alia, the existence of multiple exchange rates for capital account transactions; controls on capital account, and the stringency of requirements for the repatriation and surrender of export proceeds deter FDI (Reinhardt et al. 2010; Asiedu and Lien 2004). Assured repatriation of profits on par with rationalization of internal legal frameworks, simplified rules for investors, and improved functioning of the banking and services sector are important factors that improve FDI inflows for all markets (Jaiblai and Shenai 2019).

Why do countries impose restrictions? The primary reason is to prevent massive capital outflows and protect weak balance of payments positions (Leckow and Strauss 2010). If a country has limited foreign exchange reserves, it may try to direct the existing foreign exchange toward economic transactions it considers vital. Macroeconomic and prudential policy goals motivate controls specifically on capital flows, such as to reduce the volatility of short-term capital flows or to protect underdeveloped financial markets (Johnston and Tamirisa 1998). Countries may also impose controls during economic crises to prevent capital flight.

In South Asia, currency convertibility and repatriation are highly regulated across the region’s countries, although the nature and form of the regulation differs by country. India does not yet have full capital account convertibility. Foreign capital invested in India is generally allowed to be repatriated along with capital appreciation, if any, after payment of the taxes due (Ernst & Young 2019). Current account transactions such as dividends, import of goods, and consultancy services are repatriable except when

32. [http://bida.gov.bd/?page_id=5495](http://bida.gov.bd/?page_id=5495)
33. According to Article 6 (titled “Employment Restriction”) of the Regulation on Hiring of Foreign Nationals in Afghanistan Entities, 2005 (“Regulation on Hiring of Foreign National”), “In the case where both local and foreign employees are present, the local employees shall be given preference.”
the investment is made or held on a nonrepatriation basis. Similarly, for remittances India’s Schedule III of FEM (CAT) Amendment Rules (2015) provides the following facilities, among others, to companies and entities other than individuals: remittances up to US$10,000,000 per project for any consultancy services for infrastructure projects and US$1,000,000 per project for other consultancy services procured from outside India; remittances up to 5 percent of investment brought into India or US$100,000, whichever is less, by an entity in India by way of reimbursement of preincorporation expenses, and so on.34

In the case of Sri Lanka, under Directions No. 01 of 2017 issued under the Foreign Exchange Act, authorized dealers are permitted to release foreign exchange without restriction for current transactions after satisfying themselves regarding that the requests are bona fide and verified. Current transactions include payment for goods and services, payment of interest on loans, payment of fees, brokerage, and so on. With regard to capital transactions such as proceeds from a sale of investment assets (i.e., shares, debentures, etc.), proceeds from sales of land, and repayment of loans, the relevant amounts can be freely repatriated as long as the original investment/lending was made through monies remitted via the Inward Investment Account (IIA) of the investor/lender. In the event the original investment/loan was not remitted through an IIA, the repatriation requires the approval of the Central Bank of Sri Lanka.

Meanwhile, according to the World Bank Enterprise Surveys, currency repatriation is the most highly restricted in Pakistan due to the country’s depleting foreign exchange reserves. Despite the country’s liberal investment policy, repatriation of profits overseas by multinational companies has also become a problem in Pakistan. Under the country’s Foreign Exchange Manual, the State Bank of Pakistan prescribes certain channels of investment having general permission to repatriate funds. In the event that investment is not made under the prescribed channels, however, special permission from the State Bank of Pakistan is required to repatriate funds. Moreover, pursuant to the Foreign Exchange Regulation Act 1947, no person in, or resident in, Pakistan is allowed to make any payment to or for the credit of any person resident outside Pakistan. Unless the State Bank of Pakistan issues a general permission with respect to currency repatriation, special permission is required to be sought from the State Bank of Pakistan prior to such repatriation, and it is difficult to in practice to obtain it, given the country’s depleting foreign exchange reserves.

3.4 Governance, policy capture, and corruption

“Governance is generally defined as the traditions and institutions by which authority in a country is exercised, and includes the process by which governments are selected, monitored, and replaced; the capacity of the government to effectively formulate and implement sound policies; and the respect of citizens and the state for the institutions that govern economic and social interactions among them” (Schou-Zibell and Madhur, 2010). The importance of regulatory governance and institutional quality for economic development is already well-recognized in the development literature. The role of institutions is also about the government’s attitude toward markets and freedoms and the efficiency of its operations. Excessive bureaucracy and red tape, overregulation, corruption, dishonesty in dealing with public contracts, lack of transparency and trustworthiness, and the political dependence of the judicial system all impose significant economic costs on doing business, including in the context of BRI-engagement of countries in the region. Proper management of public finances is also crucial to ensuring trust in the national business environment.

South Asia’s rankings on the World Bank’s World Governance Indicators suggest that Sri Lanka and India are the best performers, while Afghanistan is the worst by far. The remaining three countries are also below the regional average, which suggests ample scope for improvement in these countries. Political stability, in particular, is a major challenge in both Afghanistan and Pakistan, and worrisome even in India, which fares well below Sri Lanka and even Nepal along this dimension.

Table 4: Different attributes of the World Governance Indicator in South Asia

<table>
<thead>
<tr>
<th>WGI (Percentile Rank)</th>
<th>Political stability</th>
<th>Government Effectiveness</th>
<th>Regulatory Quality</th>
<th>Rule of Law</th>
<th>Control of Corruption</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>Afghanistan</td>
<td>0.48</td>
<td>7.69</td>
<td>10.58</td>
<td>4.33</td>
<td>4.33</td>
<td>5.48</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>13.81</td>
<td>21.63</td>
<td>18.75</td>
<td>27.88</td>
<td>16.83</td>
<td>19.78</td>
</tr>
<tr>
<td>India</td>
<td>14.29</td>
<td>63.94</td>
<td>44.23</td>
<td>55.29</td>
<td>49.52</td>
<td>45.45</td>
</tr>
<tr>
<td>Sri Lanka</td>
<td>40.95</td>
<td>45.19</td>
<td>47.60</td>
<td>55.77</td>
<td>43.27</td>
<td>46.56</td>
</tr>
<tr>
<td>Nepal</td>
<td>24.76</td>
<td>16.83</td>
<td>23.56</td>
<td>33.65</td>
<td>27.40</td>
<td>25.24</td>
</tr>
</tbody>
</table>

Source: Kauffmann et al. (2011); authors’ compilation.

The World Bank’s Global Indicators of Regulatory Governance (GIRG) compare the quality of regulatory governance in 187 countries on the basis of six attributes: transparency of rulemaking; public consultation in rulemaking; impact assessment; accessing laws and regulations; ex-post review; and challenging regulations.

Where citizens know the rules that govern their society and have a role in shaping them, they are more likely to comply with those rules. Corruption is lower and the quality of regulation is higher. Thus, transparency is important. Citizen access to the government rulemaking process is also central for fostering trust in the state and ultimate adherence to the new regulations. It is also a key part of business environments in which investors make long-range plans and investments. Greater levels of consultation are associated with a higher quality of regulation.

How governments assess the possible impact of new regulations on social, environmental, and economic factors in their country affects the shape and scope of each regulation. Unfortunately, impact assessment practices are insufficient and inconsistent in many countries around the world, including in this region, where they are absent in all the six countries. Free and easy access to the laws and regulations governing society is a precondition for the rule of law and for avoiding uncertainty and minimizing corruption, both of which harm investment. This is the only attribute of the GIRG where all six countries in this region perform well.

It is also imperative to keep regulations up to date and to ensure that they remain relevant to local businesses and investors alike. Thus, opportunities for ex-post review are an important ingredient of good regulatory governance; significantly, however, only Afghanistan and Nepal in this region provide such opportunities, and even in these two countries, they remain limited.

Finally, the ability to challenge regulations after they are passed is a key component of a healthy regulatory system. This avenue for redress is particularly important for investors, as it boosts confidence if they can see an opportunity to reverse perceived discriminatory regulations. Only Bangladesh, India, and Pakistan provide such opportunities in the region, and even in these countries, the avenues are limited.

In the South Asian region, India performs the best on four of these six attributes, especially in providing access to laws and regulations, followed by Pakistan and Bangladesh (see Figure 12). In contrast, Afghanistan, Nepal, and Sri Lanka fare poorly, completely failing to provide opportunities for public consultation in rulemaking, regulatory impact assessments, and challenging regulations. Afghanistan even fails to ensure that rulemaking is transparent, while Sri Lanka fails to provide opportunities for ex-post review. The assessment is also corroborated by feedback received from respondents (see Box 5 for details).
Box 5: Shortcomings in regulatory governance in South Asia

INDIA
“Rules and regulations being announced without prior notice, consultation or impact assessments are a major obstacle for doing business.”

SRI LANKA
“All laws and regulations are publicly accessible; however, the decision-making process may sometimes be considered opaque. Overall the Government regulatory structure still needs to be reformed to become business friendly.”

“The government rarely informs businesses whether their comments were incorporated and never provides reasons why their inputs were not incorporated.”

BANGLADESH
“Transparency and predictability of rules and regulations is a serious problem in Bangladesh.”

“It is difficult to access information on business regulation, because there are multiple laws and regulations, [and] they are all published on different websites. Businesses do not even know where exactly to look for the specific requirements. There is no integrated portal.”

“Rules and regulations are often announced without prior notice, consultation or impact assessments. Consultations, if held, are not inclusive and are dominated by powerful businesses. The government rarely informs businesses whether their comments were incorporated and never provides reasons why their inputs were not incorporated.”

PAKISTAN
“Ambiguity of rules and regulations is a key problem.”

Source: Feedback received from survey respondents.

Figure 12. Global Indicators of Regulatory Governance in South Asia

Source: World Bank Global Indicators of Regulatory Governance (GIRG); authors’ calculations.
Note: Each GIRG attribute ranges from 0 (no opportunity, all “no” in the GIRG database) to 1 (full opportunity, all “yes” in the GIRG database); thus, each stacked bar in this figure ranges from 0 to 6.
3.4.1 Corruption

Weak and ineffective control of corruption can deter businesses and obstruct foreign investment from (mostly developed) economies with strict anticorruption laws. Awareness of the economic and social costs of corrupt business practices has increased sharply in recent years. The detrimental impact of corruption on the economy is well-documented in the literature. Research suggests that corruption is costly for economic development (Shleifer and Vishny 1993) and is always harmful for entrepreneurship (Dutta and Sobel 2016). Other studies find that corruption lowers investment, thereby reducing economic growth (Mauro 1995) and has a statistically significant negative impact on GDP per capita (Mustapha 2014).

With the exception of Sri Lanka, corruption has been identified as a major impediment to the operation and growth of businesses in South Asia in various World Bank Enterprise Surveys, with Afghanistan and Bangladesh in particular being the worst performers in the region. In fact, corruption has been identified by firms in India as their biggest obstacle; as the second biggest obstacle by firms in Afghanistan and Pakistan; and as the fourth biggest obstacle in Bangladesh. Medium-sized firms (defined as those between 20 and 29 employees) face the brunt of this corruption in India, Nepal, and Pakistan, compared to large firms (with more than 100 employees) in the remaining three South Asian countries studied in this report. With the exception of India, the findings of the Transparency International’s Corruption Perception Index corroborate the findings of the Enterprise Surveys on corruption, enlisting Bangladesh and Afghanistan as the worst performers. Allegations of corruption in the award of BRI-contracts (for instance, see Ghossein, Hoekman, and Shingal 2018) may be a negative spill-over of this initiative and suggest that countries in the region would do well to cure their vulnerability along this dimension.

Feedback from respondents has also identified corruption as widely prevalent in Nepal. Lack of clarity and abuse of discretion is reported to lead to harassment in Bangladesh, with public servants in both Afghanistan and Bangladesh reported as requesting gifts/tips/ bribes and so on in the following activities: operating licenses, inspection requirements, public procurement, access to infrastructure, construction permits, paying taxes, registering property, and facilitating judicial procedures (see Box 6 for details). According to the Enterprise Surveys, the percent of firms that expect to give gifts to public officials to “get things done” range from 13.7 percent in Sri Lanka to 48.5 percent in Bangladesh (see Figure 13).

**Box 6: Corruption in South Asia**

**NEPAL**

“Corruption has been found prevalent in all the [trade] corridors. The issue of informal payments and extortion needs serious attention from policymakers.”

**BANGLADESH**

“Public servants request payment like gifts/tips/ bribes, etc., when requesting operating licenses, inspection requirements, public procurement, access to infrastructure, construction permits, paying taxes, registering property, and payments to facilitate judicial procedures.”

**AFGHANISTAN**

“Businesses feel obliged to give payments like tips/gifts/bribes, etc., when interacting with a range of government officials, i.e., in the course of complying with inspections, obtaining public procurement contracts, access to infrastructure services, paying taxes, registering land/real property, and enforcing contracts.”

**PAKISTAN**

“Businesses feel obliged to give payments like tips/gifts/bribes, etc., when complying with inspections’ requirements and other requirements (customs clearances, etc.); access to infrastructure services (including electricity, water, etc.); paying taxes; registering land/real property.”
SRI LANKA
“Businesses feel obliged to give payments like tips/gifts/bribes, etc., when interacting with a range of government officials, i.e., in the course of obtaining various licenses and permits, complying with inspections’ requirements and other requirements (customs clearances, etc.), obtaining public procurement contracts, getting infrastructure services (including electricity, water, etc.), paying taxes, registering land and enforcing contracts.”

INDIA
“Businesses feel obliged to give payments like tips/gifts/bribes, etc., when getting various licenses and permits (operating licenses, construction permits, etc.) and complying with inspections’ requirements and other requirements (customs clearances, etc.) and registering land. However, due to digitization and standardization of processes and documents, CCTV operated premises, Central and state vigilance commission, the corruption is reducing dramatically.”

Source: Feedback received from survey respondents.

Figure 13. Percent of firms expected to give gifts to public officials “to get things done”


On the World Bank Enterprise Surveys’ Bribery Incidence Index, the percent of firms experiencing at least one bribe payment request while soliciting six different public services, permits, or licenses was nearly twice the regional average in Bangladesh and Afghanistan and lowest in Sri Lanka (see Figure 14). That said, South Asia seems to perform slightly better than the comparator East Asia and Pacific on this index.

Meanwhile, on Transparency International’s Corruption Perception Index, India is the best performer in the region, with a ranking of 78 out of 180 countries in 2018, followed by Sri Lanka (89), Pakistan (117), Nepal (124), Bangladesh (149), and Afghanistan (172). Figure 15 suggests that, except for Bangladesh, the perceived levels of public sector corruption have reduced over time in countries in this region. That said, the absolute score of Bangladesh on this index improved marginally from 25 to 26 since 2015, which suggests that Bangladesh’s worsening rank is largely associated with other countries undertaking more significant efforts to combat corruption compared to Bangladesh.
Figure 14. Bribery incidence


Figure 15. Perception of corruption in South Asia countries over time

Note: CPI rankings range from 1 to 180, with 1 representing the highest performance and 180 the lowest.
Predictability is one of the cornerstones of a well-functioning business regulatory environment. Regulatory predictability allows businesses to know, anticipate, and comply with the rules that affect their day-to-day operations. Effective predictability and transparency of the rulemaking and decision-making processes includes use of robust evidence. Elite capture of the rulemaking process and of implementing the law can impede regulatory predictability.

Policy and regulatory predictability have significant implications for firms’ risk management, over and above increased costs of doing business. A recent global survey of more than 700 international business executives identified “policy and regulatory unpredictability” as the second most important investment climate factor (World Bank 2017 and 2018). This includes transparency and predictability in the conduct of government agencies as firms look not only at policies on paper but also at implementation and administration of those policies. In its 22nd Annual Global CEO Survey, PricewaterhouseCoopers found that CEOs’ top-of-mind threats are less existential but rather relate most closely to the cost of doing business, with overregulation and policy uncertainty and unpredictability topping the list of concerns. At the country level, in a recent internal survey on regulatory unpredictability in Bangladesh, about 70 percent of businesses (mostly local) cited discretionary behavior of regulatory officials and inconsistency in the legal framework as major problems (Ali, Grava, and Reaz 2019).

Another perspective on regulatory uncertainty is provided by data on the variations in regulatory service delivery quality. The WBG’s Enterprise Surveys contain data not only on the average burden (such as time or cost) in dealing with various regulatory interfaces in the surveyed countries but also the variations within the countries. Such variations in the regulatory experience of firms can be a good indicator of implementation gaps because policies, laws, or regulations, if well implemented, should result in reasonably uniform experiences across firms after accounting for firm-specific factors. A large variation could also indicate the presence of regulatory unpredictability because businesses would find it difficult to predict their experience with a regulatory interface.

The Enterprise Surveys provide such data for a number of regulatory interfaces, such as obtaining a construction permit, an import license, and an export license. Figure 16 points to a wide variation across firms in the time taken to obtain these permits. For example, in both Sri Lanka and Bangladesh, the median time to obtain a construction permit is 30 days and the 25th percentile of firms obtains one in less than 15 days. It takes as long as 90 days, however, for the 75th percentile of firms to obtain a construction permit in both countries. The huge difference of around 75 days between a 25th and a 75th percentile firm suggests considerable uncertainty about the time that may be required to obtain a construction permit in Sri Lanka and Bangladesh. Similarly, a large variation in reported time estimates to obtain a construction permit is observed in Afghanistan: there the median time is 60 days, and the 25th percentile firms obtain construction permits within 23 days; the 75th percentile firms spend over 140 days to do so.

36. Note that the study draws on both Doing Business and Enterprise Survey data and that there are instances where results may vary for the same measure (e.g., “time to get a construction permit”).
Variations in reported estimates are observed for two other important regulatory interfaces, i.e., obtaining an import license and obtaining an operating license. For instance, in Bangladesh, the number of days the 75th percentile firm must wait to obtain an operating license is almost three times that of the median firm (60 days compared to 21 days). The difference is even more striking when comparing the 25th percentile firm and the 75th percentile firm (1 day versus 60 days). For an import license, the largest variation in estimates reported by the 25th percentile firm and the 75th percentile firm is observed in India (28 days difference), followed by Sri Lanka (20 days difference).

Observed variations in time may indicate lower levels of regulatory predictability, which in turn may adversely impact investment decisions: uncertainty surrounding investment regulations in a particular country may discourage investors from investing in the market and divert their attention to more secure and predictable destinations. Lower levels of investment, in turn, negatively impact private sector development and job creation.

For example, private sector experts in Bangladesh reported that “it is difficult to find business regulations, because there are multiple laws and regulations; they are all published on different websites. Businesses do not even know where exactly to look for the specific requirements. There is no integrated portal.” Also, in a recent survey on regulatory unpredictability in Bangladesh, about 70 percent of businesses (mostly local) cited discretionary behavior of regulatory officials and inconsistency in the application of legal framework as major problems, a key structural reform challenge common in the region beyond Bangladesh.

Note: The graph is based on the minimum reported time (the 0.25 quantile) and the maximum reported time (the 0.75 quantile). The graph excludes outliers and, thus, in most cases maximum reported time is not featured.
3.5 Corporate taxation

One straightforward illustration of the quality of governance is the quality of the tax system. Efficient tax systems tend to have simpler arrangements, with straightforward compliance procedures and clear laws. Transparency in tax collection and absence of discretion can help secure the trust of businesses regarding paying taxes, contributing to both growth and equality. Tax systems can also include incentives for establishing small- and medium-sized enterprises or businesses geared toward research and development (World Bank 2009b). Ample evidence suggests that countries with excessively burdensome tax systems generate perverse incentives resulting in widespread tax evasion, informality, and low levels of revenue collection. Most entrepreneurs in this region, with the exception of Bangladesh, have identified this informality as a grave concern in various World Bank Enterprise Surveys.

Simple, moderate tax rates also provide greater incentives for businesses to pay taxes. Research shows that the rate of taxation is negatively correlated with firm growth (Fisman and Svensson, 2007) and discourages firm entry (Belitski, Chowdhury, and Desai 2016). Similarly, tax complexity is found to significantly hinder the presence of FDI for a country pair (Lawless 2013). Further, evidence from Pakistan suggests that in response to the increased tax rate, firms significantly reduce earnings, move to the informal sector, and change company form (Waseem 2018).

In fact, tax rates remain a big challenge for businesses in South Asia, with close to 30 percent of firms identifying tax rates as a major constraint (Enterprise Surveys). While 54 and 46 percent of firms in Pakistan and Afghanistan, respectively, identify tax rates as a major constraint, 24 and 27 percent of firms in India and Sri Lanka do so. Interestingly, the share is even lower in Nepal and Bangladesh, where only 11 and 7 percent of firms, respectively, consider tax rates to be a major constraint for their businesses.

According to feedback received from respondents (see Box 7), inefficiency and corruption in tax administration are also pervasive problems in the South Asian region, and both are likely to deter firms’ participation in BRI projects. Figure 17, sourced from the World Bank Doing Business 2020 data for the year 2018–19, shows two elements of the tax administration system: the number of payments, and the time required in hours per year to prepare, file, and pay three major types of taxes and contributions—the corporate income tax, value added or sales tax, and labor taxes, including payroll taxes and social contributions. At 11, the number of payments required to pay these three taxes is the least in India, well below the regional average of 29.8. All other countries, except Afghanistan, fare much worse than the average for South Asia on this measure, with Nepal being the worst performer. In contrast, the time required to pay these taxes ranges from a minimum of 129 hours in Sri Lanka to a maximum of 435 hours in Bangladesh, against the South Asian average of 291 hours. This heterogeneity is also reflected in the performance of these countries on the Doing Business ranking in Paying Taxes, where India is the best performer in the region, although still ranked 115 out of 190 countries in the year 2018–2019, followed by Sri Lanka (142), Bangladesh (151), Pakistan (161), Nepal (175), and Afghanistan (178). Significantly, the comparator East Asia and Pacific performs much better than the South Asian countries on both measures depicted in Figure 17, suggesting enough scope for improvement in the latter.

Furthermore, for all countries in South Asia, their score on the DB “post-filing index” is below 50 /100; India and Sri Lanka have the highest scores at 49 points, while Afghanistan and Pakistan have the lowest, scoring 0 and 10 points, respectively. In Afghanistan, for instance, it requires 111 hours to comply with a corporate income tax correction, while the required time in Sri Lanka is only 3 hours (Doing Business 2020 report).
Box 7: Inefficiency and corruption in taxation in South Asia

NEPAL
“Taxes are either not paid timely or for long time.”

AFGHANISTAN
“Regular taxes are easy to be paid, but the audit department is corrupt; when it comes to audit, they usually create problems for everyone, as most of the officials are just after bribes, and one cannot defend their rights as all government and judiciary are corrupt. Government is just hurting businesses.”

PAKISTAN
“Paying taxes is a serious problem.”

“Yes, there is red tape and wide discretion of officials in the area of paying taxes.”

SRI LANKA
“There are some administrative bottlenecks at the Inland Revenue Department. Further, whereas national taxes can be paid online, subnational taxes still have to be paid manually.”

Source: Feedback received from survey respondents.

Figure 17. Measures of tax administration

![Bar chart](chart.png)

- Time required to pay three major taxes (hours)
- No. of payments required to pay three major taxes


According to the World Bank Enterprise Surveys, 19.4 percent of firms in South Asia identified the tax administration in their respective economies as a major business constraint. This ranges from as little as 9.2 and 10.8 percent of firms in Nepal and Sri Lanka, respectively, to as high as 34.1 and 39.1 percent in Pakistan and Afghanistan, respectively. Similarly, over 60 percent of South Asian firms were visited or were required to meet with the tax officials. While this was the case in close to 65 percent of firms in Pakistan and Nepal and 80 percent of firms in Afghanistan, only 35.3 percent firms in India were visited or were required to meet with tax officials. In Sri Lanka the figure was 54.3 percent.
The recent past has seen various changes in some of these countries. India, in July 2017, introduced a Goods and Services Tax (GST),37 replacing some 20 consumption taxes charged by the central government and states and doing away with the VAT, for example, and Sri Lanka has a system for paying national taxes online. Most tax administration systems, however, remain inefficient and prone to bureaucratic discretion and corruption. Certain sectors in particular feel the brunt of the taxation system and consider tax administration to be a major constraint; for instance, 88 percent of the motor vehicle firms in Pakistan and 29 percent of textiles firms in India have offered these assessments. Feedback from respondents identified the major problems in Pakistan’s taxation system as red tape, tax officials’ wide discretion, and corruption.

In terms of corruption in tax administration, one in five South Asian firms are expected to provide gifts when meeting with tax officials. In Afghanistan, Bangladesh, and Pakistan, 34, 41, and 29 percent of firms, respectively, are expected to give gifts, although this figure was only 7.7 percent in Sri Lanka.

3.6 Government procurement

Government procurement gives the state considerable influence over the allocation of resources in market economies. Trionfetti (2000) estimates that contestable government procurement markets account for 7 to 9 percent of GDP in developed countries. Estimates by the OECD (2017) suggest that government procurement accounts between 9 and 20 percent of GDP in developing countries.

A prominent aspect of such procurement is the preference for domestic over foreign firms in the award of public contracts, despite cost and quality considerations (Shingal 2011, 2015). This “home bias” in public purchase decisions has nontrivial efficiency effects. A home bias can reduce trade flows and influence international specialization, especially in sectors where public demand is large relative to domestic output and characterized by monopolistic competition and increasing returns to scale (Trionfetti 2000).

On average, public procurement makes up about 14.5 percent of GDP, with countries such as Eritrea and Angola going as high as 33 percent and 26 percent, respectively (Djankov et al. 2017). Across regions, South Asia has the highest share of public procurement in GDP, at 19.3 percent, followed by sub-Saharan Africa at 14.9 percent. India procures 20 percent of its GDP publicly, Pakistan 19.8 percent (Djankov, Islam, and Saliola 2016). In Nepal, according to some estimates, almost 20 percent of the GDP and 60 to 70 percent of the yearly budget is expended through government procurement (PPMO 2017),38 while in Sri Lanka, around a quarter of government expenditure is spent on public procurement, accounting for almost 15 percent of GDP.39

South Asian countries show considerable heterogeneity on this point, as seen in the World Bank Benchmarking Public Procurement (2017) data reported in Table 5. For instance, on needs assessment, call for tender, and bid preparation, Nepal performs the best in the region, followed by India, while Sri Lanka is the worst performer.40 Bangladesh and Nepal fare the best in terms of bid opening, evaluation, and award, while Afghanistan performs the worst.41 The countries seem relatively less heterogeneous, however, when it comes to the content and management of procurement contracts.

37. While the introduction of GST has assisted in creating a common experience for businesses across the country, GST rates have not yet stabilized, and the government is attempting to bring down the number of GST slabs from six to three. Several key goods, including petroleum, are still not covered by GST. The government has innovated with automation on returns filing and payment of both corporate income tax and GST, however, and the process is smooth, easy, and fast.
40. The poor quality of Sri Lanka’s needs assessment, call for tender, and bid preparation processes emanates from the absence of any consultation between procuring entities and the private sector, for needs assessment, and from the absence of any internal market guidelines during market research.
41. In Afghanistan, bid opening does not take place immediately, and the process is never electronic. Unsuccessful bidders are not notified of the results, although they can request and receive explanations for why their bids were not selected.
Table 5: Performance of South Asia countries on World Bank Benchmarking Public Procurement indicators (2017)

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Afghanistan</th>
<th>Bangladesh</th>
<th>India</th>
<th>Nepal</th>
<th>Pakistan</th>
<th>Sri Lanka</th>
</tr>
</thead>
<tbody>
<tr>
<td>Needs assessment, call for tender and bid preparation</td>
<td>56</td>
<td>60</td>
<td>63</td>
<td>72</td>
<td>58</td>
<td>40</td>
</tr>
<tr>
<td>Bid submission</td>
<td>83</td>
<td>75</td>
<td>75</td>
<td>61</td>
<td>44</td>
<td>69</td>
</tr>
<tr>
<td>Bid opening, evaluation and award</td>
<td>43</td>
<td>71</td>
<td>50</td>
<td>71</td>
<td>57</td>
<td>57</td>
</tr>
<tr>
<td>Content and management of procurement contract</td>
<td>73</td>
<td>73</td>
<td>68</td>
<td>73</td>
<td>59</td>
<td>59</td>
</tr>
<tr>
<td>Performance guarantees</td>
<td>74</td>
<td>30</td>
<td>54</td>
<td>30</td>
<td>30</td>
<td>30</td>
</tr>
<tr>
<td>Payment of suppliers</td>
<td>33</td>
<td>42</td>
<td>59</td>
<td>67</td>
<td>67</td>
<td>7</td>
</tr>
</tbody>
</table>


While open tendering is the default method of procurement in these countries, they also resort to limited and selective tendering as well as direct procurement, depending on the value and type of the good/service to be procured. Foreign participation in the procurement process is not prohibited, although there may be a de facto requirement to use local inputs and local labor as well as a de jure preference for domestic suppliers, mostly taking the form of price preferences. Corruption has also been identified as a major feature of the procurement process globally. In fact, 27.4 percent of firms globally were expected to give gifts to secure government contracts (Enterprise Surveys 2009–19). Across the region, 46.9 percent in Afghanistan, 48.9 percent in Bangladesh, 39.8 percent in India, 64.5 percent of firms in Nepal, 88.2 percent in Pakistan and 29.8 percent in Sri Lanka, are expected to pay bribes for securing government contracts. This assessment is corroborated by feedback from respondents. In Afghanistan, Bangladesh, and Pakistan, survey respondents have clearly mentioned the need to bribe public entities in matters of government procurement. Meanwhile, discretionary treatment in the area of public procurement and payment for public procurement contracts has been identified as a major issue by respondents in India, and lack of transparency by respondents in Sri Lanka (see Box 8 for details).

Box 8: Challenges in public procurement in South Asia

INDIA
“In the areas of public procurement contracts and payment for public procurement contracts discretionary treatment is observed.”

AFGHANISTAN
“Public Procurement (government tenders) is a serious problem.”
“Businesses feel obliged to give payments, like tips/gifts/bribes, when obtaining public contracts with government entities (public procurement).”
E-procurement is now a feature of modern, transparent, and efficient tendering systems. Through the introduction of e-GP, processes are standardized, streamlined, and integrated, and associated processing times and administrative costs are consequently reduced (World Bank Benchmarking Public Procurement 2017; Casaki and P. Gelleri 2005).

E-procurement can also improve transparency and governance of procurement practices by limiting political interference and in-person interaction and by encouraging new suppliers to participate in public tenders. By conducting the procurement process online, procuring authorities are compelled to execute tenders in line with legislation while, in parallel, enabling any interested party to monitor public procurement proceedings and results. As the information is available online (ideally in real time), it can be accessed by bidders, other departments of the government itself (auditing bodies, oversight agencies, government officials), and even members of the public not directly involved in the procurement process.

While Pakistan has a dedicated e-procurement portal in place, it is underutilized, that is, no electronic bid submission, bid opening, or signing of contracts is available. This indicates that the existing portals are primarily informational (used mainly to access tender information and award decisions); it would thus be beneficial to make these portals transactional in nature. In contrast in India, since 2012, all central and state government and SOE contracts above a certain minimum threshold are required to be tendered electronically. Facilities for e-procurement do not seem to be available in the remaining countries in the region, or, if they exist, they are only informational.

The analysis in Ghossein, Hoekman, and Shingal (2018) shows that procurement practices used for many BRI projects appear often to fall short of both national laws and procurement regulations of BRI host countries, the provisions on procurement that some BRI countries have made in their preferential trade agreements (PTAs), and international standards of transparency and good procurement practice embodied in the WTO plurilateral Agreement on Government Procurement (the GPA). This increases the likelihood that contracts are not awarded to the firms best positioned to attain at lowest cost the technical and performance requirements associated with a given project. It also raises potential concerns regarding the integrity of procurement processes and the projects’ financial viability.

Moving toward adoption of internationally accepted good procurement practices would help address such concerns, benefitting both China and the BRI partners. Both China and the BRI partner countries, including those in South Asia, can take steps to apply and enforce domestic procurement regulations to BRI projects and to strengthen these in areas where gaps now exist (as documented, for example, by the World Bank benchmarking procurement exercise). Joining the GPA and using PTAs more effectively are further complementary channels to help improve BRI procurement processes.
3.7. Dispute settlement

Efficient contract enforcement allows firms to enter into agreements for new financing, suppliers, and customers. Still, courts are slow and inefficient in many countries and tend to involve excessive (or illegal) administrative costs to resolve disputes. These factors are frequently cited as major impediments to investment and business operation. Economies with weak contract enforcement and unstable institutions tend to have low investment rates and slower growth. For example, Gianfreda and Vallanti (2017) find a detrimental impact of court delays on labor productivity. In contrast, countries with legal systems that enforce contracts and protect creditors’ rights tend to be more financially developed, with better developed capital markets that can translate savings into productive investment. Chakraborty (2016) demonstrates a significant positive impact of judicial quality on a firm’s performance.

Contract enforcement is poor across South Asian countries, however, being among the slowest globally. Respondents pointed out lengthy and opaque dispute settlement practices across the countries covered. Either no laws set overall time standards for key court events in a civil case and the law does not regulate the maximum number of adjournments that can be granted, as in Afghanistan and Sri Lanka, or where the law does set overall time standards for key court events in a civil case and regulates the maximum number of adjournments that can be granted, these limits are not respected in more than 50 percent of the cases, as in Bangladesh, India, Nepal, and Pakistan. Additionally, no electronic case management tools are found across countries in the region, and the courts do not use electronic information systems.

In Pakistan and Sri Lanka, no specialized grievance mechanism is available for investors seeking to lodge a complaint against a government decision or action, leaving as the only recourse instituting an action in court. Also, no institutional mechanism addresses issues between investors and the state prior to their escalation into formal legal disputes. The lack of effective grievance mechanisms is a major obstacle for businesses in Afghanistan, Bangladesh, and Pakistan, according to respondents’ feedback.

Moreover, in Afghanistan, Nepal, and Pakistan, local courts and arbitration are not considered fair and effective in resolving disputes between investors and the state government (federal/subnational agencies or SOEs). In Sri Lanka, respondents mention that domestic arbitration fora lack the expertise to arbitrate on matters involving international arbitration rules, such as LCIA Arbitration Rules, ICC Arbitration Rules, or the UNCITRAL Arbitration Rules. Notably, these arbitration rules are those most resorted to for contracts involving foreign parties in, among others, BRI projects.

Across all South Asian countries, feedback from respondents also corroborated that current grievance systems remain inadequate to address business needs. In Bangladesh, experts reported that the court system is marred by delays, and it may take from three to five years to obtain a decision or judgement on the complaint. Similarly, experts in Sri Lanka mention that courts are “overworked” and cases may be delayed for long periods of time, with a judgement taking four to five years or even longer (see Box 9 for details).

Box 9: Problems in dispute settlement in South Asia

AFGHANISTAN
“Local courts are not considered fair and effective in resolving disputes between investors and the state government (federal/subnational agencies or SOEs).”
“Lack of effective grievance mechanisms is a major obstacle for doing business.”
“Private sector would benefit from effective grievance system.”

BANGLADESH
“Bangladeshi court system is marred with delays. To my opinion, it takes not less than three to five years to obtain a decision or judgement on the complaint.”
“Even where grievance mechanisms exist, government officials do not follow up on the complaints. And even where they follow up, businesses are not informed about the rationale for the action taken.”

SRI LANKA
“The conclusion of actions filed in courts could typically take one to five years.”
“Courts are ‘overworked’ and cases can be delayed for a long period of time with a judgment taking four to five years or even longer.”

Source: Feedback received from survey respondents.

Inputs from private sector respondents corroborate the results emerging from several indicators that suggest an uncertain legal and regulatory regime in the region. For example, the WEF’s GCI exercise asks businesses about the efficiency of the legal framework in challenging regulations and in settling disputes. As can be seen from Figure 18, Bangladesh, Nepal, and Pakistan improved the efficiency of their legal frameworks since 2015–16 and managed to advance their position along both dimensions. During the same period, India retained its leading position in the region, ranking 35 on the efficiency of legal framework for settling disputes and 23 for challenging regulations. Sri Lanka’s efficiency of its legal framework for allowing businesses to challenge regulations and government decisions has deteriorated, however. The improvements in the efficiency of the legal framework for settling disputes were sustained a little longer, but this has also declined recently. These trends are reflected in the rankings. Sri Lanka ranked 34 in 2012/13 on the indicator “Efficiency of legal framework in challenging regulations”; however, it slipped to the 86th position in the 2017/18 rankings. On the indicator “Efficiency of legal framework in settling disputes” its rank was an impressive 26 in 2015/16; in the 2017/18 rankings, it slipped to 68.

**Figure 18. Efficiency of legal framework**

![Figure 18: Efficiency of legal framework](image)

Note: 1 = extremely inefficient; 7 = extremely efficient. Regional averages do not include Afghanistan, for which data is not available.

Figures 19 and 20 show two other measures of contract enforcement: cost as a percentage of the claim value and the time taken (from the World Bank Doing Business 2020 report) to receive judgment in a commercial dispute for the year 2018–19. Cost as a percentage of the claim value is highest in Bangladesh, at more than twice the regional average of 32.9 percent, and least in Pakistan. Note that the costs seem to be much higher in East Asia and the Pacific, however, relative to South Asia. In terms of the time taken to receive judgment in a commercial dispute, only Nepal and Pakistan are below the regional average of 1,305 days. Afghanistan fares the worst along this dimension, but even Bangladesh, India, and Sri Lanka

42. The questions asked are (a) “In your country, how easy is it for private businesses to challenge government actions and/ or regulations through the legal system?” with the score ranging from 1 (extremely difficult) to 7 (extremely easy); and (b) “In your country, how efficient are the legal and judicial systems for companies in settling disputes?” with the score ranging from 1 (extremely inefficient) to 7 (extremely efficient).
are well above the regional average, which is also much higher than that for East Asia and the Pacific. The performance of South Asian countries on the Doing Business 2020 ranking in contract enforcement suggests that Nepal is the best performer in the region, albeit still ranked 151 out of 190 countries in 2019, followed by Pakistan (156), India (163), Sri Lanka (164), Afghanistan (181), and Bangladesh (189).

Figure 19. Cost as % of claim Value

Figure 20. Time taken to receive judgement in commercial dispute (#days)


3.8. Trade

Access to international markets is an important factor in economic development. When economies are open to international trade, they tend to grow faster, improve productivity and innovation, and ensure higher income and better opportunities to their people (World Bank 2018b). Firms that operate in international markets not only get opportunities to expand their customer base and realize their produce in the foreign market, they are also subject to greater competition, which may positively impact their productivity and efficiency. Research shows that exporting firms are more productive than those that do not export, although exports do not necessarily increase productivity (Wagner 2007). Other findings suggest that trade can improve productivity through knowledge transmission (Madsen 2007).

Tariffs, logistics cost, and customs and border administration fees influence how easily international trade can be carried out. Efficient customs processes, developed transport networks, and simple documentary requirements can help facilitate compliance with export and import procedures and reduce costs (WTO). These factors determine global competitiveness, which has a bearing on exports and, in turn, on economic growth and job creation.

Martincus, Carballo, and Graziano (2015), using Uruguay’s export transactions data, find that customs-related delays have a significant negative impact on firms’ exports. According to the World Trade Report 2016, along with fixed entry costs, cumbersome border procedures and standards are major hurdles for SMEs. Findings from Hornok and Koren (2015) suggest that a 50 percent reduction in pre-shipment costs is comparable to a 9 percentage point reduction in tariffs, translating into a positive effect on trade.

The importance of country-specific trade reforms for realizing gains from the BRI has also been emphasized by a recent World Bank study (World Bank 2019a). The report notes that “Policy reforms facilitating trade, reducing trade policy barriers, and improving the management of corridors require country-specific actions and cooperation. Supply-chain bottlenecks in a single country could block the potential benefit of the entire corridor in unlocking new trade opportunities. Deepening trade agreements among corridor economies could reduce the current fragmentation and establish the rules and mechanisms for trade and other policy reforms.”
In fact, CGE results underlying the key messages in this report suggest that East Asia and the Pacific and the South Asian regions witness the maximum increase in their exports (3.8 and 3.7 percent, respectively) from a full implementation of the BRI, with Pakistan (9.8 percent) and Bangladesh (8.7 percent rise in exports) benefiting the most within South Asia. At the same time, the CGE analysis in the report notes that export gains for the South Asian region are nearly tripled when complementary reforms, i.e., reduced border delays and reduction in tariffs, accompany infrastructure improvement emanating from the BRI.

Another manifestation of the gains from BRI infrastructure projects would be reduced domestic transport times. The six countries in the region range between 5 and 48 hours for exports, an enormous time for exports to get to the port of departure. The BRI may thus meet the need for more efficient infrastructure and logistics on the major trade corridors within the country.

Similarly, the South Asia region has the lowest intraregional trade in the world. World Bank research (World Bank 2018a) estimates that the widening gap between actual and potential intraregional trade to be around US$40 billion. With the BRI in place, much of the cargo traveling along transport corridors could be intraregional, unlocking markets and growth potential within the region.

Businesses in the selected South Asian economies face several obstacles in exporting or importing goods and services, however, including tariffs, quotas, and a host of nontariff barriers that greatly increase the cost or prevent trading altogether (see Box 10 for feedback). According to the Enterprise Surveys, 17 percent of South Asian firms consider trade regulations to be a major business constraint. At least one in three firms in Nepal’s retail services sector and in Pakistan’s garments manufacturing sector and one in four in India’s textile manufacturing sector identify trade regulations as a major constraint.

### Box 10: Barriers to trade in South Asia

**NEPAL**
- “There is no transparency and fairness in customs administration.”
- “There are no quality certification/accreditation mechanisms, and businesses find it very difficult to comply with technical standards, which negatively affects competitiveness of Nepali products.”
- “Export is an issue. Nepal is a landlocked country and depends a lot on neighbors and their regulations at the border. For instance, requirements imposed by India.”

**AFGHANISTAN**
- “There is no transparency and fairness in customs administration.”
- “Eighty percent of firms identify customs and trade regulations as a major constraint.”

**BANGLADESH**
- “There is no transparency and fairness in customs administration.”

**INDIA**
- “Seventy-five percent of firms identify customs and trade regulations as a major constraint.”

**PAKISTAN**
- “Customs inspections present a serious problem for businesses.”
- “Customs administration is lacking transparency and fairness.”

**SRI LANKA**
- “Discretionary treatment is exercised by regulatory officials with relation to trade licenses.”
- “There is no transparency and fairness in customs administration.”

Source: Feedback received from survey respondents.
While all South Asian economies rank low in terms of trade openness and much below the comparator East Asia and Pacific region, countries across the region show considerable heterogeneity on the World Bank Doing Business indicators pertaining to trading across borders and logistics performance (see Figure 21). For instance, Nepal is the best performer in the region on the Trading Across Borders index for 2020, with a rank of 60 among 190 countries. Among other things, the time taken for documentary compliance with export procedures is seven times faster in India than the regional average. Meanwhile, Afghanistan and Bangladesh lie at the bottom of the ranking, while Pakistan fares poorly, with a ranking of 111.

**Figure 21. Rank of South Asian countries in different trade indices**

![Figure 21](image)


In terms of performance on the Logistics Performance Index (LPI) for 2018, the rest of the South Asian countries can be benchmarked against India, which tends to lead in the region, as well as placing 44 out of 160 countries. The rate at which shipments reach their destinations within the scheduled delivery time, the competence and quality of logistics services, and the ability to track and trace assignments are some of the areas that show the Indian framework to be more efficient than its regional peers. Relative to India, Pakistan is severely constrained in terms of border control agencies’ clearance processes, the adequacy of transport infrastructure, tracing and tracking, and timeliness; Nepal is found wanting on customs performance and adequacy of infrastructure, international shipment, and logistic competence; Sri Lanka lags behind on international shipment and logistic competence and timeliness; Bangladesh is especially low on clearance process efficiency and trade and quality of transport-related infrastructure; and in Afghanistan, documentary compliance is a major issue for imports, with documentary compliance requiring 324 hours, compared to an average of 113.3 hours in South Asia, and costing US$900, compared to the regional average of US$310.5.

With a ranking of 119 among 140 countries, however, Bangladesh still does relatively better on the Trade Openness Global Competitiveness Index (2019); all other South Asian countries are placed at least ten notches lower (see Figure 21).

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43. Feedback from respondents also points to the need to improve the transparency, predictability, and accountability of Nepal’s customs administration. In addition, the country is constrained by being landlocked, leaving exports, in particular, dependent on border regulations imposed by Nepal’s neighbors, especially India.
04. BUSINESS ENVIRONMENT IN SOUTH ASIA IN THE CONTEXT OF BRI
A large multicountry infrastructure initiative like the BRI is likely to have huge spillovers in host countries. At the same time, host countries need to have an enabling business and regulatory environment to benefit from BRI-induced opportunities. Recent literature (World Bank 2019a) notes that “many countries have trade policies and border management practices that inhibit cross-border trade. Making it easier to import and export goods is essential for countries to reap the full benefits of BRI investments. Not only that, but all corridor economies would benefit from open procurement processes, stronger governance, more appealing business environments, as well as fiscal and debt sustainability frameworks that allow them to fully account for the potential costs of debt-financed infrastructure.” It thus becomes necessary to examine whether business regulatory requirements in South Asian countries hinder them from fully benefiting from BRI projects’ spillovers or whether, in fact, BRI firms in these countries receive any preferential treatment in meeting different regulatory requirements.

In this context, it is also useful to discuss how the BRI is viewed in each of the region’s countries, especially in light of political sensitivities. For example, it is well understood that in both Pakistan and Sri Lanka, and in recent months Nepal, the BRI, to a certain extent, forms the backbone of national infrastructure development strategy. This gives credence to the extensive benefits and exemptions that BRI firms may be getting. Meanwhile, Bangladesh and Afghanistan seem to be taking a more circumspect approach as far as using the BRI to inform their national infrastructure development strategy. To illustrate, the CSIS database lists the Padma Bridge project in Bangladesh as a BRI project; many of the Dhaka city urban infrastructure projects are as well. These projects have been national priorities for a very long time, however, predating the BRI. As a result, BRI projects in these countries do not receive any exemptions not accorded other high priority infrastructure projects.

In Pakistan, feedback from respondents reveals that BRI firms may have received preferential treatment regarding several regulatory requirements relating to access to land, licensing and inspection, fiscal or non-fiscal incentives and state aid, currency repatriation, and public procurement (see Box 11 for procurement practices of projects in the China-Pakistan Economic Corridor). In contrast, BRI firms received no preferential treatment in meeting the regulatory requirements for the remaining thematic areas discussed in this study.

In Pakistan, while the laws and processes regarding land ownership remain the same for a BRI firm, in practice such firms may obtain facilitation agreements with the central government that provide access to land under temporary and permanent rights of way, free from any encumbrance. This, however, differs on a case-by-case basis. Moreover, the Gwadar Power Project located in Baluchistan province seems to have been given provincial regulatory approvals for what is increasingly restricted land. While no legal provision allows preferential treatment of BRI projects in terms of licensing and inspections, in practice BRI projects’ applications seem to be taken up on a priority basis. Even for license renewals, BRI firms seem to be able to renew licenses for project development without delays.

BRI firms in Pakistan also seem to have been exempted from paying customs duty on equipment and construction machinery imports. For example, the Revenue Division of the Ministry of Finance, Economic Affairs, Statistics and Revenue, vide Notification S.R.O. 642 (I)/2016, granted custom duty exemption to equipment and construction machinery imported by M/S China State Construction Engineering Corporation Limited for the construction of the Karachi-Peshawar Motorway and to M/S China Communication Construction Company for the construction of the Karakoram Highway Phase-II. The central government also seems to have granted BRI firms exemptions from paying advance income taxes (vide S.R.O 735(I) 2016). Moreover, road construction projects under the China-Pakistan Economic Corridor (CPEC) involve Chinese financing under a government-to-government agreement exempting CPEC from Section 7(2) of PEC by-laws regarding the requirement of formation of a joint venture with a Pakistani firm. In addition, by virtue of a bilateral tax treaty between China and Pakistan, certain Chinese state-owned banks receive reductions when repatriating on the profit on debt.
Apropos government procurement, the modalities for executing CPEC projects differ slightly from that used for other projects. As part of CPEC, the Chinese government nominates three to four Chinese companies, and bidding for the project takes place among these short-listed firms. But Chinese contractors and consultants, like any other foreign participants, must be registered with the PEC (see Box 11 for details).

**Box 11: Procurement of China-Pakistan Economic Corridor projects**

Procurement of high-value projects associated with the Chinese-funded China-Pakistan Economic Corridor (CPEC) and financed through the EXIM Bank of China is restricted to Chinese contractors. The Chinese CPEC authorities nominate three Chinese firms for bidding purposes. Procuring entities then issue the bidding documents to the three nominated Chinese contractors, seeking bids for the contract. Contracts make allowance for domestic contractors to collaborate with Chinese counterparts via joint ventures. The processes used during the initial selection of the three Chinese contractors is not known, e.g., whether a competitive procedure guides the shortlisting of the three bidders. Thus, information is lacking to assess the extent to which collusive practices are controlled for. Since competition is limited, little or no opportunity exists for the domestic construction industry to take advantage of the available financing, other than by becoming a subcontractor. The feasibility of subcontracting depends on the Chinese contractors and the extent to which the borrowing government, in this case Pakistan, is willing and able to pursue “local content” objectives when negotiating BRI projects. A provision in the agreement between Pakistan and China covers subcontracting up to a maximum of 30 percent of the contract value, subject to the procuring entity’s agreement. The perception of interviewees is that Chinese contractors use their own labor and that BRI procurement contracts are not very helpful in providing employment opportunities within Pakistan. This supports other assessments that, even when local capacity exists, BRI projects show a strong tendency to use Chinese labor, equipment, and processing (Saalman and Dethlefsen 2017).

The interviews also revealed that, although requirements in the procurement of CPEC projects to provide bank guarantees are met, addenda amend the agreed bidding documents. These resulted from pre-bid meetings and were suggested by the three preselected bidders. For instance, liquidated damages for delays were reduced from 10 percent to 5 percent and the bonus for early completion was also changed. This indicates the nominated contractors’ influence on the procurement process. Moreover, the Instruction to Bidder Clause describing the procuring entity’s right to accept any bid and to reject any or all bids was amended to make an explicit provision for negotiations. The amendment stipulates that after evaluation of bids, the technical proposal may be discussed and adjusted to obtain the desired project objectives, with associated price adjustments to be made by mutual consent. No independent probity assurance providers were involved in these negotiations, and transparency in such negotiations/discussions cannot therefore be guaranteed. The bid price received for engineering, procurement, and construction (EPC) contracts under CPEC-financed projects have been described as more than double the prevailing item rate contracts and engineers’ estimates. No technical analysis was provided to justify the higher bids. The respective procurement contracts are amended following bid evaluation and prior to award of the contract at a cost higher than that estimated by the engineering studies, also highlighting a disregard for transparency in the procurement of these contracts.

In Sri Lanka, BRI firms may have received preferential treatment in access to land, government procurement bidding, and FDI policy. For instance, the Board of Investment in Sri Lanka facilitates large-scale foreign infrastructure investment and grants preferential treatment to such projects. While the projects are governed in line with the Foreign Exchange Act No.12 of 2017, if a project is granted SDP status (Strategic Development Project) under the Strategic Development Projects Act No.14 of 2008, certain exemptions may be involved. Similarly, while access to land in Sri Lanka is governed by the Land (Restriction on Alienation) Act 2014, which restricts foreigners’ property ownership, exceptions to the rule may be made to provide access to land for BRI projects with government involvement.

While BRI firms or projects in Afghanistan seem not to receive preferential treatment, those in Nepal seem to receive preferential treatment for both taxation and trade. For instance, both Chinese and Indian respondents have reported that Kathmandu has offered Chinese investors preferential terms, including substantial corporate income tax rebates. Illustratively, “there is a 100 percent exemption for ten years and 50 percent exemption in the following five years in the field of energy, and a 100 percent exemption for five years in the tourism industry when investing more than 2 billion Nepalese rupees ($17.5 billion).” Similarly, local small companies seem to depend heavily on large Chinese firms, and a local SME must team with a big Chinese exporter to export.
05. CONCLUSION
While the business regulatory environment in South Asia has improved over time, significant challenges remain that not only stifle the growth and development of private enterprise but also prevent the region’s countries from reaping the spillover benefits of large infrastructure projects like the BRI. Systemic issues like corruption, lack of transparency, and cumbersome and often discretionary bureaucratic procedures continue to prevail throughout the full firm lifecycle and in all the thematic areas addressed in this study.

A good strategy for improving competitiveness in the South Asia region and allowing firms to compete domestically and globally is to reduce transaction costs, strengthen institutions and property rights, and provide efficient infrastructure services, a smoother business environment, and more effective public services. Productivity growth can be driven by movement in resources from less to more productive firms within narrowly defined economic activities. Below are some examples of actions that policymakers could take to address administrative, regulatory, and institutional constraints faced by firms in South Asian countries:

- Set time limits for reviewing and issuing permits by law; introducing e-government G2B services, including the possibility to track the status of permit applications (this will ensure that it is clear to the business when the time has lapsed and when they require a response from the regulator).
- Introduce or refine risk-based approaches to sector regulations and undertake a cost-benefit analysis of licensing in the region.
- Introduce obligations for government to provide ex-ante justification and impact assessment of new regulations, in particular when introducing new administrative burdens.
- Establish a centralized and accessible informational portal on permit/license requirements and automate issuing of priority permits/licenses (by economic significance/frequency/number of business affected).
- Adopt risk-based approach standards for licensing and inspection that adapt the government’s degree of regulatory control to the actual hazards and level of severity posed by industry sectors, economic activities, or businesses.
- Use data (evidence-based) for improved policy making.
- Establish a centralized consultation portal for upcoming regulations.
- Post regulatory requirements (time, cost, procedures, documents, etc.) online.
- Introduce rule-based decision making by establishing clear criteria for allocating public resources, such as procurement contracts, public land, energy subsidies, and investment incentives; make such criteria transparent; and make information on who benefitted from provision of such resources public.
- Introduce appropriate oversight mechanisms on agencies providing such resources.
- Introduce effective grievance mechanisms giving aggrieved parties recourse.
- Lower barriers to entry, trade, and investment, both de jure and de facto.
- Reduce the scope for discretionary behavior by regulatory officials that may lead to harassment of competitors of well-connected businesses.

The procedures for building projects in South Asia continue to be complicated and costly, involving licensing requirements from several different agencies and thus increasing opportunities for rent-seeking and corruption. Streamlining these procedures will also reduce the number of interactions with government officials, reducing opportunities for rent-seeking and corruption.
Access to resources—land, finance, and electricity—remains a challenge across the region. In addition to poor-quality land administration, restrictions on foreign ownership of land also exist across South Asia. Similarly, access to finance is considered one of the biggest obstacles for business operation and growth in South Asian countries. Access to electricity, too, remains challenging in the South Asia region, with inadequate electricity supply and considerable disparities both within and across South Asian countries.

FDI involves multiple administrative approvals from the concerned domestic authorities, and these processes must be streamlined to make them less cumbersome for foreign investors.

Regulatory restrictions in the form of local content requirements and restrictions on currency convertibility and repatriation must be liberalized to incentivize foreign firms to operate in the region.

Streamlining procedures for paying taxes and, in general, limiting contact and interactions with government officials would go a long way toward reducing corruption, which various World Bank Enterprise Surveys have identified as a major impediment to the operation and growth of businesses in South Asia.

The use of selective, limited, and direct procurement must be minimized to ensure competition and efficiency and curb corruption in procurement processes in countries across the region.

Dispute settlement practices must also be streamlined in the region’s countries, with a heavy emphasis on early settlement of disputes. At the moment, it takes between three and five years to resolve a commercial dispute, representing a huge deterrent to business in South Asia.

Businesses in South Asian economies face a number of obstacles in exporting or importing goods and services, including tariffs, quotas, and a host of nontariff barriers that greatly increase the cost of or prevent trading altogether. These need to be eliminated.

Improving the business environment of South Asian countries will not only benefit all firms and boost their competitiveness, leading to job-creation and economic transformation, but it will also enable the region to gainfully reap the benefits and spillovers from BRI projects and regional connectivity. Attaining this will require better coordination between local, state, and federal authorities, given that three of the South Asian countries in the study (India, Nepal, and Pakistan) are federations with highly decentralized political systems.

Finally, the world is confronting an unprecedented health and economic crisis emanating from the Covid-19 pandemic. In addition to public health concerns, a significant contraction is occurring in both global and regional GDP due to disruptions to global value chains, falling consumer demand for a subset of goods (e.g., textiles), and a decline in tourism (especially significant for Nepal and Sri Lanka). Services trades, in particular, are being severely affected as three of the four ways in which services are transacted require physical interaction between service providers and consumers, making these the first casualties of social distancing and related practices in the wake of Covid-19 (Shingal 2020a, 2020b). That said, the region’s countries can also use this crisis as an opportunity for regulatory reform in many crucial areas, but especially insolvency, access to finance, commercial disputes, and government procurement.
References


**ANNEX TABLE.**

COMPARATIVE SNAPSHOT OF REGULATORY PRACTICES ACROSS SOUTH ASIA
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<td>Percentage of firms considering corruption as the biggest obstacle, WBES</td>
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<td>45.8</td>
<td>14.3</td>
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<td>Percentage of the firms visited by or required to meet with the tax officials, WBES</td>
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Source: Authors’ compilation.

Note: BPP = Benchmarking Public Procurement; DB = Doing Business; GCR = Global Competitiveness Report; GIRG = Global Indicators of Regulatory Governance; WBES = World Bank Enterprise Surveys; WGI = World Governance Indicators.