

SCOPE OF PRIVATIZATION - LOGISTIC SERVICES OF THE BANGLADESH ARMED FORCES

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Many countries have inducted privatization in their respective Armed Forces since long. The aim of such privatization is to provide with a required level of defence at a minimum cost by tapping on to the resources, potentiality and expertise available in the private sector. Experiences of these countries depict that private sector's competitive nature and economy of scale provided the required services more efficiently and cost effectively. Though Bangladesh is strongly pursuing privatization in the civil sector, but defence is one sector that remains out of its scope. The orthodox dogma prevailing amongst us that privatization of defence sectors may compromise with the required degree of operational readiness required by the Armed Forces, is not based on substantial facts and figures. This paper, attempts to analyze the prospect of inducting privatization in the Bangladesh Armed Forces, particularly in the areas of logistics. In fact, privatization of logistics functions is a viable and cost-effective option, which is expected to render various advantages considering our meager budget and manpower constraints. However, such privatization will require policy shift, establishment of organizational framework and change in our attitude towards the subject.

INTRODUCTION

The Armed Forces of Bangladesh, in its present realities, have resource constraints and are under intensifying pressure to manage increasing volume of tasks within a tight budget allotment. The broader concept of privatizing suitable sectors/functional areas of our Armed Forces has not yet been addressed in its core essence. No known formal approach has been carried out to conceive the viability and suitability of identifying sectors under which privatization may be considered as an alternative option considering the experiences of other foreign armed forces, based on its cost-beneficiary ratio, qualitative, operational and security dimensions.

Armed forces of today are increasingly seeking commercial support for their in-house functions. This is motivated by the need to tap into competitive markets to reduce cost and to improve performances. US Secretary of State for Defence¹ stated: "Our Armed Forces deserve the very best. By working in new partnerships with the private sector, we in the Ministry of Defence (MOD) will deliver the best possible training, equipment and support to our service personnel."

Though civil sector's privatization of sick industries in Bangladesh has gone through various phases since independence, but privatization of defence related units has always remained out of its scope. The basic question that needs to be dealt with is, what benefit do some countries achieve through privatizing defence related sectors, and whether those benefits are applicable to the Bangladesh Armed Forces? Therefore, it is probably interesting at this stage to study the existing Bangladesh Defence Services' logistics system in a critical and analytical way, comparing its cost effective ratio against the private sector; and subsequently derive alternative schools of thought, if any. This paper has sought to summarize generic understanding of the basic pertinent issues, studies and practices of other countries including regional countries as to how privatization has been inducted in their armed forces; and subsequently focuses on the core issues relating to the scope of privatization in the Bangladesh Armed Forces. It will further review, whether such privatization will meet the particular requirements of a fighting force as a quality and cost effective service provider while retaining operational demands. Finally, the paper will attempt to reflect broadly on the institutional framework required for the fusion of privatization and put forward some attainable recommendations by limiting the scope within the logistic services only.

OBJECTIVE

The objective of the paper is to study the scope of privatizing logistic services of the Bangladesh Armed Forces.

1. Stated by Rt Hon Geoffrey Hoon MP.

SCOPE OF PRIVATIZATION

Privatization

In its simplest form, to privatize is "to make private".² The UNDP Guidelines on Privatization (1991) defines it as the marketisation of public sector activity. However, privatization does not merely dictate total handing over of functions and operations to a private body. Privatization can take various forms, for example, by blending ownership and functional activities between a state and a private body. A private company in today's context can, therefore, be totally private owned or partly government owned. Similarly, in its functions a private body could be either autonomous or semi-autonomous or even managed under government control in administrative respects. The objective of privatization is often to increase the efficiency of government activities.

Logistics

In military science, logistics include all activities of armed forces units in roles of supporting combat units, including transport, supply, signal communication, medical aid, and like. In general term, "logistics" is the science of planning and carrying out the movement and maintenance of forces. In its most comprehensive sense, it includes aspects of military operations, which deal with the followings:

- a. Design and development, acquisition, storage, movement, distribution, maintenance, evacuation and disposition of material.
- b. Movement, evacuation and hospitalization of personnel.
- c. Acquisition, construction, maintenance, operation and disposition of facilities.
- d. Acquisition or furnishing of services.

The overall gamut of activities covered under the term "logistics" is shown in the following diagram:³

2. Privatisation of Public Sector Activities with a special focus on telecommunications, energy, health and community services, United Nations Department of Economic and Social Affairs, 1999, p.1
3. JP 4-0, Chapter I, para 2, "US Doctrine for Logistics Support of Joint Operations".

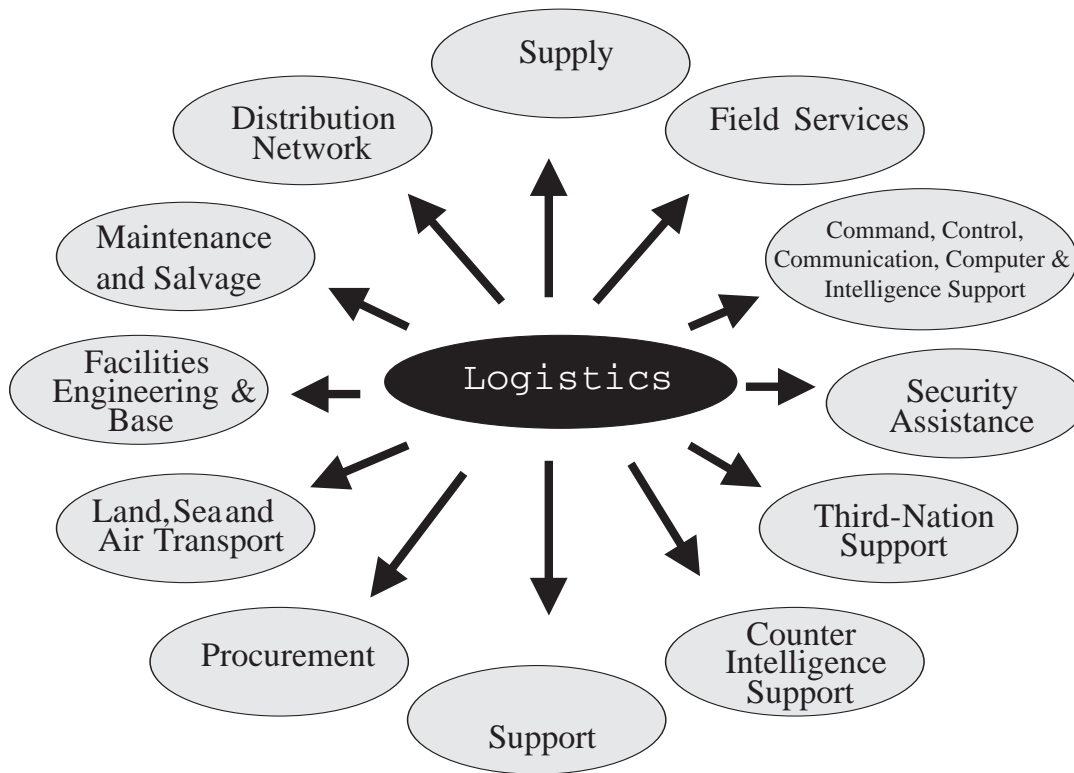


Figure 1: Scope of Logistics

PRIVATIZATION POLICY IN BANGLADESH

Reasons

The three basic reasons, which prompted the Government of Bangladesh to divert to privatization are⁴:

- a. Positive effects on Government's fiscal situation.
- b. Improvement of efficiency through privatization, as government's effort of reforms failed.
- c. To promote greater investment for higher growth.

4. Handout on "Privatisation in Bangladesh", Privatisation Commission, Cabinet Division, p.1

Policy

Article 13 of the constitution of Bangladesh emphasized on "creation of an efficient and dynamic nationalized public sector", which lead to the nationalization of all industries in the beginning. Unfortunately, this caused the state to suffer losses⁵ due to various reasons like poor infrastructure, under developed system and bad governance. Private enterprises that subsequently flourished created pressure by emerging more competition. Bangladesh Government, therefore, focused on the issue of privatization of state-owned industries.

Privatization in Defence

The "Revised Investment Policy" of December 1975⁶ paved the way to reorient the economy towards more dependence on private sector activities while "arms, ammunition and allied defence equipment" was kept reserved for the public sector.⁷ Subsequently, as the New Industrial Policy (NIP) was announced on June 1, 1982;⁸ where defence related industries were further kept reserved for the public sector, a state, which has not changed till today.

Existing Institutional Frame Work

"Privatization Board" was formed in 1993 to expedite privatization process. Eventually it was elevated to "Privatization Commission" in 2000 with more authority.⁹ This structure, though has relevance in regard to policy formulation, but is considered insufficient in respect of privatization of defence sector. Roles and status of the Armed Forces Division (AFD), Ministry of Defence (MOD) and the Services Headquarters are not clearly delineated within this structure. Any privatization of defence sector will, therefore, demand policy changes at the highest government level. Such privatization, if considered, should reflect the core policy values stated under the privatization policy and industrial policy adopted by the nation.

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5. Loss of Tk 17 billion incurred by the SOEs in the financial year 2002, which amounts to Tk 105,000 per minute. Commodore M S Kabir, "Privatisation in Bangladesh" NDC Study Paper, 2003, p.1
 6. Clare E. Humbphrey, Privatization in Bangladesh - Economic Transition in a Poor Country, 1992, p.47
 7. Clare E. Humbphrey, Privatization in Bangladesh - Economic Transition in a Poor Country, 1992, ibid, p.48
 8. Clare E. Humbphrey, Privatization in Bangladesh - Economic Transition in a Poor Country, 1992, ibid, p.65
 9. Status and Authority elevated by the "Privatisation Act 2000 (Act No 25)" published in Bangladesh Gazette Extraordinary dated 11 July 2000.

PRIVATIZATION PRACTICES IN OTHER ARMED FORCES

Requirement

Today's challenge for nations is to render the required level of national defence at a minimum cost. A significant number of foreign countries have introduced privatization in the armed forces in some form or the other. The nature and scope of this privatization varies between nations. In general, the promotion of outsourcing and privatization in the armed forces have only been considered when they met the following fundamental conditions:

- a. Private sector firms must be able to perform the activity and meet war-fighting missions.
- b. Privatization must focus on to improve quality, to increase efficiency and to reduce costs.
- c. Outsourcing and privatization activities must result in best value for the government and the services.
- d. Must meet the specialities and operational requirements.

The US Experience

The US Armed Forces technical/industrial base is and has virtually always been in the hands of private industry. In 1945, the US industrial, logistics and maintenance services, in private hands but under close government supervision provided support as shown in Table 1 below :¹⁰

| | | Table - 1 |
|-----------------------------------|---------------------|------------|
| S N | Item | Quantity |
| 1. | Aircraft | 310,000 |
| 2. | Tanks | 88,000 |
| 3. | Landing Craft | 82,000 |
| 4. | Rifles and Carbines | 12,500,000 |
| 5. | Trucks | 2,400,000 |
| US Private Sector Support in 1945 | | |

10. "Defence Industry Privatization And National Security Requirements: The United States Experience", website : scheurweghs@hq.nato.int.

"Public Private Partnerships (PPPs)"¹¹ offers new ways of doing armed forces business more efficiently, making best use of the available skills in the public and private sectors to deliver better services. There is no predisposition towards either public or private sector. The main drive is the better use of resources in defence and the maintenance or enhancement of operational effectiveness. US MOD has a rich-wide-ranging "Private Finance Initiative (PFI)" programmed that includes accommodation, training, equipment, logistics, communications and utilities. To date, 45 deals have been signed that have brought over \$2.3 billion of private sector investment into defence.¹²

The current policy vision on privatization of defence, in simple terms, is one that hopes to minimize the size of "defence-only" capacity and maximize the size of "dual-use" capabilities, which can be sustained.

The United Kingdom (UK) Experience

In UK Armed Forces, PFI remains the cornerstone of the PPP programmed. PFI provides a service, based on the creation or replacement of capital assets by the private sector. "PFI and other forms of PPP play an important part in modernizing defence and changing the way in which MOD does business, to the mutual benefit of the armed forces, industry and the taxpayer".¹³ "Sponsored Reserves" is a category of employees, whose terms of employment would require them to accept reserve forces liability. Sponsored reserves are used in a number of PFI deals.¹⁴ Partnering arrangements¹⁵ are emphasized in the British Armed Forces and outsourcing remains a key method of achieving targets set under the Public Service Agreement. Outsourcing contracts are often in the order of 5 to 7 years in length and other forms of PPP prove to be more appropriate when a longer-term relationship is envisaged or capital investment is needed. Under "Defence Estate Prime Contracting Programmed", the UK Defence Department retains ownership and responsibility for the full capital and running costs of new facilities, but looks for a single contractor to take responsibility for the integration and management for the

11. PPP is an umbrella term covering a variety of procurement initiatives, all of which benefit from a close, and normally long term, relationship with a private sector partner. The main techniques are the Private Finance Initiative, (PFI), Partnering Arrangements, Outsourcing, the Wider Markets Initiative and the Defence Estates Prime Contracting Programme.

12. Download from Internet "Public-Private Ventures Could Ease the Pains of Privatization in USA".

13. Stated by Kevin Tebbit, Permanent Secretary, British MOD.

14. http://www.mod.uk/business/ppp/ppp_defence.htm.

15. A Partnering Arrangement is a term used to describe one form of long-term contract based on the partnering ethos. It establishes a framework within which the Department's relationship with a contractor can grow over time. In a Partnering Arrangement, it is not necessarily needed to be clear about final outcomes. Generally, such arrangements promote a developing relationship with a private sector partner over a range of possible activities. The partner is given opportunities to achieve innovation and value for money.

entire design and construction supply chain, including the delivery of the completed project on time, within budget and fit for aimed purpose. British Armed Forces privatization projects include equipment, storage, transportation, communications, logistics support, environmental control services, etc.¹⁶

The Singapore Experience

Since the early seventies, Singapore Armed Forces have adopted a more deliberate policy to contract out logistics functions like the management of supply bases, intermediate and even organizational level maintenance support. This is part of the 'Total Defence Concept' so that local industries and civil resources can be involved in the defence effort. Logistics functions, which have been privatized, involve supply, maintenance, and catering, training and logistic services.¹⁷

The Malaysian Experience

Logistic support services in the Malaysian Armed Forces (MAF) are gradually being privatized. In all functions, integration of various logistics corps and several civilian departments has been coordinated through MAF Headquarters. The base level assets and services functions, which have been privatized, are very static.¹⁸

The Indian Experience

India, at present, is promoting private sector initiatives particularly in logistics and maintenance sectors. The production by the eight public sector undertakings particularly "Bharat Earth Movers" and "Bharat Electronics" have gone up. In 1987, procurements from ordnance factories were shifted from the defence production head to defence allocation. Research & Development (R&D) funding registered a growth in the last ten years, which had an effect on the total defence allocations. R&D for defence also has bearing on other allied research agencies, including private sectors. Private firms and agencies are being involved increasingly.¹⁹ Major overhauling and maintenance are increasingly allocated to private sectors. Increasing involvements in indigenous defence hardware production also made logistics dependable on private sectors. Indian experience has relevance to the realities of Bangladesh.

16. <http://www.mod.uk/business/ppp/index.htm> and http://www.mod.uk/business/ppp/guidelines/annex_a.htm

17. Download from "Commercial Support for Singapore Armed Forces Logistic Functions", website : <http://www.pasols.org/Log%2018-%206.html>.

18. <http://www.pasols.org/Log%2016%20-%204.html>.

19. <http://www.geocities.com/TheTropics/3328/idr00010.htm>.

PERFORMANCE EVALUATION - LOGISTIC SERVICES OF BANGLADESH ARMED FORCES

To analyze the scope of introducing private sectors in the Bangladesh Armed Forces, performance of defence logistics infrastructures needs to be evaluated. For this, a number of case studies have been highlighted to evaluate existing logistic practices in the Bangladesh Armed Forces, with a view to determine scope and feasibility of privatization.

Case Study 1: Performance of Bangladesh Ordnance Factory (BOF)

A total of TK 35.55 Crore budget was allocated in the year 2002-2003 to the BOF. Table 2 below shows the expenditure in this regard.²⁰

| | | | Table - 2 |
|-------------------|---------------------------|-------------|------------|
| Allotment | Expenditure | | Percentage |
| (TK in Crore) | Item | TK in Crore | |
| 35.55 | 1. Foreign Loan Payment | 0.75 | 2% |
| | 2. Pay and Allowance | 11.09 | 31% |
| | 3. Supply and Services | 8.69 | 24% |
| | 4. Repair and Maintenance | 1.78 | 5% |
| | 5. Purchase/Capital Items | 11.70 | 34% |
| | 6. Construction & Works | 1.54 | 4% |
| Total Expenditure | | 35.55 Crore | |

Table 2: Expenditure in 2002-2003

At present, 31% of the allocated budget was consumed for pay and allowances, which is very high. Table 3 below, further analyses the comparison between the actual expenditure involved in production against the overhead/auxiliary costs:

²⁰. Interview with Col Mustafa Kamal, afwc, psc, Director Production, BOF.

Table - 3

| S No | Expenditure directly related to Production | | | Overhead Expenditure | | |
|------|--|-------------|-----|----------------------|-------------|-----|
| | Item | TK in Crore | % | Item | TK in Crore | % |
| 1. | Foreign Loan Payment | 0.75 | 2% | Pay an Allowance | 11.09 | 31% |
| 2. | Repair and Maintenance | 1.78 | 5% | Supply and Services | 8.69 | 24% |
| 3. | Purchase/ Capital Items | 11.70 | 34% | Construction & Work | 1.54 | 4% |
| | TK in Crore | 14.23 | 41% | TK in Crore | 21.32 | 59% |

Table 3: Expenditure Related to Production vs. Overhead Expenditure

As 59% of the budget is expended on non-productive heads, the BOF compared to private industries needs to be more cost effective. Ratio of production cost against overhead cost per unit production is given below in Table 4:

Table - 4

| S No | Nomenclature | Production | | Overhead | |
|------|-----------------|--------------|--------|--------------|--------|
| | | Cost (In TK) | % | Cost (In TK) | % |
| 1 | 7.62 SAR | 12454.19 | 24.5% | 38507.22 | 75.5% |
| 2 | 7.62 Ammunition | 5.46 | 34.15% | 10.53 | 65.85% |

Table 4: Production Cost vs. Overhead Expenditure per Unit

The overhead cost of 75.5% and 65.83% have been exorbitantly high and this clearly dictates the need of outsourcing to make BOF a cost effective production unit. Pakistan and Malaysia in this region have opened the door of outsourcing in their respective ordnance factories.

Case Study 2: Military Engineering Services (MES)

MES ensures basic services like electricity, water, sewerage and other day-to-day maintenance of barracks, messes, offices, utilities and accommodation buildings for the Armed Forces. For this, MES depends on other primary services providers²¹ for providing such services. Figure 2 below shows the dependency of MES organization in this regard:

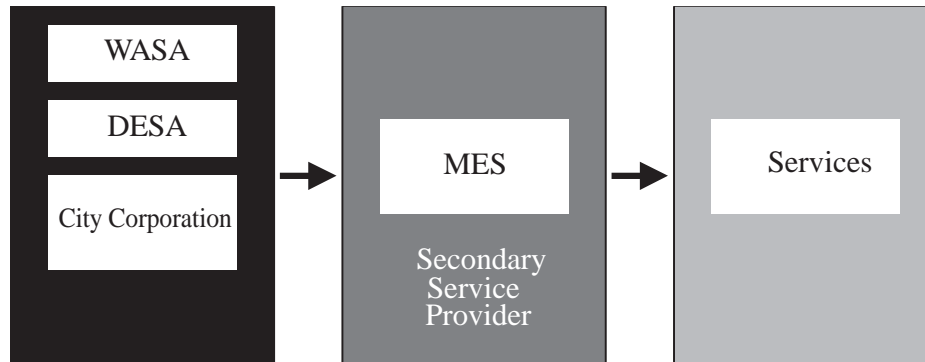


Figure 2: Flow Diagram of MES Maintenance Services

While civil consumers receive similar services directly from the primary sources, MES, on the other hand, is an additional link between primary service providers and the consumers in the case of armed forces. Whether, these services can be provided more cost effectively and by reducing administrative bureaucracies is studied in this section.

The total strength of personnel of BN including civilians is approximately 10,500 against which the strength of MES Navy is 1029. Therefore, an organization of 9471 personnel is supported by 1029 MES personnel. The ratio between consumer and maintainer is shown below in Figure 3:

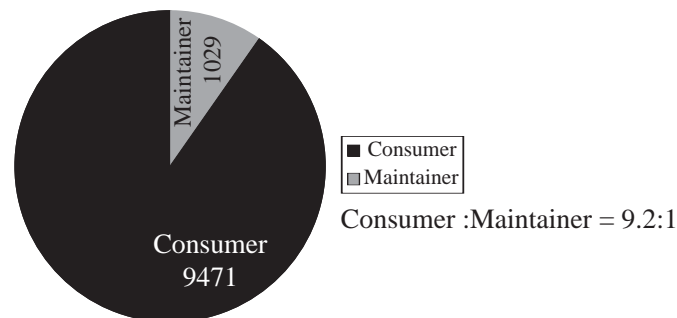


Figure 3: Ratio between Consumer and Maintainer

21. Such as Dhaka Electricity Supply Authority (DESA), Power Development Board (PDB), Water and Sewerage Authority (WASA), City Corporations, etc.

The majority of the 872 Casual Person (CP) and Regular Temporary (RT) personnel presently employed in MES (Navy) had initially joined against project works, which have been already completed.²² On completion of those project works, they were subsequently retained without considering the actual need of personnel required for efficient maintenance and service support.²³ TK 5,12,80,000/00 was remitted to these CP & RT personnel as pay and allowances in the year 2002-2003. TK 6,75,52,800/00 (35%) was spent on pay and allowances of all MES staff against maintenance and repair works allocation of TK 12,60,47,300/00 (65%).²⁴ This analysis does not include other overhead costs such as ration, medical facilities, accommodations, etc. The existing MES organization is, therefore, not cost effective and manned on requirement basis. In almost all European countries, Singapore, Malaysia and the US, preliminary maintenance and repair functions of the armed forces have already been privatized.

Case Study 3: Medical Services

Combined Military Hospital (CMH) at Dhaka started its "Cardiovascular Surgical Section" in 1990, which gradually developed into "Cardiovascular Thoracic Surgery Department (CTVD)". More than Tk. 42,82,00,000/00²⁵ has so far been expended in the CTVD considering fixed and variable expenses excluding pay and allowances. Cost of cardiac surgery in India, Thailand and Singapore varies around Tk 3-5 lac per procedure depending on the nature of treatment. A study²⁶ reveals that, the expenditure of any particular type of cardiovascular surgery conducted in CTVD and number and type of investigations carried out during pre-operative, intra and post operative period are significantly high, in comparison to other renowned hospital abroad. An article published by Tucson Medical Center in the USA mentions: "to run a cardio vascular hospital is a very expensive affair and maximum expenses involve pay and allowances of personnel. Next to it equipment, facilities and supplies are among the biggest expense areas in the hospital". At least 4 operations per day are to be conducted to ensure financial viability of such hospitals. This indicates that the CTVD of CMH Dhaka is under utilized and is less likely to be a cost effective venture. Bangladesh Heart Foundation at

22. Source : Interview with DW & CE (Navy).

23. The sources of these employees are as following:

- a. Supervisory Staffs for past projects (ie, Overseer, Superintendent, UDC/LDC, Storeman, etc).
- b. Tradesman of the corps of Engineer (ie, Valveman, Carpenter, Painter, Plumber, Wireman, etc).

24. Figures collected from DW & CE (Navy) Office.

25. This includes initial establishment cost Tk 9,00,00,000/00, maintenance expense Tk 42,00,000/00, supporting pre-surgical investigation machines Tk 12,00,00,000/00, yearly post surgical laboratory support expenditure Tk 1,40,00,000/00 and construction expenditure Tk 20,00,00,000/00.

26. Source : "A Study on Cost Analysis of Cardiovascular Patient Undergoing Surgical Intervention in Combined Military Hospital, Dhaka" carried out by Major (Dr) Syed Iftekhhar Uddin.

government level and Sikder Medical Hospital in the private sector provide much cost effective cardio vascular treatments, as each of these deal with considerable numbers of patients per day.

Case Study 4: Issue of Ration

Significant numbers of service and civilian personnel are employed for providing ration facilities to the Bangladesh Armed Forces personnel. This study analyses the probability of privatizing the collection, store keeping and distribution process associated with issuance of ration, as an alternative option.

State of BN personnel authorized to draw ration in 2002-2003 is given below in Table 5:

Table - 5

| Name of Base | Married | | | Single | | |
|--------------------------|---------|--------|----------|---------|--------|----------|
| | Officer | Sailor | MODC (N) | Officer | Sailor | MODC (N) |
| BNS ISSA KHAN | 190 | 1132 | 64 | 74 | 503 | 72 |
| Base Supply Organization | 300 | 2100 | 60 | 204 | 3465 | 40 |
| BNS HAJI MOHSIN | 275 | 793 | 44 | 110 | 582 | 15 |
| BNS TITUMIR | 97 | 1007 | 42 | 34 | 337 | 15 |
| BNS S/MOZZAM | 22 | 240 | 20 | 29 | 256 | 10 |
| Grand Total | 6386 | | | 5750 | | |

Table 5: State of Personnel Authorized to Draw Ration

Thirteen servicemen and 12 civilian labors²⁷ are employed for victual ling functions in each major base. In case of privatized ration management, at least 60 to 65 personnel could be spared from the 5 bases and detailed for operational functions. BN has also expended at least Tk 15 crore²⁸ for constructing stores and other facilities.²⁹ Such investment will not be necessary in case of privatized management of the ration collection. The life cycle cost per civilian employee is much less, compared to service personnel. As such, outsourcing in this particular sector will certainly lower the overall expenditure and administrative complicacies to a great extent. Furthermore, it will allow significant numbers of servicemen to be deployed in operational functions. Such practices have been introduced in Pakistan, Singapore and Indian Armed Forces.

27. 1 x Lt Cdr, 1 x Chief Petty Officer, 1 x Petty Officer, 2 x Leading rates and 8 x Able rate.

28. Source : Interview of Assistant Chief of Naval Staff (Logistics), Navy.

29. Considering Tk 2 crores per base.

Case Study 5: Construction of Accommodation Building

It is a general practice in Bangladesh Armed Forces to construct accommodation facilities for officers, servicemen and civilian staff. A number of countries, particularly western countries, do not construct accommodation building for government employees, including defence personnel. Accommodation is provided through leasing private buildings. This section studies the facts and figures of recently completed 15-storied building at NHQ complex, as an example, to determine alternative options for providing accommodation facilities.

The 15-storied building provides 52 'D' type quarters, each of 1650 sqft area to BN officers. Total cost of the construction is Tk 15,83,67,500/00.³⁰ This figure does not include pay, allowances, ration and medical expenditures of MES personnel. Such apartments of 1650 sqft area can be hired in and around NHQ location, at a monthly rent of Tk 12000/00. Hypothetically, if it is considered that Tk 15000/00 per family is allocated per month as house rent, then it will require approximately 17 years to expend the construction cost of the building. In addition, BN will have to bear regular and periodic maintenance costs for the building. Therefore, for practical reasons, private accommodation leased by the government is considered a long-term viable and cost effective option for providing accommodations to service personnel.

Case Study - 6: BN Action Speed Tactical Trainer (ASTT)

In 1999, BN procured³¹ ASTT from Canadian manufacturer. Prior to the expiry of the warranty period, Naval Headquarters opted for negotiating a maintenance contract with the manufacturer. Subsequently, ATLANTIS Canada forwarded a " Proposal for Post Warranty Maintenance Contract - BN ASTT".³² Upon detailed scrutiny, it was calculated that the manufacturer's proposal for Post Warranty Support requires a minimum cost of US\$ 1,716,827/00, excluding material and repair costs. This would mean an expenditure of approximate Tk 8.5 crore, which was irrational as the total procurement cost of the ASTT was Tk 13,01,18,617/00.

BN, in consultation with the manufacturer, subsequently identified the compatible hardware components, which were commercially available in Bangladesh. During the process, it was learned that, a number of local reputed

30. All figures collected during interview with DW&CE (Navy) and Director Works, Naval Headquarters.

31. As per DGDP Contract No 218/4463/235/TS/DGDP/NP-3 dated 30 June 1996.

32. Source : ATLANTIS, Canada offer of 26 Jun 2001.

IT companies were, and are, capable of handling some of such high-tech system maintenance. However, major system/component defects, for which it is essential to replace specialized hardware / software provided by the manufacturer, need to be replaced or repaired by the manufacturer. BN also faced difficulty concerning availability of trained personnel to run and maintain the system. A viable option could be to train private company employees, who would have subsequently run and maintained the BN ASTT; as it is done in most of the NATO countries. Privatization of maintenance service of the ASTT will allow to form skilled and trained personnel within the country.

Case Study 7: Bangladesh Air Force's (BAF) Mess Service³³

BAF Officer's Messes are run by BAF servicemen and civilian personnel for whom no vacancy has been created in the Table of Organization and Equipment (TO & E). A typical mess organization of the BAF consists, as a whole, 37-40 personnel³⁴ who are employed for each mess. If we calculate then we will see that each of them dedicate only one hour per day, meaning 365 working hours are spent on the mess per year; i.e. each of them has wasted 40-45 working days in a year considering 8 hours in a working day. For the other service men, which are permanently attached, the whole year is lost. If the management and operation of the mess could be vested to private companies, then the committee members comprising BAF officers could be abolished and the airmen/civilians staff could be returned to their original functions as per the TO&E. Required degree of control over budget, expenditure, development, quality, etc could be exercised through negotiation and contract details. Like mess functions, it may also be considered to privatize catering services, libraries, swimming pools, entertainment facilities, cinema halls, golf clubs, computer clubs, internet services, etc to private managements.

Case Study 8: Khulna Shipyard

Management of KSY was handed over to BN on 5 May 1999.³⁵ Under BN supervision, KSY retained its status and modus operandi as a private company, the management being supervised by BN only. Numbers of permanent personnel, especially officers were drastically reduced in accordance with

33. Collected through interview of PMC, Air Force Officers Mess, Dhaka.

34. It includes President Mess Committee (PMC), Deputy PMC and Mess Secretary as nominated staffs, who carries out these responsibilities in addition. Other 8 to 10 selected Officers are also allocated with various duties (such as treasurer, entertainment, food, bar, library, sports members etc) of the mess. In addition, there are approximately 11 airmen and permanent air force civilians staffs employed for the smooth function of each mess, such as batman, washer-man, cook, table boy etc.

35. Handing over process coordinated between AFD, MOD, Privatisation Commission and the BN.

industrial norms. Cost analysis for each project was carried out to determine its viability. For business, KSY competed through quotations against other government owned and private dockyards. In this way, KSY was transformed quickly to a cost effective organization through better financial managements supervised by defence personnel. Financial state of KSY at the time of taking over and as on January 2003 is compared below in Table 6:³⁶

Table - 6

| Main Heading Sub Heading During Taking on January | | Over (Crore Tk) | 2003 (Crore Tk) |
|---|-----------------------|-----------------|-----------------|
| Asset | Fixed Asset | 2.40 | 16.16 |
| | Current Asset | 22.45 | 96.63 |
| | Accumulated loss | -- | 22.36 |
| Total Asset | | 24.85 | 135.15 |
| Liabilities | Shore Capital | 3.00 | -- |
| | Long term loan | 13.75 | -- |
| | Government equity | -- | 64.84 |
| | Leave, Pay & Gratuity | 11.67 | 11.20 |
| | Current Liabilities | 66.88 | 42. |
| Land | 0.11 | 13.30 | |
| Total Liabilities | | 95.41 | 132.13 |

Table 6: Comparison of Financial State

Adopting a private body approach, KSY did not depend on the armed forces only, but developed dual technical capabilities to compete for ship/pontoon constructions and maintenance works in the civil sectors as well. The process resulted into the diversification of production and maintenance capability. Therefore, outsourcing of defence related industry is a viable option. KSY can be taken as a successful model in this respect.

36. Interview with Naval Headquarters Plans Directorate and Naval Engineering Directorate.

OPTIONS FOR BANGLADESH ARMED FORCES

Analysis of Existing Logistics System

At present, logistics services of Bangladesh Armed Forces including maintenance are government controlled. Majority of logistic items procured by the Bangladesh Armed Forces are primarily manufactured in foreign countries and supplied locally by their local agents or contractors. 100% of spare parts and techno-based logistics are procured from foreign sources. No significant attempt has yet been under taken to reduce almost total dependence of the armed forces through development of indigenous capability. The orthodox dogma, that Bangladesh's economy does not permit sustainable development of indigenous defence capability; led to pre-conceived decisions, which prevented indigenous production capability.

Large numbers of government officials including service personnel are involved in the procurement process at Armed Forces Division (AFD), Ministry of Defence including Director General Defence Purchase (DGDP), services headquarters and concerned services depots/ maintenance establishments. The overall system is complex, slow, top-heavy and costly. Many countries do not possess such complex logistics infrastructure and generally appoints commercial firms that are responsible for designing, preparation of tender specification, preparation of contract papers, supervision of timely execution of the contract, quality control, and other associated functions. Such arrangement, if allowed, is cost effective considering the long time overhead expenditures.

Cost effectiveness, quality and diversity of product of defence production units such as BOF, BMTF, KSY, etc need to be further improved. Possibility of inducting controlled outsourcing or outsourcing similar to that of British or US PFI systems may be exploited, which will entail following advantages:

- a. Less government budget needs to be poured.
- b. It directly forces the management to focus on commercial cost management system, gradually transforming it cost efficient.
- c. Modernization process could be accelerated ensuring diversity of production, increase of capacity and quality.

There is a misconception that privatizing ordnance factory/units such as BOF, will compromise vital security aspects of the nation. In USA, UK and other western countries, private companies manufacture majority of armament productions. General perception of security prevailing amongst us, as stated above, is not based on evidence or experience. However, personnel associated with security affairs may be provided from the armed forces. British mode of the "Sponsored Reserves" may be considered for the civilian production and maintenance personnel in whom the private company may employ personnel, after thorough vetting by the concerned security agencies. Similarly, BMTF and KSY though placed respectively under Bangladesh Army and BN, are to function strictly as per financial norms of private companies.

Management of basic MES services such as water supply, electricity, sewerage and other day-to-day maintenance functions may be considered for privatization. Careful balance has to be drawn to retain minimum self-maintenance and repair capabilities by the services. Such privatization is likely to reduce governmental expenditures and administrative burdens drastically. This will require reviewing of the existing governmental policy.

The armed forces will have to decide at the highest level whether, non cost effective and expensive specialized medical facilities are required to be established in CMHs. An alternative policy could be adopted with a focus on the improvement of basic medical facilities relevant to the majority of the personnel of the armed forces, while depending on private sectors for specialized and costly treatments. Long time contracts with private, semi governmental or even with other governmental hospitals may provide similar medical services cost effectively.

Expansion of the existing personnel strength of the armed forces is less likely to happen considering our national economy. A viable option could be to reorganize the existing services TO & E, retaining the existing personnel strength but reducing personnel from logistics, maintenance and other supporting roles. Spared personnel may be subsequently deployed on operational tasks. Such restructuring, per nature, will have to invite participation of private sectors on long term/ mid term basis.

Private accommodation leased by the government on long-term basis is considered a viable and cost effective option for providing accommodations to service personnel. This will reduce initial bulk expenditure incurred in the

construction, maintenance/ repair facilities, and thus curtailing administrative functions involved in the process. In such case, number of MES personnel and maintenance budget can also be reduced significantly.

At present approximately 75-82% of the defence budget is spent on supporting functions. Particularly 50-58% of the budget is consumed for pay, allowances and pensions. Many foreign countries have reduced personnel by assigning majority of logistics functions to the private sectors, which has proved to be generally cost effective and efficient in man management. It also reduces medical, pension and other associated expenditures. As defence budget of Bangladesh is less likely to increase significantly, privatization may prove to be a viable option.

Many countries have adopted alternative arrangements to increase defence budget indirectly. Though official defence budget was not raised, but instead, funds were allocated for defence industries in private sectors. Privatization of defence industries will exclude running cost of these institutions from defence budget. Therefore, allocation of the present budget will, in fact, have an effect of substantial increase in the budget allowing more finance for essential priorities.

Any privatization of the logistics sector of Bangladesh Armed Forces needs to put emphasis on technology, which can be offered by the private sector either by their own or through their foreign business partners.

Scope of Privatization

Considering the various case studies mentioned above, following areas might be considered for the privatization of logistics services of the Bangladesh Armed Forces:

- a. All 3rd and 4th line repair and maintenance depot and services of vehicles, ships, aircraft, and heavy machineries.
- b. All MES repair, maintenance and construction functions except financial and major supervisory functions, which could be retained by permanent MES staff.

- c. Management of logistic depots.
- d. Specialized non cost-effective sectors of medical services.
- e. All defence related industrial/ production units providing security personnel from defence services.
- f. All messes, libraries, clubs, catering services, entertainment services, swimming pools, stadiums, Armed Forces Medical College, etc.
- g. Transportation not related to operation and field training, particularly transportation services provided as welfare.
- h. Accommodation buildings for service personnel considering long time cost effectiveness.
- j. Consultancy services for all procurement and MES projects may be privatized under defence control through qualified consultancy firms.

Long Term Partnership

Long-term partnership between the armed forces and private sector is required for items that are regularly required, e.g. provision, small arms, etc. This will provide the following advantages:

- a. Better assurance of continuous long-term support.
- b. Better ability to specify performance measures and targets that are critical to operations, and to provide incentives for the supplier to meet them.
- c. Better ability to define and measure supplier capability.
- d. Better integration of the contractor into the support system to cater for operational surge.
- e. Better control of cost escalation, especially after accounting for supplier's efficiency improvements.

Policy Considerations

Non-core functions of privatization are practicality and cost-effectiveness. But to ensure an over-all balance between the two essentially different sectors, some policy level guidelines should be followed. Such guiding principles are suggested below:

- a. It must not affect operational readiness.
- b. It must be economical.
- c. Business and operational activities of supplier and customer must be integrated.
- d. Contract terms should leverage on the inherent economics of suppliers.
- e. Risk and benefits should be shared.
- f. There should be continuous improvement with incentives for performance.

Ensuring Operational Readiness

The most important pre-requisite for commercial support is that the operational readiness and support to the services must never be compromised when activities are contracted out. To ensure this, following measures are needed:

- a. **Accountability:** Clear lines of accountability must be established for contracted out work.
- b. **Competence:** It is of prime importance that commercial contractors have the skills and expertise to provide the support, especially for highly technical jobs. Where certain skills are not readily available in the market, the services may retain skeleton group of such skilled personnel.
- c. **Sustainability:** It must be ensured that there is sustainability of the expertise in the market, especially when such skills are specialized and take a long time to nurture.
- d. **Surge Requirement:** Surge capacity for emergency needs must be catered for, during privatization of logistics functions. The contractor should have the flexibility to increase its capacity to cope with this surge requirement.

Partnership with Private Suppliers

This partnership aims to establish a mutually beneficial relationship for both parties. Essential elements of the framework are:

- a. **Long-Term Contracts.** This not only reduces the administrative cost of frequent renewal of contracts, but also allows for long-term focus on capability build-up and sustainment, and efficiency improvement.
- b. **Clear Performance Specifications.** In ensuring that performance requirements are clear, contractors' attention will be focused on areas that are truly important to the services as having a direct impact on their mission and operations.
- c. **Incentives to Improve Performance.** Direct and explicit rewards like monetary incentives are given to contractors who exceed pre-determined performance thresholds.
- d. **Incentives for Investment.** As a further incentive for continuous improvement, joint capital investments, sharing risks and benefits with contractors as strategic partners may be considered.
- e. **Optimization and Capacity Planning.** Close supervision is maintained to understand the trade-off between performance and cost. Joint capacity planning with the contractor, involving the three services may also be exploited.
- f. **Control of Cost Escalations.** Regular comparison of contractor's cost with original in-house cost, adjusted for changes in volume and cost escalation, and benchmark with market pricing where available to be made.

Safeguard

Whilst making every effort to ensure that contracting out would not fail, contingency plans are to be made to guard against the possibility of the commercial operator, for whatever reason, failing to meet its obligations. The easiest way is to go for an alternative source. Where this is unlikely to be available, it should be planned to retain some similar skill set in-house, enabling the services to build up the expertise again, if deemed necessary.

Legal Aspects

Concerned articles of our constitution need to be amended to allow privatization and outsourcing in Bangladesh defense forces. The "Privatization Policy" of the Government may also be changed to allow such effort. The "Privatization Commission" may issue policy directives identifying the roles of AFD, concerned ministries, services headquarters and the private companies associated in the process. National consensus on the issue may also be sought in the parliament.

Organizational Framework

A central organization under the MOD may be set for inducing privatization in the logistics sector of the Bangladesh Armed Forces. The government may determine composition, status and modus operandi of this central organization. A high level committee may be formed at the services headquarters level to conduct detailed studies for determining scope of privatizing logistics in each service. Report of the services headquarters forwarded to the MOD may subsequently be vetted by the central organization assisted by committee/defence personnel. Feasibility of standardization and joint logistics support may also be exploited at this stage. Services headquarters may allocate additional responsibilities to the existing R & D Directorate for arranging studies and carry out periodic cost effectiveness analysis of respective service's logistics functions to determine their viability. Additional and qualified staffs may be provided to this directorate accordingly.

CONCLUSIONS

Fusion of privatization in the defence forces, particularly in areas of logistics, has been practised by many nations. The scope and extent of such privatization in western armed forces have gradually increased emphasizing on the fact that partial privatization were viable and cost effective. Regional Armed Forces of India, Pakistan, Malaysia, Singapore are also depending on the private sectors for various services. Thus, the lessons derived from foreign armed forces clearly suggest that privatization in armed forces is a viable option, even for developing countries.

The sector specific case studies concerning Bangladesh Armed Forces highlight that introduction of privatization in the logistics services is a viable

option considering different realities. Initial privatization may involve 3rd/4th line repairs, maintenance and logistics depots, MES functions, specialized medical services, messes, libraries, clubs, swimming pools, catering services, transportation (other than operational), etc. All production units placed under the MOD requires being more cost effective and efficient in man management adopting strict private sector norms.

Article 13 of the Bangladesh Constitution and other relevant legal frameworks need to be amended at the onset to open any scope of privatization in defence services. National policy directives from the government; approved by the parliament; "Privatization Commission, AFD and MOD will be required.

Formulating policy approaches and methods to induct privatization in armed forces vary from country to country. Bangladesh needs to formulate own policies and methodology considering own ground realities. Furthermore, it is needed to set up an appropriate organizational framework involving the AFD, concerned ministries including MOD, privatization commission, services headquarters and private bodies to institutionalize the desired privatization process. Long-term partnership provides better integration of the private bodies for bulk and common logistics items. Policy consideration must focus to ensure operational readiness of the armed forces as a whole, which should be economical providing best value for the government and the services.

State-owned defence industries need to be more vibrant in terms of cost efficiency and man management. Compromising with these values, in the pretext of security consciousness, does not necessarily bring significant advantage to the government and the services. The attitude of relating operational concerns overriding core management aspects has not been validated through facts and figures. Awareness in this regard needs to be cultivated in the minds and hearts of defence personnel so that they can be more conscious in financial management. The study also reveals the need and suitability of privatizing concerned logistics functions of the defence services.

RECOMMENDATIONS

The paper recommends the followings :

- a. Existing bar on private investment in defence sector may be withdrawn by amending Article 13 of the Constitution.
- b. Subsequently, government may be persuaded to formulate a "Privatization Policy" to promote privatization in logistics sectors of Bangladesh Armed Forces. The same may be reflected in the NIP.
- c. Privatization commission may be persuaded to issue detail "Modus Operandi" and procedures, which may be followed to induct privatization in defence sectors.
- d. A central organization may be setup under the MOD for institutionalizing privatization in Bangladesh Armed Forces.
- e. Services Headquarters may allocate additional responsibilities to the R&D directorate to determine scope of inducting privatization in their respective services. Government may also pursue to sanction additional qualified staffs to the R&D directorates of each services headquarters and the AFD accordingly.
- f. Government may direct all defence industries, tri-service logistics institutions and services headquarters to infuse cost analysis procedures in all logistics functions including maintenance. Necessary directives may be issued either through AFD or MOD in this regard.
- g. Initially privatization may be considered in associated sectors of logistics as mentioned earlier. Subsequently, the scope may be broadened after observing its suitability and viability over a period.
- h. Steps to change the existing psyche of defence personnel against any privatization efforts may be induced through training, discussions, study periods and research works.

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