
Policy Reforms and Trade Liberalization in Bangladesh

by Nurun N. Rahman



1. Introduction

1.1. Main features of the Bangladesh economy

1.1.1. GDP and its composition

The rate of growth of GDP in Bangladesh has picked up in recent years. During the period 1980–1990, it grew at an average annual rate of 3.7 per cent, barely exceeding the population growth rate; but subsequently, during the period 1999–2004, it exceeded an average annual rate of 5 per cent, to reach about \$54 billion in the fiscal year 2003–2004. There were only modest changes in the relative shares of consumption and savings in GDP in recent years. In 1991, consumption accounted for nearly 86 per cent of GDP, but fell to 82 per cent in 2004, while the share of savings in GDP rose from 12 per cent to 8 per cent over this period. The investment/GDP ratio increased from 17 per cent to 23 per cent; within this, the ratio of public investment to GDP remained stagnant, at around 7 per cent, while that of private investment increased from 10 per cent to 17 per cent.

1.1.2. Changes in sectoral distribution of GDP

Changes in the sectoral distribution of GDP indicate that Bangladesh's economy has undergone important structural transformations over the past three decades. At independence in 1971, agriculture was the dominant sector, accounting for over half of total GDP. The industrial sector was small, contributing less than 10 per cent of GDP, while services, including transportation and power, accounted for the rest. However, following remarkable growth in the ready-made garments sector, its share began to change. By 1990, the contribution of industry to GDP had almost doubled to over 20 per cent. The share of agriculture fell to 29 per cent that year, while that of services rose to nearly 50 per cent (Table 1). To the extent that the growth of the ready-made garments sector was driven by international market conditions in textiles and clothing, the structural changes in the economy were influenced by external factors. In 2004, the industrial sector accounted for 27 per cent of GDP, while the share of agriculture dropped to 23 per cent, and that of the services sector remained steady around 50 per cent. Total manufacturing value added increased from \$3.8 billion in 1990 to nearly \$7 billion in 2002. Within the manufacturing sector, textiles and clothing alone accounted for one third of the total manufacturing value added in 2002, followed by food, beverages and tobacco at 22 per cent, machinery and transport equipment at 16 per cent and chemicals at 10 per cent.

Despite these changes in the sectoral composition of GDP, agriculture continued to account for the bulk of employment. During the period 2000–2002, it contributed to 53 per cent of male and 77 per cent of female employment, compared with 11 per cent and 9 per cent, respectively, by the industrial sector. The services sector absorbed 30 per cent of the male and 12 per cent of the female labour force. This sectoral and gender distribution of employment has important policy implications, especially for poverty reduction and gender equity.

1.1.3. Prices and wages.

Inflation has important implications for savings, investment, growth and income distribution. Keeping inflation low has been an important policy objective, and the country has done well in that respect. Indeed, inflation in Bangladesh in the 1990s remained lower than the average for South Asia. This is discussed in greater detail later. Real wage rate indices in recent years indicate an upward trend, but display urban-rural disparities. Agricultural real wage indices rose at an annual average rate of 3.2 per cent during the period 1991–2003, but slower than those for manufacturing. Despite such divergences, it has been observed that labour has moved very little from agriculture to industry, contrary to the predictions of some growth models such as the Lewis model. (Muqtada 2004).

Table 1. Sectoral Share in GDP and growth rate at constant prices (Base year: 1995-96)

Share (in per cent)

Sector	1979-80	1984-85	1989-90	1994-95	1999-00	2003-04
Agriculture	33.21	31.46	29.52	26.02	25.58	22.83
Industry	17.08	18.70	20.78	24.28	25.70	27.80
Service	49.72	49.84	49.70	48.70	48.72	49.37
Total	100.00	100.00	100.00	100.00	100.00	100.00

Average growth rate (in percent)

	FY 81-04	FY 81-85	FY 86-90	FY 91-95	FY 96-00	FY 01-04
Agriculture	2.77	2.68	2.40	1.55	4.88	2.23
Industry	6.51	5.70	5.86	7.47	6.44	7.24
Service	4.33	3.83	3.58	4.15	4.81	5.51
Total GDP	4.41	3.72	3.74	4.39	5.21	5.12
Per Capita GDP	2.54	1.54	1.50	2.36	3.83	3.70

Source: Bangladesh Government (2004).

2. Role of foreign trade

2.1. Exports

The external trade is currently dominated by exports and imports of manufactures. This is vastly different from the situation prevailing in the early 1980s when jute and jute products were the principal export items. In 2003, manufacturing accounted for 92 per cent of total merchandise exports, up from 77 per cent in 1990. On the other hand, the share of food fell from 14 per cent in 1990 to 7 per cent in 2002, and that of agricultural raw materials from 7 per cent to 1 per cent. Among exports of manufactures, textiles and clothing (ready-made garments and knitwear) accounted for nearly 75 per cent of total merchandise exports in 2003-04 indicating an exceptionally high export concentration in this sector. Further, exports of ready-made garments comprise mainly low value items. Given the predominance of textiles and clothing in Bangladesh's exports, any significant change in external market conditions affecting this sector, particularly in the context of the expiry of the WTO Agreement on Textiles and Clothing (ATC) at the end of 2004, could have serious implications for the trading prospects of the country.

2.2. Imports

On the import side, too, the share of manufacturing increased substantially. In 2002, its share in total merchandise imports stood at 69 per cent, up from 56 per cent in 1990. Food imports remained significant, at 16 per cent in 2002, compared with 19 per cent in 1990, reflecting a continuing gap in domestic production and consumption. Food shortages have been a major problem in Bangladesh, although over the last two decades there has been a significant increase in domestic production. Given its low agricultural productivity, Bangladesh needs to bridge the food gap and reduce its import dependence. As a net food importing country, it has continued interest and concerns regarding the WTO negotiations on agriculture.

2.3. Current-account balance and the role of remittances

As Table 2 indicates, with imports exceeding exports, Bangladesh had a continuous trade deficit, averaging around \$2 billion a year, during the period 1999-2003. However, the current-account balance turned positive during the fiscal year 2001/02, and remained so in the subsequent year. The current-account balance, according to the table turned positive only in 2002. This was mainly as a result of remittances by expatriate workers, which amounted to \$3 billion in 2003/03. On a net basis, remittance receipts are more important than export earnings from textiles and clothing, because the latter reflects “export illusion” caused by the high import content of those exports; thus its export earnings do not reflect the true extent of domestic value added. From this standpoint, it is not difficult to appreciate the importance attached by Bangladesh to WTO negotiations on services, particularly on the temporary movement of natural persons supplying services (Mode 4).

2.4. Trading partners

Nearly 75 per cent of Bangladesh’s exports in 2002 went to developed countries/regions. In particular, the EU accounted for 43 per cent of the country’s exports, followed by the United States and Canada, which together absorbed 29 per cent, and Japan 1 per cent. The picture is quite different on the import side, as developing countries accounted for more than half of Bangladesh’s imports, indicating the importance of South-South trade for its imports. In 2001, it sourced nearly 18 per cent of imports from the four members of the Association of South-East Asian Nations (ASEAN-4) – Indonesia, Malaysia, Singapore and Thailand – and 11 per cent each from China (excluding Hong Kong) and India (Bangladesh Bureau of Statistics, 2002). However, official figures tend to underestimate the true magnitude of imports from India due to the existence of illegal cross-border trade. Although reliable estimates of the overall volume or value of smuggling are not available, illegal imports are believed to be widespread and substantial (Rahman and Razzaque, 2003). Of Bangladesh’s imports from developed countries, 10 per cent came from the EU, 7 per cent from Japan, and nearly 4 per cent from the United States and Canada combined (UNCTAD, 2002).

Table 2. Balance of Payments (in million US\$)

Particulars	1999-00	2000-01	2001-02	2002-03	2003-04
Trade Balance	-1865	-2011	-1768	- 2215	- 2319
Receipts	5701	6419	5929	6492	7521
Payments	-7566	-8430	-7697	-8707	-9840
Services	-645	-914	-4989	-691	-874
Receipts	849	759	865	887	924
Payments	-1494	-1673	-1364	-1578	-1798
Income	-221	-264	-319	-358	-374
Receipts	97	97	50	64	63
Payments	-318	-361	-369	-422	-437
Current transfers	2394	2171	2826	3440	3743

Official	165	72	69	82	61
Private	2229	2099	2757	3358	3682
of which worker's remittances	1949	1882	2501	3062	3372
Current account balance	-337	-1018	240	176	176
Capital account	561	432	410	428	196
Capital transfers	561	432	410	428	176
Financial account	-185	407	71	413	78
(i) Direct investment	194	174	65	376	385
(ii) Portfolio investment	0	0	-6	2	6
(iii) Other investment	-379	233	12	35	-313
MLT loans 2/	806	790	733	918	544
MLT amortization payments	-396	-416	-421	-452	-397
Other long-term loans (net)	127	-13	-42	-20	-41
Other short-term loans (net)	56	86	20	142	13
Other assets	-55	-68	-52	-125	-125
Trade credit (net)	-641	-260	-253	-499	-321
Commercial Bank	-276	114	27	71	14
Assets	-161	147	-90	217	86
Liabilities	-115	-33	117	-146	-72
Errors and omission	125	-47	-356	-202	-279
Overall balance	164	-226	365	815	171
Reserve assets	-164	226	-365	--815	--171
Bangladesh Bank	-164	226	-365	-815	-171
Assets	-79	302	-276	-887	-235
Liabilities	-85	-76	-89	72	64

Note: Figures for 2003-04 are provisional

Source: Government of Bangladesh (2004).

2.5 External Market conditions

As least developed country (LDC), Bangladesh enjoys duty- and quota-free access to the EU market. However, to avail itself of preferential market access, it needs to meet the EU rules of origin. This puts Bangladesh at a disadvantage compared to certain other developing countries with relatively better-developed backward linkages. Under competitive export market conditions, these countries have a margin of advantage in maintaining cost competitiveness due to such linkages.

Another difficulty relates to the high tariffs faced by Bangladesh's ready-made garment exports in the United States market. Nearly half of its clothing exports to the United States face an ad valorem duty of 15 to 20 per cent, while another 13 per cent are subject to tariffs in excess of 25 per cent (Government of Bangladesh, 2004). The total tariff on Bangladesh's exports of \$2.3 billion to the United States in 2001 stood at \$331 million as compared with a tariff of \$330 million from French exports of \$30 billion to the United States the same year (Oxfam, 2004). This high tariff puts Bangladesh exports at a serious disadvantage vis-à-vis more than 70 African and Caribbean countries that are eligible for duty-free treatment under the Trade Development Act, 2000. As mentioned below, some sources are already predicting a loss of United States market share for Bangladesh's ready-made garment exports by 25 to 50 per cent following the expiry of the ATC.

Sanitary and phytosanitary measures have been another barrier to Bangladesh's exports, particularly its fisheries. This partly reflects the weakness of Bangladesh in effectively applying

uniform standards. Ongoing efforts to improve standards and quality control need to be supported by capacity building assistance to improve institutional and human capacities in this area.

3. Reform and liberalization policies

3.1. Historical background

Over the last three decades, Bangladesh's economic and policy orientation has evolved considerably, from a highly interventionist regime with widespread control on trade, the exchange rate and investment, to a substantially liberalized economic regime. At independence in 1971, Bangladesh faced the daunting challenge of rehabilitating its economy, which had suffered serious dislocation and devastation during a bloody war. The situation with regard to the external sector was particularly difficult. Faced with very low foreign exchange reserves, a shallow export base and rising import prices, the Government resorted to severe import controls, ranging from extensive use of non-tariff barriers (NTBs) to high and even prohibitive import duties. These protectionist measures were not dictated by a deliberate industrialization strategy aimed at influencing intersectoral or inter-industry resource allocation. Instead, these policies reflected desperate attempts to rein in a worsening balance-of-payments situation.

The principal underlying causes of external sector difficulties were a combination of a large and growing domestic deficit and an expansionary monetary policy, leading to an overvaluation of the real exchange rate. The policy-makers responded by treating the symptoms rather than addressing the root causes. It was perhaps difficult for the immediate post-independence government, which proclaimed socialism as a fundamental State policy, to abruptly change course. A case in point relates to public sector enterprises, which occupied a dominant position in the manufacturing and services sectors of the economy. Most of them had come under public ownership as part of the Government's declared socialist economic programme. Thus, while the State-owned 34 per cent of fixed assets of the industrial sector in 1970, its share rose to 92 per cent in 1972 as the result of a spate of nationalization. Collectively, these enterprises became a major drain on the budget, yet the policy orientation of the regime, coupled with the vested interests created by nationalization, prevented policy-makers from undertaking any serious reforms to improve efficiency or privatize.

3.2. Initial phases of reforms

The beginnings of policy reform and liberalization can be traced to deregulation measures starting in 1976 under a new government, which increasingly distanced itself from the earlier socialist approach. However, initial reform efforts had neither a clear direction, nor a broad time frame for implementation. This phase of muddling through lasted for about a decade. Four notable features of policy during this period of greater market orientation were: reduction of restrictions on investment; gathering momentum of denationalization of public sector enterprises; limited reduction of tariffs and NTBs; and incentive packages for the emerging ready-made garments sector. During the latter half of the 1980s, a more coherent picture of reforms began to emerge under structural adjustment policies (SAPs). In the area of tariff reforms, SAPs emphasized rationalization of the import regime, simplification and reduction of effective protection, elimination of negative and restricted lists of industrial imports, and facilitation of imports of raw materials and intermediate and capital goods, including the imports needed for direct and indirect exporters. However, political commitment to policy reforms remained problematic due to the Government's continued preoccupation with the need to gain political legitimacy, which greatly restricted its ability to implement actions deemed unpopular. There were also genuine concerns over the policy prescriptions of the donors, particularly with regard to the design and implementation of the SAPs and their distributive implications.

3.3. Recent reforms and liberalization policies

The policy reform process gained substantial momentum following the restoration of democracy in 1991. The main political parties embraced a liberal economic agenda, which augured well for

genuine and sustained political commitment to reform and liberalization. Since then, wide-ranging reforms and liberalization measures have been initiated and implemented, which have virtually transformed the policy landscape. These measures include tariff reductions, the elimination of a large number of quantitative restrictions (QRs), a flexible exchange rate regime, and the provision of a range of fiscal and financial incentives for export promotion.

The import policy for 2003–2006 aims at the following objectives: (a) further simplification of the import regime to respond to globalization and to facilitate increased liberalization in the light of the WTO agreements; (b) strengthened provisions for technology imports to enable the widespread dissemination of modern technology; (c) provision of simplified import procedures for export-oriented industries to enable the development of a robust export supply capacity; and (d) gradual removal of import protection to make available industrial raw materials and enhance competitiveness, competency and efficiency (Government of Bangladesh, 2003). At the same time, the overall trade policy emphasizes regional economic and trade cooperation. The key aspects of recent reforms and liberalization measures are discussed below.

3.4. Tariff reform

Throughout the 1990s, Bangladesh consistently reduced its import duties. The average unweighted customs duty fell from 47 per cent in 1993 to less than 16 per cent in 2004 (Table 3). During the same period, the average weighted import customs duty fell from 23 per cent to 12 per cent. The share of bound duties remained unchanged between 1997 and 2003, at 13.2 per cent, while the share of duty-free tariff lines increased nearly fourfold in a decade, from 4 per cent in 1992 to over 15 per cent in 2002. The maximum import duty was reduced drastically from 350 per cent in 1992 to 30 per cent in 2003. The 2004/05 budget provided a further reduction of the maximum tariff rate. The percentage of tariff lines with duties over 15 per cent fell from 80 per cent in 1992 to 42 per cent in 2002.

Table 3. Impact of tariff reforms on average customs duty rates

Financial Year	Unweighted Average (%)	Import Weighted Average (%)
1992-93	47.4	23.6
1993-94	36.0	24.1
1994-95	25.9	20.8
1995-96	22.3	17.0
1996-97	21.5	18.0
1997-98	20.7	16.0
1998-99	20.3	14.1
1999-00	19.5	13.8
2000-01	18.6	15.1
2001-02	17.13	9.73
2002-03	16.51	12.45
2003-04	15.62	11.48

Source: Government of Bangladesh (2004a)

However, due to the application of a number of other charges, such as supplementary duties and surcharges on imports, the average unweighted customs duty does not reflect the true extent of nominal protection. According to World Bank estimates, if these charges are taken into account, the average nominal protection rate stood at 27 per cent in 2002 (Ahmed and Sattar, 2004). This should be contrasted with the enterprise-level effective protection rate of 78 per cent for the same year, which points to the existence of tariff escalation. This observation is supported by Table 4, which shows the weighted average of custom duties on imports at different stages of production. Duties are higher on primary and intermediate goods than on final consumer goods, although, since 2001, weighted average duties on final consumer goods fell below those on intermediate goods. Thus, despite progress with tariff reforms, there is room for further liberalization.

Table 4. Impact of tariff reforms on average customs duties classified by type of imports

Classification	Financial Year											
	1997-98	1998-99	1999-00	2000-01	2001-02	2003-03	2003-04					
	W	UW	W	UW	W	UW	W	UW	W	UW	W	UW
	AV	AV	AV	AV	AV	AV	AV	AV	AV	AV	AV	AV
Primary goods	21.913	6.214	9.515	6.136	20.991	11.992	10.943	20.991	11.991	9.901	11.28	
Intermediate goods	19.221	3.319	0.213	1.317	115.114	9.115	7.815	6.116	16.131	4.911	5.781	4.415
Capital goods	12.1	8.212	3.8	116.1	9.9	8.03	7.70	6.97	3.26	8.03	7.70	7.85
Final consumer goods	30.620	129.217	631.016	522.641	11.942	6.001	3.962	2.641	11.942	1.271	0.68	

Source: Government of Bangladesh (2004a)

3.5. Elimination of QRs

There has been a substantial phasing out of quantitative restrictions, which took place in three stages since the early 1990s, to the extent that there may not be much room for their further removal. The first major slashing of QRs took place under the import policy order for 1991–1993, which reduced the number of items on the import control list from 325 to 193. During the period 1993–1997, the number of restricted items was cut to between 111 and 120. The import policy order for 2003–2006 reduced the number further, to 63, of which only 23 are for trade reasons (Table 5). As a result, the share of total Harmonized System (HS) 4-digit tariff lines subject to QRs fell more than threefold, from over 6 per cent in 1993 to less than 2 per cent in 2003. Today, the remaining restrictions are in large part maintained on public interest grounds, such as health and environmental concerns and for cultural and religious considerations. Although there is some room for further removal of controls, this will not be easy. A case in point is the current restriction on salt imports. Its removal can be argued on efficiency grounds, but needs to be weighed against the possible impact on the employment and livelihoods of nearly 40,000 raw salt producers.

Table 5. Progressive reductions of import restrictions

	IPO 1991-93	IPO 1993-95	IPO 1995-97	IPO 1997-02	IPO 2003-06
Number of items in the control list at the HS4-digit level	193 (15.65%)	111 (9.0%)	120 (9.7%)	122 (9.8%)	63 (5.1%)
Number of trade-related items in the control list at the HS 4-digit level	79 (6.4%)	19 (1.5%)	27 (1.9%)	28 (2.2%)	24 (1.9%)

Source: World Bank (2004)

Although a range of formalities still exists for customs clearance of controlled items, as well as permits and clearance for certain categories of imports, the situation is significantly better than it was in the early 1990s. For example, the requirement for export industries with a bonded warehouse facility to declare the country of origin of their imported raw materials has been discontinued, and the administrative complexities for obtaining prior approval from different ministries to establish industrial units have been significantly eased. An important institutional indication of progress in the elimination of import restrictions is the downsizing of the Office of the Chief Controller of Imports and Exports, regarded as an institutional symbol of import controls, as a result of the abolition of import licensing.

3.6. Exchange rate management

There have been significant improvements in exchange rate management since the 1990s, with the introduction of a flexible exchange rate policy. The multiple exchange rate system gave way to a unified rate in 1992, to be followed up by making the taka convertible for the current account in 1994. Adjustments in the rate of exchange have been undertaken from time to time, taking into account the

rates of inflation, movement of exchange rates and trade weights with partner countries. Finally, in May 2003 Bangladesh opted for an open market exchange rate policy by free float of the taka.

3.7. Export facilitation measures

To support export expansion, a number of incentives have been in place, such as lower interest rates on bank loans, duty-free imports of machinery and intermediate inputs, cash incentives, duty drawback and certain tax exemptions. The ready-made garments sector, in particular, has derived substantial benefits from a range of facilitation measures, comprising three main elements: (i) back-to-back letters of credit, whereby ready-made garment exporters are allowed to import their required inputs on a deferred payment basis against a master letter of credit; (ii) bonded warehouse facilities under which the ready-made garments exporters are allowed to import their required materials duty and tax free; and (iii) a mix of miscellaneous measures such as tax holidays, export credits and repatriation of profits by foreign investors.

3.8. Regional cooperation

Regional trade agreements (RTAs) can offer an opportunity for trade liberalization, including tariff reductions among participant countries, which can go beyond multilateral commitments. Bangladesh is currently a member of two RTAs: the South Asia Free Trade Area and BIMSTEC, an economic cooperation arrangement between Bangladesh, India, Myanmar, Sri Lanka and Thailand. These agreements are due to become operational in 2006. To what extent they will open up trade among participating countries will depend upon the outcomes of ongoing negotiations, including the depth and breadth of tariff cuts, disciplines on NTBs, the scope of negative lists, rules of origin and contingency provisions.

4. Implications of the reforms and liberalization

That policy reforms and trade liberalization policies pursued by Bangladesh have had manifold implications for its economy in general, and trade in particular, cannot be denied. However, the precise impact of these policies and actions is difficult to disentangle, as these are not the only factors that affect the economy. Whether a country is able to take full advantage of liberalization depends critically on its capacity to improve the supply of tradables and its flexibility in adjusting to changing price conditions. If its policies succeed in generating supply-side stimulus while enabling the economy to adjust to changing prices relatively quickly and smoothly, a positive impact on economic and human development might be expected.

The impact of policy reforms and trade liberalization in Bangladesh appears to be mixed: an improved, but not strong enough growth performance; the expansion of trade, but without adequate diversification; a reduction of poverty, but an increase in inequality.

4.1. Increased openness of the economy

As reform and liberalization measures were being pursued, the economy also became increasingly open to the world. This is indicated by Table 6, which shows export propensity, import penetration and the trade-GDP ratio for Bangladesh for the period 1990–2000. All three indicators rose steadily, in particular the trade-GDP ratio increased from over 26 per cent in 1990 to 42 per cent in 2000. This ratio compares favourably with some other countries in South Asia. For example, in 2000, the trade-GDP ratio for India was about 20 per cent, for Pakistan it was 34 per cent, and for Sri Lanka it was nearly 89 per cent. The contribution to greater openness was due mainly to exports, as Bangladesh's export-GDP ratio rose faster than that of some other South Asian countries. This has implications for regional trade cooperation among countries in the region.

4.2. Growth performance

A comparison of GDP growth rates in constant prices between the 1980s and the 1990s indicates that there was an improvement in growth performance. The average growth rate in the 1990s was 4.8 per cent compared with 3.6 in the 1980s. Also, the growth rate was higher during the period 1996–2000, at 5.2 per cent, than during 1990–1995, at 4.4 per cent. It reached the highest point at 5.9 per cent in 2000, but fell back to an average of 5 per cent in the early years of the present decade. Some observations need to be made in this regard. First, while there can be many causes for this rise in the growth rate, reforms and liberalization played an important role through greater openness of the economy and improved macroeconomic management. Second, the increase has been modest and remained rather flat, without displaying a breakthrough. It has remained significantly below the 7 per cent target of the Programme of Action for the LDCs for the current decade, which would be necessary to generate a relatively robust supply capacity and make an accelerated and substantial dent in poverty. Third, the relatively weak supply response raises the question as to whether the type of policy reforms being undertaken by the country are enough to address underlying structural, institutional and related constraints on growth and diversification. A more strategic and calibrated approach might be better suited to the particular needs and circumstances of the country, while also taking full advantage of the various special and differential provisions under the WTO agreements that offer policy flexibility.

Table 6. International openness of the economies of selected South Asian countries

Year	Bangladesh			Pakistan			Sri Lanka			India		
	Export Propensity (%)	Import Penetration (%)	Trade Ratio (%)	Export Propensity (%)	Import Penetration (%)	Trade Ratio (%)	Export Propensity (%)	Import Penetration (%)	Trade Ratio (%)	Export Propensity (%)	Import Penetration (%)	Trade Ratio (%)
1990	8.3	16.7	26.7	14.8	19.2	35.1	30.2	35.3	68.2	7.1	8.4	15.7
1991	8.8	15.1	25.0	17.0	18.3	35.6	28.7	35.3	67.6	8.6	8.6	17.2
1992	10.0	15.3	26.3	17.4	19.9	37.9	31.8	37.6	72.8	9.0	9.7	18.8
1993	10.6	16.5	28.2	16.3	21.1	38.6	33.8	39.6	77.1	10.0	10.0	20.0
1994	11.8	17.1	30.0	16.3	18.5	35.3	33.8	40.8	79.4	10.0	10.3	20.4
1995	14.2	20.8	36.6	16.7	18.9	36.1	35.6	41.7	81.6	11.1	12.1	23.3
1996	14.2	21.8	38.1	16.9	20.5	38.3	35.0	40.3	78.9	10.6	11.7	22.5
1997	15.4	21.6	38.7	16.1	19.8	36.9	36.5	40.7	80.1	10.9	12.0	23.1
1998	17.2	22.2	40.9	16.5	17.3	34.0	36.2	39.9	78.5	11.2	12.5	23.9
1999	16.7	22.1	40.3	15.6	16.7	32.5	35.5	40.1	78.8	n.a.	n.a.	18.26
2000	17.5	23.0	42.1	16.2	17.9	34.5	39.1	44.9	88.8	n.a.	n.a.	19.41

Notes: (i)

Export Propensity: (Exports of goods and services/GDP) as percentage of GDP.

(ii) Import Penetration: (Imports of goods and services/Domestic Demand).

(iii) Domestic Demand: = GDP + Imports of goods and services - Exports of goods and services

(iv) Trade Ratio = (Exports of goods and services + Imports of services/GDP *100

Source: Bangladesh Government (2003)

4.3. Competitiveness: Inflation and the real effective exchange rate

As noted above, keeping inflation low has been an important policy objective, which has been well achieved by Bangladesh, especially compared with other countries in the South Asian region (Table 7). For every year during 1990–2000, except 1999, inflation in Bangladesh was lower than the average for South Asia. Moreover, all the other countries in the region faced double-digit inflation at some point during the decade, while Bangladesh managed to keep inflation at single-digit levels, and in some years below 4 per cent.

Table 7. Inflation in selected South Asian countries

Country	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000
Bangladesh	8.9	5.1	1.3	3.3	8.9	6.6	2.6	7.0	9.0	3.9
India	13.5	9.6	7.5	8.4	10.9	5.7	4.8	6.9	3.3	4.8
Pakistan	12.7	10.6	9.8	11.2	13	10.8	11.8	7.8	5.7	5.0
Sri Lanka	12.2	11.4	11.7	8.4	7.7	15.9	9.6	9.4	4.7	6.5
South Asian Average	13.1	9.6	7.6	8.3	10.9	6.7	5.6	7.1	4.1	5.0

Source: Islam, M.A. The Impact of Exchange Rates on Selected Economic Indicators in Bangladesh in Centre for Policy Dialogue, Employment and Labour Market Dynamics: A Review of Bangladesh's Development 2002 (Dhaka, University Press Limited, 2003).

An important result of exchange rate reform and liberalization is that the real effective exchange rate (REER), another important indicator of competitiveness, has remained quite stable (Table 8) (Islam, 2003). For much of the 1990s the Central Bank seems to have opted for a stable REER. However, since 1998 the currency has seen stronger depreciation, reflecting the increasing interest of policy-makers in more actively using the exchange rate as a policy tool to promote trade, particularly in the context of currency depreciation by some other countries in the South Asian region.

Table 8. Trends in nominal and real effective exchange rates

Year	NER	NER Index	REER Index
1991	36.60	100.0	100.0
1992	38.95	106.6	100.2
1993	39.57	108.1	104.6
1994	40.21	109.9	102.2
1995	40.28	110.1	102.9
1996	41.79	114.2	103.8
1997	43.89	119.9	105.5
1998	46.91	128.2	105.4
1999	48.00	131.4	112.8
2000	52.00	142.1	116.2
2001	56.80	155.2	...

Source: Islam, M.A. The Impact of Exchange Rate Changes on Selected Economic Indicators in Bangladesh. Centre for Policy Dialogue, Employment and Labour Dynamics: A Review of Bangladesh's Development 2002 (Dhaka: University Press Limited, 2003)

4.4. Impact on government revenue

Despite a substantial reduction in tariffs, overall revenue receipts from customs duties have displayed a steady increase (Table 9). This can be explained by a rising level of imports, coupled with improved revenue collection. Customs duties continue to account for a substantial share of total government revenues. The impact of further substantial cuts in tariff rates in the future may not be offset by any increase in the quantity of imports, and could consequently reduce the overall level of

revenue. A more broad-based revenue structure, along with greater efficiency in collection, would be needed to address the possible revenue implications of further tariff liberalization.

Table 9: Sources of and trends in tax receipts

(In million taka)

Type of tax	1997-98	1998-99	1999-00	2000-01	2001-02	2002-03	2003-04
1. Tax on income and profit	21000	23350	29800	36000	41000	47880	52700
2. Tax on transfer of property and assets	110	100	20	00	00	10	...
3. Value added tax (VAT)	46920	48000	54050	61320	69600	80710	85750
4. Customs duty	44600	47550	45360	47700	53500	58750	73000
5. Excise duty	2140	2050	2400	2750	3000	3100	1700
6. Supplementary duty	23840	2540	26640	33630	38500	43900	54300
7. Electricity duty	1200	900	450	200	80	100	...
8. Other taxes and duty	1190	1150	1280	1400	1620	3050	3050
9. Narcotics duty	280	400	270	400	300	350	400
10. Motor vehicles tax	1150	1250	1110	1440	1450	2250	2410
11. Land tax	1970	2150	2660	2140	2140	2060	2590
12. Stamp (non-judicial)	5610	6250	6920	7920	8110	7340	7100
Total tax receipts	150010	158550	170960	19490	219300	2495000	28300

Source: Government of Bangladesh (2004)

4.5. Levels of employment

In the manufacturing sector, the employment impact of reforms and liberalization depends on a number of factors. There could be employment gains, particularly in the ready-made garments sector. However, there could also be employment losses due to import competition and privatization as well as downsizing and closing down of public sector enterprises, which are often characterized by low labour productivity. In the absence of reliable statistics, especially for the latter two categories, it is difficult to obtain an aggregate picture of the employment implications of reform efforts.

In the case of the ready-made garments sector, the number of workers employed has increased nearly tenfold during the last 15 years (Table 10) (Ahmed and Sattar, 2004). Most of the increase took place in the 1990s when liberalization gathered serious momentum. Even as the expiry date of the ATC drew nearer, the number of ready-made garments factories and the number of workers employed by the sector continued to increase. The significance of employment in the ready-made garments sector does not concern merely numbers; it also has social implications, as nearly 90 per cent of ready-made garment workers are women from the poorer strata of the society. Despite rapid growth in this sector's employment, overall manufacturing employment has fallen in relative as well as absolute terms (Muqtada, 2003). This may have been caused by deindustrialization, or a rise in productivity, or a combination of the two. In particular, reform of public sector enterprises witnessed job losses in varying degrees. On the other hand, the rise in the manufacturing sector's contribution to GDP concurrently with the reduction in its share of employment point to an improvement in productivity. This is further supported by the fact that there were increases in manufacturing wages relative to agriculture throughout the 1990s.

Table 10. Growth of the ready-made garments sector

YEAR	Export Volume 000 doz	Export mill US	Share in total exports	Employment workers (in millions)	Number of garment factories
1985-86	4762.58	131.48	16.05	0.198	594
1990-91	30566.63	866.82	50.47	0.402	834
1995-96	72005.00	2547.13	65.61	1.290	2353
1999-2000	111905.77	4349.41	75.61	1.600	3200
2001-2002	140444.59	4583.75	76.57	1.800	3618

Source: Ahmed, S and Sattar Z (2004)

4.6. Implications for poverty

Available estimates indicate that during the 1990s Bangladesh succeeded in reducing poverty on average by 1 per cent per annum (Government of Bangladesh, 2004b). According to World Bank estimates, the poverty headcount index declined from 58.8 per cent in 1991–1992 to 49.8 per cent in 2000. Compared with a headcount index of 88.15 per cent in 1972–1975, this represents a substantial reduction in the incidence of poverty over the past three decades (Ahmed and Sattar, 2004). It is difficult to say the extent to which policy reforms and liberalization have contributed to this decline in poverty, because a variety of factors, policies and institutions have combined to produce this result, and their respective contributions are difficult to isolate. Nonetheless, a general equilibrium analysis indicates that the reforms and liberalization efforts of Bangladesh have been pro-poor in general, although the resulting gains have been small and distributed unevenly across different households, with relatively well-off households gaining more and the extremely poor less (Mujeri and Khondker, 2002).

This raises the question of the links between liberalization, poverty reduction and income distribution. Available evidence indicates that income inequality increased during the 1990s and reached a relatively high level (Government of Bangladesh, 2004b). The Gini coefficient for urban areas rose from 0.33 per cent in 1991–1992 to 0.44 per cent in 2000, and for the rural areas, from 0.26 per cent to 0.36 per cent over the same period. This growing income disparity has particular relevance for poverty reduction in the context of the current GDP growth rate, which is not strong enough to lift the incomes of the poorer segments of the population, given the rise in inequality. This raises the issue of the role of policies in influencing both quantity and quality of growth: since growth has been modest and has increased the degree of inequality, policies should aim simultaneously to improve growth performance and income distribution in favour of the poor.

5. Adjustment costs arising from trade agreements

The realities of the external sector and related domestic compulsions have raised concerns and interest among policy-makers with regard to the adjustment implications of trade agreements in three key areas: textiles and clothing, food, and remittances by expatriate workers. As noted above, textiles and clothing and remittances are the major items of Bangladesh's export economy, while the country remains a net food importer.

5.1. Textiles and clothing

The ready-made garments sector has grown from an infant industry to become the dominant player in the merchandise trade sector. This was facilitated by external market conditions, particularly by quotas under the Multi-Fibre Arrangement (MFA), as well as by domestic support measures. This sector plays a central role in the economy and in society because of its contribution to manufacturing output, exports, imports, investment, business development and employment – including female employment – and because of the variety of linkages it has created with the rest of the economy. While the possible implications of the expiry of the ATC, which provided for the phase-out of the MFA by the end of 2004, are by no means clear, an adverse change in the external market conditions

might have serious economic and social consequences for Bangladesh. According to an IMF paper (Mlachela and Yang, 2004) as much as over a quarter of Bangladesh's garment exports, along with a sizeable share of employment in ready-made garments could be lost within a year of the ATC's expiry. A WTO study has also warned that Bangladesh may lose up to 50 per cent of its market in the United States (Nordas, 2004).

Bangladesh's strength in the textiles and clothing sector lies in its considerable experience and reputation in production and trade, competitive labour costs, abundant and trainable labour force, and duty-free access to the EU markets. On the other hand, the causes of uncertainty include continued high dependence on imported inputs and on buyers' agents, low labour productivity, limited backward and forward linkages within the sector, long lead-times, and weaknesses in the investment climate, including FDI.

In the immediate future, there may not be pronounced changes, as the global market would need time to adjust to post-MFA conditions. For importers, a shift in sources of supply carries with it opportunity costs. They may also like to maintain a degree of diversification of their imports. Further, the terms of accession of China to the WTO, which is expected to make substantial gains from the expiry of the ATC, provide that WTO Members can invoke safeguard protection measures against its textile exports under certain conditions. This could also discourage importers in relocating sources of inputs to China at least in the short-run. The United States has already moved to apply restrictions on certain categories of Chinese textiles that are of interest to Bangladesh. As a result, policy-makers and industry leaders in Bangladesh remain cautiously optimistic about the short-term prospects of the ready-made garments industry in Bangladesh. This is reflected in the view of industry leaders that they did not expect a fall in export orders in 2005 (*The Daily Star*, December 24, 2004).

Beyond the immediate term, all this might change. A realistic assessment of adjustment requirements and costs needs to be undertaken at an early date to help policy-makers fully appreciate the possible opportunities and challenges, and to formulate a strategic approach. Policies and measures should aim not merely at the survival of the sector, but also at strengthening export presence on a longer-term basis, with an emphasis on progressively enhancing participation throughout the value chain and increasing domestic value added, including by entering into more dynamic segments of the textiles and clothing sector. Meanwhile, the international community could help maintain and improve the competitiveness, export presence, domestic value added and employment of this sector. Major markets (particularly the United States market) could offer duty-free access to Bangladesh's exports, if they have not already granted such access; other areas of assistance could include infrastructure support, facilitation measures to reduce transaction costs, and capacity building assistance to improve productivity and the quality of decision-making.

5.2. Agriculture

Bangladesh has combated its chronic food shortages rather well, and famine appears to be a thing of the past. However, occasional and localized food shortages do occur because of natural disasters and inefficiencies in food distribution. As noted earlier, agricultural productivity remains low, and its substantial improvement could reduce import dependence, at least as far as the main cereals are concerned. However, a major difficulty is that of securing regular water supply. A solution to this issue is not entirely in the hands of policy-makers since much depends on how the issue of sharing the water resources of the major common rivers with India is resolved. At any rate, should domestic support and export subsidies by developed countries to this sector materialize as a result of the Doha Round negotiations on agriculture, there might be increases in the prices of agricultural items during the adjustment period. This is a source of disquiet as far as food security for Bangladesh is concerned. Policy-makers as well as donors will need to study the implications for food availability during the negotiations on agriculture, to ensure that the Marrakech Ministerial Declaration on the Net Food Importing Countries is not undermined.

On the other hand, possible price increases may have a positive impact, particularly with regard to food production by smallholders. The competitiveness of Bangladeshi farmers, over 60 per cent of whom have an average farm size of less than one acre, is being undermined by low profitability. This is due to higher costs of material inputs relative to prices in the overall context of low labour productivity and low yield per acre. An increase in output prices could possibly change the current cost–price balance and make agricultural production more profitable. This, in turn, could encourage investment in this sector and raise overall productivity. Agricultural and trade policies need to bear in mind this scenario, while also paying attention to the implications for food security.

5.3. Temporary movement of natural persons supplying services (Mode 4)

The experience of Bangladesh shows that foreign market access for service provision by natural persons through temporary movements can have important positive effects in terms of improved availability of scarce foreign currency, improving the current-account balance, financing of higher levels of imports, economic growth, employment generation and poverty reduction. Bangladesh has a large reservoir of low-skilled or unskilled labour, and it is mostly these workers, drawn from the lower income groups, who seek work abroad, especially in the Middle East (Government of Bangladesh, 2004). Their foreign employment has had a direct positive impact on their economic status.

Mode 4 offers an important opportunity for Bangladesh for substantial development gains from services exports, and an improvement in skill levels could significantly add to such gains. However, the initial offers by developed countries are yet to involve any significant liberalization of Mode 4 in respect of categories of particular interest to developing countries. Specifically, the elimination of quantitative restrictions such as economic needs tests, delinking Mode 4 from commitments on commercial presence, and the introduction of simplified visa schemes would help Bangladesh strengthen its export performance in this sector. At the domestic level, Mode 4 needs to be better linked with human resource development policies and strategies to improve the skills profile. It is also important to improve the capacity to closely monitor offers under Mode 4 for access to major markets and to identify opportunities.

5.4. Potential new and dynamic sectors

Trade agreements can have implications for the participation of countries in dynamic and new sectors of world trade. For example, the exemptions for Bangladesh from obligations under the WTO Agreement on Trade-related Aspects of Intellectual Property Rights (TRIPs), arising from its status as a least-developed country (LDC), as well as the WTO Decision on TRIPs and Public Health. The country has a long-established pharmaceutical base with over 200 licensed manufacturing units, employing an estimated 50,000 skilled workers (Anwar, 2003). It exports high quality pharmaceutical products to over 50 developing countries at what are reported to be competitive prices (Chakraborty, Anwar and Ahmad, 2003). A major difficulty is that the active ingredients of these pharmaceutical products are externally sourced. To become competitive on a sustainable basis, the sector needs to establish strong backward linkages.

Other possible export sectors and products include leather goods, high-value-added textiles and clothing, information, communication and technology (ICT) products and ICT-enabled services, specialized and niche products (including those of interest to expatriate Bangladeshi and other South Asian nationals), and agro- and marine products. Besides identifying potentially new export opportunities and formulating appropriate strategies and policies, Bangladesh needs to carefully monitor and effectively participate in the NAMA negotiations, since their outcome will not only have important implications for its future global trade, but also affect its international competitiveness in existing and potential export sectors. At the same time, it would be necessary to undertake detailed sectoral and subsectoral studies to identify export opportunities based on revealed comparative advantage and identify supply-side constraints, including access to infrastructure and credit. There is also a need to rationalize the incentives structure, which currently focuses mainly on the ready-made

garments sector, by making the incentives more coherent and broad-based so that they can effectively respond to the requirements of other sectors with export potential.

References

- Ahmed, S and Sattar Z (2004). Trade Liberalization, Growth and Poverty Reduction: The Case of Bangladesh. Washington, D.C., World Bank.
- Anwar, SF (2003). Pharmaceutical sectors of Bangladesh: Trade prospects with Nepal and the impact of TRIPs. In FE Cookson and AKMS Alam Towards greater Sub-Regional Economic Cooperation. Dhaka, University Press Limited.
- Bangladesh Bureau of Statistics (2002). Statistical Pocketbook 2002.
- Chakraborty, P, Anwar SF, and Ahmad, M (2003). Strategies under the WTO Regime: The Pharmaceutical Sector of Bangladesh, Journal of Bangladesh Studies, Vol. 5, No. 2, Pennsylvania State University, 2003.
- The Daily Star (2004). International agencies sceptical about Bangladesh's RMG future. December 24, 2004 issue, Dhaka.
- Government of Bangladesh (2003). Bangladesh Economic Review 2003.
- Government of Bangladesh (2004a). Bangladesh Economic Review 2004.
- Government of Bangladesh (2004b). Unlocking the Potential: National Strategy for Accelerated Poverty Reduction.
- Islam, MA (2003). The Impact of Exchange Rate Changes on Selected Economic Indicators in Bangladesh. In Centre for Policy Dialogue, Employment and Labour Market Dynamics: A Review of Bangladesh's Development 2002. Dhaka, University Press Limited.
- Mlahela, M and Yang, Y (2004). The end of textiles quotas: A case study of the impact on Bangladesh IMF Working Paper WP/04/108. Washington DC., International Monetary Fund.
- Mujeri, M and Khondker, B (2002). Poverty Implications of Trade Liberalization in Bangladesh: A General Equilibrium Approach Globalization and Poverty Globalization and Poverty Programme funded by DFID, UK, 2002.
- Muqtada, M (2003). Promotion of employment and decent work in Bangladesh: Macroeconomic and labour policy considerations. In: Centre for Policy Dialogue, Employment and Labour Market Dynamics: A Review of Bangladesh's Development, 2002. Dhaka, University Press Limited.
- Nordas, H (2004). The Global Textile and Clothing Industry post the agreement on Textiles and Clothing. WTO Discussion Paper No. 5 Geneva, World Trade Organization.
- Oxfam(2004). Stitched Up: How rich-country protectionism in textiles and clothing trade prevents poverty alleviation. Oxfam Briefing paper, April, 2004.
- Rahman, A and Razzaque, A (2003). Informal Border Trade between Bangladesh and India: An Empirical Study in Selected Areas. In FE Cookson and AKMS Alam Towards greater Sub-Regional Economic Cooperation. Dhaka, University Press Limited, 2003.
- UNCTAD (2002). Least Developed Countries Report, 2002.

World Bank (2004). *Trade Policy in South Asia: An Overview*. Washington, D.C., World Bank, September 2004.