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International  
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# Export Performance of Bangladesh

Global Recession and  
After



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## **Abstract**

### **Export Performance of Bangladesh: Global Recession and After**

World trade was severely disrupted by the global recession of 2008-09 with exports of most countries declining sharply. The economies of both of the major export markets of the world, the USA and the EU, shrank very substantially. This reduced their aggregate domestic expenditure, which in turn reduced their import demand for goods from the rest of the world. Curiously the export of Bangladesh, especially the export of ready made garments, which constitute more than three-quarters of the total export of the country, did not decrease much despite the fact that most of it is sold to the EU and the USA. It is argued that this favourable outcome is due to two factors. First, the exports of Bangladesh are almost entirely consumer goods whose demand does not fall as sharply as income; and second, Bangladesh has acquired a competitive edge in the world apparel market. Since most other competing countries did not fare as well during the recession, the share of Bangladesh in the total ready made garments import of the EU and the USA increased significantly. Although the impact of the recession has not fully played out, it seems certain that Bangladesh would emerge out of the recession as a more competitive economy than most of its rivals due to its intrinsic comparative advantage in ready made garments manufacturing. Recent export data that show an explosive growth of ready made garments export confirm that Bangladesh is consolidating its position in the world market.

## Introduction

The development strategy of Bangladesh underwent a significant change in the early 1990s. After experimenting with domestic demand based import substitution strategy for nearly two decades, the country finally opted for a more open market-based economy where the private sector would take the lead role in the development of the economy. Meaningful trade liberalisation reforms were introduced that slashed tariff rates, reduced tariff slabs and largely eliminated quantitative restrictions. Exports were encouraged through various measures. As a result the trade ratio increased steadily.

An essential aspect of export trade is that the demand for a country's exports depends on the import propensities of the people of other countries. Such propensities are known to be influenced by their economic growth. The recession that ravaged much of the world, especially the western world, during 2008 and 2009 had profound implications for export efforts, and hence economic growth, of the world. As the western economy moved in the negative growth zone, their imports plummeted. Consequently the exports of the rest of the world also plummeted.

Initially the economy of Bangladesh was not much affected giving rise to a false hope that Bangladesh may be able to escape the adverse impact of the recession in the West. Indeed, many a people thought that since Bangladesh specialised in producing cheaper apparel products, and since the economic hardship caused by the recession would force consumers in the western world to cheaper products, import demand for Bangladeshi apparel, and hence import from Bangladesh, would increase. The argument was based on false premises. It is abundantly clear from recent data that apparel export of Bangladesh did not escape the impact of the recession, the impact was delayed.

This paper examines the recent performance of the export sector of Bangladesh with special emphasis on apparel exports to the major markets during the recession. The overall reduction in imports of the West due to the recession appears to have hit the apparel exports with a lag of about two quarters. The impact has been mild relative to that of other commodities. One of the principal reasons for this is that the recession has had a relatively mild impact on apparel imports of the West compared to imports of other commodities. Another reason is that the apparel exporters of Bangladesh have competed very vigorously in the shrinking market and actually increased their market share. Bangladesh has emerged out of the recession as a major source of apparels for the world market and is poised to further consolidate its position.

## Export Trade of Bangladesh

When it emerged as an independent country Bangladesh was a relatively closed economy with the trade ratio at less than one-seventh.<sup>1</sup> Since then merchandise exports and imports of Bangladesh have increased greatly in quantity and variety. In the early years, the country's exports comprised mostly raw jute and a few jute good items. These accounted for about nine-tenths of the total export revenue of US\$377 million during the fiscal year 1972-73.<sup>2</sup> By the end of the 1970s this ratio fell to about three-quarters of the total export revenue of

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<sup>1</sup> Trade ratio is defined as the ratio of the value of import and export to the GDP of the country.

<sup>2</sup> Fiscal year in Bangladesh runs from July to June.

US\$761 million. The export composition changed dramatically since then; ready made garments (RMG) comprising knitwear and woven apparel products (HS61 and HS62) emerged as the principle export items of the country while jute export stalled.<sup>3</sup> The country achieved remarkable success in export expansion, mainly because of the stellar performance of the RMG industry. The total merchandise export exceeded US\$16 billion mark by 2009-10, which was shipped to about 200 countries and custom territories around the world. The export earnings of the country are now equivalent to 18 percent of GDP suggesting considerable and growing importance of the export sector in the national economy.

The importance of RMG in the country's export basket has increased steadily. From its humble beginning in the late seventies, the RMG sector now accounts for more than three-quarters of the total exports of the country. Thus, during the last three decades Bangladesh has moved from an excessive dependence on jute products to RMG products in its export trade. Any efforts to significantly diversify export beyond jute and apparels did not bear fruit.

Although Bangladesh sells its products to numerous countries, only two markets account for most of the export earnings. It earned 50.8 percent of the total export revenue from the European Union market and 24.4 percent from the US market in 2009-10.<sup>4</sup> Canada of late has become a significant export destination and provided market for 4.1 percent of the total export. Turkey accounted for another 3 percent of the total export of Bangladesh.

The USA is the single largest importing country of Bangladeshi products with Germany and UK as the second and the third largest. Japan, India, China, Australia, South Korea and Brazil are considered the future major destinations of Bangladeshi exports although the current export volume to these countries is small relative to that to the EU and the USA.

The market for the principal export item of Bangladesh, ready made garments, is even more concentrated. About 56.5 percent of the exported apparel items go to the EU countries and 27.8 percent to the USA. Canada has emerged as a significant importer of apparels from Bangladesh since it granted duty-free access to the least developed countries (LDC) of the world in January 2003; it now takes in 5.0 per cent of the RMG export of Bangladesh. Thus the North American and the European market together provide outlet for about 90 percent of the RMG export of Bangladesh. The growth in the total RMG export of Bangladesh will thus depend to a large extent on the pattern and growth of RMG demand in these countries in the short to medium term.

## **Import and Income**

Import of a country is strongly linked to the health of the economy. As shown in Figure 1 below, there is a very close correspondence between the world real GDP growth and export (import) growth.<sup>5</sup> It is noteworthy that import of a country fluctuates a great deal more than

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<sup>3</sup> HS, short for Harmonized Commodity Description and Coding System, is an international system of classifying traded goods.

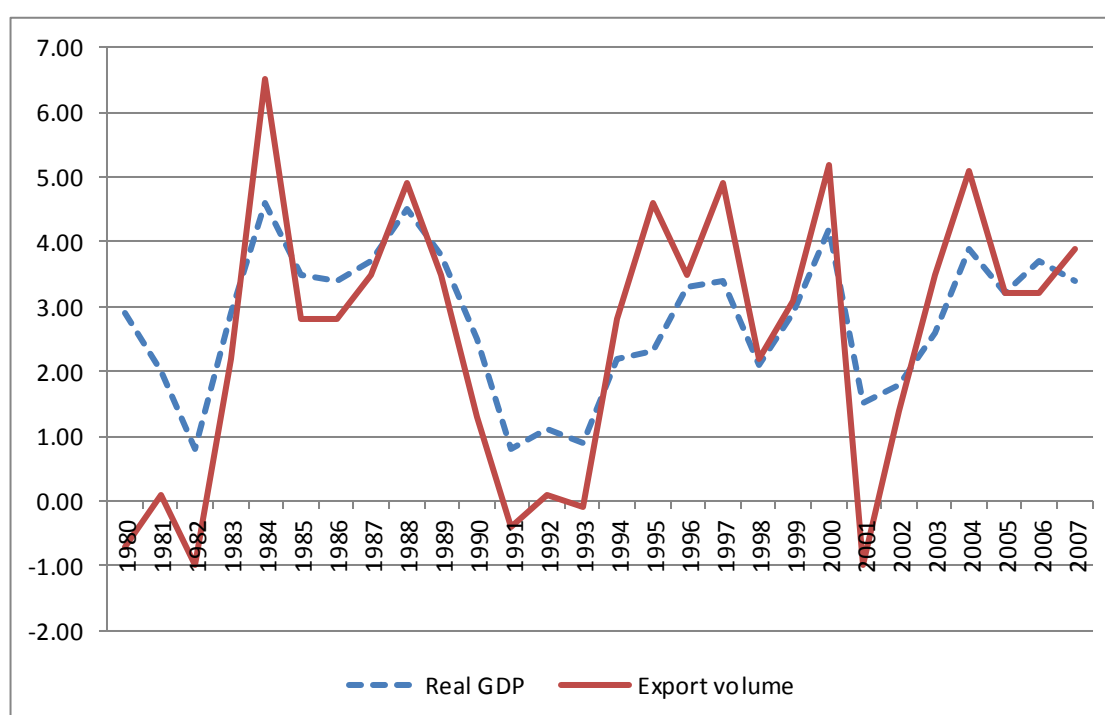
<sup>4</sup> Throughout this paper European Union refers to the Union of all 27 member states. Thus 28 countries take in 78.5 percent of the total exports of Bangladesh. It may be mentioned that only 6 member countries, viz. Germany, UK, France, Netherlands, Italy and Spain, account for 84 percent of the total EU imports from Bangladesh, and 10 countries account for 96 percent.

<sup>5</sup> World exports differ from world imports by the transport and associated costs since exports are usually recorded on FOB basis, while imports are recorded on CIF basis.

GDP, i.e. the impact of a change in GDP growth rate falls disproportionately on import. Hence the trade sector bears the brunt of any fluctuations in the economy. The recent recession in the global economy sharply reduced the import demand of the major economies, including the principal markets of Bangladesh, the EU and the USA. This impacted adversely on the export performance of Bangladesh. There was only a limited scope (through productivity improvements, sales promotion and price cuts) to gain at the expense of other exporters to these destinations.

The adverse impact of the recession fell on the import demand of the EU and the USA across the entire commodity spectrum. The EU countries had negative growth in the import of 89 of the 97 commodity codes (chapters) at the two digit level of the Harmonised System, frequently by very large amounts. The total import declined by 23.4 percent between 2008 and 2009. The situation was worse in the USA. Its import demand fell by whopping 25.9 percent. Only 6 of the commodities at the two digit level of the HS code escaped negative growth.

**Figure 1: World GDP and export growth**



Source: WTO: *International Trade Statistics* 2008

## The Global Crisis and Bangladesh

The recent global economic crisis had its origin in the sub-prime crisis in the US housing market. The failure to foresee and contain the astronomical growth of highly toxic assets brought about a full-scale financial crisis in the USA in 2007. The tightly integrated global financial market soon transmitted the US financial crisis to the developed countries of the world whose economies, especially their financial sectors, were more closely integrated. Eventually the crisis also spread to the emerging markets such as China and India. The financial market of Bangladesh was largely immune from this crisis since it did not have much exposure to the world financial market because of the inconvertibility of the capital account of the balance of payments.

However, the bankruptcies of many reputed financial institutions in the USA and the EU and the consequent credit crunch brought about by the financial crisis soon caused a full-scale economic recession in the western world from the second half of 2008. Indeed, this recession was the worst since the Great Depression of the 1930s both in terms of depth and duration. Since the economies of all countries of the world are now linked via trade, economic downturn in the West also had adverse implications for the non-Western countries. It reduced the import demand of the West, much of which was supplied by developing countries including Bangladesh. The consequent reduction in aggregate demand engendered an economic slowdown in these countries, too. Their exports decreased, in some cases drastically, which in turn brought about a sharp reduction in their growth rates. Bangladesh did not escape the global impact of the recession in the West although the severity of the impact was much less than that on other countries. Exports declined by only 1.9 percent between 2008 and 2009.<sup>6</sup> On a fiscal year basis exports in 2009-10 were only 4.1 percent greater than that in 2008-09.<sup>7</sup>

The seasonally adjusted quarterly real GDP growth rates of the principal markets of Bangladesh the EU, the USA and Canada from the first quarter 2007 to the third quarter of 2010 on a year-on-year (y-o-y) basis are shown in Figure 2.<sup>8</sup> The EU and the USA are the two major economies accounting for more than one-half of the global GDP and trade. The GDP of the USA declined for five quarters commencing from the third quarter of 2008, while the GDP of the EU declined for five quarters beginning fourth quarter of 2008. (On a quarter-on-quarter basis the negative growth started a quarter earlier for both.) The growth rate in both economies reached the lowest level during the first half of 2009. The USA climbed out of the recession in the fourth quarter of 2009, but the EU was still in the negative zone. (On a quarter-on-quarter basis both posted positive growth by the third quarter of 2009.) The EU suffered much deeper recession than that suffered by the US economy. The EU quarterly GDP growth rates during the first and second quarters of 2009 were -5.11 and -5.08 percent respectively whereas in the USA the growth rates were -3.80 and -4.11 percent respectively. Canada was also battered by the recession, which lasted five quarters with the trough (-3.19 percent) reached in the second quarter of 2009. The financial crisis and the recession that had originated in the USA had a greater impact on the EU than in the USA itself. In a global economy, inappropriate policies or activities in one country can have an adverse impact on

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<sup>6</sup> Export Promotion Bureau, Bangladesh, *Export Performance*.

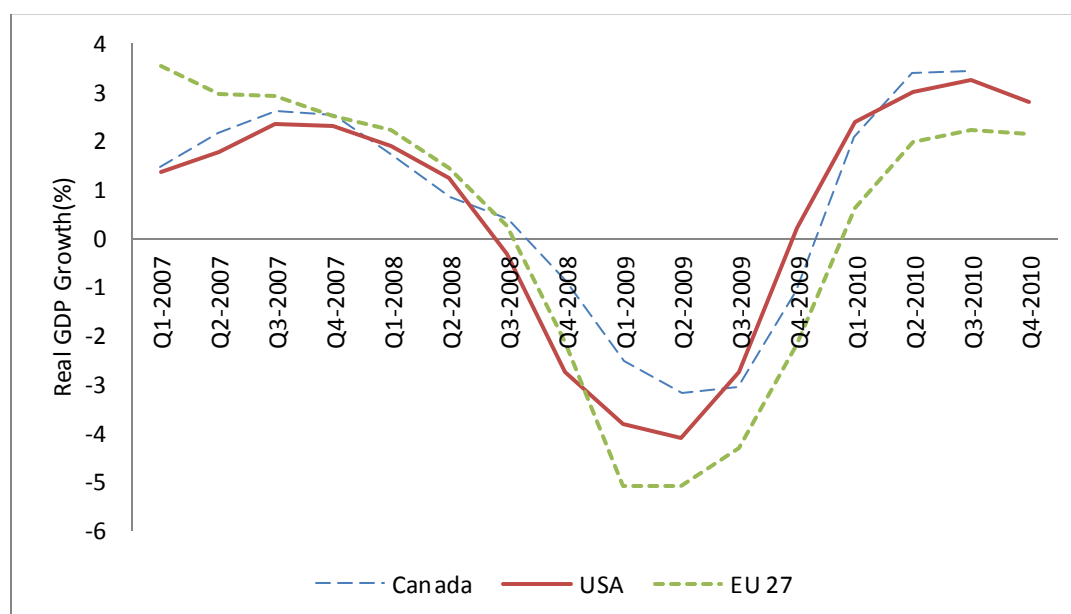
<sup>7</sup> The annual average growth rate of exports during the previous 5 years was 15.4 percent.

<sup>8</sup> Year-on-year compares the value of a variable in any quarter (or month) of a year with the value in the same quarter (or month) of the previous year. It is sometimes also termed point-to-point change.

partner countries, which could be sometimes greater than that in the source country. Hence, there is a legitimate concern in partner countries about domestic policies and happenings in a country.

Both the EU and the USA had very low positive growth for a quarter at the end of the recession, but thereafter both bounced back to their normal growth patterns with the US economy performing better than the EU economy. Canada had fairly strong growth exceeding both the EU and the USA from the beginning of 2010. The close correlation between the growth patterns of these economies is noteworthy; when a large economy does poorly, the economies of its trade partners are not immune from its adverse impact.

**Figure 2: Quarterly real GDP growth (percent, y-o-y) of EU, USA and Canada**

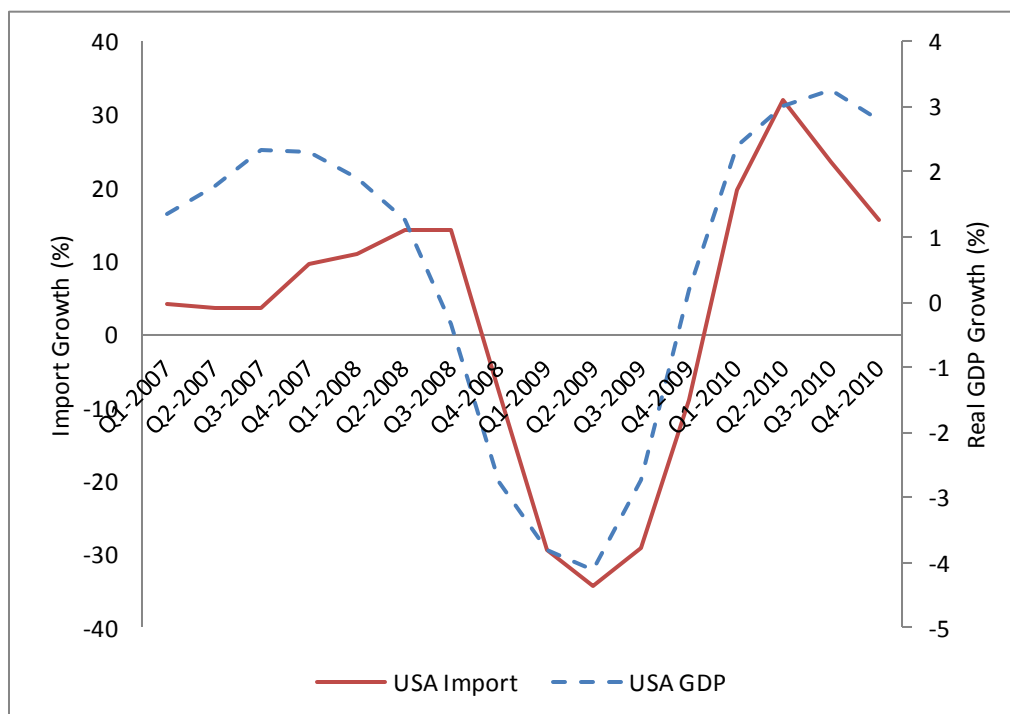


Source: *OECD database*

A fall in the real GDP adversely affects the economy; it reduces the purchasing power of the consumers and firms, reduces profitability, and hence reduces both consumption and investment spending, which in turn reduces the import demand for final consumption and further production. The lower GDP growth of the EU and the USA during the recent recessionary period reduced their import volume as shown in the figures below. What is significant is that import demand fluctuates far more than GDP; i.e. any change in GDP has an amplified impact on import demand. The 2009 second quarter GDP growth rate of -4.1 percent was accompanied by a reduction in import of about 34.2 percent in the USA. The total import of the EU decreased by 27.9 percent during the same period. This has the obvious implication that countries exporting to each of these countries lost export demand of the same magnitude, which would eventually show up in their export earnings statistics.

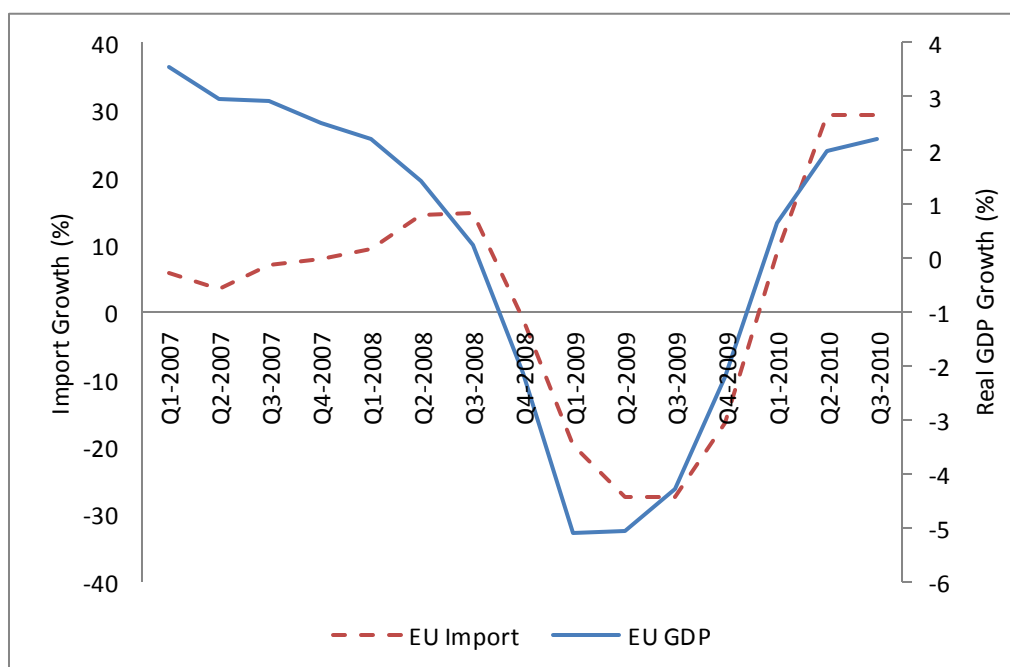


**Figure 3: USA import and GDP growth (percent, y-o-y)**



Source: OECD and USITC Trade Data Web

**Figure 4: EU import and GDP quarterly growth (percent, y-o-y)**



Source: OECD and Eurostat

## Major Export Items of Bangladesh: Export Concentration

As indicated earlier, RMG products comprise more than three-quarters of the total export of the country; knitwear is the largest export category with 40.0 percent share of the total export earnings (2009-10) followed by woven garments with 37.1 percent share (see Figure 5 below). Although many categories of other goods are exported from the country, none of them earn a substantial amount. The third most important export item is jute and jute goods. Export of this sector contributed 4.5 percent of the total export revenue followed by home textiles that accounted for 3.3 percent. Frozen food (principally shrimp) contributed 2.8 percent, leather and leather products 2.8 percent, and engineering products 1.9 percent.

However, none of these sectors have shown sufficient and sustained dynamism to reduce the importance of the RMG sector in the export trade of the country, which in fact has increased over time especially after the recession that badly mauled most of these other sectors. Jute and jute goods exports have surged during the last two years as did home textiles, but it is too early to say if the higher growth would be sustained, although the prospects seem bright. Bangladesh has not yet succeeded in diversifying the sources of its export revenue; on the contrary it has become even more concentrated with overwhelming dependence on RMG products. However, it should be mentioned that the number of products under the RMG rubric has multiplied over time.

Export concentration is sometimes quantitatively expressed by Herfindahl-Hirschman Index, which is given by the formula:

$$HHI = \sum_i \left( \frac{x_i}{x} \right)^2$$

where  $x_i$  = export receipts from the  $i$ -th product and  $x$  = total export receipts. If exports are so extremely concentrated that all export receipts come from only one product, then  $HHI=1$ . If on the other hand export receipts are equally distributed among all products,  $HHI = \frac{1}{n}$ , where  $n$  is the number of products exported. If a large number of products are exported, the value of  $HHI$  will tend to be small:

$$\lim_{n \rightarrow \infty} \frac{1}{n} = 0$$

Hence, the realised value of  $HHI$  will be in the range (0, 1).

Export receipts recorded at the 2-digit HS code level yield a value of  $HHI=0.347$  for Bangladesh. A uniform distribution of export revenue would have yielded a value  $HHI=0.010$ , whereas if all export receipts were derived from only the top-5 products (HS 3, 57, 61, 62 and 63), the value of the index would have been  $HHI=0.411$ .<sup>9</sup> Thus, the realised value of the index 0.347 would appear to be fairly high signifying a high degree of export concentration.

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<sup>9</sup> International Trade Centre (ITC), *Trade Map*.

The Herfindahl-Hirschman Index is highly susceptible to the degree of product disaggregation. If the index is calculated with export receipts of Bangladesh (2007) recorded at the 6-digit level, the value is only  $HHI=0.045$ . However, this value should be compared with the corresponding minimum index value when the export receipts are evenly distributed,  $HHI=0.0006$  since Bangladesh exported 1700 products at the 6-digit level. Greater product disaggregation reduces both the realised value of the index as well as the minimum possible value.

The Herfindahl-Hirschman Index could also be calculated to give a measure of the destination concentration of exports. In this case the subscript  $i$  in the  $HHI$  formula above should be interpreted as country or custom territory rather than product. The calculated value of the index for 2009-10 is  $HHI=0.103$ . The minimum value if exports were evenly distributed among countries is  $HHI=0.005$ . These numbers would suggest a fair degree of concentration of export destinations.<sup>10</sup>

Bangladesh has secured an important place in the world apparel market. The major competitors of Bangladeshi exporters in the EU and the US market are China, Turkey, Vietnam, India, Indonesia, Mexico, Honduras, Cambodia, Pakistan and Sri Lanka. Bangladesh is the third largest supplier of Knitwear to the world market with 3.8 percent global market share in 2008, where China is the top supplier with 33.8 percent market share. Turkey stands second with 4.4 percent share of the world market for knitwear. In the woven garment market Bangladesh is again the third largest supplier in the world with 3.3 percent share of the global trade in 2008. China is the largest supplier with a market share of 29.3 percent followed by India (3.3 percent).<sup>11</sup> The world markets for knitwear and woven are almost equal in size and both are growing steadily. Bangladesh has gradually increased its share of the world apparel market from 2.6 percent in 2000 to 3.4 percent in 2009.<sup>12</sup>

The global downturn has reduced export demand for Bangladeshi goods, the total export earnings decreased by -1.9 percent in 2009. Total export had grown by 23.4 percent in the previous year. Both knitwear and woven garments exports withstood the recession well. The former decreased by only 0.42 percent while the latter increased by 0.73 percent in 2009. Export of ready made garments as a whole remained stagnant with a growth of 0.13 percent. Such growth was achieved despite the fact that the global imports of these items declined markedly in both the EU and the US market (see Figure 9 and Figure 12 below).<sup>13</sup> Other mentionable export items that achieved positive growth in 2009 are jute products, engineering and agricultural products, terry towel, chemical products and footwear. However, the growth in the exports of these items did not offset the reduction in other items in the export basket such that the overall growth rate for 2009 was negative.

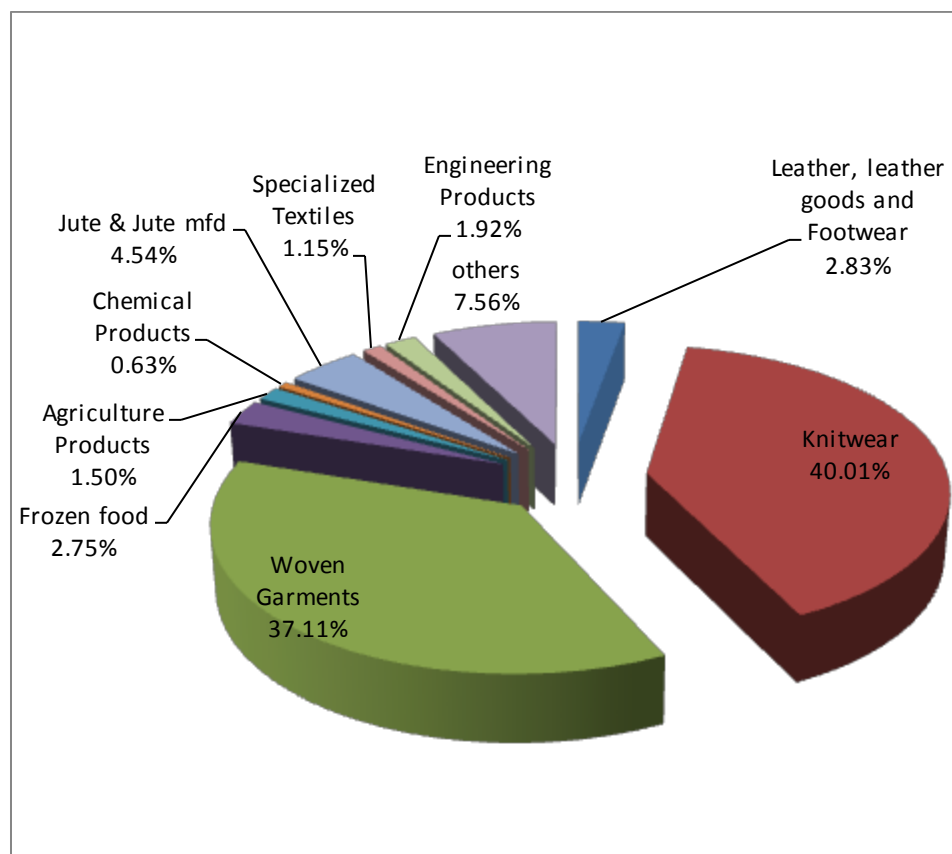
The recession badly affected the export of lesser items. The export of frozen food declined by 22.3 percent, leather by 27.7 percent, chemical products by 31.2 percent and petroleum products by 16.8 percent in 2009. The impact of the recession on frozen food was exacerbated by sanitary and phytosanitary problems that led to a voluntary suspension of export to the EU for several months.

<sup>10</sup> The data source is Export Promotion Bureau, Country-wise Export 2009-10, [www.epb.gov.bd](http://www.epb.gov.bd).

<sup>11</sup> If the EU countries are regarded separately, then Bangladesh is the fifth largest exporter of both knitwear and woven garments (see *ITC Trade Map*).

<sup>12</sup> WTO, *International Trade Statistics 2010*.

<sup>13</sup> Global import/export of a country refers to its import/export from (to) the rest of the world.

**Figure 5: Composition of Export of Bangladesh FY 2009-10**

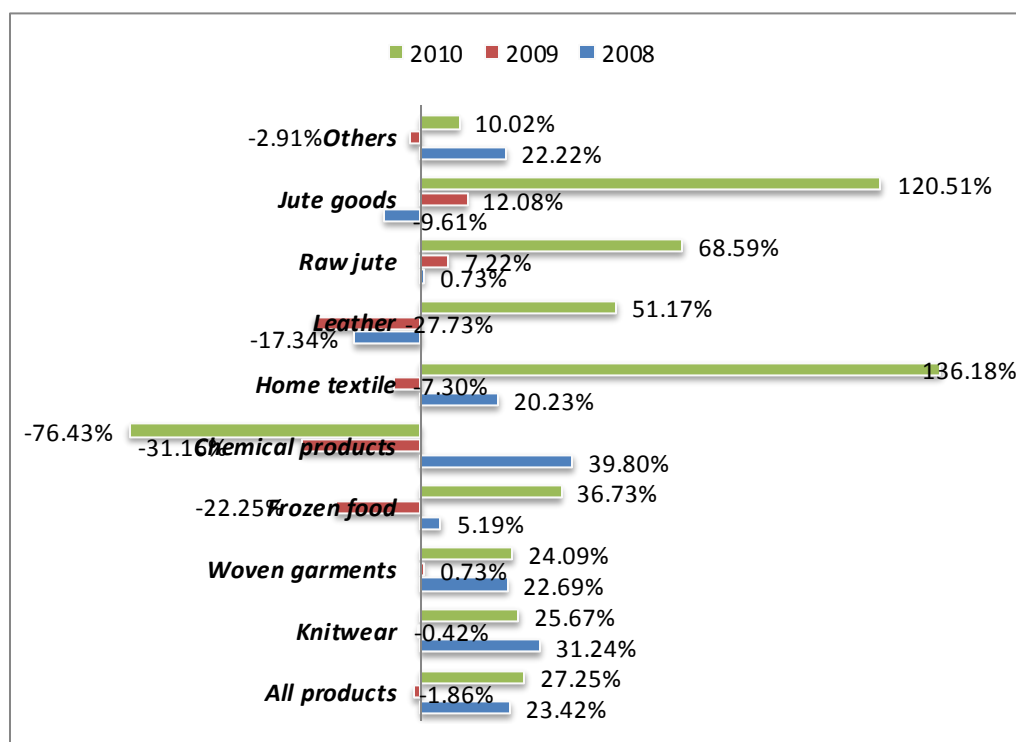
Source: *Export Promotion Bureau (EPB)*

During this global recession the RMG sector of Bangladesh fairly conclusively showed its maturity. Very few countries that export substantial amount of RMG products competed as effectively as the exporters of Bangladesh. Their competitiveness in the world market helped them to maintain, and indeed increase, the market share. This is analysed in more detail in the following sections in the context of the principal markets of Bangladesh, viz. the EU, the USA, and Canada.

An interesting aspect of the export composition of Bangladesh is worth noting. Although the export earnings are extremely concentrated with only four HS code chapters (2-digit level classification) out of 96 commodity-specific chapters accounting for 85 percent of the total export earnings (and ten chapters accounting for 94 percent), Bangladesh actually exported products under all chapters in 2009-10. In other words its export basket is actually far more diversified (in terms of the number of goods) than is conveyed by the concentration of export earnings as shown earlier by Herfindahl-Hirschman Index. Export from Bangladesh exceeded \$10 million for each of 41 commodity chapters (2-digit level), while export under 65 chapters exceeded \$1 million.

A similar picture also emerges in respect of destinations. About four-fifths of the total exports of Bangladesh go to only three markets, viz. Canada, the EU and the USA. Turkey, Japan and India take in another 7 percent. However, Bangladesh actually exported goods to nearly 200

**Figure 6: Annual export growth of major items of Bangladesh 2010**



Source: Export Promotion Bureau (EPB)

countries and custom territories of the world.<sup>14</sup> It exported in excess of \$1 million worth of goods to about 100 countries and custom territories including EU countries in 2009-10. Hence, exports would appear to be quite diversified destination-wise too.

Obviously, the crux of the problem is that all the products except RMG and jute, and all the markets except the EU, the USA and Canada yield only small export revenue despite the fact that the country demonstrably has the skill and ability to profitably produce and export these products to many countries. Over time the importance of RMG and the dependence on the established export markets have not decreased such that export concentration has not declined despite the resolve of successive governments to diversify exports. Indeed, the *HHI* (at 2-digit level) has increased from 0.258 in 2006 to 0.347 in 2009 suggesting a significant increase in export concentration. It is essential that the reasons for such high and increasing export concentration should be rigorously investigated and clearly understood if appropriate policies are to be designed and put in place to reverse the trend.

## The US Market

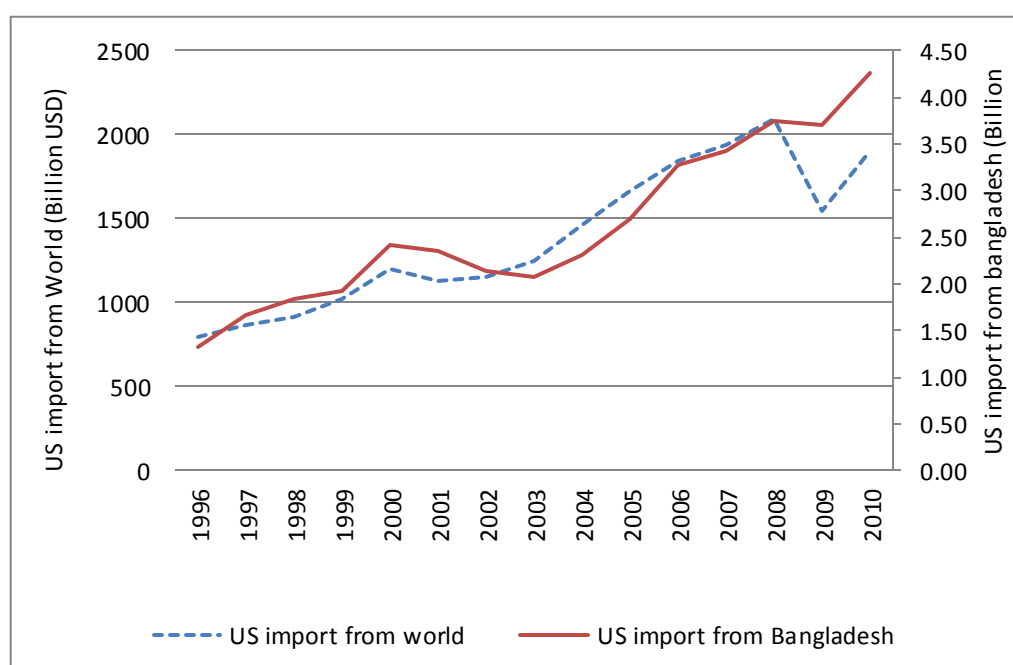
The USA is the largest importer of the world with a total import bill of about \$1.9 trillion in 2010 (\$1.5 trillion in 2009) or about 12 percent world imports. This is the amount that the rest of the world exported to the USA, and hence, the export performance of these countries

<sup>14</sup> Export Promotion Bureau, Country-wise Export 2009-10.

depends crucially on the size of the US import bill. Figure 7 shows the value of US total import measured on the left vertical axis and the value of US imports from Bangladesh only on the right vertical axis. Total import of USA increased by 58 percent during the new millennium, but its import from Bangladesh increased by 77 percent. Until before the recession, import of the USA from Bangladesh moved in line with its total import. But during the recession US total import nosedived, but its imports from Bangladesh remained almost unchanged. After the recession both seem to have again moved in line. Hence, it would appear that the growth of the US import of Bangladeshi products roughly follows the growth of the total import of the USA. Whatever be the other determinants of export growth, it would seem that the total import bill of the USA has an overriding influence on the total export of Bangladesh to the USA.

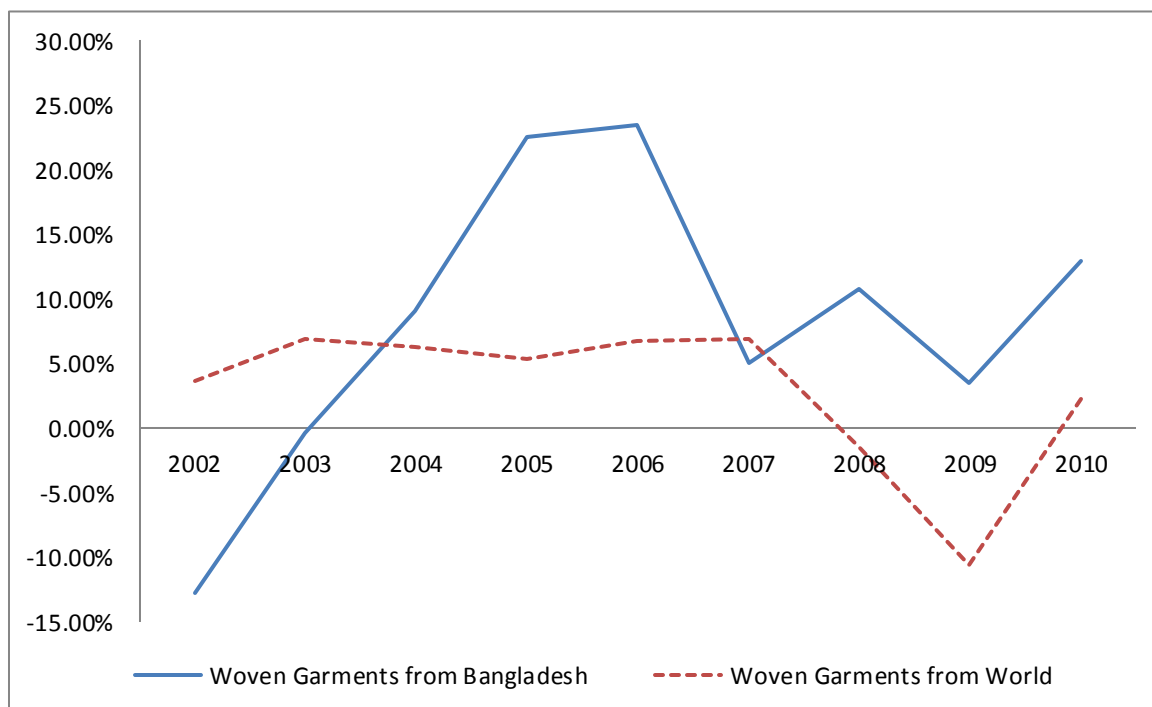
The main export item of Bangladesh to the USA is RMG, especially woven garments. Figure 8 shows that the export of RMG from Bangladesh to the USA is also sensitive to the total RMG import of the USA; Bangladesh gains from a robust growth of the total RMG import of the USA. This obviously also implies that a contraction of the US global import adversely impacts on its import from Bangladesh, which is evident from the figures.

**Figure 7: Import of USA from the world and Bangladesh (billion US\$)**



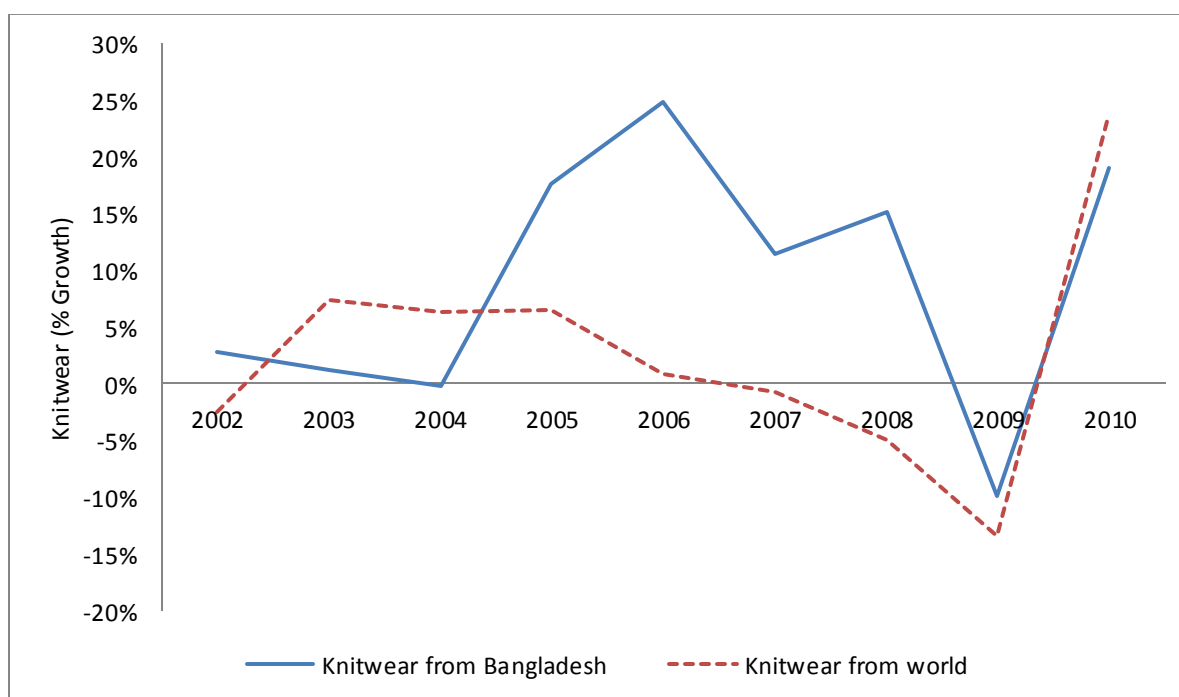
Source: *USITC Trade Data Web*

**Figure 8 (a): US Woven garments annual import growth from the world and Bangladesh**



Source: *USITC Trade Data Web*

**Figure 8(b): US knit garments annual import growth from the world and Bangladesh**



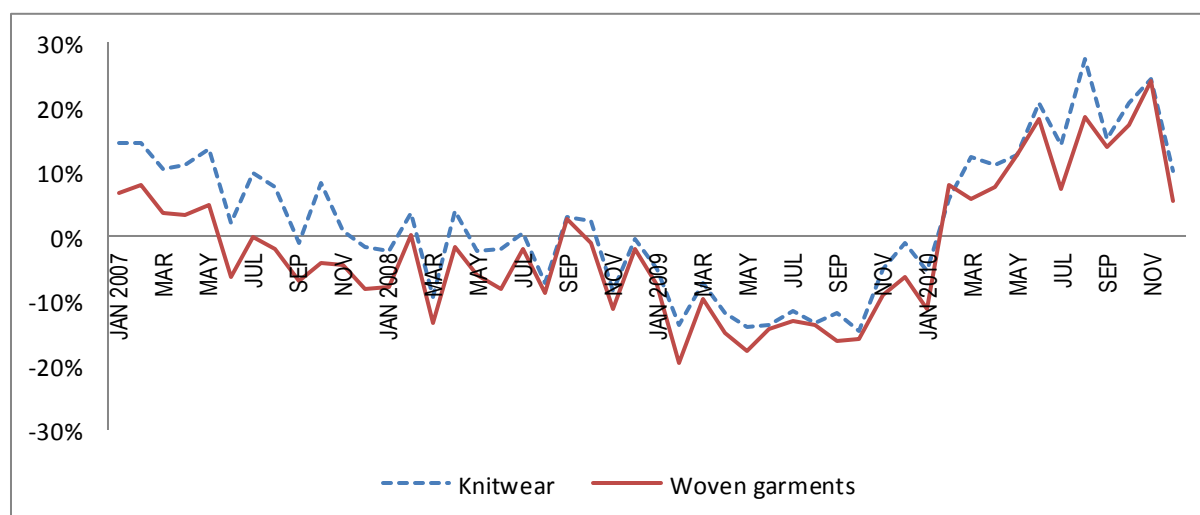
Source: *USITC Trade Data Web*

Knitwear did not feature prominently in the export of RMG products from Bangladesh to the USA; but there has been a turnaround in recent years. Knitwear now comprises nearly a quarter of the RMG exports to the USA. During 2006-08, knitwear achieved a higher growth than that of woven garments, but the reduction in 2009 was also sharper. It is difficult to explain from these data alone why knitwear has performed so much poorer in the USA compared to woven garments. One reason could be that most knitwear exports receive duty-free treatment in the EU market since the end of the last century. Most other developed countries have also granted duty free access to RMG exports including knitwear from Bangladesh. However, the USA has stubbornly declined to provide duty-free access to most Bangladeshi products. Indeed, the US importers of Bangladeshi apparels pay very high custom duties. Hence, knitwear is more profitable in the EU and other markets relative to the US market. This might have encouraged the exporters to concentrate their efforts in these other markets rather than the US market. In the case of woven garments, most of the exported items to EU do not qualify for duty-free treatment since these do not satisfy the rules of origin. Consequently there is no special advantage in exporting to EU. The US market being long established (by virtue of MFA quota) and more profitable attracts much of the woven exports from Bangladesh.

The economic downturn in the USA has affected the exports of both woven and knit garments. As shown in Figure 9 there has been a trend decline in exports of both these categories of export to USA after December 2008, i.e. after almost two quarters of the onset of the recession in the USA. Since import orders are placed several months ahead of the actual imports, some lag in the impact of a recession is not unexpected.

During 2009 US imports declined by a whopping 25.9 percent, which was the steepest contraction since the Great Depression. Both knitwear and woven exports fell. This adversely impacted on the imports of apparels from individual countries. Table 1 below shows the apparel exports of the top-10 exporters to the USA. Except for China every other country suffered reductions in their exports. However, Bangladesh had the smallest and an insignificant reduction.

**Figure 9: Monthly (point-to-point) growth of global RMG import of USA, 2007-10**



Source: USITC Trade Data Web



**Table 1: Top-10 apparel exporters in the US market**

<b>Country</b>	<b>(Million US dollar)</b>					
	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>	<b>2010</b>
China	16774	19865	23955	23983	24337	28699
Vietnam	2664	3153	4292	5147	4998	5760
Indonesia	2868	3666	3984	4028	3867	4418
Mexico	6230	5448	4630	4129	3482	3668
Bangladesh	2268	2808	2996	3353	3345	3829
India	3064	3235	3217	3110	2878	3140
Honduras	2685	2518	2587	2668	2113	2476
Cambodia	1703	2131	2421	2369	1866	2206
Pakistan	1274	1426	1514	1510	1319	1500

Source: *USITC Trade Data Web*

The yearly growth rates of major competitors of Bangladesh in the US market are shown in Table 2. Only China, Indonesia and Vietnam obtained positive growth in knitwear export to the USA in 2009 while the rest had negative growth rates, in some cases very large negative rates. All countries except Honduras and Hong Kong bounced back in 2010.

In woven garment export, only Bangladesh achieved positive growth in 2009. All other countries including China had negative growth. Some countries such as Hong Kong, Thailand Cambodia and Honduras suffered very heavily. However, the recession may not be the only factor behind the decline of such countries as Hong Kong and Thailand. Both countries suffered from negative growth since 2004, long before the recession. Hong Kong appears to have been almost eliminated from the woven garment market of the USA; it has experienced a massive 95.5 percent reduction in its woven export to the USA since 2004. Thailand has suffered a decline of 44.2 percent during the same time. It seems unlikely it will make a come back. As its economy develops and wages increase, it is likely to become less competitive in the global apparel market and hence lose market share progressively just as Hong Kong did

It is apparent that Bangladeshi apparel exporters to the US market withstood the ravages of the recession much better than most of the exporting countries, including all SAARC countries. Very few apparel exporters achieved positive growth in 2009; on the contrary most suffered very large negative growth of apparel exports. Only China among the top-12 exporters managed to avoid negative growth of RMG exports to USA. Bangladesh escaped with an insignificant reduction in apparel exports; Vietnam and Indonesia also had small reductions.

The sustained good performance of Bangladesh in RMG export has secured for it an increasing share of the total import of RMG products by the USA since the termination of the MFA at the end of 2004 (see Figure 10). Curiously the shares of Bangladeshi exports of both knit and woven products were on a decline during the last few years of MFA. The quota regime, contrary to the common belief, would appear to have constricted the growth of RMG exports of Bangladesh to the USA in the later years of MFA as the industry matured under the very quota cover provided by the MFA. The elimination of the quota regime allowed the

RMG exporters to aggressively compete to raise their share of the US market. Since the end of the MFA, the share of Bangladesh in the US woven garment import has more than doubled from 3.9 to 8.3 percent. The share of knitwear rose from 1.8 to 2.6 percent of US total import of knitwear. The rapid increase in the share of the RMG export of Bangladesh since 2004, especially woven export, is a testimony to the maturity and competitiveness of the Bangladeshi exporters serving the US market. Bangladesh is now the fourth largest exporter of RMG to the US market behind China, Vietnam and Indonesia.

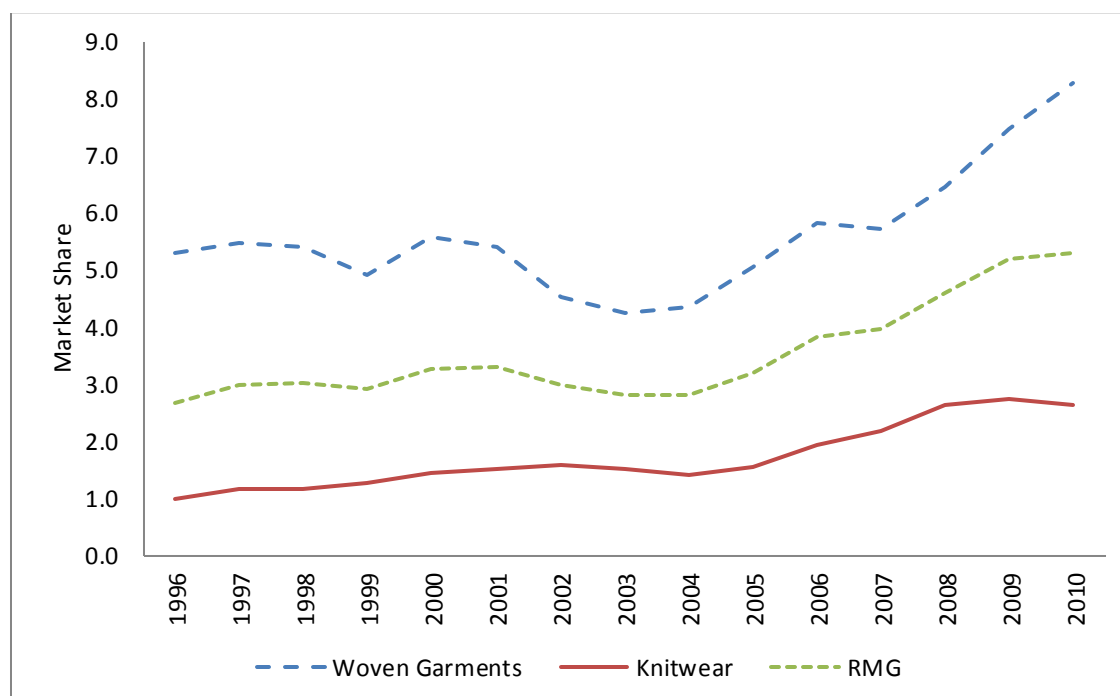
RMG products (HS61 and HS62) constituted more than 90 percent of the total exports of Bangladesh to the USA in 2010. Only other significant exports were frozen fish and shrimp (HS3), home textiles (HS63) and headgear (HS65). Exports under these five HS codes amounted to more than 98 percent of the total exports to the USA. Noting that HS63 and HS65 are basically textile products, the share of all types of textile products in the total exports to USA exceeded 96 percent. Bangladesh has not yet discovered any other product in which it has a comparative advantage high enough to compete in the US market.

**Table 2: Growth (percentage) of apparel exports of major suppliers to USA**

Items	Country	2000	2004	2005	2006	2007	2008	2009	2010
Knitwear	China	0.4	28.3	59.98	22.44	31.71	1.12	7.21	22.47
	Indonesia	30.39	4.99	36.26	65.11	23.81	14.78	6.32	17.05
	Vietnam	49.11	-1.44	3.98	23.22	55.64	30.3	2.74	16.08
	India	8.1	15.39	39.37	23.61	13.42	0.8	-7.02	14.55
	Bangladesh	29.27	-0.12	17.58	24.88	11.48	15.12	-9.89	19.12
	Pakistan	21.49	9.6	8.24	11.26	3.59	-1.8	-11.01	14.83
	Cambodia	25.23	26.58	36.74	48.15	22.13	0	-19.12	18.41
	Mexico	5.67	-7.55	-11.76	-7.44	-17.85	-12.14	-20.14	5.45
	Honduras	14.4	6.68	0.14	-4.83	3.44	7.5	-20.62	-32.56
	Sri Lanka	22.3	12.37	30.18	20.88	-0.97	-4.46	-21.54	4.78
	Thailand	24.6	4.23	1.31	9.61	0.91	-6.2	-23.39	10.61
	Hong Kong	3.45	3.91	4.55	-23.68	-26.4	-19.87	-84.07	-32.56
Woven Garments	Bangladesh	26.14	9.03	22.47	23.44	5.01	10.73	3.53	12.88
	China	11.06	20.36	55.14	15.86	13.07	-0.68	-3.12	13.89
	India	20.49	7.28	34.26	-2.39	-8.36	-6.17	-7.81	5.02
	Vietnam	18.97	14.56	8.32	14.82	20.86	9.46	-9.66	14.12
	Mexico	15.61	-0.81	-7.13	-15.74	-13.08	-9.98	-12.82	5.24
	Indonesia	18.89	13.35	14.18	11.94	-0.84	-9.61	-14.25	10.81
	Sri Lanka	13.32	6.99	-3.53	-8.43	-9.96	-6.97	-15.36	-0.82
	Pakistan	32.42	19.53	20.63	13.65	12.73	3.55	-16.35	10.95
	Honduras	0.94	7.19	-8.37	-10.48	0.56	-11.17	-21.53	385.92
	Cambodia	46.18	7.34	6.58	0.8	0.35	-6.15	-25.55	13.89
	Thailand	16.1	5.01	-0.27	-7.45	-9.35	-4.62	-30.46	0.50
	Hong Kong	6.57	4.47	-21.97	-15.88	-28.88	-27.45	-79.74	-33.33
RMG	China	7.33	23.28	56.99	18.43	20.59	0.12	1.48	17.92
	Bangladesh	26.89	6.43	21.17	23.81	6.7	11.93	-0.24	14.46
	Vietnam	28.27	7.06	6.44	18.36	36.13	19.93	-2.9	15.25
	Indonesia	21.81	11.03	19.98	27.82	8.67	1.11	-3.99	14.26
	India	17.06	9.57	35.79	5.57	-0.55	-3.32	-7.47	9.10
	Pakistan	24.9	11.94	11.35	11.91	6.12	-0.23	-12.64	13.70
	Mexico	11.36	-3.59	-8.96	-12.56	-15.01	-10.83	-15.65	5.32
	Sri Lanka	15.52	8.5	6.26	2	-6.17	-5.85	-18.15	1.61
	Honduras	9.99	6.81	-2.12	-6.24	2.75	3.15	-20.8	17.18
	Cambodia	37.13	15.26	20.21	25.14	13.6	-2.13	-21.25	18.21
	Thailand	20.64	4.61	0.54	1.4	-3.59	-5.55	-26.34	6.63
	Hong Kong	4.97	4.2	-9.19	-20.21	-27.56	-23.37	-82.18	-32.95

\*Refers to growth of exports in Jan-Oct 2009 over that of Jan-Oct 2008

Source: *USITC Trade Data Web*

**Figure 10: Share of Bangladesh in the total US garment import (percent)**

Source: *USITC Trade Data Web*

## The EU Market

As indicated earlier, the European Union went into a recession during the fourth quarter of 2008 and reached the trough of the downturn in the first quarter of 2009 (see Figure 2). It moved out of the recession in the first quarter of 2010. The recession dragged the total import volume of the EU to the negative zone in the fourth quarter 2008 (Figure 4). However, on an annual basis, the import bill of the EU maintained the trend growth till 2008 as shown in Figure 11.

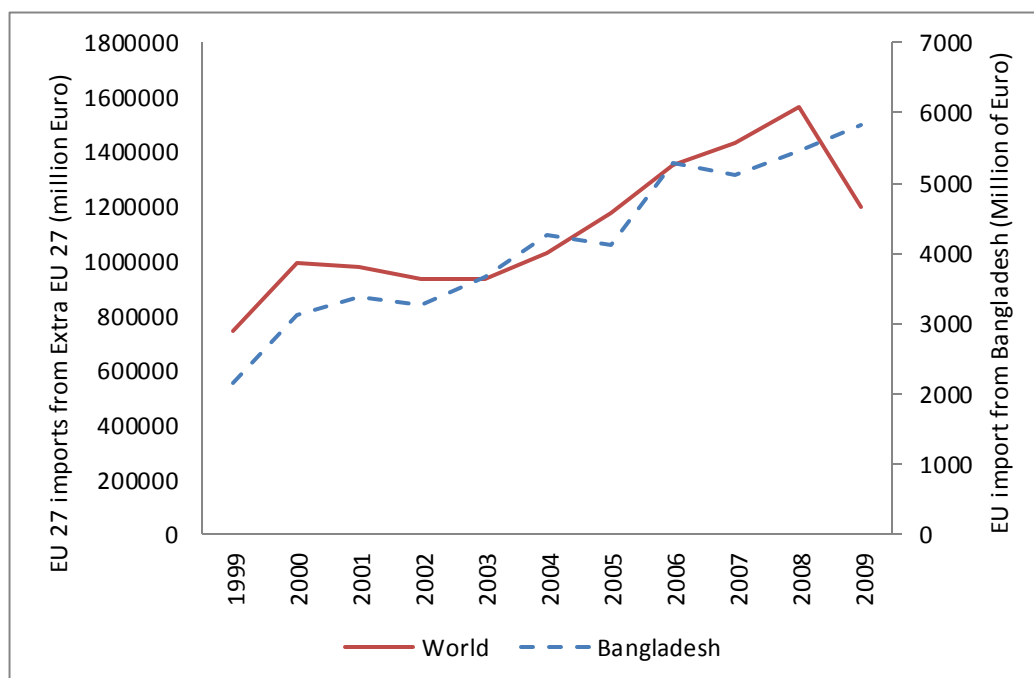
The negative impact of the recession on import was no less severe than that in the USA. Monthly imports of the EU started declining slowly from November 2008, but from January 2010 the reductions became really large (year-on-year basis). Imports declined by 23.4 percent for the whole year 2009.

Figure 11 shows the value of EU import from the world and the value of EU import from Bangladesh during 1999-2009. Despite occasional divergences (as in the recession year) the two series moved together. There is little doubt that the principal driver of Bangladesh's export to the EU is the EU global import. Exports of other countries to EU fell in 2009, frequently quite sharply, due to the large fall in global import of EU, but the export of Bangladesh showed a healthy upward trend. The good performance of the total export of Bangladesh to the EU market is due almost entirely to the competitive strength of the RMG

sector achieved over the years benefitting from the duty-free and quota-free access given by the EU.

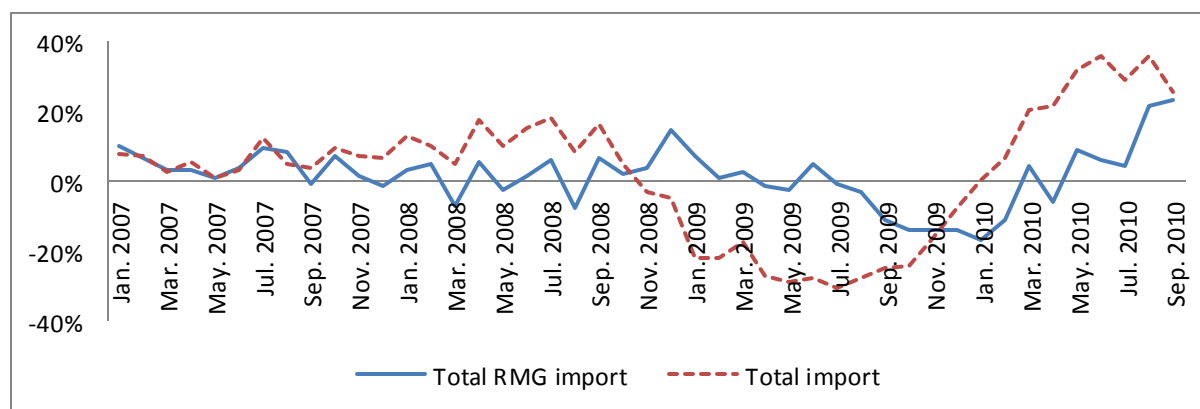
A noticeable aspect of the recession was that even when the economy went into a deep recession and the total import nosedived by a massive 23.4 percent, the import of apparels did not decline much; it remained virtually stagnant until July 2009 (Figure 12). It then started falling, but by a much smaller rate than that of the total import. Import of knitwear during 2009 was only about 2.5 percent lower than that during 2008, while the import of woven garments was 4.7 percent lower. The total RMG import was lower by 3.6 percent.

**Figure 11: EU import from the world and Bangladesh (million Euro)**



Source: *Eurostat*

**Figure 12: Point-to-point monthly growth rates of RMG and total import of EU**



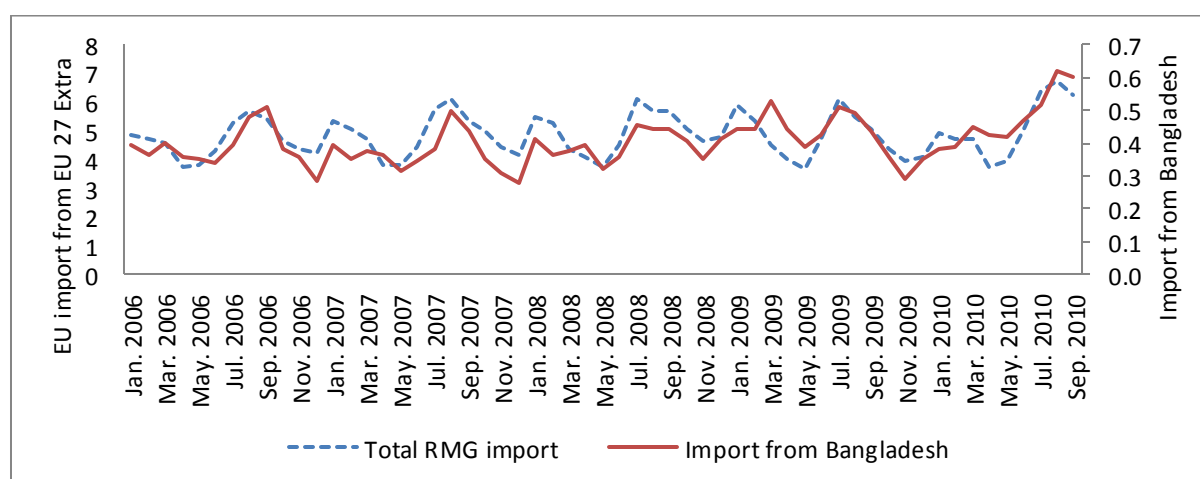
Source: *Eurostat*

Since nearly nine-tenths of the exports of Bangladesh to EU comprise RMG, the demand for its exports in the EU market did not decline on account of the recession. The total export volume showed a healthy increase of 6.7 percent between 2008 and 2009. The increase was driven by the robust growth of RMG export of 8.4 percent. Figure 13 below shows that the Bangladesh's export of RMG products to the EU fairly closely followed the trend of the total RMG import of the EU from the world. The RMG exporters of Bangladesh managed to extract a greater share of the global apparel import of EU. This suggests an increasing competitive strength of RMG exporters in the EU market.

Exporters of other products, except footwear and fish and crustaceans, did not fare as well. Export of footwear increased by 19.5 percent and fish and crustaceans by 9.7 percent. Export revenue from the rest of the items decreased by 12.6 percent.

The rapid growth of the RMG export from Bangladesh to the EU market was greatly facilitated by several factors including duty-free and quota-free access from 1986 onward under a bilateral textile agreement, the easing of the EU rules of origin for apparels from three to two-stage domestic production with quota restrictions in 1997 and without quota restrictions from 1999, and Everything But Arms (EBA) scheme of GSP that granted duty-free and quota-free access to virtually all export products of the least developed countries of the world commencing from 2001.<sup>15</sup> There seems little doubt that the preferential treatment of the LDC exports to EU that gave LDC exports an edge over non-LDC exports was instrumental in building the export capacity of Bangladesh fairly rapidly (Taslim 2007) and in this sense the GSP of EU served its purpose. The duty free access was especially helpful to the ready made garments exports since the average duty on garment imports to the EU is quite high (11.5 percent).

**Figure 13: EU import of RMG from the world and from Bangladesh (Billion Euros)**



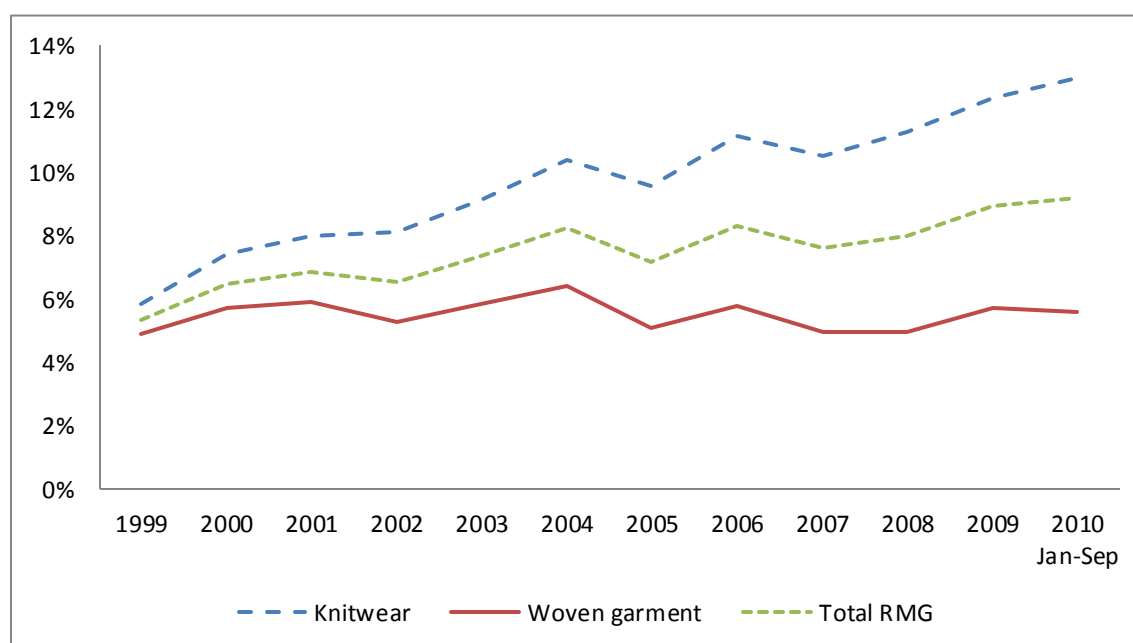
Source: Eurostat

<sup>15</sup> Three-stage requirement for apparel meant that in order to access GSP in the EU market the exported apparel items had to be manufactured from domestically produced or imported cotton; i.e. the country had to manufacture yarn and fabric domestically. Two-stage reduced the requirement to producing only fabric domestically, yarn could be imported.

The two-stage production requirement to satisfy the EU rules of origin for GSP conferred special advantages to knitwear export since the garment manufacturers could profitably produce knit fabric locally and cut and make (CM) the fabric into knit garments. Knit garments, therefore, satisfied the two-stage domestic production requirement and could obtain duty-free access into EU market. Riding on this advantage knitwear export to EU expanded very rapidly. The share of Bangladeshi knitwear in EU total import increased rapidly as shown in Figure 14. As in the case of the US market, the share of Bangladeshi apparels in the total EU import rose markedly during the recession. Bangladesh is now the second largest supplier of knitwear to the EU market. However, it has not fared as well in the woven garment export whose share remained virtually unchanged from the beginning of this decade.

The manufacture of woven garments to take advantage of the two-stage relaxation posed greater difficulties. The sunk cost requirement for the establishment of a woven fabric production facility is very large (several times the requirement of that of knit fabric). The cost of production is significantly higher than that in the competing countries. Hence, most woven products are made from imported fabric. Consequently, these woven exports do not qualify for GSP treatment. EU importers of woven garments from Bangladesh are required to pay fairly steep custom duties, pushing up the cost of procurement from Bangladesh.<sup>16</sup> On the other hand some developing countries that have a textile base, such as Pakistan, can obtain GSP duty concessions. Thus, the profitability of export of woven garments to EU countries is lower. As shown in Figure 14, the share of woven garment export of Bangladesh in the total EU import of woven products is much lower than that of knitwear export.

**Figure 14: Share of Bangladesh in EU global RMG import**



Source: *Eurostat*

<sup>16</sup> The average duty on knit and woven apparel import from Bangladesh to US was 16.4 percent in 2009. The US government collected \$548 million in duties on apparel import of only \$3345 million from Bangladesh.

Table 3 below shows that the growth of knitwear exports to EU during the last decade was much higher than the growth rate of woven garments. In 1999 knitwear export was about the same as woven export, but by 2009 knitwear export was more than twice the woven export.<sup>17</sup>

The differential capacity of the two sub-sectors of RMG in accessing GSP in the EU market is evident from Table 4. Since the new millennium the GSP utilisation rate of knitwear increased rapidly. By 2008 nearly 94 percent of knitwear exports received duty free treatment.

**Table 3: RMG import of EU from Bangladesh (million Euro)**

Year	Knitwear	Growth (percent)	Woven garments	Growth (percent)	Total RMG	Growth (percent)
1999	896	16.8	895	3.1	1792	9.6
2000	1346	50.2	1244	39.0	2590	44.5
2001	1485	10.3	1338	7.6	2823	9.0
2002	1531	3.1	1213	-9.3	2744	-2.8
2003	1770	15.6	1343	10.7	3113	13.4
2004	2186	23.5	1533	14.1	3719	19.5
2005	2202	0.7	1337	-12.8	3539	-4.8
2006	2923	32.7	1699	27.1	4622	30.6
2007	2894	-1.0	1511	-11.1	4405	-4.7
2008	3216	11.1	1524	0.9	4740	7.6
2009	3443	6.74	1684	10.45	5117	7.93

Source: *Eurostat*

The GSP utilisation rate of woven exports on the other hand was much lower at about one-seventh of the total woven export at the turn of the millennium. The low utilisation rate was due to the fact that most of the fabric used for producing apparels was imported, and hence the exported products did not satisfy the EU rules of origin. The GSP utilisation rate rose to about one-quarter by the end of the MFA era in 2004. Thereafter it increased fairly rapidly and by 2008 nearly two-fifths of the woven export to EU enjoyed duty-free access. This was made possible by the growth of domestic textile manufacturing, especially denim. Denim garments quickly became an important export item taking advantage of the EBA duty free facility.

About three-fourths of the total RMG exports to EU currently enjoy duty free access. Bangladesh RMG products thus have a considerable price advantage over non-LDC countries since the average duty rate on the RMG products is quite high (about 11.5 percent). Further expansion of woven fabric manufacturing will raise the proportion of RMG export receiving EBA duty-free facility. The outlook for RMG export to EU seems bright.

The growth of knitwear export to the EU market exceeded the growth of woven export since knitwear obtained a change of rules of origin to two-stage conversion, which permitted

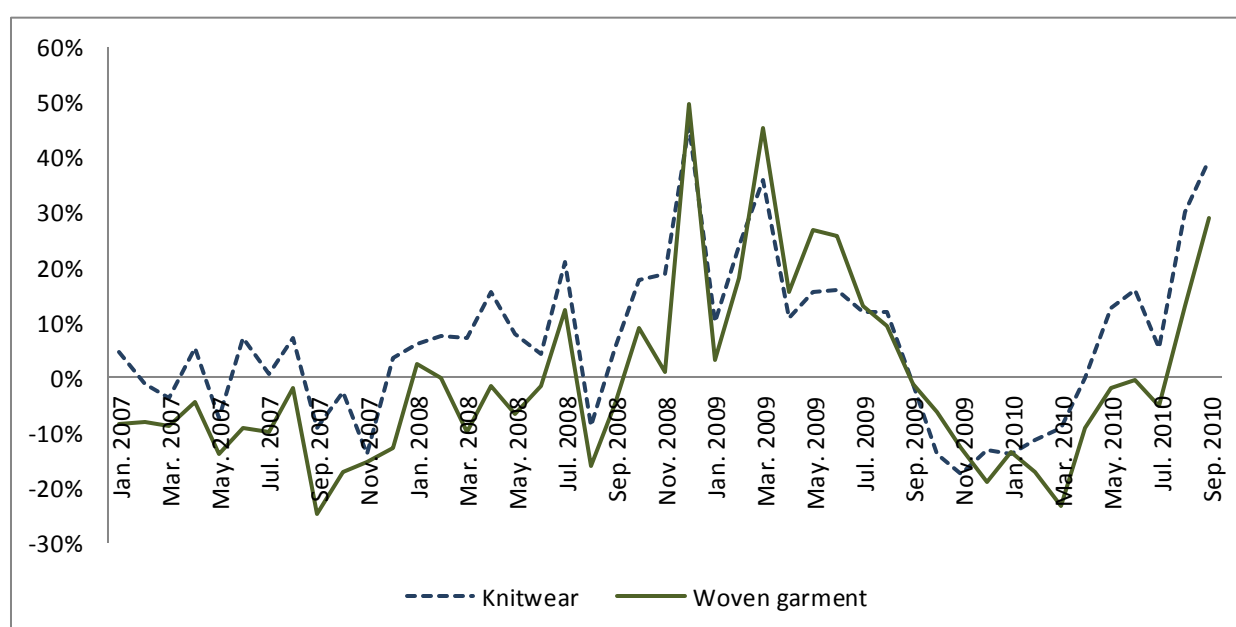
<sup>17</sup> The export volume of knitwear to EU was less than three-fifths of the export of woven garments in 1995.



**Table 4: GSP utilisation rate (percent)**

	2000	2001	2002	2003	2004	2005	2006	2007	2008
Knitwear	59.9	76.6	79.4	77.8	80.3	84.9	86.0	87.1	93.6
Woven garments	14.4	19.2	23.2	22.2	24.1	28.0	35.1	36.5	39.4
RMG	33.4	49.4	54.6	53.8	57.2	63.4	67.3	69.7	75.9

Source: *Eurostat*

**Figure 15: Monthly growth of apparel import of EU from Bangladesh (2007-2009)**

Source: *Eurostat*

knitwear to obtain duty-free access. Most of woven exports did not get duty free access as it did not satisfy the two stage conversion rules of origin. However, the EU has finally changed the rules of origin to a single stage conversion with effect from January 2011. This will essentially permit all woven garment exports from Bangladesh to obtain duty free access. It is very likely that there will be a surge in woven export to the EU. There could be some diversion of exports of RMG products from the US to the EU market.

Recent data show that Bangladesh is the best performer in the EU RMG market during 2009 with a growth rate of nearly 8 percent. India posted a growth rate of 5.2 percent while Sri Lanka managed 3.4 percent. China, Mexico and Pakistan barely managed a positive growth rate of less than 1 percent. The very few exporters who had positive growth of RMG export to EU increased their market shares – a reflection of the fact that other exporters had negative growth. Bangladesh, China and India are the major gainers. Bangladesh increased its Market share from 8.0 percent in 2008 to 8.9 percent in 2009. China increased its market share from 42.6 percent in 2008 to 44.7 percent during the same period and India's market share increased from 6.6 to 7.2 percent. Sri Lanka also increased its share marginally.

**Table 5: Major competitors' annual growth of apparel export in EU (percent)**

<b>Product</b>	<b>Country</b>	<b>2000</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>	<b>2007</b>	<b>2008</b>	<b>2009</b>
<b>Knitwear</b>	Bangladesh	50.07	23.55	0.66	32.75	-0.99	11.13	6.74
	China	19.72	16.73	55.45	7.27	19.78	28.20	4.09
	Hong Kong	4.82	-9.19	13.56	49.23	-20.99	-56.20	-56.57
	Honduras	1061.29	22.59	-23.09	21.07	9.20	39.30	-9.49
	Indonesia	22.52	7.15	-12.60	24.04	-18.51	-16.65	-6.45
	India	18.00	15.00	22.59	19.12	5.56	-0.10	0.88
	Cambodia	28.03	25.45	-1.87	20.77	-2.69	7.09	-1.01
	Mexico	27.78	15.36	-2.67	18.19	-6.33	-8.50	-7.74
	Pakistan	3.22	28.09	-26.54	22.04	-0.49	-6.84	-5.02
	Thailand	26.19	9.07	-13.97	16.00	-12.83	0.53	-4.20
	Vietnam	27.06	43.77	18.61	76.65	6.38	12.54	-8.86
	EU import	18.23	9.06	8.92	13.92	5.28	3.65	-5.68
<b>Woven garments</b>	Bangladesh	38.97	14.17	-12.88	27.15	-11.06	0.87	10.44
	China	17.50	10.02	42.04	14.25	13.17	7.78	-1.40
	Hong Kong	16.10	-4.99	-32.20	44.97	-47.42	-36.10	-41.09
	Honduras	50.26	-22.61	-9.74	99.17	-52.50	60.96	-33.29
	Indonesia	33.01	-9.81	-7.87	13.40	-13.41	4.82	-0.58
	India	22.67	-4.79	38.54	16.64	-4.07	3.43	9.36
	Cambodia	14.37	15.13	-26.81	-0.17	-15.59	-0.25	-15.17
	Mexico	49.79	-5.64	-27.55	126.21	6.80	10.31	7.54
	Pakistan	23.46	0.89	-4.24	12.86	0.28	0.48	4.87
	Thailand	24.08	-1.68	-9.33	7.59	-4.56	-4.00	-10.80
	Vietnam	26.11	15.75	5.77	40.12	11.04	9.97	-2.20
	EU import	17.70	3.31	9.89	11.74	3.68	1.42	-8.62
<b>RMG</b>	Bangladesh	44.52	19.50	-4.92	30.63	-4.69	7.61	7.92
	China	18.45	12.43	47.04	11.49	15.68	15.80	0.99
	Hong Kong	11.66	-6.78	-13.21	47.28	-32.88	-49.11	-49.72
	Honduras	503.18	15.44	-21.71	30.68	-2.33	41.32	-11.95
	Indonesia	28.65	-1.73	-10.33	18.79	-16.11	-6.22	-3.26
	India	20.60	4.13	30.60	17.80	0.48	1.67	5.22
	Cambodia	24.36	22.58	-8.39	16.40	-5.00	5.92	-3.13
	Mexico	39.98	6.05	-12.48	53.47	-0.03	1.17	0.82
	Pakistan	13.91	12.49	-15.07	16.71	-0.06	-2.72	0.73
	Thailand	25.39	4.85	-12.26	12.80	-9.83	-1.21	-6.67
	Vietnam	26.27	21.09	8.67	49.14	9.68	10.70	-4.12
	EU import	17.94	5.93	9.44	12.76	4.43	2.48	-7.25

Source: *Eurostat*

Turkey, the second largest exporter of RMG to EU, suffered badly, its export declined by 11.3 percent in 2009. Its share nosedived from 17.2 percent in 2004 to 12.2 percent in 2009. Other major exporters who lost out during the recession are Morocco and Tunisia. Morocco's apparel export to EU went down by 16.5 percent, while that of Tunisia by 12.6 percent. The share of the latter in EU import declined from 5.8 percent in 2004 to 3.9 percent in 2009, while that of the former went down from 5.4 percent to 3.5 percent.

The recession seems to have caused some restructuring of international sourcing of apparel by EU importers. Firstly, an increasing proportion of their apparel import is being sourced from outside EU. Non-EU countries supplied 50.2 percent of the intra- and extra-EU import in 2004; by 2009 this proportion has risen to 54.3 percent. Secondly, they are increasingly concentrating their purchases from a handful of efficient RMG producers - all of them Asian countries. The major beneficiaries of this restructuring of RMG import sourcing are Bangladesh, China, India, Sri Lanka and Vietnam. These countries together with Morocco, Tunisia and Turkey accounted for more than 85 percent of the extra-EU import of apparels. However, the latter group of countries, especially Turkey, are finding it difficult to maintain their shares of the EU market due to rising costs and stiff competition from the Asian countries. China, which now has a 44.7 percent share of the extra-EU apparel import, is likely to face the same difficulties as faced by the richer countries in the earlier phases of development; its wage cost will inexorably rise if the current breakneck pace of economic progress is maintained. When this transpires Bangladesh will be in a position to further strengthen its position in the global market provided it can maintain competitive cost conditions in the industry.

## **The Emerging Export Markets: Canada**

Canada was not a major destination of exports of Bangladesh only a few years ago. During the five year period 1997-98 to 2001-02 exports of Bangladesh to Canada languished at slightly above US\$100 million or about 1.5 percent of the total export. Canada, like the USA, did not grant duty-free access to Bangladeshi apparel products, which were the major export items to Canada. In the absence of preferential treatment, the apparel exporters of Bangladesh could not compete effectively against other major exporters such as China and USA.

However, the situation changed dramatically after January 1, 2003 when Canada introduced a new GSP scheme that granted nearly all export products of LDCs duty free access to the Canadian market. This was aptly complemented by fairly relaxed rules of origin for apparels, which effectively permitted garments stitched or knitted from imported fabric duty free access to Canada. Such preferential treatment and the high duties on garments (about 17 percent) gave the RMG exporters of Bangladesh an edge to compete in the Canadian market. RMG exports, and consequently total exports, to Canada increased by leaps and bounds. By 2008-09, the total value of exports of Bangladesh to Canada was more than 6 times greater than that in 2001-02, ie, an average annual growth rate of exports of 35 percent. Canada is now the third largest destination of Bangladeshi apparels after EU and USA. Bangladesh has already established itself as the second largest source of RMG import of Canada.

The RMG exporters performed particularly well during the 2008-09 recession despite the fact that Canadian imports declined substantially. The share of Bangladeshi RMG in Canadian import in January-November 2009 climbed to 9 percent from about 7 percent in 2008. RMG imports from Bangladesh into Canada during this period increased by more than 16 percent over the corresponding

period in 2008. No other major RMG exporter achieved such a high growth rate; most countries including China, USA and India suffered significant negative growth rates. The recession has further consolidated Bangladesh's position as the second largest exporter of RMG to Canada. China remains the top exporter with more than half of the market.

**Table 6: Canadian RMG imports and market shares of major exporters (percent)**

Exporters	HS	2006	2007	2008	2009	2010	Growth 2010
World (Million US\$)	61	2933	3331	3707	3,429.03	3,856.00	12.45
	62	3219	3546	3713	3,408.05	3,668.23	7.63
	RMG	6152	6877	7420	6,837.08	7,524.23	10.05
China	61	47.8	51.8	52.5	51.54	50.79	10.82
	62	50.5	53.7	54.0	53.48	53.48	7.63
	RMG	49.2	52.8	53.3	52.51	52.10	9.20
Bangladesh	61	7.5	6.7	7.6	8.62	9.50	23.93
	62	6.5	6.1	6.6	9.40	9.63	10.30
	RMG	6.9	6.4	7.1	9.01	9.56	16.84
USA	61	7.3	5.9	6.4	6.05	5.72	6.34
	62	5.8	5.6	5.6	5.21	4.99	3.01
	RMG	6.5	5.8	6.0	5.63	5.36	4.80
Cambodia	61	2.6	3.4	4.6	5.24	6.25	34.11
	62	1.6	2.0	2.0	2.07	2.39	24.57
	RMG	2.1	2.7	3.3	3.66	4.37	31.42
India	61	6.0	5.3	4.3	4.50	3.60	-10.01
	62	5.1	4.2	4.0	4.13	3.69	-3.81
	RMG	5.5	4.7	4.2	4.31	3.64	-7.05
Vietnam	61	1.6	2.1	2.8	3.40	3.49	15.25
	62	2.4	2.4	3.0	3.59	3.50	5.09
	RMG	2.0	2.2	2.9	3.49	3.49	10.05

Source: [http://www.ic.gc.ca/sc\\_mrkti/tdst/tdo/tdo.php#tag](http://www.ic.gc.ca/sc_mrkti/tdst/tdo/tdo.php#tag)

## **Recession and the Wal-Mart Effect**

The relatively good performance of RMG export of Bangladesh during the worst global recession of the last seven decades has been the subject of much speculation. Initially it was thought that there would be some lag for the impact of the recession to show up on the RMG exports of Bangladesh. While this might have had some grains of truth, the continued good performance of RMG export needed a more cogent explanation.

Some people, especially the industry leadership, came out with the hypothesis that this counter-intuitive behaviour of RMG export, i.e. increased shipment with falling income of the importing countries, was rooted in the nature of the demand for the type of RMG products exported by Bangladesh. It was argued that Bangladesh specialised in the production and export of cheap mass products at the lower end of the price spectrum of the RMG products. Bangladesh had a comparative advantage in the export of these products because of the extremely low wages of its workers that helped to keep the prices low.

The recession in the EU and the USA, the two principal markets of Bangladesh, reduced their income and consumption spending. To cope with the reduced income and spending, it was argued, the consumers in these countries switched from the more expensive RMG items to the cheaper varieties such that the demand for these cheaper products actually increased. Bangladeshi RMG exporters cashed on this increased demand helped by its low costs. Consequently, the RMG exports from Bangladesh increased when most other countries suffered large reductions in their exports. This phenomenon was given the fancy eponymous title of “Wal-Mart effect”, presumably because the giant retailer Wal-Mart of USA, which sells mostly cheap basic consumer products, did relatively well during the recession, and many people thought this was due to switching of consumer spending to cheaper products in order to meet ends at a difficult time.<sup>18</sup>

It may be noted that the goods that are susceptible to Wal-Mart effect are what economists call ‘inferior goods’. Such goods are characterised by negative income elasticity of demand. At low incomes people are forced to consume these relatively cheaper goods as they cannot afford the more pricey ones. When income increases, they substitute these goods for the more desirable and expensive goods. Thus, the demand for these cheaper goods is higher at lower incomes. The obverse must also hold true; ie. the demand is lower at higher incomes.

Whether a good is inferior or not is an empirical question and must be settled by an appeal to empirical evidence. However, some preliminary remarks are possible on the basis of what is widely known. The demand for most of the knit and woven products that Bangladeshi exporters specialise in has been increasing over the years when both the EU and the US economies were growing strongly. Since average prices of these products did not decline, it stands to reason to assume that the income elasticity of demand for these goods were positive, i.e., these were normal goods. There is no compelling reason to believe that they have turned into inferior goods just because the world economy entered into a recession during 2008-09. If its main export items were really inferior goods, Bangladesh should be greatly worried, since the demand for its products will progressively fall as the western economy climbs out of the recession and marches onward.

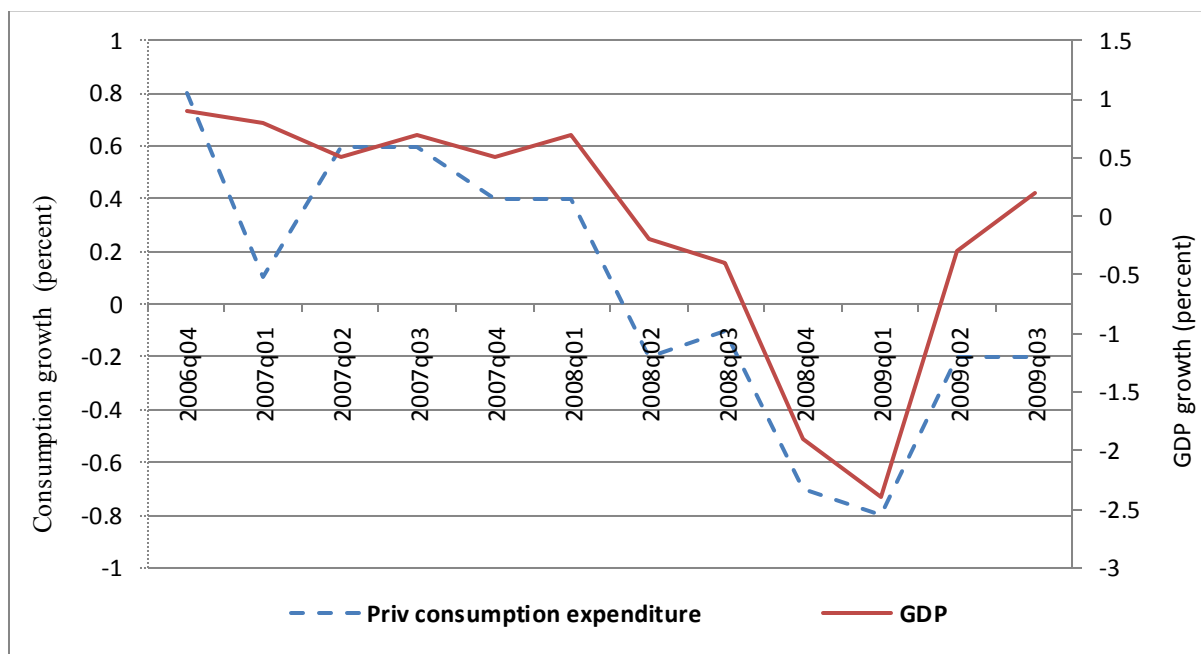
The first part of the arguments of the Wal-Mart effect implies that the recession, i.e. negative growth of income (GDP), has induced a reduction in consumer spending. This is borne out by data of both the EU and the USA as shown in Figure 16 and 17.<sup>19</sup> A fall in quarterly income growth rates has been matched by a fall in consumer spending as would be predicted by the standard theories of consumption.

The second part of the argument that a fall in income and consumer spending increased the demand for cheaper clothing items that are exported by Bangladesh is, however, not unambiguously corroborated by data currently available. Table 7, 8, 9 and 10 show the global import payments of the EU and the USA on the top 15 knitwear products and top 15 woven garment items exported to them by Bangladesh. It will be seen that during the five year period 2003-08 the global import demand for all the items save one increased markedly in the EU market. During the recession year 2009 the demand for 9 of the top 15 knit items and 12 of the top 15 woven items actually decreased. The demand for all but 1 of the 9 knit and woven items, whose demand had increased during 2009, also increased during the first three

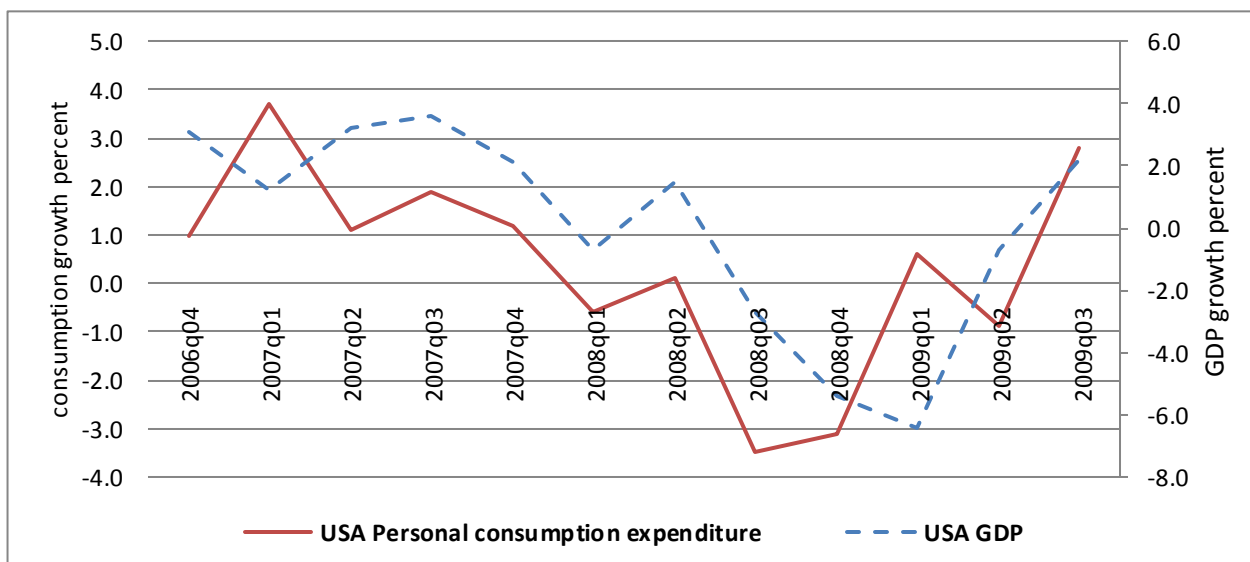
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<sup>18</sup> Wal-Mart effect implies a host of different things in the USA.

<sup>19</sup> This relationship also holds for Canada.

**Figure 16: EU GDP and consumption growth (quarterly)**

Source: *US Bureau of Economic Affairs*

**Figure 17: US GDP and private consumption spending growth (quarterly)**

Source: *US Bureau of Economic Affairs*

quarters of 2010 when the EU income increased. Hence, it is rather difficult to argue that these could be inferior goods. The modest increase in demand for these 9 products during

2009 could be due to a host of factors such as switch in demand due to fashion changes, price competitiveness, aggressive marketing etc. rather than falling income.

**Table 7: EU global import of knitwear (top-15 knit export items of Bangladesh)**

(Million Euros)

HS code	2003	2004	2005	2006	2007	2008	2009	Jan-Sep 2009	Jan-Sep 2010
61091000	3812	4577	5086	5772	5938	5669	5205	4250	4343
61103099	2057	2076	2355	2427	2163	2442	2574	1837	1930
61102099	1526	1516	1625	1948	2102	2552	2406	1799	1676
61099020	0	0	0	0	0	1072	1099	851	1045
61102091	705	743	865	1009	1110	1258	1232	911	931
61112090	746	826	891	1020	1120	1148	1155	898	921
61051000	511	538	642	809	948	1005	949	790	850
61046200	0	0	460	565	633	730	806	613	718
61061000	279	344	421	521	620	700	639	529	480
61044200	71	84	89	114	226	270	333	263	349
61083100	0	0	402	445	489	483	456	340	337
61103091	439	457	471	469	412	460	467	335	329
61034200	0	0	142	182	214	226	208	162	175
61072100	173	179	192	208	203	210	200	152	155
61142000	130	169	143	192	197	185	175	141	146

Source: Eurostat

**Table 8: EU Woven imports from the world (top-15 export items of Bangladesh)**

(Million Euros)

HS	2003	2004	2005	2006	2007	2008	2009	Jan-Sep 2009	Jan-Sep 2010
62052000	1518	1504	1595	1830	2019	2008	1885	1470	1547
62034231	954	1036	1281	1393	1501	1734	1777	1337	1435
62034235	1441	1550	1675	1878	1931	1937	1777	1448	1406
62046239	1688	1670	1884	2073	2072	2058	1829	1473	1329
62063000	654	604	714	1026	1178	1323	1406	1155	1209
62046231	695	811	1113	1179	1205	1323	1323	1022	1068
62121090	1015	1011	1067	1184	1296	1283	1243	946	1019
62046318	831	804	693	702	713	670	595	458	453
62064000	554	478	484	506	584	557	551	424	444
62045200	555	620	949	1008	785	565	522	444	384
62034290	162	184	186	248	316	333	352	324	368
62092000	341	366	406	490	497	492	482	379	359
62034319	418	443	436	425	422	418	417	337	338
62046290	147	163	132	223	328	258	238	213	246
62053000	382	323	288	283	265	229	199	157	148

Source: Eurostat

**Table 9: US global import of knitwear (top-15 knit export items of Bangladesh)**

(Million US Dollar)

HS code	2003	2004	2005	2006	2007	2008	2009	2010
61102020	6728	7073	7585	8230	9145	8874	8035	8747
61091000	3046	3220	3424	3732	3510	3816	3363	4052
61103030	3105	3282	3123	3047	3244	3071	2765	3144
61051000	1417	1285	1548	1890	2008	1700	1365	1525
61046220	987	933	948	1124	1299	1194	1129	1407
61112060	931	963	987	1063	1179	1111	1034	1136
61082100	637	716	681	755	753	771	665	808
61071100	760	733	782	688	680	772	631	795
61061000	779	740	863	1033	1075	926	676	676
61044320	136	113	119	234	441	487	544	662
61034315	480	508	523	516	577	535	537	625
61012000	145	201	257	383	640	701	553	605
61083100	415	418	484	466	511	478	381	425
61013020	201	241	285	287	329	323	295	353
61034210	279	257	236	267	257	244	241	269

Source: *USITC Trade Data Web***Table 10: US total import of woven items (top-15 woven export items of Bangladesh)**

(Million US dollar)

HS code	2003	2004	2005	2006	2007	2008	2009	2010
62046240	5261	5396	5909	5752	5795	5573	5026	5184
62034240	4841	4766	5050	5275	5208	5133	4639	5083
62052020	2070	2350	2663	2407	2532	2379	2100	2577
62121090	1149	1312	1343	1465	1448	1469	1327	1647
62063030	1360	1356	1407	1553	1571	1433	1383	1494
62034340	962	986	1029	1046	1033	922	740	865
62019330	713	647	674	667	706	644	541	601
62045220	618	709	1017	1039	687	527	463	406
62053020	645	676	610	565	530	421	345	394
62104050	188	247	247	299	355	347	309	375
62019220	266	302	291	339	344	295	244	274
62092050	237	224	235	257	231	186	184	192
62092030	127	135	156	189	201	183	181	173
62082100	163	162	183	175	159	145	126	123
62111110	125	132	125	115	120	103	92	84

Source: *USITC Trade Data Web*



The evidence from US import data is quite unambiguous. The global import demand of USA for all but two of the top 15 knit export items of Bangladesh to USA increased very considerably during 2003-07 when the US economy was buoyant. In the case of woven garment the global import demand of USA for 10 of the top 15 export items of Bangladesh increased. Since the recession began in the USA in the third quarter of 2008, part of its effect was already evident in 2008. The US import of 10 of the 15 knit items and 13 of the 15 woven items fell in 2008. There were steeper fall in 2009 when the recession was at its worst. All but one knit items and all woven items had significantly lower import in 2009 than in 2007. It is noteworthy that the import demand for all knitwear items and all but 4 woven garment items increased in 2010 when the US economy grew well. There is little doubt that the income elasticity of demand is positive for most of these items.

The demand for these apparel products increased during rising incomes in the EU and the USA, and the demand for most of them fell when the recession took effect. Thus the pattern of demand in the EU and the USA does not lend much support to the view that the RMG products that Bangladesh sells in these markets are inferior goods. Hence, the relatively better performance of the RMG exports of Bangladesh to the EU and the USA cannot be explained by the so-called Wal-Mart effect.

### **Inexpensive Export Products**

When it became abundantly clear that the Wal-Mart effect could not explain the pattern of import demand of the RMG exports of Bangladesh, a more sophisticated version of the hypothesis was propounded and for a while gained some currency. It claimed that the global import demand for the low priced export items of Bangladesh did not suffer as badly during the recession as the more expensive items that the more developed countries exported, and consequently exports of Bangladesh did not suffer much.

There is no ambiguity that the Wal-Mart hypothesis above suggests that the unit price of the products that Bangladesh typically exports is cheaper than the unit prices of the exports of the *same* products (at 6 or 8 digit HS code level) by the relatively more developed countries. But it is not clear if the second hypothesis implies the same. If yes, then the two hypotheses essentially say the same thing. However, if the latter implies that the unit prices of Bangladeshi export products are cheaper than the unit prices of the products exported by the more developed countries which may be different, then we run into the difficult problem of comparing the values of dissimilar goods, which is further compounded by the fact that they could be measured in different units. For example, how do we compare the price of a shirt with that of wine or timber?

Abstracting from these difficulties, the hypothesis is still difficult to sustain since the global export of many products of the more developed countries did not fall during the recession. Indeed, the export of some products such as pharmaceuticals, tobacco, cocoa and cocoa preparations, food preparations etc. by the EU and the USA actually recorded *positive* growth rates. Furthermore, a large number of the relatively less developed countries export the same “cheap” goods (for example, apparels) that Bangladesh exports. Most of them, especially those in Africa and Central America, suffered large reductions in their exports. Obviously the hypothesis above cannot explain the better export performance of Bangladesh when most other countries in a similar situation performed poorly.

## Competitive Strength

One of the principal reasons for Bangladeshi exports holding out well during the recession is the competitive strength of the apparel industry of Bangladesh. This strength derives from the innovativeness of the domestic entrepreneurs, conducive domestic policies, duty-free access in all developed countries (except the USA), and most importantly, an abundant supply of cheap labour. This is discussed below in more detail.<sup>20</sup>

While competitiveness provides an explanation of the better export performance of Bangladesh, it does not explain why some other countries such as China and India, which are by all accounts equally, or perhaps more, competitive than Bangladesh did not fare as well. This paper suggests that the answer lies in the composition of the export basket of these countries and the nature of the demand for these export products.

## Permanent Income and Consumer Spending

It has been mentioned earlier that the import demand for apparels declined less than most other products. This raises an important question why the import of apparels by the major importers declined less during this recession than the import of most other products. Import statistics of the EU and the USA given in Table 11 below reveal that the import of knitwear by the EU declined by only 2.7 percent and that of woven garments by 4.8 percent when the total import declined by 23.4 percent. US import of knitwear declined by 10.7 percent and that of woven garments by 13.4 percent. These reductions are much less than the average 25.9 percent reduction of the total US import in 2009.

Although the rates of decrease of imports of apparel in both the EU and the USA were modest, there are several other commodities at HS two-digit level whose import either *increased*, or fell by less than or at about the same rate as the import of knitwear or woven garments. Some of these commodities are arms and ammunitions, pharmaceuticals, tobacco, cocoa and cocoa preparations, fruits and nuts, footwear, fish, coffee, tea and cereal, vegetable and meat preparations, etc. in the case of the USA (see Table 11 below). The corresponding products for the EU are cocoa and cocoa preparations, pharmaceuticals, tobacco, footwear, head gear, cereal preparations, etc. To anticipate the discussion below, note that a commonality among these commodities is that they are all final consumption goods, most of them being non-durable consumption goods.<sup>21</sup>

The imports of railway and tramway locomotives, aircraft and ships and boats by the EU also increased significantly. These goods are very long lasting investment goods. One would expect their demand to fall off during a recession. However, their production requires a long gestation period, especially that of large aircraft and ship. Orders for such goods have to be placed long before the actual delivery (import), and once an order is placed, it is not easy to cancel it. Import (export) of cereals is dependent on weather conditions, which greatly influence total production, and hence the import requirements. Therefore, their imports may

<sup>20</sup>For a discussion of the sources of competitive advantage see World Bank (2005).

<sup>21</sup> Final consumption goods are sold to final users and are not resold or used for further production.

not always bear a strong relationship with the current state of the economy. The demand of a country for arms and ammunition is significantly influenced by the security policy and the state of belligerence such that the effect of income could be sometimes offset.

Import growth (decline) rates in the EU and the USA at the two-digit HS code level for 2009 and 2010 are reported in Table 11. There is a remarkable similarity between the two markets in respect of the pattern of import growth. The correlation coefficient between the two series for 2009 is 0.81, which is very high. The correlation for 2010 is also high at 0.66. Hence, it can be said that the import demand of the commodities at the HS Code 2-digit level were affected due to the recession in a similar manner in both the markets. Especially noteworthy is the fact that the import of final consumption goods in both markets suffered relatively smaller declines during the recession than the non-consumption goods.

It is well known from the theories of consumption that consumer spending does not depend on current income, but rather on permanent or life cycle income.<sup>22</sup> Permanent (or life cycle) income is *less* than the actual income during business booms and *greater* than the actual income during recessions. In other words, permanent income, being in the nature of expected income over the long term, fluctuates less than the actual short term income.

**Table 11: Chapter wise import growth of EU and USA in 2009 & 2010 (percent)**

HS	Products	EU 27		USA	
		2009	2010* (Jan-Nov)	2009	2010
72	IRON AND STEEL	-61.32	56.75	-61.4	73.5
75	NICKEL AND ARTICLES THEREOF	-54.42	104.96	-50.43	73.6
10	CEREALS	-50.98	-8.79	-25.76	-10.3
31	FERTILIZERS	-47.87	48.44	-50.28	60.2
81	BASE METALS NESOI; CERMETS	-47.42	42.61	-45.22	42.3
80	TIN AND ARTICLES THEREOF	-45.87	82.79	-35.33	52.5
26	ORES, SLAG AND ASH	-45.69	86.89	-34.75	16.4
25	SALT; SULFUR; STONE; LIME & CEMENT	-44.27	31.74	-45.96	32
74	COPPER AND ARTICLES THEREOF	-41.94	56.47	-45.24	40.2
76	ALUMINUM AND ARTICLES THEREOF	-40.99	55.26	-33.89	24.2
51	WOOL & ANIMAL HAIR, YARNS & FABRICS	-38.26	45.24	-33.46	18
78	LEAD AND ARTICLES THEREOF	-38.26	59.81	-38.07	37
50	SILK, SILK YARNS AND FABRICS	-37.58	25.59	-41.88	9
79	ZINC AND ARTICLES THEREOF	-37.43	87.2	-28.68	35.8
41	RAW HIDES AND SKINS AND LEATHER	-35.53	50.02	-34.64	31.9
27	MINERAL FUELS, OILS, WAXES AND PRODUCTS BITUMINOUS SUBSTANCES	-35.03	24.54	-45.16	30.5
44	WOOD & WOOD ITEMS	-30.11	20.54	-30.66	16
43	FURSKINS AND FUR PRODUCTS	-30	30.04	-20.2	26

<sup>22</sup> These concepts were first developed by Modigliani and Brumberg (1954), Ando and Modigliani (1963) and Friedman (1957).

97	WORKS OF ART, PIECES AND ANTIQUES	-29.64	29.19	-32.49	23.8
15	ANIMAL OR VEGETABLE FATS & OILS	-28.9	16.7	-28.17	14.3
87	MOTOR VEHICLES	-28.52	14.05	-32.61	38.7
73	ARTICLES OF IRON OR STEEL	-27.95	12.96	-35.67	9.5
40	RUBBER AND ARTICLES THEREOF	-27.92	44.22	-24.25	40.4
53	VEGETABLE TEXTILE FIBERS NESOI	-27.76	40.11	-53.34	26.5
47	PULP OF WOOD RECOVERED	-26.95	56.28	-39.03	58.6
54	MANMADE FILAMENTS, FABRICS	-24.17	32.27	-24	22.8
68	STONE PRODUCTS, PLASTER, CEMENT	-23.23	26.15	-27.44	12.2
82	TOOLS, IMPLEMENTS, CUTLERY, SPOONS	-22.31	24.69	-23.24	28.5
69	CERAMIC PRODUCTS	-21.33	22.15	-26.07	27
52	COTTON, YARNS AND FABRICS	-20.93	30.58	-28.76	32
55	MANMADE STAPLE FIBERS, FABRICS	-20.93	29.72	-29.76	31.3
84	NUCLEAR REACTORS, BOILERS	-20.5	24.24	-18.07	22.9
71	NATURAL OR CULTURED PEARLS,IMITATION JEWELRY; COIN	-20.29	40.52	-22.27	39.3
70	GLASS AND GLASSWARE	-19.9	24.55	-21.71	22.1
83	ARTICLES OF BASE METAL	-19.7	28.11	-22.46	24.8
28	INORGANIC CHEMICALS; COMPOUNDS OF PRECIOUS METALS, ISOTOPES	-19.5	24.95	-36.46	27.4
39	PLASTICS AND ARTICLES THEREOF	-18.82	30.39	-20.59	23
32	TANNING OR DYEING EXTRACTS	-18.47	35.75	-21.06	28.2
1	LIVE ANIMALS	-18.45	2.02	-27.26	17.5
37	PHOTOGRAPHIC GOODS	-18.16	1.99	-21.8	2.7
59	TEXTILE FABRICS FOR INDUSTRIAL USE	-17.84	29.06	-12.26	28.2
12	OIL SEEDS AND OLEAGINOUS FRUITS	-17.52	2.25	-19.67	2.5
46	STRAW, PLAINTING MATERIALS;BASKETWARE AND WICKERWORK	-16.85	19.95	-19.6	13.3
38	MISCELLANEOUS CHEMICAL PRODUCTS	-16.31	19.46	-27.42	19.1
85	ELECTRICAL MACHINERY ANDEQUIPMENT TELEVISION RECORDERS	-16	32.46	-15.29	20.8
95	TOYS, GAMES AND SPORTS EQUIPMENT	-15.43	2.62	-13.23	7.8
56	WADDING, SPECIAL YARNS	-15.17	31.79	-16.79	21.8
94	FURNITURE; BEDDING, CUSHIONS ETC.; LAMPS AND LIGHTING FITTINGS NESOI	-15	24.04	-21.58	25.5
29	ORGANIC CHEMICALS	-14.94	24.63	-21.39	11.8
58	SPECIAL WOVEN FABRICS	-14.19	12.35	-24.37	18
91	CLOCKS AND WATCHES AND PARTS	-13.52	17.61	-28.14	19.7
92	MUSICAL INSTRUMENTS; PARTS	-13.49	14.03	-25.74	12
34	SOAP ; WAXES, CANDLES & PASTES	-13.28	21.84	-13.92	17
17	SUGARS AND SUGAR CONFECTIONERY	-12.59	-1.1	4.33	30.8
57	CARPETS & TEXTILE FLOOR COVERINGS	-12.19	13.11	-22.44	17.4
20	OF VEGETABLES, FRUIT, NUTS PREP.	-11.84	5.49	-11.95	4.9
96	MISCELLANEOUS MANUFACTURED	-11.84	19.37	-11.64	15.4
42	LEATHER ITEMS; TRAVEL GOODS	-11.82	14.27	-19.22	21.6
66	UMBRELLAS, WALKING-STICKS	-11.58	15.6	-13.1	24.6
49	BOOKS, NEWSPAPERS, PICTURES	-10.98	3.88	-21.72	8.4
67	PREPARED FEATHERS AND ARTIFICIAL FLOWERS; ARTICLES OF HUMAN HAIR	-10.92	22.73	-12.28	21.5

7	EDIBLE VEGETABLES & ROOTS & TUBERS	-9.79	8.39	-4.3	20.3
23	FOOD INDUSTRY WASTE; ANIMAL FEED	-9.74	5.51	-4.1	14.8
99	SPECIAL IMPORT REPORTING PROVISIONS	-9.28	-5.31	-25.56	-19.1
8	EDIBLE FRUIT & NUTS; MELONS	-8.5	6.42	4.23	13.1
14	VEGETABLE PLAITING MATERIALS	-7.74	31.92	-15.19	-23.5
48	PAPER AND PAPERBOARD	-7.66	10.94	-19.76	5.7
4	DAIRY PRODUCE; BIRDS' EGGS; HONEY	-7.65	8.96	-13.68	4.8
11	MILLING IND. PRODUCTS; STARCHES	-7.43	10.15	-8.1	4.7
2	MEAT AND EDIBLE MEAT OFFAL	-7.13	2.07	-8.47	14.7
13	LAC; GUMS; RESINS & VEGETABLE SAPS	-7.11	18.14	-7.63	22.6
16	MEAT, FISH, CRUSTACEANS (EDIBLE)	-7.01	2.76	-6.45	7.2
22	BEVERAGES, SPIRITS AND VINEGAR	-6.8	-0.46	-12.86	5.3
45	CORK AND ARTICLES OF CORK	-6.6	-7.56	-22.67	3.3
35	ALBUMINOIDAL SUBSTANCES; GLUES	-6.31	9.02	-19.61	14.6
33	ESSENTIAL OILS AND RESINOIDS	-6.15	18.64	-10.49	12.5
3	FISH AND CRUSTACEANS, MOLLUSCS	-5.82	13.39	-7.49	12
63	MADE-UP TEXTILE ARTICLES NESOI	-5.28	16.77	-9.4	19
9	COFFEE, TEA, MATE AND SPICES	-5.26	22.38	-9	22.1
5	PRODUCTS OF ANIMAL ORIGIN, NESOI	-5.15	1.7	-11.32	13.4
6	TREES & PLANTS; BULBS, CUT FLOWERS	-4.98	3.9	-8.15	9.8
62	WOVEN GARMENTS	-4.65	4.19	-13.43	10.3
90	OPTICAL, PHOTOGRAPHIC, INSTRUMENTS & APPARATUS; PARTS & ACCESSORIES	-4.65	13.19	-13.06	18.1
93	ARMS AND AMMUNITION	-4.16	25.68	19.69	-3.4
65	HEADGEAR AND PARTS THEREOF	-3.85	18.9	-15.1	21.8
64	FOOTWEAR, GAITERS AND THE LIKE	-3.8	13.43	-9.18	17.2
60	KNITTED OR CROCHETED FABRICS	-2.81	28.84	-16.29	11.4
61	KNITWEAR	-2.52	8.53	-10.7	14.7
36	EXPLOSIVES; MATCHES; ALLOYS	-2.51	5.58	-4.67	18.6
21	MISCELLANEOUS EDIBLE PREPARATIONS	0.88	6.88	-0.2	13.6
19	CEREALS, FLOUR, STARCH OR MILK PREP.	1.34	7.83	-1.41	11.2
86	RAILWAY OR TRAMWAY LOCOMOTIVES, ROLLING STOCK, FITTINGS, & PARTS	4.07	-34.97	-30.59	12.3
88	AIRCRAFT, SPACECRAFT, AND PARTS	4.45	3.86	-14.84	3.2
89	SHIPS, BOATS AND FLOATING ITEMS	9.29	58.6	-18.82	18.9
24	TOBACCO AND TOBACCO SUBSTITUTES	15.03	11.13	6.79	-9.2
30	PHARMACEUTICAL PRODUCTS	15.77	9.38	6.11	10.8
18	COCOA AND COCOA PREPARATIONS	17.51	16.15	5.37	23.5
98	SPECIAL CLASSIFICATION PROVISIONS			-5.62	7.4
Total				-25.89	22.6

\*over January-November 2009

Source: Eurostat and USITC Trade Data Web

Since consumption spending is related to permanent income in a stable manner, it fluctuates less than the actual income. This implies that consumer spending fluctuates less than the fluctuations in actual income. This makes the short run consumption function flatter than the

long run consumption function as Simon Kuznets had discovered many decades ago in his pioneering work.

That consumer spending fluctuates less than the current income has solid empirical foundations. For an illustration Figure 19 shows the quarterly changes of GDP and consumer spending of the USA since 1995. It is immediately obvious that consumer spending tends to fluctuate less than GDP. This tendency is known in the economic literature as consumption smoothing.

The demand for non-consumption goods, such as raw materials and intermediate goods, on the other hand responds directly to current production i.e. current income. Consequently, their demand fluctuates in line with the fluctuation of the current income. Inventory adjustments and expectations could amplify these fluctuations.

If there is a stable relationship between imported and domestic component in the consumption of a tradable good as implied by Armington (1969), the consumer theory implies that the import of consumer goods will fluctuate less than the non-consumption goods. The patterns of the import demand of the EU and the USA appear to be consistent with this story.

The export basket of Bangladesh comprised mostly non-durable consumer goods as shown in Figure 5. Indeed more than 90 percent of the total exports, including knitwear and woven garments, frozen food, pharmaceuticals, footwear and home textiles, are final consumer goods. More than seven-tenths of the exports were shipped to the EU and the USA. As evident from Table 11 below the import demand for the consumer goods of both the EU and the USA either increased or did not decline much during 2009. Consequently, the global demand for the export products of Bangladesh in these markets also did not suffer as badly as the demand for other commodities.

China and India's export of consumption goods such as apparels or pharmaceuticals to the USA actually did quite well. Indeed, if the export baskets of these countries comprised mostly these goods, their export performance during the recession could have been much better.<sup>23</sup>

However, in sharp contrast to the composition of the export basket of Bangladesh, a large part of the export products of the large exporters such as China, India, EU and USA are non-consumption and investment (or durable) goods. The import demand of these goods usually fluctuate a great deal more with the state of the economy because the total demand is directly related to actual production, future outlook and business confidence, or because their purchase could be delayed.

As the world economy recovered, import demand for commodities that had suffered large declines due to the recession bounced back strongly. However, the import demand for the

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<sup>23</sup> Export of apparels, food products and pharmaceuticals brought in less than one-fifth of the total export earnings of India. For China, the proportion was even lower.

export products of Bangladesh did not show a large increase. The very reason that prevented a sharp fall in the global import demand during the recession in 2009 also ensured a slow increase during the recovery in 2010. In order to accelerate its export earnings beyond this rate, Bangladesh will have to expand supply capacity, improve productivity and establish new markets and products. The growth rate of exports in July-January 2010-11 suggests that Bangladesh has successfully met the challenge.

## Comparative Advantage

The most cogent explanation of the competitive strength of the RMG exporters of Bangladesh would appear to lie in the comparative advantage of the country. It is a labour-abundant country with a large base of unskilled and semi-skilled labour force with very low wages. Over the last three decades it has developed some skill in garmenting, especially CM (cutting and making). A fairly rapid population growth has ensured that there is always a substantial pool of underemployed or unemployed people, which prevents the wage rate from rising. Consequently the RMG manufacturers of the country can employ workers at a very low wage. Indeed the average hourly wage rate of Bangladesh RMG workers is among the lowest in the world.

**Table 12: Labour costs in apparel manufacturing, 2008**

Country	Labour Cost (US \$/ Hour)
Bangladesh	.22
Cambodia	.33
Vietnam	.38
India	.51
China	.55-1.08
Turkey	2.44

Source: *Jasin-o'Rourke Group, LLC*

The average wage rates in China and India are about 150 percent higher, while that in Cambodia about 50 percent higher than that of Bangladesh (see Table 12). Despite the fact that the productivity of the workers in Bangladesh is also relatively low, the extremely low wages are sufficient to offset the low productivity of the workers, and to impart a competitive edge to RMG exports by keeping the prices of RMG items low. The RMG sector is essentially riding on the back of the low wage of these workers.

The tables below (Table 13 and Table 14) show that Bangladesh was by far the most price-competitive exporter of most of the major RMG export items during 2009 and 2010. A noteworthy point is that all the countries except China paradoxically increased the unit prices of most of the items in 2009 (relative to that in 2008) despite the recession. However, the rate of increase was lower in the case of Bangladesh such that its competitive edge actually increased during the recession against these other countries.

The only major exporter which reduced the prices of all the apparel products listed in the Table 13 and 14 since 2008 is China. Some prices were slashed by China by as much as 20-25 percent. It is obvious that China drastically undercut the other exporters in the EU market in order to retain (or expand) its market share. The substantial reduction in prices allowed

China to achieve significant growth in apparel export to the EU at the expense of other exporters most of whom experienced large decreases in exports.

The competitive edge imparted to RMG products of Bangladesh by its modest labour cost is further amplified by the duty free access that it enjoys as a least developed country in all developed countries of the world except the USA, which has stubbornly resisted providing duty free access to LDCs as per several UN and WTO resolutions. Most of the competitors of Bangladesh in the world RMG market are developing countries such as China, Vietnam, India and Pakistan. Their exports do not enjoy duty free access in these markets unless the products are MFN duty free (or they have free trade agreements in this regard). Since textile products attract very high trade duties in most developed markets, the margin of preference enjoyed by the least developed countries in the export of such products vis-à-vis developing countries is substantial provided they satisfy the rules of origin. This makes the least developed countries such as Bangladesh and Cambodia attractive sources of import into these markets.

To encourage export, the backward linkage industry of RMG, i.e. the textile sector, was given generous cash incentives by the government since 1994. Initially the incentives were set at 25 percent of the export value, but over time it has been reduced to 5 percent. The cash incentives greatly facilitated the quick growth of the textile sector. It now provides about nine-tenths of the fabric for the knitwear and three-tenths of the woven garment exports. The local availability of yarn and fabric allowed the RMG exporters to access the duty free facility in the EU market under the two-stage requirement of the rules of origin.

The continued dependence of the RMG manufacturers of Bangladesh on the relatively cheap mass products might seem somewhat puzzling. With more than three decades of experience in garmenting that catapulted it to one of the largest RMG exporters of the world, Bangladesh should have made inroads in the market for more pricey apparel (and other) products. However, the low wage rate works as a deterrent to graduating to higher value products. A low wage rate necessarily implies low productivity of the workers. It effectively condemns the RMG workers into low productivity manufacturing. The only apparel products that low productivity workers can profitably produce are the cheap mass products that do not require much skill. The RMG manufacturers of Bangladesh will continue to specialise in cheap mass products as long as the RMG wage rate remains at the current pitiful level and the market is sufficiently large. The wage rate is unlikely to rise much as long as the population keeps on growing at a rate that outstrips the growth of more productive employment opportunities. The minimum wages of the RMG workers remained unchanged for many years. After prolonged and widespread labour unrest and violence the government and the manufacturers finally agreed to some increase in the wage rate at the end of 2010. The government also agreed to provide the workers with subsidised rice. However, steeply rising house rent and food prices have already eroded much of the benefits of the wage increase.

The history of manufacturing shows that when the wage rate is low, a country specialises in the production of labour-intensive goods such as apparel products. Japan, Italy, Korea, Singapore and such other countries all had a very vibrant RMG sector in the earlier years of their development when their wage rates were low. As their wage rates rose with rapid economic development, their RMG sector lost the comparative advantage in producing the cheaper apparel items. They have all but abandoned this segment of the apparel market. Only very high value designer clothing items that require highly skilled labour are still manufactured in some of these countries since the high prices that consumers are willing to



pay for these items justify employing labour at the high wage rates attained by the workers of these countries.

## **Restructuring of Apparel Sourcing**

The current recession has badly affected the major RMG exporters that have attained relatively high wage rates, such as Mexico, Turkey, Hong Kong, Malaysia and Thailand. All these countries suffered large reductions in export of apparels during the recession. It is unlikely that they will return in force to the RMG market in future. Rising wages is also likely to whittle away the current competitive edge of China in apparel exporting. These may open up new opportunities for export expansion of low wage countries such as Bangladesh, Cambodia, India and Vietnam. Bangladesh must have a congenial manufacturing environment in order to position itself in the emerging market for apparels.

Many importing countries such as Japan and Australia that depended heavily on China for the supply of apparels have become aware of the disadvantages that China could soon face in competing effectively with low wage countries. They are now urgently looking for alternative and reliable sources of supply. Major apparel trading companies are hunting for reliable vendors able to continuously replenish their shelves at reasonable costs. There are not many countries which can fill up the space expected to be vacated by China and other high wage countries. Major importers are also likely to concentrate their buying operation in a few highly competitive countries to economise on the costs of procurement. Bangladesh is reported to be at the top of the list of most major companies. The surge in RMG exports by 41.1 percent during the first 8 months of 2010-11 is a pointer in this regard.

The global recession has opened up a once-in-a-lifetime opportunity for rapid industrial expansion of Bangladesh, which will be spearheaded initially by the RMG sector. Whether it will translate into a sustained increase in RMG exports depends on how well the manufacturers can meet the requirements of the international market, especially in respect of lead time, quality and timely despatch of orders.

**Table 13: Unit price of major export items of Bangladesh to USA****(US\$/dozen)**

<b>2010</b>										
	Bangladesh	Cambodia	China	Honduras	India	Indonesia	Mexico	Pakistan	Sri Lanka	Vietnam
61051000	35.28	42.43	56.34	35.75	46.61	43.15	57.85	38.57	68.72	51.88
61082100	6.37	7.47	7.75	6.47	11.26	9.79	18.85	10.76	13.11	6.24
61091000	15.43	21.80	24.00	15.17	21.45	25.12	19.73	19.03	36.06	23.39
61102020	29.15	34.70	62.93	20.88	42.38	38.16	32.79	36.56	47.92	40.06
61103030	39.45	36.90	52.04	42.04	68.52	54.16	43.50	29.93	72.88	51.33
62034240	57.31	76.75	70.35	66.70	80.36	58.87	88.52	64.40	96.06	67.39
62034340	62.99	58.87	66.34	75.42	82.52	75.41	82.49	31.37	109.24	71.07
62046240	53.62	68.45	63.54	28.35	71.54	66.79	100.86	66.09	86.98	64.38
62052020	49.78	66.63	77.04	78.40	86.51	66.13	110.22	35.42	88.27	62.80
62063030	42.88	44.13	61.75	34.82	66.06	72.36	47.31	27.46	80.08	48.89
62092030	33.79	28.85	31.56	24.36	46.31	35.79	39.45	56.76	46.08	33.25
<b>2009</b>										
	Bangladesh	Cambodia	China	Honduras	India	Indonesia	Mexico	Pakistan	Sri Lanka	Vietnam
61051000	31.54	40.81	57.11	33.97	49.39	45.46	71.11	37.44	65.92	51.09
61082100	6.73	5.62	9.12	6.91	10.85	6.91	21.07	10.03	12.98	6.38
61091000	13.31	23.48	23.31	16.20	21.76	25.52	20.11	17.82	36.46	25.01
61102020	28.92	34.38	64.15	22.29	41.25	38.37	32.63	36.55	51.04	39.22
61103030	41.04	38.17	53.17	40.19	60.70	51.22	48.92	24.99	67.71	50.26
62034240	55.83	75.22	73.59	64.40	79.51	59.92	88.09	60.56	87.13	65.61
62034340	62.14	59.17	68.65	76.00	84.78	76.81	80.58	37.45	77.69	71.37
62046240	54.04	66.32	67.63	34.86	67.04	68.49	101.84	61.90	88.34	62.19
62052020	48.80	55.78	78.31	82.90	85.57	70.63	98.30	35.62	79.42	59.89
62063030	41.24	42.31	60.94	31.35	63.16	74.10	49.43	25.77	70.80	43.63
62092030	32.94	30.66	31.51	42.26	48.16	38.24	40.97	54.78	46.63	32.39

<b>2008</b>										
	Bangladesh	Cambodia	China	Honduras	India	Indonesia	Mexico	Pakistan	Sri Lanka	Vietnam
61051000	33.24	45.36	67.51	35.74	54.17	46.72	88.56	39.13	69.79	53.18
61082100	7.38	7.24	11.26	5.76	10.35	6.73	17.32	8.41	13.18	8.48
61091000	14.41	25.87	31.46	15.50	26.42	21.95	20.52	19.01	38.69	25.42
61102020	30.19	37.68	71.74	20.53	44.38	41.60	35.98	38.69	52.38	42.52
61103030	39.96	36.66	61.64	39.77	73.83	58.38	50.37	28.03	65.54	56.59
62034240	55.09	67.15	89.41	60.75	85.24	60.39	91.63	60.36	91.42	65.23
62034340	56.08	62.04	75.55	71.08	94.19	70.96	79.88	33.33	66.21	69.56
62046240	52.40	68.69	81.06	36.16	70.97	66.93	97.61	62.32	82.51	61.22
62052020	49.12	56.10	84.92	74.22	81.68	74.71	96.46	39.60	79.30	60.69
62063030	41.25	46.12	65.59	32.00	65.58	69.93	59.37	23.12	70.06	49.85
62092030	34.95	31.37	34.19	45.22	49.23	43.49	39.91	30.17	42.28	31.59

Source: *USITC trade dataweb*

**Table 14: Unit prices of major export items of Bangladesh in EU market**

**(Euro/kg)**

<b>Jan-Sep 2010</b>											
	Bangladesh	Cambodia	China	Hong Kong	India	Indonesia	Pakistan	Thailand	Turkey	Vietnam	
61091000	7.88	11.13	11.06	16.91	14.21	13.83	n.a	14.39	18.92	9.07	
61102091	10.84	11.14	13.29	19.12	14.06	14.23	n.a	19.46	19.21	12.48	
61102099	11.22	14.67	15.88	25.52	15.03	14.22	n.a	19.05	20.06	13.51	
61103099	10.43	14.62	14.25	23.76	15.92	14.44	n.a	15.02	22.82	11.35	
62034231	8.19	11.28	10.14	11.94	18.15	14.28	n.a	12.16	19.92	12.63	
62034235	10.16	11.33	10.51	13.85	14.83	17.98	n.a	10.62	21.78	14.15	
62046231	9.68	8.87	9.67	15.07	20.00	12.87	n.a	16.40	23.38	17.60	
62046239	10.91	12.20	9.70	15.03	17.47	15.76	n.a	16.49	22.75	12.96	
62052000	11.62	15.02	15.19	25.96	20.16	19.18	n.a	24.67	35.93	19.68	
62063000	15.27	13.28	21.58	34.37	27.57	32.09	n.a	23.58	28.22	22.67	
62121090	22.02	16.07	23.62	43.85	35.97	29.91	n.a	47.58	33.90	46.58	

<b>Jan-Sept 2009</b>										
	Bangladesh	Cambodia	China	Hong Kong	India	Indonesia	Pakistan	Thailand	Turkey	Vietnam
61091000	8.51	13.26	11.03	24.76	14.98	18.19	13.26	17.6	19.5	10.2
61102091	8.97	10.74	11.98	26.67	15.3	13.81	10.74	19.3	21.1	14.95
61102099	11.02	12.88	14.29	34.4	12.79	14.55	12.88	22.04	21.5	15.29
61103099	9.02	12.47	16.09	30.62	18.44	14.68	12.47	17.67	24.7	12.19
62034231	9.4	0	11.93	13.95	20.27	12.94	n.a.	13	22.8	10.62
62034235	11.12	11.91	11.22	14.89	18.11	20.33	11.91	14.91	23.4	13.56
62046231	10.22	0	11.56	12.52	15.34	12.48	n.a.	16.16	25.9	9.09
62046239	11.25	15.09	9.95	15.11	20.75	20.46	15.09	15.61	23.8	11.61
62052000	11.44	0	12.64	26.35	19.85	19.04	n.a.	27.69	38.9	19.43
62063000	16.85	0	25.31	37.45	31.87	28.46	n.a.	36.24	32.6	29.27
62121090	29.53	0	27.95	34.21	92.04	24.27	n.a.	48.21	38.6	57.82
<b>January-September 2008</b>										
	Bangladesh	Cambodia	China	Hong Kong	India	Indonesia	Pakistan	Thailand	Turkey	Vietnam
61091000	7.47	11.70	13.62	18.84	13.83	13.01	8.42	17.05	18.7	5.76
61102091	8.30	9.52	14.39	19.88	14.66	9.36	6.80	17.83	18.9	6.79
61102099	9.52	12.82	17.76	26.01	13.53	13.97	7.54	18.51	19.1	10.67
61103099	7.98	14.30	17.05	26.85	20.03	13.46	6.83	15.10	24.6	9.32
62034231	7.31	9.45	10.95	10.36	10.48	12.20	10.15	10.44	19.4	11.95
62034235	9.37	10.46	13.28	14.48	16.99	18.66	8.96	8.17	21.9	8.28
62046231	7.92	n.a	11.12	11.67	13.45	12.86	10.56	15.01	22.5	7.46
62046239	9.18	13.51	12.87	16.81	18.27	17.04	9.22	11.93	22	5.41
62052000	9.75	n.a	12.86	28.23	18.89	17.83	6.92	17.74	30.4	17.53
62063000	15.14	n.a	26.58	35.03	28.63	25.98	n.a	26.03	26.8	16.68
62121090	29.95	n.a	29.75	28.24	n.a.	28.97	n.a	39.73	40.5	38.62

Source: *Eurostat*

## Conclusion

Notwithstanding some reduction in the export of RMG products during 2009, the industry has emerged out of the global recession of 2008-09 as a stronger and more efficient competitor in the world apparel market. It has captured a larger share of the RMG (import) market of Canada, EU and USA. The RMG exporters are now exploring other duty-free markets such as Japan and Australia. The recent stimulus package that provides financial incentives for exporting to new markets should raise the competitive strength of the industry in these markets. It seems likely that the RMG sector will expand its market shares even more in the coming years and will become a major sourcing hub for apparels for all major importers.

A chronic problem that has adversely affected the productivity of the RMG sector is the poor state of infrastructure services, especially gas and electricity. Frequent outages and uncertainty of supply of gas and electricity have increased costs. These problems have become more acute in recent months. Unless there is a quick resolution of these and other infrastructure related problems the competitive strength of the apparel exporters will suffer.

Bangladesh is still a supplier of cheap basic apparel items that can be profitably produced by unskilled and semi-skilled workers. If it wants to move up the value chain as new opportunities emerge in the post-recession global market, it will need to improve the quality (productivity) of its workforce and management. Such improvements will not be possible without a substantial increase in the skill, and hence, remuneration of the workers. If the sector fails to do so, and the wage rate rises nonetheless in response to positive developments in other sectors, it will find its comparative advantage pared away steadily.

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