



The Challenge of Export Diversification

Presented by
Dr Zaidi Sattar
Chairman, Policy Research Institute

What this Presentation Covers?

- EXPORT CONCENTRATION AND VULNERABILITY IN BANGLADESH
- LESSONS FROM INTERNATIONAL EXPERIENCE
- CONSTRAINTS TO TRADE DIVERSIFICATION IN BANGLADESH
- TRADE POLICY AND EXPORT DIVERSIFICATION
- EXPLOITING GLOBAL VALUE CHAIN FOR EXPORT DIVERSIFICATION
- ROLE OF FOREIGN DIRECT INVESTMENT (FDI) IN EXPORT DIVERSIFICATION
- POLICY AND INSTITUTIONS FOR EXPORT DIVERSIFICATION

OBJECTIVES

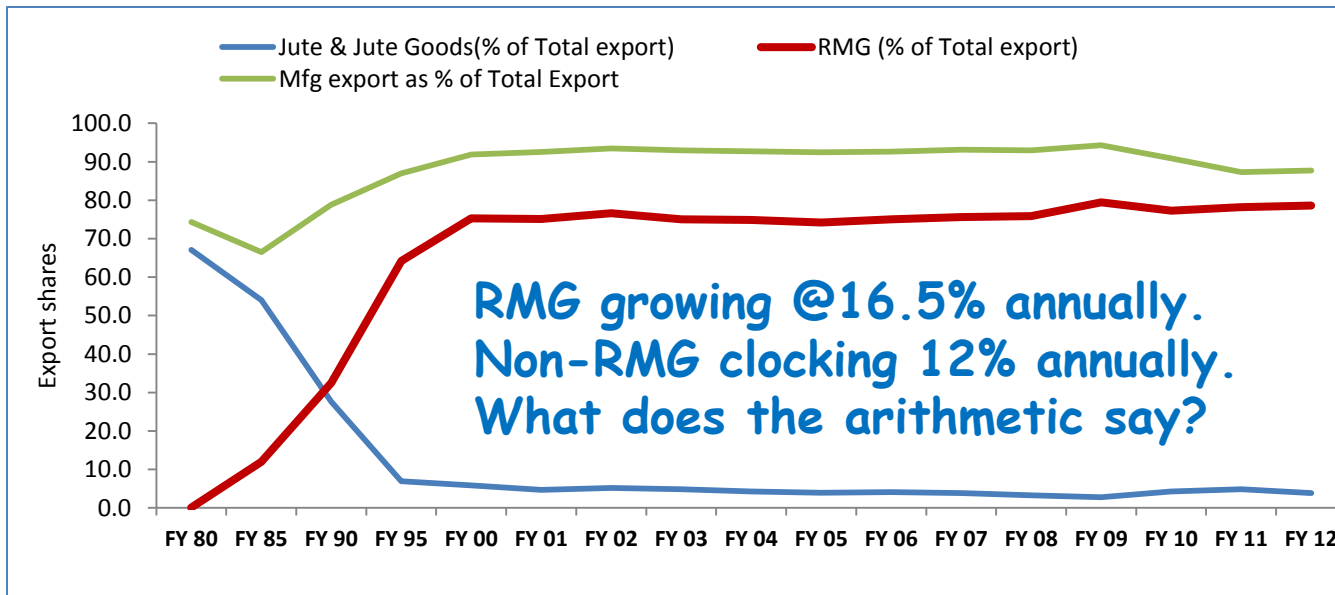
Objective:

- To look at the **major constraints to export diversification** in Bangladesh and provide some **relevant policy options** to address those constraints.
- The paper draws on relevant literature and for the first time **provides a framework for analysis** and pulls together the various concepts of diversification and the constraints to diversification.

EXPORT CONCENTRATION AND VULNERABILITY IN BANGLADESH

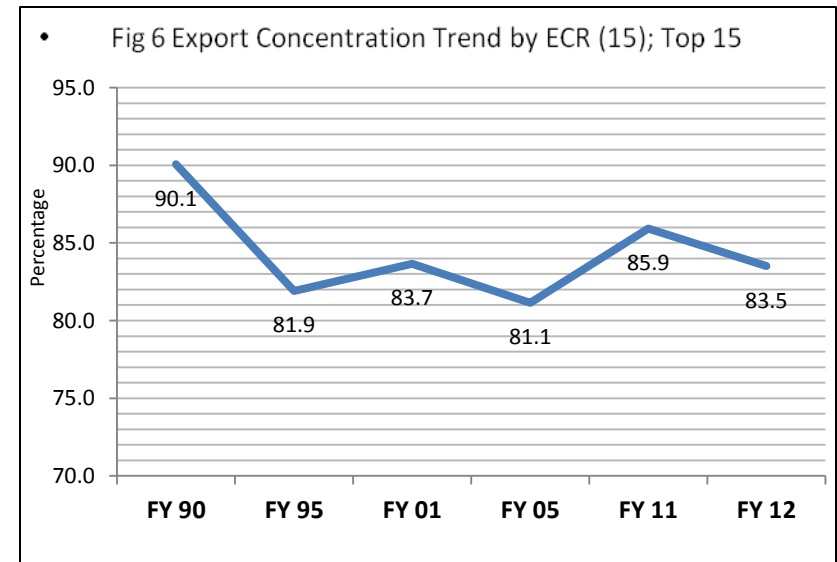
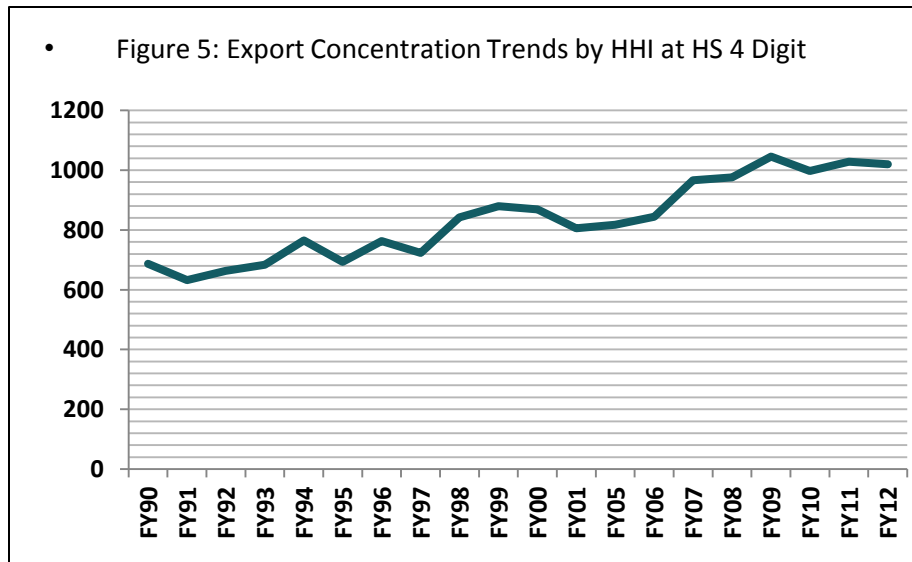
- Before RMG, **jute and jute goods** dominated the export sector making up 70 percent of exports in 1981 (Figure 3).
- Bangladesh experienced **vertical diversification** of its exports (from primary to manufactures). By 2000, it became a unique LDC exporting predominantly manufactures (over 90%).
- Bangladesh is a **small open economy in international trade**, a price taker in the world market, for its exports as well as imports. It faces the consequence of adverse movements in its terms of trade (TOT), stemming from exogenous price shocks in its imports or exports.

Fig 3: Export Concentration Trends (F Y 1980-2012)



EXPORT CONCENTRATION AND VULNERABILITY IN BANGLADESH

- What is disconcerting is that when one studies export concentration trend in Bangladesh exports for the past two decades, there is no discernible improvement in the situation. There is a substantial increase in the concentration index measured by HHI (Figure 5), although ECR suggests a slight decline (Figure 6).



LESSONS FROM INTERNATIONAL EXPERIENCE

TWO TYPES of DIVERSIFICATION NOTED

- **Thailand** -- a successful example of export diversification -- adopted a dual strategy (a) to **upgrade natural resource-based industries** (such as agricultural and fish products) and (b) to **encourage labour-intensive manufactured exports**, most notably clothing and electronics.

- **All East Asian economies along with China** benefited from the rise in regional economic integration through the **development of cross-country production networks** -- vertical integration of production chains -- as multinational companies (MNC) sought lower-cost manufacturing facilities beyond national boundaries and capitalized on supportive local policy initiatives. Result? **Diversification into intermediate goods.**

TYPOLOGY OF EXPORT DIVERSIFICATION

- Product diversification.
- Geographical diversification.
- Intermediate goods diversification
- Vertical diversification.
- Quality diversification.
- Goods to Services diversification.

CONSTRAINTS TO TRADE DIVERSIFICATION IN BANGLADESH

Incentive system:

- **Exchange rate management**: RMG exports are partly shielded from exchange rate movements because of the special import credit system (back-to-back LC) that covers import costs from export proceeds. Non-RMG exports could be hurt by appreciation of REER. ER management has to be right for them.
- **Trade Policy**: For export diversification to happen, anti-export bias of the tariff regime must be eliminated for non-RMG exports to pick up steam.

Export competitiveness: 4 dimensions: cost, quality, time, reliability. RMG is ahead of the others in all these factors.

CONSTRAINTS TO TRADE DIVERSIFICATION IN BANGLADESH

Enabling environment for trade: Globally, two commonly used indicators are the WEF’s Enabling Trade Index (ETI) and WB’s Trade Logistics Performance Index (LPI). Bangladesh does poorly on most of the indicators included in this index, but scores especially low on transport and power which have emerged as serious constraints to manufacturing sector.

Table: 5 The Enabling Trade Index 2012 Bangladesh

	Rank (out of 132 countries)
BORDER ADMINISTRATION	100
Efficiency of customs administration	103
Efficiency of import-export procedures	86
Transparency of border administration	115
TRANSPORT AND COMMUNICATIONS INFRASTRUCTURE	123
Availability and quality of transport infrastructure	126
Availability and quality of transport services	104
Availability and use of ICTs	110
Market access	65
Physical security	96

Table:6 Trade Logistics Performance (LPI 2010)

Country	LPI ranking	Customs	Infra-structure	Logistic competence
Germany	1	4.00	4.34	4.14
Singapore	2	4.02	4.22	4.12
China	27	3.16	3.54	3.49
Thailand	35	3.02	3.16	3.16
India	47	2.70	2.91	3.16
Vietnam	53	2.68	2.56	2.89
Indonesia	75	2.43	2.54	2.47
Bangladesh	79	2.33	2.49	2.44
Pakistan	110	2.05	2.08	2.28

CONSTRAINTS TO TRADE DIVERSIFICATION IN BANGLADESH

- **Ease of Doing Business** . In terms of specific regulatory constraints in doing business, investors in Bangladesh face a particularly difficult challenge in **getting electricity; in registering property; and in enforcing contracts**. Bangladesh, however, does a good job in protecting investors.

- **Skills**: Bangladesh is a beneficiary of the demographic dividend. But skills mismatch is serious and constraints productivity.

- **Lack of FDI**. Poor FDI inflows are a constraint to export diversification.



Tariff Regime is unfriendly to exports

- The trade policy stance that is suitable for globally competitive export production must be characterized by low and uniform tariffs and a seamless export-import regime.
- **Tariff regime is unfriendly to exports**....creates anti-export bias of incentives, particularly for non-RMG production.

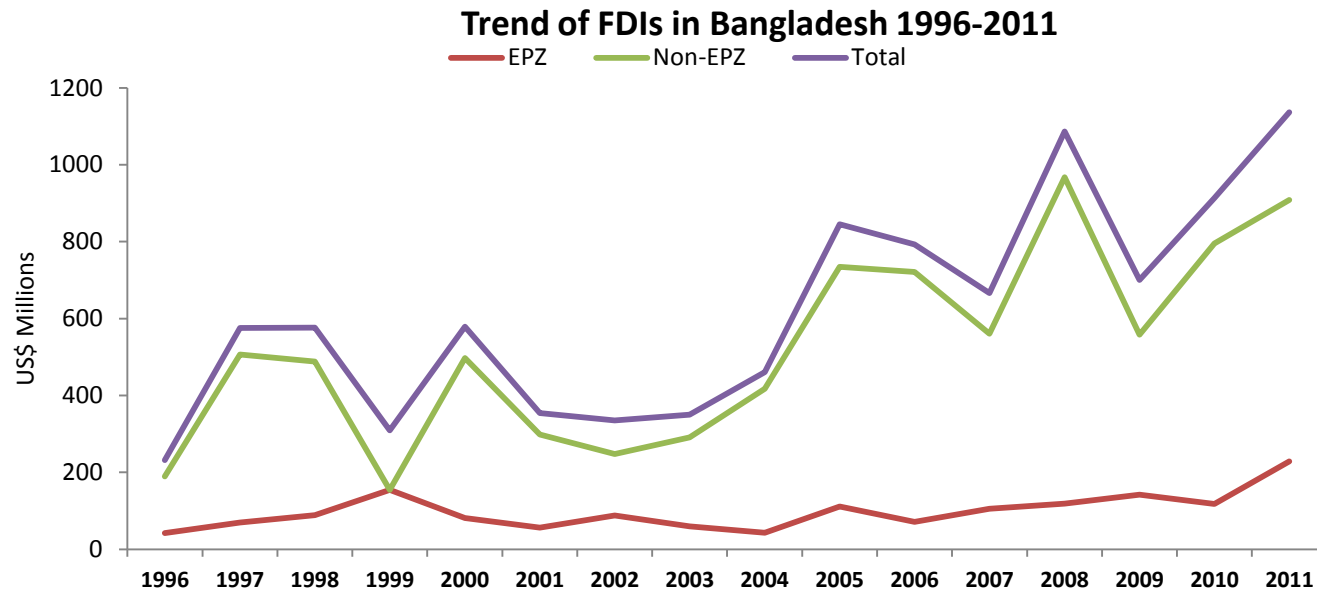
Table 1: Tariff Trends FY 01-14

	FY 01	FY 05	FY 10	FY 11	FY 12	FY 13	FY 14
Avg. CD (un-weighted)	21.1	16.3	13.7	13.6	13.6	13.9	13.2
Avg. para-tariffs	7.1	10.2	10.2	10.2	12.9	15.1	14.1
Avg. Nominal Protection	28.2	26.5	23.9	23.8	26.5	28.9	27.3
Top CD rate	37.5	25.0	25.0	25.0	25.0	25.0	25.0
Top NPR*	59.0	60.0	79.0	79	88.0	117.0	108.0

(*) excludes tariffs on cars, alcoholic beverages, and cigarettes

ROLE OF FOREIGN DIRECT INVESTMENT (FDI) IN EXPORT DIVERSIFICATION

The performance remained lack luster until 2004, around \$400- 500 million. FDI inflows increased after this to the recent \$1 billion mark, but unstable. Much of the FDI's were mainly outside the export-processing zone (EP Zs). Recent spurt in Telecom. This is in sharp contrast with the experience in China where much of the FDI's went into the free trade zones. Vietnam and Indonesia each received \$11-12 billion in 2010.



EXPLOITING EMERGING TRADE PATTERNS FOR EXPORT DIVERSIFICATION

- In last 2 decades, **trade in intermediate goods** formed the most dynamic sector of international trade, changing the character of export-led growth.
- Made possible by **fragmentation of production processes across countries** (in line with their comparative advantage), with assembly operations moving to lower wage economies while higher-value added components headed to more developed economies.
- Fragmentation of production processes gave rise to **global value chains (GVCs)** creating opportunities for intra-industry trade globally & also between economies within a region.

EXPLOITING EMERGING TRADE PATTERNS FOR EXPORT DIVERSIFICATION

(CONTD)

- For Bangladesh to exploit GVCs to produce parts and components of final products, FDI and joint ventures are absolutely essential:
- Trade infrastructure needs upgrading:
 - Efficient Containerization
 - Efficient Land Ports
 - Automation (with ICT)
 - Export Processing Zones or Special Economic Zones
- Other issues that also merit attention are: corporate tax regime with appropriate incentives, import liberalization, strong intellectual property rights, rule of law, and a developed financial system, including modernization of Foreign Exchange Regulation Act (FERA) 1947.

EXPLOITING EMERGING TRADE PATTERNS FOR EXPORT DIVERSIFICATION (CONTD)

- Furthermore, in order to promote integration into *GVC* (and attract FDI with this objective), the following steps would be essential:
 - Eliminating anti-export, and anti-intermediate goods bias of the incentive regime.
 - A liberalized investment policy regime, which offers scope for international firms to have unlimited stake in the local firm.
 - Joint ventures with established actors within the *GVC* will allow the diffusion of technology, which ultimately boost the export potential of the local firm.
 - Availability of appropriately skilled labor at a competitive price, which motivates established foreign actors to participate in joint ventures with local players.

POLICY AND INSTITUTIONS FOR EXPORT DIVERSIFICATION

The following policy and institutional mechanisms need to be put in place if export diversification is to be attained within a reasonable period.

Trade policy. Tariff structure and anti-export bias.

Efficiency of customs administration. All exports must be brought within the fold of priority clearance mechanism that is equipped with state of the art hardware and software.

Efficiency of import-export procedures. Modernization of import-export clearance by using better technology and IT softwares complements export diversification.

Transparency and efficiency of behind-the-border services. Industrial and investment policies need to be brought in line with those of trading partners and comparators for long term export sector sustainability. Furthermore, a friendly investment climate should foster FDI into GVCs linking Bangladesh with transnational companies elsewhere.

POLICY AND INSTITUTIONS FOR EXPORT DIVERSIFICATION

Availability and quality of **transport infrastructure** and services. Improving trade logistics will definitely enhance competitiveness of exports. First, **land and sea ports** must be equipped with state of the art facilities – container depots, gantry cranes, IT-enabled port clearance services, etc. -- for rapid clearance of import-export cargo.

Availability and **use of IT**- Export competitiveness and diversification demands state of the art IT equipment and software at the ports but also inland for handling activities.

Regulatory environment- Export success and diversification requires moving into new markets with new products and is facilitated by a friendly regulatory environment, supported by ease of doing business.

Upgrading skills -Public and private sector partnership to provide specialized and on the job training can play a major role in upgrading skills.

Thank You