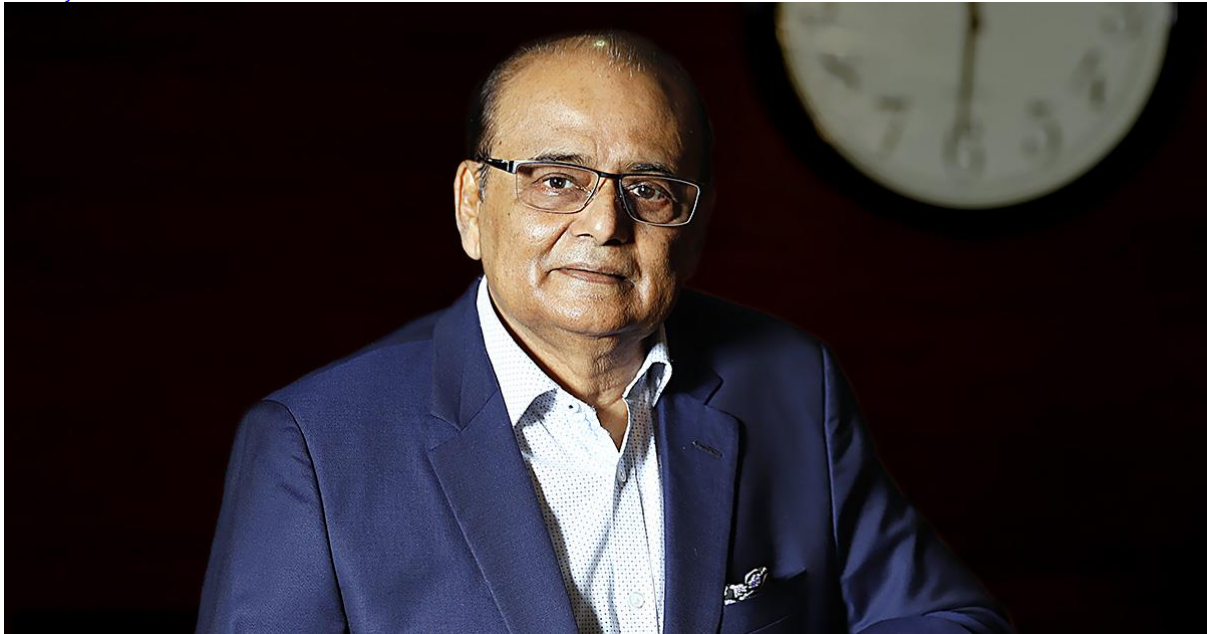


## Dr. Zaidi Sattar, Chairman, Policy Research Institute

by Marjiya Baktyer Ahmed

January 12, 2020



### INTERVIEWS

In a conversation with Marjiya Baktyer Ahmed, Dr. Zaidi Sattar expounds on the importance of trade openness, and the crucial need to properly equip our demographic dividend to reap the benefits of the ongoing industrial revolution.

***Bangladesh economy has experienced growth acceleration for the past three decades. Was the change in its trade orientation during the 1990s that sparked the uptick in GDP growth and poverty reduction?***

To answer and clarify the context we need to go back a little bit, before the 1990s. We had spent two decades in which we just followed economic policies, and particularly policies of trade and industrialization that were essentially legacies of the past. We didn't really get into any new approach to industrial development or to a new approach to trade orientation. In the 1990s we made the course correction that was essential to bring dynamism into the economy. The change in policy direction was inspired by the new paradigm of growth coming out of East Asian countries. They were called the East Asian Tigers – Korea, Taiwan, Hong Kong, Singapore. – These countries showed the world that there was a new paradigm of growth — export-led growth which is dependent on trade openness and integration with the world economy. The new paradigm showed that open trade, exporting and exploiting the world market

through exports allows faster growth and also reduces poverty much faster than the old paradigm of import-substituting industrialization where you tried to produce things at home, by raising barriers to import competition. At the end of the day, you do have some industries, but they are not competitive in the world market.

India, for instance, realized that, but it took India 50 years to reach that conclusion. Thankfully Bangladesh took about 20 years to realize the folly of an inward-looking closed economy strategy. In the 1990's Bangladesh changed its trade orientation. Not just in trade orientation, but also in the domestic economy, Bangladesh went in for deregulation, privatization, trade openness, trade liberalization, import liberalization, exchange rate flexibility, and so on. All of these were part of the changing direction of economic strategy. That created a spurt in economic growth. In the previous 20 years, there were three 5-year plans which all targeted 5% GDP growth but never got anywhere close. For the first time, Bangladesh achieved 5% growth on average in the 90's decade. The growth rate kept going up 1 % every decade. In fact, in the last 10 years, it has been going up 1 % every five years.

One can ask what is it that was different during this period. The one big difference is we followed the trade orientation of the East Asian economies relying on the export push and export promotion through which we achieved success, not necessarily in so many sectors, but in one sector which is the Readymade Garment sector. We did really well in that one sector. It's a textbook case of where Bangladesh competitive advantage lies because in RMG the final process of assembly, of fabricating the apparel, is a labour-intensive process and Bangladesh took advantage of its cheap unskilled and low skilled labour force and we know the result.

I would argue strongly that it was this radical change in the direction of Bangladesh's economic policy and of course moving towards a trade-oriented, outward-oriented policy that gave this accelerated growth. That was one critical factor. Of course, it had to come with all the other things like macroeconomic stability, along with other strategies for human development and poverty reduction. Alongside the high growth during these three decades, there was a very high rate of poverty reduction; as a result, we are at a stage now that our poverty level is down to about 21% of the population, with extreme poverty down to about 12-13%. This growth is not just growth in wealth of the economy, but it also has had a substantial impact on reducing poverty.

***Alongside the high growth during these three decades, there was a very high rate of poverty reduction; as a result we are at a stage now that our poverty level is down to about 21% of the population, with extreme poverty down to about 12-13%. This growth is not just growth in wealth of the economy, but it also has had a substantial impact on reducing poverty.***

***We rely on our RMG, and it has contributed significantly to our GDP growth. But haven't we reached a peak of RMG, and isn't it time to diversify our products. Which is the next sector poised to become as vastly significant as our RMG sectors?***

Just about everybody in town has been asking this question. In the first half of the 1990s when RMG exports became the predominant export of Bangladesh, it superseded the earlier export dominance of jute and jute goods. We used to have jute as our leading export. Everybody knows we need to diversify our export basket, but why are we unable to do it? Why is it that RMG exports continue to grow and grow faster than the non-RMG exports? Is it that we don't have any other product to export? That is illogical. If we could succeed in RMG export, it is because we exploited our comparative advantage in low skilled, unskilled labor which is cheap in Bangladesh, though productivity is not that great. Is there no other labour intensive product in which we also have a comparative advantage? There are numerous items, and the fact of the matter is Bangladesh has been exporting large numbers of products alongside RMG garments. If you look at the export basket of the fiscal year 2018, we exported 1392 non-garment products. That's a lot, but only 292 of them were higher than 1 million dollars. That is about 97% of the 6 billion dollars of non-garment exports that we did in 2018. The remaining 1100 export products, — I am talking HS code at 6-digit level. At HS-6 digit level is how you identify each traded product. The 1100 products I mentioned were really small, less than 1 million dollars. What is worse is that we have been exporting 1200, 1300 products since 2000 or even before. The number of export products is huge, and some of the products may be similar but they are not the same. RMG is not one product, it covers 215 products that we have exported.

People will say our infrastructure is bad, our transport is bad and ports are not functioning, there is a power shortage, customs is incompetent. All of that might be true, but RMG is being exported from within this environment, so why can't other products do it? Everybody will tell you that they are perhaps not competitive. We have researched the competitiveness aspect and found that we are competitive in about 40% of those export products that are non-garment. We are competitive with 30 other countries, who also export to the same destinations. Competitiveness is measured by some standard measure of competitiveness that economists use. If we are competitive, then how come we are not increasing the exports of these non-garment products. Year after year you find RMG export growing faster than non-garment products. If RMG exports are growing faster than non-garments, what will happen to the export basket? It will get more and more concentrated on RMG. Right now we have 84% of our exports made up of RMG. It is not going to fall unless the non-garment exports really grow much faster. In the last 10 years, we have seen the concentration

going up from 75% to 84%.

In my view and after much research in this area, I have come to the conclusion that it's not the competitiveness issue, it's not the infrastructure alone. Those are problems for both exports and import substitute industries we have here. The problem that prevents exporters from really trying to become proactive and expanding their exports in the non-garment sector is the policy environment. The policy environment that creates a negative incentive for exporting, a policy that overwhelmingly favours import-substituting production for sale in the domestic market. This happens because of high tariffs. You have high tariffs to protect the domestic industries and restrict import and import competition. The non-garment sector is not a 100% export-oriented sector whereas RMG is 100% export-oriented – they can't sell in the domestic market even if they wanted to. They are meant for exports, but others like footwear, leather goods, plastic industry, agro-processing industry, ceramic industry – they export and also sell in the domestic market. When they sell in the domestic market, their profit margins are at least 2-3 times the profit margins from exports because in exports margins are very thin. If you get 5% or 7% it's great, but in the domestic market you have to do 20% or 25%, otherwise, you won't be able to pay the loans that you take out at 12-15% interest. The fact of the matter is, it is much more profitable to sell in the domestic market because you need much less effort to get high returns.

Bottom line: (a) Gaining a foothold in the export market is not easy (b) margins are very thin. And then in the domestic market, you have protective tariffs of 85% or 100% which artificially raises the price of the product in the domestic market. Bangladesh middle class is growing. It's growing, and it's buying, apart from food and shelter you are buying so many other consumer goods. All of these consumer goods are priced at 50-100% above international prices, that's what our consumers are paying. It's a question of incentives – why would they produce for exports if the domestic market is so profitable? But what we are missing out is that our economy is growing because of our exports. Bangladesh economy cannot grow more than 8% without additional export success. No country in history has grown at 8%, 9% or 10%, without really integrating with the world market, because the world market is huge. Once you get a foothold there the world market opens up for you. The domestic market has a scale problem. We have a 300 billion dollar economy, but the world market is 80 trillion dollars. India is ten times Bangladesh's economy, China is 30 times our economy and the world market is several hundred times bigger. So once you are able to get a foothold in that larger market, you can create jobs here. You don't export just for foreign exchange, you export to create jobs. RMG has shown us that you create a huge number of jobs through exports and then it's not just the direct jobs, there are indirect jobs like those

who live on the profit and income and salaries that come from the RMG sector. The impact is greater than the 35 billion dollars' worth of RMG exports that we do. It is a lesson on what export does. We talked about this growth acceleration which came from our trade orientation and export success. If that is not maintained, and we cannot continue to be an export success then this growth could slow down. That is historical evidence.

***It is time for the World Trade Organization to go through constructive reforms. To improve its performance to make an inclusive multilateral system that benefits all of us, not necessarily equally. If there are some losers, then they will have to be compensated. There has to be a system of compensation to bring people who are not benefitting from the system and how to bring them to the fold.***

***Has the paradigm of export-led growth reached a dead end in light of the backlash against globalization seen across the developed world giving rise to economic nationalism, protectionism, and unilateralism?***

Anybody who is looking at the current state of the global economy would say globalization has run its course, and you have these developed economies of Europe and North America that are suddenly realizing that open trade meant they are not necessarily going to benefit or everybody in their country is not benefitting. There are pockets in every developed country with people who lost out because the competition from low-cost countries like China, India and even Bangladesh is too severe, and we lost jobs. That's a political backlash, and there has been a political backlash that gave rise to what we call economic nationalism. They want to limit their market and it is the same thing as protectionism, you want to protect your market; another word for it is unilateralism instead of multilateralism. Globalization is about multilateralism, and we see this tendency to backtrack from globalization by those same countries who are the protagonists, who are the first promoters of globalization. Thankfully, Bangladesh is one country that is a significant beneficiary of globalization and multilateralism so we should, if anything, for the future stand by this particular paradigm of trade openness, of globalization and harness the opportunities that are created by this particular paradigm of export-led growth. I would qualify the statement by saying it's not just export-led growth but trade-led growth. Because export also involves import. Readymade garment sector did not grow up on just exporting and making things from domestic resources, it was a classic case of integrating with the global value chain. We started by importing fabrics, yarn and accessories and making them into apparels. Today we have much better backward linkage. We started by importing and that is essential for export success (China, for instance, is the number one exporter of the world but it is also the number two importer of the world). The world economic order is such that there is a lot of cross-border integration in production; it doesn't mean you produce everything from in-house; you import

things, you assemble and you export and if you have a seamless trade regime that is the best for producers and it is also good for consumers because that way you produce things cheaply, and you make products available to consumers at cheaper prices. So, the point here is that I for one, would like to believe that this is a sort of temporary phenomena, the backlash against globalization. The other thing is multilateralism, which is symbolized by the World Trade Organization, which sets the rules of trade, has come under criticism due partly to its ineffectiveness in many areas. But it does not mean you throw the baby out with the bathwater. What that system needs is reform. It is time for the World Trade Organization to go through constructive reforms. To improve its performance to make an inclusive multilateral system that benefits all of us, not necessarily equally. If there are some losers, then they will have to be compensated. There has to be a system of compensation to bring people who are not benefitting from the system and how to bring them to the fold. So I would not write an obituary on the multilateral system as yet, but as far as Bangladesh is concerned, we should support and uphold the system so it lasts longer, with reforms that are necessary.

***If you look at the export basket of fiscal year 2018, we exported 1392 non-garment products. That's a lot, but only 292 of them were higher than 1 million dollars. That is about 97% of the 6 billion dollars of non garment exports that we did in 2018.***

***Bangladesh's working-age population (15-64) has risen from 47% in 1974 to 66% in 2018 symbolizing the demographic dividend. What should Bangladesh do to convert this demographic dividend into a high growth opportunity?***

Bangladesh is a young country, in terms of its population. Half the population is under 30 years of age. The working population, which is from the age group of 15-64 has been growing over the past several years. More importantly, the youth population which is from the ages 15-29 has been growing also. So the working-age population, as well as the youth population, has been a bonanza for Bangladesh and any country that has a growing working population is likely to be able to grow faster. Because in order to grow faster, you need a labour force that is growing, unlike Japan or some other developed country which has a larger ageing population and the labour force is contracting. With labour force contracting, I agree that there is some productivity increase that they always get because of technological advancement, but that productivity is very limited. Unless labour force grows fast enough you can't get the benefit of growth acceleration. Japan has suffered from zero growth for two decades at a stretch. Bangladesh is a young country in that respect. Bangladesh's working-age population as well as the youth population is rising. That is what we call and what has been described as the demographic dividend. But it is not enough, you have to make sure that they get to work and also that they are productive.

So there are these challenges to create jobs, to make them more skilled, more productive, and in step with the technological revolution which we now call the Fourth Industrial Revolution. In order to do all of that, we have to make sure that jobs are being created. And here is the link between the trade orientation we talked about, the strategy for getting growth acceleration. If you have this kind of open trade orientation, greater integration with the world economy, then you've integrated with the larger market in the world and if your industrialization is linked with that wider market, then you are going to be able to create the jobs that you need. The domestic market is limited in scale, no matter how fast the economy grows. If you are relying entirely on the domestic market, the historical record is, you cannot grow fast enough. In order to create the jobs, for exploiting the demographic dividend, you need to grow much faster, you need to integrate with the vast global marketplace so that it creates more jobs. In order to convert the demographic dividend into a growth opportunity, you have to make sure you have got jobs for the young labour force; if you don't have jobs for them then the demographic dividend becomes a demographic burden. Creating job opportunities depends on the growth strategy you adopt. And I would strongly argue that our growth strategy should be outward-oriented rather than inward-oriented. Because if you fail to do that then you cannot exploit the demographic dividend. The demographic dividend doesn't last very long. The increasing share of the working-age population, the increasing share of the youth population, that increase would start falling after a certain number of years. If we delay in exploiting this growing share of working-age population now, by giving them jobs and skills, then we will end up with a larger population which is not skilled and don't have a job.

***In order to create the jobs, for exploiting the demographic dividend, you need to grow much faster, you need to integrate with the vast global marketplace so that it creates more jobs. In order to convert the demographic dividend into growth opportunity, you have to make sure you have got jobs for the young labor force; if you don't have jobs for them then the demographic dividend becomes a demographic burden.***

***What skills do you think are the most relevant right now?***  
Two things; we have to continue to industrialize; to industrialize faster, you got to look outwards, you have got to link up with the world economy. Then we have this whole connectivity issue coming from ICT, the technological transformation that is taking place. For this, the youth population is much better equipped than the older generation. So we have to make sure that we have the right scope and opening for greater exploitation and utilization of ICT opportunities that are being created. The younger generation has had greater access to education than the older counterparts, but there is a question of the quality of that education. The quality is not that great, everybody would agree, we still have created a pool of savvy internet-based, computer-based professionals that can

still give us an extra push to improve our livelihoods and the state of our economy. So we have to be mindful to not lose the opportunity. Right now is the time when we have to create those opportunities and make the best use of our younger generation in handling the ICT revolution that is ongoing.

Bangladesh has shown that it can do things, and Bangladesh population has shown that we can no longer be left out and considered to be a basket case anymore, This is not the time to be complacent, we have challenges, particularly the challenges coming out of Bangladesh's impending graduation out of LDC status. We become a developing country in 2024 by UN classification. We are already a lower-middle-income country by the World Bank classification, so we are moving towards Upper Middle Income Country (UMIC) status but that will take some more time. Once we graduate out of LDC status, we have more challenges coming our way, we will have to observe various standards and rules of international trade and at the moment we are not very up to date on the rules. Since we said we are a significant beneficiary of the multilateral system, we have got to play by the rules a bit better than we did in the past.

<https://ibtbd.net/dr-zaidi-sattar-chairman-policy-research-institute/>