

Chapter 1: Introduction

1.1 Background

The analysis of the role of international trade in economic growth has attracted a considerable attention in development economics. Precisely, how trades affect economic growth has been much debated. Analysts generally agree that trade plays a central role in economic growth, serving as a mean of specialisation in sectors with comparative advantage and of acquiring better technology. In general economic growth occurs mainly in three ways. It may take place,

- (i) through an increase in the available factors of production, i.e. addition to the supply of capital, labour and natural resources;
- (ii) by achieving a more efficient allocation of the factors of production; and
- (iii) by the technological advancement.

International trade in goods and factors of production may affect economic growth of a country through these channels. When a country's exportables enter the world market, its economy expands by appropriating the gains from trade. Production of exportables requires specialisation which in turn leads to a fine division of labour and more efficient allocation of resources. It is widely believed that trade yields dynamic benefits of dissemination of technical know-how, transmission of ideas, skills, managerial talent and entrepreneurship in addition to the direct benefit from specialisation. Analytically, the indirect benefits represent a trade induced shift in the production possibility frontier (Haberler, 1959). The foreign trade-link acts as a conduit whereby the impulses of economic activity can be transmitted from one country to another (Greenaway and Milner 1987).

As foreign sales continue to multiply, the prosperity of the export sector spreads to the rest of the economy. However, those linkage effects of the exports directly depend on the share of manufacturing in total exports. Hence in the world market, less developed countries (LDCs) should promote those manufacturing industries in which they have comparative advantage.

Bangladesh has a long history of colonial domination. Even during Pakistan period (1947-1971), politically powerful western region dominated over the eastern (now Bangladesh). It used to export primary commodities, and trade showed a persistent deficit with West-Pakistan. However East Pakistan enjoyed a surplus with the rest of

the world. West Pakistan used the inter provisional trade surplus to finance the international trade deficit of Pakistan. This practice greatly weakened East Pakistan's development potential (Sobhan 1982). Bangladesh had virtually no foreign currency reserve while departing but had huge demand for foreign currency to rebuild its economy after the liberation war of 1971.

In the early years of independence, domestic resource mobilisation was the main strategy for development. This was justified on two grounds. First, the country would not depend at the mercy of external event, which is beyond her control. Second, the country would be less vulnerable to political manipulations by major donors. In an increasingly interdependent world, international division of labour and specialisation are inevitable, and the external dependence is the price that any international division of labour extracts (Cairncross 1962).

But from the stand point of growth and industrialisation, the trade policy generates considerable controversy. Protectionist theories infact became dominant and for decades the majority of the countries implemented import substituting industrialisation strategy. Export pessimism had surfaced in the immediate post World-War II and was popular until 1970s due to the reasons of deteriorating terms of trade, oil shocks, global recession and rising protectionist threat. Economists argued that because of very limited backward, forward and final demand linkages between the export sector and the domestic economy, the export sector rapidly developed without any substantial benefit to other sectors. Thus the export sector turned out to be an enclave of growth and development. The orthodox economists tend to attribute this phenomenon on the institutional and structural rigidities in LDCs and emphasise on the favourable contribution of trade. The critics argued that trade has always been and will continue to be one of the main determinants of the unequal growth of productive capacities in different countries. The LDCs, endowed with abundant unskilled labour specialise in products that intensively utilised unskilled labour. They often find themselves locked into a stagnant situation that perpetuates their comparative advantages in less productive activities. This in turn will inhibit the domestic growth of required capital, entrepreneurship, and technical skills (Todaro 1989).

An outward oriented development strategy has become a key consideration for achieving a high rate of growth in LDCs since early 1980s. The miraculous ability of NIEs to penetrate into export markets and their spectacular performances have influenced the developing nations towards the export led growth strategy. The protectionists' view adopted by most developing countries during 1950s, 1960s and 1970s provided, in many cases somewhat disappointing result. So in the 1980s, many development economists, following the lead of the World Bank and International Monetary Fund (IMF), began to recommend a

development strategy towards reduction of both domestic and foreign trade barriers and opening of the trade sector to foreign competition.

Bangladesh, one of the least developed countries of the world is undergoing transformation towards export led growth and more liberalised market oriented economy response to the worldwide openness view of 1990s. Bangladesh is a densely populated country with per capita income of U\$220 in 1992 (World Bank 1994). The density of population is over 800 per square kilometre that is about three times that of India and seven times that of China. Agriculture, industry and service-sector contributed 37, 16, and 47 percent of GDP respectively in 1991-92 as against 50, 14 and 37 percent respectively in 1972-73 at constant prices of 1984-85 (Bangladesh Bureau of Statistics 1993). The development of industrial sector has been insignificant.

The external trade sector of Bangladesh has been characterised by chronic and severe balance of payment deficits since its inception in December 1971. Being a small open economy, Bangladesh is a price taker and exposed to external demand shocks. The external sector is confronted with problems of inelastic demand for exportable and unstable export earnings. Bangladesh has inherited an export structure with an overwhelming dependence on few traditional products such as raw jute, jute goods, tea, leather, hides and skins and fish, which constituted 96 percent of total export in 1973-74. The export sector of Bangladesh has undergone a significant change during 1980s. These changes represent a shift towards labour intensive manufacturing from primary products and a shift towards non-traditional commodities from traditional ones. After independence (1972-73) primary export in total merchandise export was 43 percent which declined to 23 percent in 1989-90. During the period between 1981-82 to 1991-92 the share of traditional exports (raw jute, jute goods, loose tea etc,) declined from 82.8 percent to 36.7 percent in constant dollar prices of 1980-81 (Rahman 1992). However, absence of backward linkages, poor infrastructures, non-price factors and technological backwardness kept domestic value added low. To achieve higher economic growth rate through an improvement of export performance the country needs to strengthen its competitiveness, improve the quality of exports, explore new markets and diversify commodities.

An empirical analysis of the effectiveness of export-oriented growth strategy is the main thrust area of this study. In addition, we attempt to investigate the structure of export and its possible impacts on growth.

1.2 The Nature of the Problem

Beset with serious limitation of market size, but abundant labour force, it is widely argued that Bangladesh should expand its market size by specialising in labour-intensive export industries. Historical data and recent empirical studies suggest that the current account deficit problem in Bangladesh is a structural, rather than a short-run cyclical problem. Hence, a persistent improvement in export performance is required for a favourable change in trade balance. Like many developing countries, Bangladesh pursued an 'import substitution' strategy in the last three decades without any significant success in economic growth and employment generation. The recent success of Bangladesh in labour intensive exportable indicates that export led growth has the potential to make significant contribution in employment generation as well as improving merchandise trade deficit. As the labour costs in newly industrialising countries (NICs) and some ASEAN countries (Malaysia, Thailand) are growing rapidly, they are likely to lose the competitive edge in labour intensive industries in the near future. Hence, the labour intensive export industries in Bangladesh is likely to gain competitiveness in the world market.

Over the past decade or so, there have been waves of changes in terms of the trend and composition of exports. The 'export pessimism syndrome' seems to have been replaced by 'export optimism' and Bangladesh has adopted the strategy of export led growth. But the merchandise export share in Bangladesh still ranks nearly at the bottom of the South Asian league table. The heavy weight garment sector (54 % share in 1992) is heavily dependent on imported inputs and more vulnerable to changes in the quota system in the OECD countries and its possible demise under GATT practices. So whether Bangladesh should rely heavily on the export sector or on the import competing sector is an important researchable area.

1.3 Objectives

The study is designed to achieve the following objectives.

- (i) To determine the effect of export performance on economic growth. An empirical investigation of the linkage between export growth and economic growth will be conducted using an extended neoclassical growth model;
- (ii) To investigate the structure of export and its relationship with economic growth. A comprehensive analysis of the export sector including its trend and structure will be presented;

- (iii) To identify the determinants of export performance in Bangladesh and assess the effectiveness of government policies on export performance;
- (iv) To derive macro-economic policy implications in relation to export promotion and economic growth.

1.4 Significance of the study

An econometric analysis of the impact of export expansion on economic growth is essential in determining the effectiveness of an outward-oriented development strategy. In addition, this study conducts a preliminary investigation of the structure and determinants of Bangladesh export. Though some studies have been conducted in this area, no well structured empirical model is used to determine the effect of exports on GDP growth of Bangladesh. This study attempts to fill the gap in the literature by employing an augmented neoclassical growth model.

1.5 Hypotheses

Based on a two sector neoclassical model the study hypothesise that GDP growth depends on the investment-GDP ratio, the growth rate of labour force and the weighted growth rate of export (share of export in GDP multiplied by the export growth rate) . Alternative versions of this basic model were estimated to address a wide range of empirical issues. The following hypotheses will be empirically tested in this study:

- (i) An increase in the investment-GDP ratio positively affects the GDP growth rate;
- (ii) The labour force growth rate positively affects the GDP growth rate;
- (iii) The export growth significantly increases the GDP growth;
- (iv) The marginal productivity of capital in a normal year will be greater than that of an abnormal year. Abnormal years include the periods of liberation war, political turmoil and natural calamities.
- (v) As the trend variable in the GDP growth equation measures the net marginal impact of state of technology, skill composition of labour force, and malpractices and rent-seeking activities, the sign of the coefficient of the trend variable is a priori indeterminate.

If the testing of hypotheses suggests no significant effect of export growth on GDP growth, the current export led growth strategy needs to be reviewed. Depending on the marginal productivity gap between export and non-export sector factor and the extent of potential positive externality effect of the export sector, the policy makers may decide whether emphasis should be put on external sector or domestic sector development for achieving high rate of growth.

1.6 Organisation of the Dissertation

The thesis is divided into seven chapters. Chapter two contains a review of previous studies relating to export performance and economic growth. Chapter three includes a description of the nature of the Bangladesh economy including its salient feature and macro economic performance. Export performance measured by the trend, structure, composition and direction of exports of Bangladesh is discussed in chapter four. This chapter also includes the graphical representation of the factors determining the growth rate of gross domestic product. The analytical framework and empirical model are discussed in chapter five. Chapter six presents the empirical results with a detailed analysis. The final chapter consists of summary, conclusion, policy implications, and directions for future research.

2: Literature Review

2.1 Introduction

The less developed countries of the world include approximately three quarters of the world population but account for only about one-quarter of world's income. The problem of making these poor countries richer is complex but vital and there is no single solution for every case. Consensus for expansion of the external sector is gaining importance in recent years to enhance growth and the export-oriented growth strategy has been a recurring issue in the history of development literature.

It has been long perceived that nations benefit by trading. The role of international trade in the pursuit of domestic economic goal gained prominence in the last three decades. Trade across national borders extends economies of scale, specialisation and increases competitiveness, which in turn lower cost of production and hence prices, and ensures efficient resource allocation (Hughes 1994). The policy of outward development strategy is gaining its ground in most developing countries in the era of globalization.

Based on the prediction of Prebisch (1950), Singer (1950) and Nurkes (1961) that demands for primary exports of developing countries are inelastic, export pessimism had surfaced in the immediate post-World War II period. Another episode of export pessimism appeared in the post 1973 period which was induced by various oil shocks and global recession and rising protectionist threat. It was also argued that while export promotion may work better under steady state condition, it exposes the domestic economy to downside risks in the world economy, and make the economy vulnerable to international instability.

But now many intellectual and academic arguments convincingly refuted the hypothesis of the export pessimism. The economic miracles of the post-war era Japan, Germany and the four tigers of East Asia have been the subject of much study and the analysts accept that the policy of export development is the root cause of their rapid growth.

Many economists and lending agencies such as the World Bank and the International Monetary Fund (IMF) are currently recommending the

adoption of more liberalised outward oriented policies for the less developed countries (LDCs). Indeed the world economy in the late 1980s and early 1990s observed a strong support for the market economy.

The present chapter consists of four sections. Section 2.2 deals with the theoretical models on export and economic growth. In section 2.3, a review of empirical literature on export performance and economic growth is presented with particular attention to empirical studies on Bangladesh economy. Section 2.4 summarises the historical debate on import substitution versus export oriented industrialisation strategy and assess the foreign trade performance and development experience of Bangladesh.

2.2 Export and Growth: Theoretical Literature

2.2.1 An overview of growth models

Economic growth can best be described as a process of transformation which involves increase of a country's gross domestic product over time. Gross domestic product (GDP) measures the economic size of a country and it is often used as a rough measure of the level of welfare. The continuing increase in GDP can raise the average living standard and per capita income. Economic growth occurs more rapidly in some countries than others, over time. It is the increase in the size and quality of factors of production that underlies growth, but certain forces, innovations and entrepreneurship, the role played by the government deserve special attention.

It is often argued that most growth theories, such as Harrod-Domar and Solow-Swan models deal with already developed countries. Accordingly to Harrod-Domar model, the growth in total output (g) is equal to the saving-income ratio (s) divided by the capital-output ratio, (k) i.e. $g = s/k$. In this model capital accumulation is the key to economic growth. The weakness of this type of exercise arises from the assumption of a fixed overall capital output ratio, which assumes away all the vital problems affecting the developing countries' capacity to absorb capital and invest their savings in productive purposes. The neoclassical approach to growth which is considered to be routed in the seminal works of Solow (1956) and Swan (1956) remain influential in explaining the process of growth.

In the neoclassical framework, the rate of growth of output is determined by the rate of growth of capital, the growth rate of labour force, the rate of change in land/natural resources and the rate of change in the state of technology.¹

In the original neo-classical model nothing has been said about foreign trade. Yet growth in most economies is very much dependent upon imports and the ability to export in order to pay for imports. The exceptionally high growth in Japan and Germany after World War II compared to the general sluggishness of the British economy are related to foreign trade. Economists have pointed to the periodic balance of payments crisis experience of Britain and the lack of such crisis in Germany.²

¹There are further growth models, incorporating, government, human capital fertility, investment etc. Barrow (1991) emphasized on the 'special role' that human capital plays in models of endogenous economic growth. The important role of human capital in the process of economic growth cannot be overemphasised as evidence in the works of Schultz (1961), Lucas (1988), Romer (1989, 1990, and Barrow (1991), to name a few. Human capital accumulation, in terms of skill and education, has been regarded as a major driving force to economic growth. The theory of endogenous growth, largely influenced by Romer (1986) and Lucas (1988) establishes a long run equilibrium relationship between trade openness and economic growth (Edward 1993).

²In the Omnibus Trade and Competitiveness Act of 1988, USA trade representative entered into negotiations with countries running excessive unwarranted trade surplus with the United States and mandate retaliatory action against such countries if negotiations fail. This shows the element of New Mercantilism in the modern era (Appleyard and Field 1992)

2.2.2 Modern theory of trade and export-oriented growth

The theory of comparative advantage provides the intellectual basis for the export-oriented development strategies.³ David Ricardo argued that a country should specialise in the production and export of those commodities which it could produce with greatest comparative advantage, i.e. for which the costs are comparatively lowest and import commodities in which it has a comparative disadvantage. Since the seminal work of Ricardo, many economists attempted to identify the causes for the differences in comparative advantage across countries. The Heckscher-Ohlin (H-O) theory provides a widely accepted explanation for the difference in comparative advantage between two countries. This theory depicts that, the nations will tend to export the goods that use their relatively abundant factors more intensively in exchange for the goods that use their scarce factors more intensively. The capital-poor developing countries are recommended by the H-O theorem to specialise in labour or land-intensive products and export these in return for the capital intensive products of the developed economies. The H-O model therefore provides a plausible⁴ explanation for the source and the pattern of mutually beneficial trade but one with explicit implication for domestic income distribution. It is relatively easy to demonstrate with the aid of the Stolper-Samuelson theorem that trade benefits the 'abundant' factor. For example, in case of a labour abundant economy like Bangladesh an opportunity to sell labour intensive exportable at a higher price to foreigners will increase the wage-rental ratio.

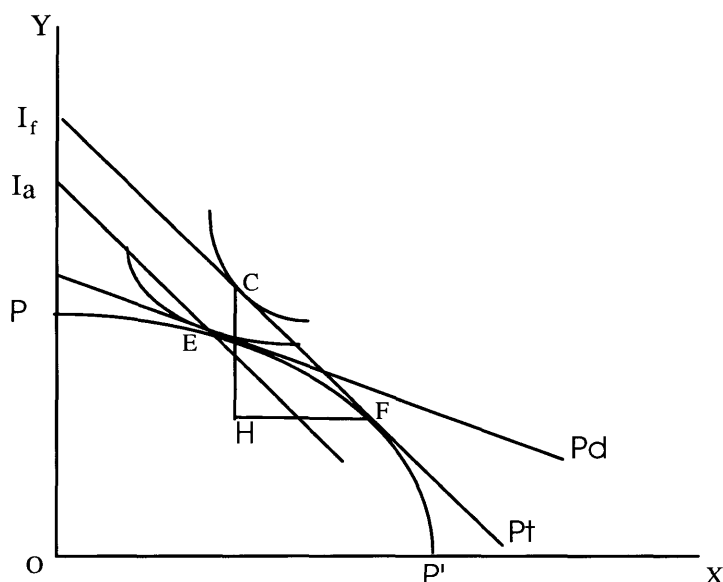
³ In his Absolute Advantage theory, Adam Smith (1776) suggests that countries should specialise and export those commodities in which they had an absolute advantage and import those commodities where the trading partner had an absolute advantage. Smith's prescription was a Laissez Faire approach (no government intervention) within the bounds of law.

2.2.3 Trade and growth : The case of a small open economy

Exposing a small economy to international trade means it will face a new set of relative prices (world price ratio). When the new set of prices are available, the home country's producers and consumers will adjust to these prices by changing their production and consumption pattern. This re-allocation leads to gains from trade. The ultimate source of gains from international trade is the difference in autarky relative prices between countries. In figure 2.1, the home country's autarky equilibrium occurs at point E, where the domestic price ratio line, P_D is tangent to the production possibility curve PP' . With the opening of trade indicated by the line P_T it now faces the international terms of trade. Given the relatively higher world price of X, production moves to F, the point of tangency between the world price line and the production possibility curve PP' . The consumption equilibrium occurs at point C, where the terms of trade line is tangent to a higher community indifference curve. Point C lies outside production possibility curve and is obtained by exporting HF amount of good X and importing HC amount of good Y. The country is obviously better off because international trade permits it to consume on a higher commodity indifference curve. This welfare gain can be expressed in terms of change in gross national product. In figure 2.1, I_f and I_a measure gross national product in terms of good Y_a in the free trade and autarky equilibrium respectively. Thus, a move from autarky to free

trade has raised GNP by the rate, $\frac{I_f - I_a}{I_a}$

Figure 2.1 Autarky and free trade in a small economy



2.2.4 Import-substitution strategy and growth of a small open economy

In the last sub-section, we have explained the effect of free trade on GNP in the context of a small open economy. During 1950-1980, most LDCs had pursued the policy of import substituting industrialization using tariff and non-tariff protection. The effect of tariff protection on economic growth is illustrated by graph 2.2. In this figure the free trade equilibrium production occurs at point F while consumption takes place at point C. An imposition of tariff on good Y at the rate t will lower the

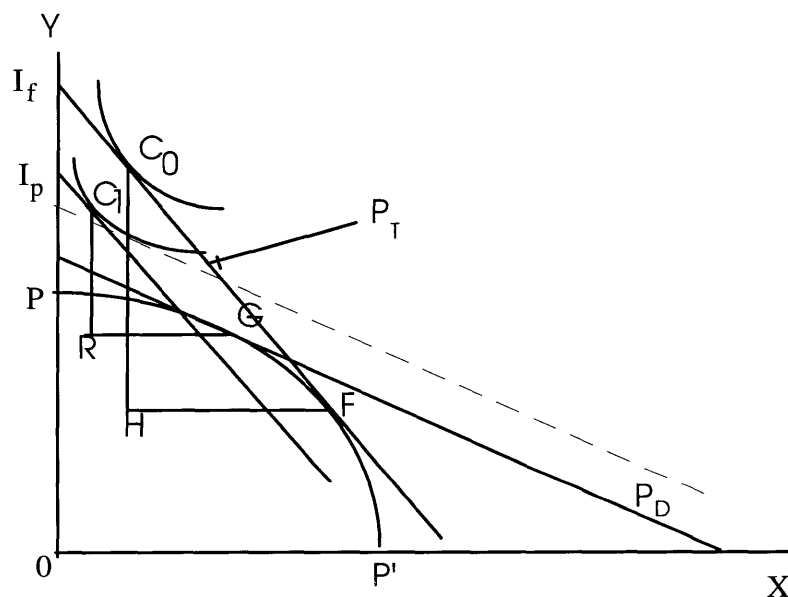
domestic price ratio to $\frac{P_x}{P_y(1+t)}$ which is represented by the line PD. Both

the domestic producer and the consumer price ratio have changed. For the value of imports to be exactly equal to the value of exports, consumption must occur along the world price ratio line. The post-tariff production and consumption equilibrium are shown by the point G and C1 respectively. A consumption of the post-tariff equilibrium with the free-trade equilibrium suggests that an import tariff leads to

- (i) an expansion of import competing industry, Y;
- (ii) a decrease in export from HF to RG;
- (iii) a decrease in the welfare level, as indicated by the move to a lower commodity indifference curve and
- (iv) a decrease in gross national product by the rate, $\frac{I_p - I_f}{I_f}$, where I_p and I_f stand for post and pre-tariff GNP measured in terms of Y.

From the preceding discussion it is clear that for a small open economy free trade is better than tariff protection on efficiency ground.

Figure 2.2 Effect of tariff protection



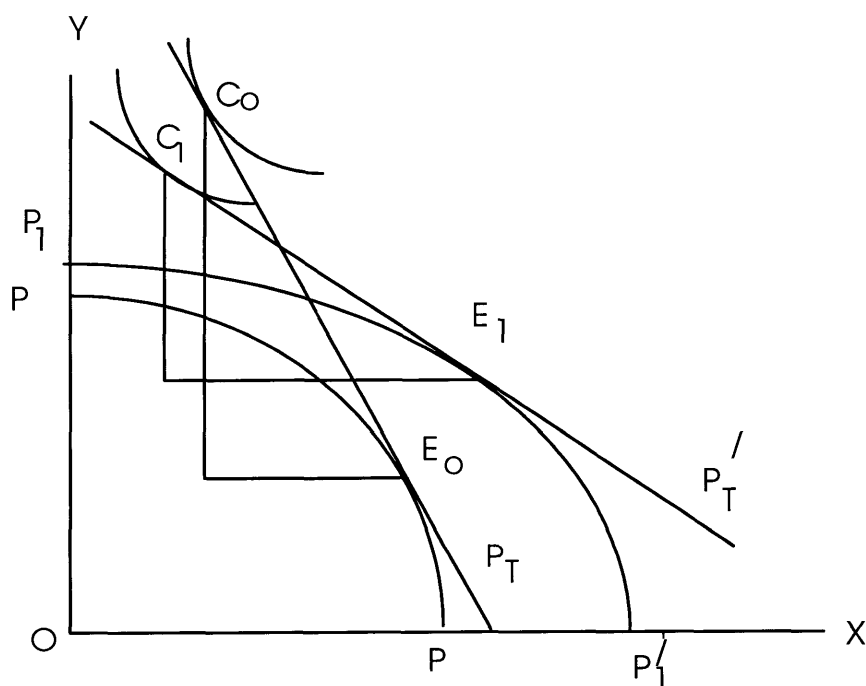
2.2.5 The case of immeserizing growth in a large open economy

A big open economy can affect world price ratio and an export-based growth straightly may decrease its welfare. In figure 2.2 an outward shift in the transformation curve generates excess supply of exportable

commodity, X in the world market which in turn is likely to change the terms of trade against the country in question. For example, Brazil expands its capacity to grow coffee beans more rapidly. Brazil already has a large share of the world coffee export market and because the demand for coffee is price inelastic in the world market, Brazil's expansion of coffee supply bid down the world price. The adverse effect on Brazil's terms of trade can be severe that her own improvement in supply capacity actually make the economy worse-off (Lindert 1986).

Figure 2.2 shows that a deterioration of the terms of trade, represented by the shift of the world price line from P_T to P_T' , leads to a shift of the consumption equilibrium from C_0 to C_1 . Therefore free trade and specialization could hurt a large open economy.

Figure 2.3 The case of immiserizing growth



2.3 Export and Economic Growth: Empirical Literature

Much of the empirical literature on trade and development deals with middle income countries such as semi industrial, and newly industrialised economies. Most of the economic testing of the relationship between the

trade and economic growth have excluded least developed countries, on the ground that the data are not readily available.

2.3.1 Evidence in favour of export oriented industrialisation

The literature stresses the success of fast growing East Asian Countries, the heavy cost of import substitution and virtues of outward oriented policies. Among them are academics such as Balassa, Bagawati, Harry Johnson, Krueger, Lewis, Maizels, Ram and Singer.

The empirical literature on the relationship between export and economic growth is suggestive but still ambiguous. Early studies observed a positive correlation between export performance and overall growth (Emery 1967, Maizel 1968, Kravis 1970, Michaely 1977, Balassa 1978, Porter 1979). In an influential paper that has generated significant further research. Michaely (1977) used simple rank correlation on a sample of 41, LDCs for 1950-73 to analyse the association between the rate of growth of export and the GDP growth. Michaely focused on the relation between the rate of growth of exports share in GDP and the growth of GDP; in order to avoid spurious results stemming from the fact that the exports are components of GDP. He found that the Spearman rank-coefficient was significant and positive for the sample as a whole. Later authors conducted a more sophisticated econometric analysis under neoclassical aggregate production function framework. They found significant positive relation between export growth and economic growth. (Michapoulos and Jay, 1973; Feder, 1983 and Ram 1985 and 1987, Tyler 1981, Kavoussi 1985 and others). These investigations usually employ a GDP or GNP growth equation similar to the following:

$$(2.1) \quad \frac{\Delta Y}{Y} = \alpha \frac{\Delta K}{K} + \beta \frac{\Delta L}{L} + \theta \frac{\Delta X}{X} + \mu$$

Where, Y, K, L and X represent GDP, capital, labour and export respectively.

Employing the data from 55 middle income developing countries for the period of 1960-1977, Tyler (1981) observed that a significant positive association prevailed between economic growth and export growth. Balassa (1978), following Michapoulos and Jay (1973) estimated the

effects of exports on economic growth for a sample of 55 semi-industrial countries for the period 1960-73. Balassa introduced export in addition to capital and labour in the production function. Balassa's basic purpose was to test the hypothesis that export orientation raises total productivity through its effects on the efficiency of resource allocation, economies of scale, capacity utilisation and technological change. The results indicate that export significantly contributed to the rate of economic growth. In his 1983 cross-section study, Feder developed and applied an intuitively appealing model of GDP growth. Dividing the economy into two sectors (export and non-export), Feder identified the channels through which export affects GDP growth. In his model, the growth of the export sector can affect GDP growth if factor productivity in the export sector differs from that of the non-export sector and/or the export sector generates production externality in the non-export sector⁵ Feder's major empirical results are presented in Table 2.1.

⁵The current study employed Feder's model as the theoretical basis. Further discussion of this model is presented in Chapter 5.

Table 2.1 Feder's regression result for semi-industrialised LDCs, 1964-1973

Variable	Parameter	Conventional Neo-classical Model	Augmented Neoclassical Model
I/Y	α	0.284 (4.311)	0.178 (3.542)
\dot{L}/L	β	0.739 (1.990)	0.747 (2.862)
$(\dot{X}/X)*(X/Y)$	(γ)		0.422 (5.454)
Constant		-0.010 (0.554)	0.002 (0.180)
\bar{R}^2		0.370	0.689
No. of observations		31	31

Source : (Feder 1983, p 65)

Note : Numbers in parentheses are t-values.

L/\dot{L} = growth rate of labour force, I/Y = share of Investment in GDP,

X/\dot{X} = growth rate of export.

The adjusted \bar{R}^2 is almost doubled when the specification includes the

weighted growth rate of export, $\frac{\dot{X}}{X} \left(\frac{X}{Y} \right)$. The results lend strong support to the hypotheses that the sum of the productivity differential and externality effect is positive and significantly different from zero. The sign and magnitude of the co-efficient related to investment are within the range expected. He found specifically, when the conventional neo-classical

formulation is used, the estimated parameter is within the range observed in earlier studies. When the augmented neoclassical model is adopted the coefficient of investment declines sharply. The parameter associated with labour growth is significantly greater than zero. The empirical findings suggest that even when entrepreneurs optimise resource allocation given the prices they face, there are substantial gains to be made due to externality effects, because social marginal productivity of an input in the export sector is greater than private marginal productivity.

Balassa (1985) re-examined the relationship between export and economic growth for 43 countries covering the period 1973-79, after the external oil shock.⁶ Unlike earlier studies, Balassa's sample included least developed countries. In order to control for the effect of the stage of development on growth, per capita income in the initial year has been introduced as an additional variable in GNP growth equations. Growth equations further include the share of manufactured products in total export as an indicator of the product composition of export. Balassa estimated several versions of the following GNP growth equation :

$$(2.2) \quad g = f\left(\frac{S_d}{Y}, \frac{S_f}{Y}, \frac{\dot{L}}{L}, \frac{\dot{X}}{X}, \frac{Y}{P}, \frac{X_m}{X}\right)$$

Equation (2.2) states that inter country differences in GNP growth rate depends on differences in domestic ($\frac{S_d}{Y}$) and foreign saving ratios ($\frac{S_f}{Y}$), the growth of labour force ($\frac{\dot{L}}{L}$) the growth of export ($\frac{\dot{X}}{X}$), per capita income ($\frac{Y}{P}$)

⁶ He has also investigated policy responses to the external shocks (1981, 1984 a,b,c)

and the share of manufacturing in total export ($\frac{X_m}{X}$). The introduction of export variable increases the explanatory power of the regression equation to a considerable extent. The export variables are statistically significant at 1% level and its introduction reduces the level of significance of capital and labour variable. The estimated linear regression equation based on equation (2.2) is presented in Table 2.2.

Table 2.2 Balassa's GNP growth model, 1973-79

Constant	S_d / Y	S_i / Y	\dot{L} / L	\dot{X} / X	Y / P	X_m / X	R^2
4.148 (0.241)	0.117 (2.130)	0.117 (2.130)	0.614 (0.958)	0.161 (2.035)	-12.662 (-2.289)	0.256 (1.800)	0.375

Source: Balassa (1985, p 33)

The result shows that for a given increment of capital, labour and exports, the rate of economic growth will be higher, the lower is the level of development. This view is opposite of often expressed opinion that a certain level development is required to get the benefits from export expansion, this implies that the lower income countries have limited possibilities of economic growth than middle income countries. Subsequently, Balassa's study was criticised for lack of the role exchange rate in explanation of export performance, using only export growth as trade orientation, and inability to deal convincingly with causality issues. Most of the studies also have been criticised as they are based mostly on cross country data rather than time series data.

Pack, Page and Young (1986) in a study of cross country regression concludes that the superior performance in number of Asian countries is not totally explained by unusual investment ratios and initial level of education. The growth of manufacturing exports may have allowed the industrial sector in these countries to increase its productivity. The rapid growth of per-capita income in these countries is attributable to their excellent export-performance.

Bairam (1991) tested Kaldor's engine of growth hypothesis for Turkish economy during the period of 1925 to 1978. He consistently supports the hypothesis that the growth of industrial sector, which is also applicable to

manufacturing export, totally or partially determines the growth in the other sectors namely agriculture and services and consequently determines the overall economic growth.

Ghartey (1993) examined the casual relationship between export and economic growth in Taiwan, The USA. and Japan. Using vector auto regressive model he observes that exports growth causes economic growth in Taiwan, economic growth causes export growth in the USA. and feedback casual relationship exists in Japan. Only terms of trade improvement causes economic growth in Japan.

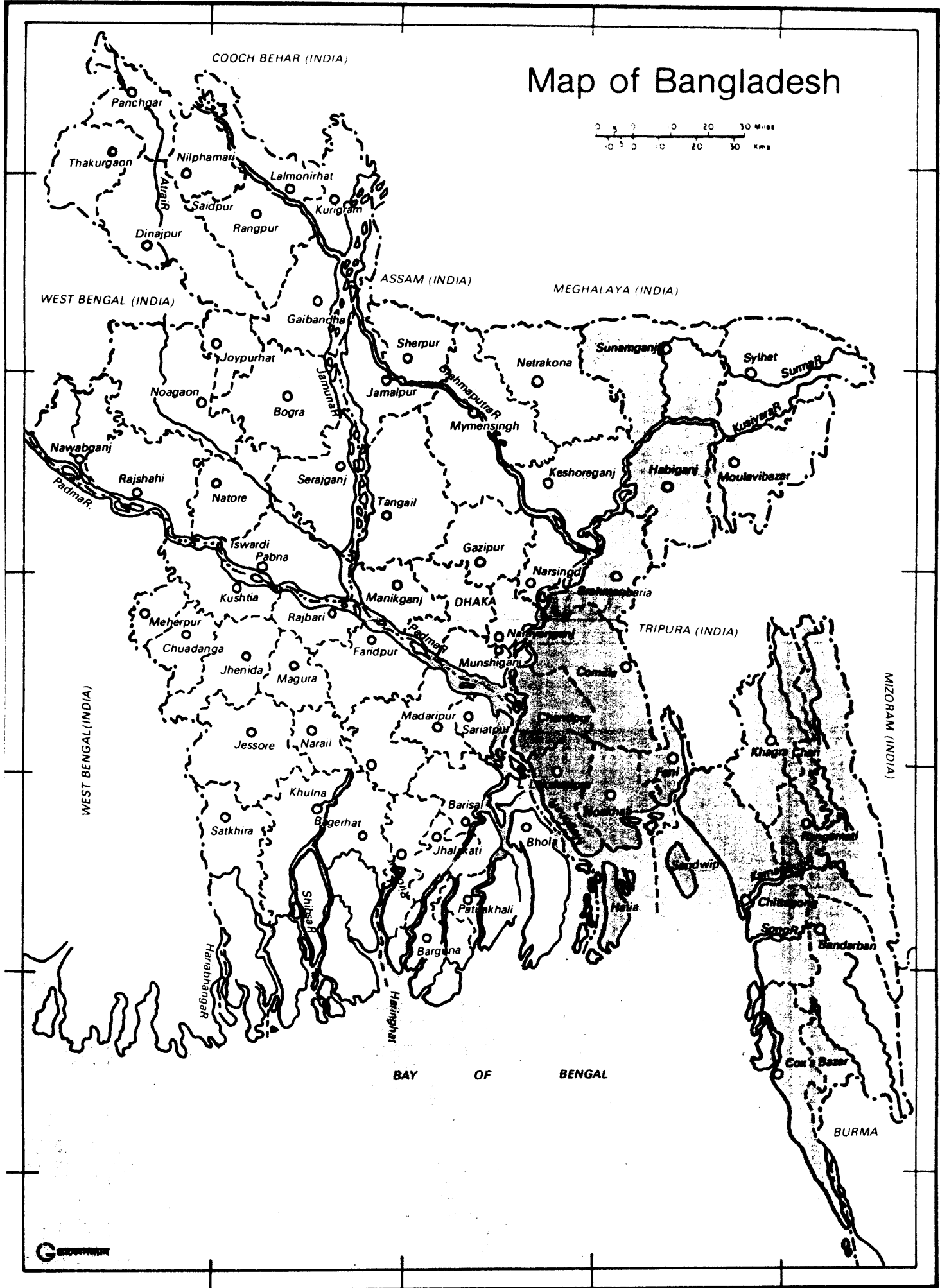
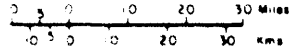
Peter Kugler (1991), using quarterly data for USA, Japan, Switzerland, Germany, UK. and France, concluded that in four cases (USA, Japan, UK, Switzerland), exports did not reveal cointegrating relation with any of three key macroeconomic variables, GDP, consumption and investment. This means that long-run equilibrium relationship exists between exports and GDP.

Jung and Marshall (1983) used Granger causality test which cast considerable doubt in the validity of the export promotion hypothesis. Their time-series study for 37 developing countries provide evidence in favour of export-oriented growth strategy only in four cases: Indonesia, Egypt, Costa-Rica, and Ecuador. They argue that the evidence in favour of export promotion as an effective development strategy is weaker than previous statistical studies have indicated. Darrett (1987), Levine and Renett (1991) also questioned about the robustness of the relationship between export and growth. Using the OLS and the white test for causality between GDP and export growth . Darrett rejected the export led growth hypothesis in 3 countries out of 4. A selection of empirical studies on the relationship between export growth and economic growth is presented in the Table 2.3 at the end of this section..

2.3.2 Foreign exchange constraint and export oriented growth

In recent years researchers have been advocating an export promotion policies, as a superior development strategy for semi-industrialised countries. This positive and significant export GDP relationship has attributed to the possible externalities of competition in world market, e.g. efficiency of resource allocation, economies of scale, and various labour

Map of Bangladesh



training and demonstration effects. Esfahani (1991) observes that the correlation mainly has been due to the contribution of exports to the reduction of import shortage, specially inputs, which restrict the output in many developing countries. In this sense export promotion is particularly important for countries that cannot obtain sufficient foreign aid or capital. He developed a simultaneous equation model to deal with the potential simultaneity problem between GDP and export growth rates. His empirical work is based on the data of 31 semi industrialised countries for the periods 1960-73, 1973-81 and 1982-86. For the lack of the data on input of intermediate goods he takes some selected inputs of the products such as fuel, lubricant, minerals, metals, equipment as proxy for intermediate inputs. He observes that export raises GDP growth rate primarily by relieving import shortage that many developing countries confront. Once the input supply effect taken into account, there does not seem to be significant externality effect left.⁷ Moreover contrary to some previous studies, increase in the share of manufactured goods in export does not seem to generate any of the export externality effect. His results shows that impact of manufactured exports on GDP growth rate is unexpectedly negative in most cases.

Esfahani's analysis suggests that the reduced impact of export expansion on GDP growth rate in semi industrialised countries (SIC)s during the 1970s must have been due to a reduction in the supply of foreign exchange for these countries.

He argues that, export promotion policies in these countries can be quite valuable in supplying foreign exchange for import of inputs to expansion of domestic output. Though this note of export may be temporarily replaced by foreign assistance, but long time growth of any developing country depends on the steady and strong expansion of its export sector.

⁷When the import variables are left out the estimate is in line with Ram (1987) and Rana (1988) who find, based on models similar to those of Feder (1983) and Balassa (1985) that externality effects of exports had declined between the periods 1960-73 and 1973-1981.

2.3.3 Factors influencing export performance in LDCs

Export performance is defined by some economists as the volume of exports or value of exports or the growth rate of value of export. An economic analysis of export performance includes both demand and supply factors contributing export. With respect to the determinants of exports, world demand, relative export price and foreign policies affect export performance from the external demand side while the variables like effective rate of assistance (incentives), exchange rate, and non-price factors such as skills, learning process etc., are considered to be supply side influences on export growth. Economic and political relations together, with proximity to the market may also be the important determinants of export performance of a country (Islam 1990). The factors on the supply side include natural calamities, inefficiency and instability in marketing arrangements. Most of these factors are not directly measurable and there are problems with data availability.

Kravis (1970) observed that while external demand factors provided a stimulus to exports and growth, actually it was mainly the result of increased market share and diversification of exports. Kravis implied that internal factors were more important in influencing mobility of resources rather than external conditions.

Arthur Lewis (1980) established a relationship between economic growth in developed countries and export growth in developing countries. Criticizing the Lewis study, Ridel (1984, 1988) claimed that both causal observations and econometrics evidences in the Lewis study were misleading due to neglecting the supply side influences and he asserted that supply rather than demand factors had principally determined LDCs export performance in manufacturing.

Wheeler (1984) examined the sources of stagnation in Sub-Saharan Africa during the 1970s by considering several domestic policy variables and exogenous factors like climate, violence and export prices. Svedbing (1991) observed that the Sub-Saharan exporting countries were negatively affected by the external forces due to deteriorating barter terms of trade over the years 1954 to 1985.

During the post war period prior to 1960s, it was widely accepted that the export performance in LDCs were influenced by external demand factors.

Various authors notably Nurkes (1961), Kravis (1970), Love (1984), Athukorala (1991) argued that the favourable external demand of their exports helps the less developed countries to grow faster. He argued that better policy regime might favourably increase the growth performance of these countries for the period.

Differentiating the internal supply factors as competitiveness and diversification, Love (1984) and Athukorala (1991) confirmed Kravis's (1970) proposition that export performance in most countries was sensitive to domestic supply factors. The limitations of the aggregate approach of the constant market share analysis (CMSA) have lead to the development of econometric model in which the components of CMSA are desegregated into dependent and independent variables. A recent development by Krarvis (1970), Love (1986) and Athukorala (1991) provided a simple model for analysing the determinants of export. The model can be expressed as follows :

$$X_v = f(WD_t, CH_t, DV_t)$$

where,

X_v = Volume or value of exports

WD = World Demand

CM = Competitiveness in Export Performance.

DV = Export Diversification and

t = time.

Faru (1994) in her dissertation, made an attempt to analyse the aggregate demand and supply factors influencing export performance of Tanzania. Her results indicates that both external demand and supply factors represented by competitiveness and diversification, have significant influence on export performance of the agriculture sector in Tanzania. She again divided the period into restrictive and liberal regime. She concluded that for both regimes, export performance was relatively more responsive to diversification. For the liberal trade regime, world demand had more influence on export performance. But the response of export earnings to competitiveness during the liberalised period was low.

In 1989, Rostam Kavousi published a qualitative analysis of a sample of 52 developing countries, dividing the countries as free trade, outward oriented, and trade restrictive inward oriented countries. His results showed that for the first period of 1967-73, when world market conditions were generally favourable there was strong positive correlation between export orientation and growth performance, when market demand was unfavourable, the correlation was weaker and doubtfully significant. When world demand is strong, the benefits of openness clearly outweighs its danger.

The demand deficiency hypotheses of trade traced the causes of slow growth of LDCs export as

- (i) the low income elasticity of demand for primary products
- (ii) development of synthetic substitute
- (iii) economies in the use of raw materials in the industrialised countries.
- (iv) shift in the industrial output composition towards goods with lower import content and the restrictive import policies of developed countries (Banerjee 1974).

Primary exports suffer from sluggish growth of world demand, declining terms of trade, unstable export earnings and weak linkage effect. Ironically, primary export boom can cripple development, if not managed carefully. Islam and Subramanian (1980) suggest that, attempts by all developing countries to expand traditional agricultural exports with low price elasticity of demand may not yield rising earnings rather may result falling export revenue. However in some cases, the exports of primary products can indeed serve as an engine of growth (Gillis et al 1992). For example, Malaysia sustained relatively rapid growth over the past 30 years through a primary export led strategy of development.

2.3.4 Trade liberalisation and export growth

Most cross country econometric works on the relationship between trade-orientation and growth assumed that more liberalised outward economies experienced faster growth of export and economic growth.

The cross country studies by the World Bank (1988, 1990), Harrigan and Mosley (1991), Whalley (1991) and Choksi (1992) all support that liberalisation and export are positively related. Greenways and Sapsford (1994), using production function approach find little support for the positive impact of liberalisation on export growth. In their cross country analysis, they find that in eight out of twelve cases liberalization has no discernible impact on export growth. But many authors claim that domestic distortion, induced by government policies hinder to get opportunities from international market isolating domestic economy from foreign influences (Bhagawati 1972; Balassa 1988). Price and other exchange control give rise to distortion in product market, inducing arbitrariness in government decision and thereby creating uncertainty for private firms (Balassa 1988). Policies such as export orientation, competitive exchange rates, other fiscal and monetary policies, state enterprises, industrial and agricultural policies are all important as they are the means that the state can take to assist the economy in taking advantage of market forces (Macomber 1987). When intervention in the economy is undertaken with the clear intent of strengthening the ability of the economy to take advantages of the market forces, it may work well, but if it is under taken in contravention of market forces, it appears to work poorly.

In export development, government can act as a promoter or facilitator. It can pursue favourable policy, such as development of infrastructure, product and market exploration, enhancing fiscal and financial incentives etc or government can play one of the role of exporters if socio-economic and structural factors suggest.

Devaluation is considered an important aspect in a liberalisation policy as evidenced from Bhagwati (1978), Krueger (1978) and Michaely et al.(1991). They argue that in the presence of quantitative restrictions a real devaluation will reduce the rents accrued to those with licence allocation, and thus reduce the anti export bias.

2.4 Trade Policy: Import Substitution Versus Export-Oriented

The issue of trade policy and industrialisation in LDCs have been the subject of exhaustive analytical and empirical investigations during the past three decades. Yet our understanding of the effect of different trade policies on industrial growth and economic development remains

incomplete (Kirkpatrick 1987). A broad distinction is normally drawn between two trade related industrialisation strategies. Import Substitution Industrialisation (ISI) and Export Oriented Industrialisation (EOI). In practice, most LDCs have employed elements of both strategies, while emphasis given to each approach has altered through time.

Neo-classical paradigm suggests that gains from trade are generally positive and mutual, which have been endorsed by modern trade theorists. It is contended that in the absence of distortion free-trade will be the optimal policy for a small open economy. Structuralist and Radical commentators argue that free trade will rarely be the optimal policy for a small LDC due to existence of structural distortions and gains from trade may be unequally distributed at the expense of the LDCs. This school of thought have been influential in fashioning trade policy in LDCs over the post war period.

In 1950s and 1960s, ISI dominated the industrialisation strategies of the larger Latin American countries (Brazil, Argentina and Mexico) and a number of large countries in South and South-East Asia (India, Pakistan and Philippine). Some smaller countries in Latin America, Sub-Sahara Africa (Nigeria, Kenya, Ghana and Zambia) and South East Asia adopted ISI in 1960s. ISI embraces the idea of protection, which represents a policy of encouraging home industry by the use of bounties, ie, by imposing tariff and non tariff barriers and restriction on imports. The main arguments for protection are infant industry, diversification of industry, employment, national defence, tax revenue and current account deficit.

The criticism of both the implementation and outcome of ISI was widespread and overwhelming consensus was that ISI had been a failure. This view was shared by both neoclassicists and Latin American structuralist who were among the advocates of ISI (Kirkpatrick 1989). The neoclassical attack on ISI was initiated by a publication of the influential comparative studies by Little, Scitovsky and Scott (1970), Balassa and associates (1971), Balassa (1982), Bhagwati (1978) and Krueger (1978). Their studies applied the neoclassical analysis to a large number of LDCs that adapted ISI strategies.

Again there has been a various attempts to demonstrate empirically that EOI has resulted in better growth performance (Balassa 1978, Tyler 1981, Bhagwati 1978, Krueger 1978, 1983). Export promotion seems to be

replacing import substitution as the dominant development policy in Third-World manufacturing. This export led growth policy with special emphasis on manufacturing, is in line with the emerging international division of labour through which capital in the West seeks to reduce labour costs of production by shifting some industrial processes to the East and South. Labour intensive industries particularly textile, garments, footwear, leather products, electronic manufactures, other leading industries such as automobile, steel, petro-chemical industries are being increasingly located in the Third World and former socialist countries. It has been argued by some neoclassicists that an EOI strategy based on labour intensive is not only beneficial in terms of economic growth but also results in improvements in income distribution (Balassa 1982a, Fields 1984, Rams 1985b).

The dichotomy between ISI and EOI may be misleading. If a longer time horizon is considered, ISI and EOI can be seen as sequential phases in the industrialisation process in most LDCs. The issue is perhaps the determination of the optimal sequence of ISI and EOI phases in the industrialisation process than the relative merits of EOI and ISI as alternative competing strategies (Kirkpatrick, 1987). Most observers have favoured the Asian NIC pattern of a relatively short lived period of ISI, followed by early EOI and secondary ISI, arguing that it avoids many of the economic inefficiencies associated with prolonged period of market based ISI, while at the same time reducing unemployment and improving distribution of income (Ranis and Orrock 1985). Table 2.3 presents the World Bank (1987) classification of 41 developing economies based on their trade orientation.

Table 2.3 World Bank classification of forty-one developing economies by trade orientation

Period	Strongly outward oriented	Moderately outward oriented	Moderately inward oriented	Strongly inward oriented
1963-73	Hong Kong Korea, Republic Singapore	of Brazzil Cameroon Colombia Costa Rica Cote d'Invoire Guatemala Indonesia Israel Malaysia Thailand	Bolivia El Salvador Honduras Kenya Madagascar Mexico Nicaragua Nigeria Philippines Senegal Tunisia Yugoslavia	Argentina Bangladesh Burundi Chile Dominican Republic Ethiopia Ghana India Pakistan Peru Sri Lanka Sudan Tanzania Turkey Uruguay Zambia
1973-85	Hong Kong Korea, Republic Singapore	of Brazil Chile Israel Malaysia Thailand Tunisia Turkey Uruguay	Cameroon Colombia Costa Rica Cote d'Ivoire El Salvador Guatemala Honduras Indonesia Kenya Mexico Nicargua Pakistan Philippines Senegal Sri Lanka Yugoslavia	Argentina Bangladesh Bolivia Burundi Dominican Republic Ethiopia Ghana India Madagascar Nigeria Peru Sudan Tanzania Zambia

Source : World Development Report (1987), World Bank.

Note: Since 1985 Bangladesh, India, Nepal and Sri Lanka have been pursuing a moderately outward oriented development path. After 1992, they adopted more liberalised trade and foreign exchange policy.

World Bank classification was criticized by Helleiner (1992). World Bank used qualitative assessments of overall incentives structures and these categorisation were fuzzy in their distinction and have not been very well received. Unlike the World Bank, Heitger (1987) developed a quantitative measurement of trade orientation using computed effective rate of protection (ERP) on 47 countries during 1960-70. He estimated a GDP growth regression equation including as regressors, the average and standard deviation of ERPs across commodities, the investment ratio, initial GDP and adult literacy. He found that the co-efficient of ERP was significantly negative providing support that trade distortions (inward orientation or protection) negatively affect GDP growth.

In their empirical study of 106 countries, Syrquin and Chenery (1975) found generally higher growth rates in outward oriented economies than in inward looking economies. Contrary to this finding, Pritchett (1991) concludes from an analysis of the cross-country data that no reliable robust estimates of the impact of general outward orientation on economic performance or export performance is likely to be possible from cross country data.

Helleiner (1992) noted that low income countries cannot expect to draw much policy advice from the results of cross-country regressions of growth upon measures of trade policy orientation. The constant advice to low-income countries to look to Korea for their trade policy model ignore the fact that Korea practised import substitution under heavy protection. Korea maintained a highly depreciated competitive exchange rate and heavily regulated its market and political system over the years.

In the words of Sir Arthur Lewis (1978), international trade become an engine of growth in the nineteenth century, but this is not its proper role. The engine of growth should be technical change, with international trade serving as lubricating oil and not as fuel. International trade cannot substitute for technological change, so those who depend on it as their major hope are doomed to frustration. Supporting this development strategy Adelman (1984) argues that in very low-income countries where the majority of the labour force is still in agriculture and where

agriculture productivity is low and stagnant primary attention must be directed to a broad-based effort to get agriculture moving via technical change.

2.5 Development Experience of Bangladesh and Selected LDCs

In the late 1960s and in the early 1970s, substantial variations were recorded in the development experience of (Asian, Latin American and African) countries. Some countries showed impressive rates of economic growth, others stagnated or declined. This diversity of the development experience is slowly inching its way into the development literature.

By the 1970s it has become clear NIEs were emerging in East Asia, South-East Asia and Latin America, while most of the developing nations were left behind. In recent years, NIEs have grown twice as fast as Japan, the most successful industrial country in the post war era (Choudhury and Islam 1993). Their exports of goods and services contributed significantly in their GDP which can be shown from the table 2.4.

Table 2.4 Exports of goods and services (% OF GDP)

Economy	1980	1987	1992
Bangladesh	8	8	11
Hongkong	88	123	-
Korea	34	45	31
Singapore	205	191	191
Taiwan	-	53	58
Argentina	7	10	7
Brazil	9	9	11
Mexico	11	20	14
India	7	6	11

Sources :1.UNCTAD, compiled by Chowdhury and Islam, 2.World Bank 1994.

Most of these countries are small, natural resource-poor, labour surplus and human resource-rich. After primary import substitution, East Asian countries entered a phase of export of labour intensive consumer non-durables, while South Asian countries adopted the policy of secondary import-substitution, and develop the domestic ability to produce consumer durables. The East Asian countries can be characterised as pursuing a steady process to economic maturity, while South-East Asian countries oscillating along a path which is less certain to achieve steady growth consistent with enhanced equity (Ranis, 1992). Considering the recent economic reforms in South Asia, Hardling (1993) states :

"Trade and investment liberalisation in South Asia passed some notable milestones in 1992. India and Pakistan further reduced tariffs on imports, and Nepal and India made their currencies fully convertible for trade. Brighter prospects for economic growth in the region combined with trade liberalization should produce a stronger US export performance in 1993."

The whole periphery of the South Asian countries is lagging behind. Though India has progressed far in industrialisation yet percapita income and other development index shows a dismal picture; it is also true in case of Pakistan, Nepal, Sri Lanka and Bangladesh. Bangladesh, a tiny land with vast population is trying to achieve a sustained level of growth through export promotion and other fiscal, financial and monetary reforms.

2.5 Export Performance and Growth Empirical Literature on Bangladesh

There are few studies on export performance and economic growth in Bangladesh. Roy (1991), found a significant correlation between export and GNP growth, Since export is a component of GNP, one would expect a positive correlation coefficient. Hence correlation between the proportion of exports in GNP and GNP net of export is used. Table 2.5 presents the estimated correlation coefficients. The spearman rank correlation coefficient between the proportion of exports in GNP net of exports and per capita GNP is found to be 0.78 and it is highly significant at the 1% level.

Further he studied that the relative importance of demand and supply sides factors influencing exports. His result demonstrate that world

demand, trade-weighted exchange rate, and efficiency index, effective rate of export assistance and non-price factors significantly and positively affect export. Devaluation has a moderate positive effect. He argues that from the supply side, exporters respond more readily to changes in nominal exchange rate and export incentives.

Table 2.5 Correlation coefficients

		Period	Rank Correlation
		Coefficients	
1.	Ratio of Exports to GNP Net of Exports and Per Capita GNP	1975/76-1987/88	0.78 (6.57)
2.	Exports and GNP Net of Exports	1975/76-1987/88	0.94 (9.11)
3.	Ratio of Exports to GNP and Per Capita GNP	1975/76-1987/88	0.97 (13.72)
4.	Exports and GNP Net of Exports	1975/76-1987/88	0.91 simple (3.66) corelation

Source : Roy (1991, p 29)

Note : t-statistics are given in parentheses below the coefficients

Finally he concludes that liberalisation of trade and industrialisation policies have important consequences for the composition of export as well as economic growth and stability in Bangladesh.

Rahman (1992) observed that the average annual growth rate of exports in US\$ in 1980s was 7.7 percent per annum. Real growth rates of traditional exports and non-traditional export were 0.7 percent and 20.4 percent respectively, during 1981-89. Although the share of manufactured export was high (77 % in 1989/90), primary export remained vulnerable to commodity price instability in the world market. Exchange rate depreciation, quick government support in the form of bonded warehouse facilities, back to back letter of credit for raw material import, export

performance benefit, concessional interest rate for credits from banks, helped enormously to create the needed incentives. The export sector of Bangladesh evolved directly in response to world market demand. It did not emerge through a process of dynamic learning and maturity of import substituting industries (Rahman, 1992).

Rob (1993) attempted to offer some recommendation along with a brief evaluation of the recent export performance record and the existing export policy. He argued that recent (1986-92) export performance record suggest that Bangladesh need to pursue vigorously export development through expansion of existing export as well as through market and product diversification. Sattar (1993) observes that switch from the dependence on traditional to non traditional export offers a substantial gain to the economy, improved macro economic stability, higher output and employment, economic use of capital stock and scope of reaping advantages from future world income. Rahman (1992) infers that export increases national income by multiplier operation. He argues that when export increases, the import capacity of the economy increases, as a result the country can import more capital equipment for investment as well as foreign capital penetrates for attraction of higher profit in the export sector. Thus the export multiplier becomes operative. His causality test indicates a significant causal relationship running, from export to industrialisation. He concludes that export led growth strategy has a good chance of success in Bangladesh.

2.6 Summary

The issue of export performance and economic growth in LDCs has been the subject of exhaustive analytical and empirical investigation, during the past three decades. Several studies concludes that a robust positive relationship exists between export growth and economic growth. Some studies are throwing doubtful image for choosing export led growth as the best strategy for LDCs. While export promotion strategies are widely advocated for LDCs, there appears to be no conclusive empirical evidence that it will be applicable to all individual LDCs regardless of world demand condition and country specific factors.

Some analysts argued that export not only needed for growing requirements of import of raw materials and capital goods for economic

development, narrow base of domestic market and barely substantial squeeze of foreign aid program made the export sector, strategic for development.

Table 2.6
A selection of empirical studies on the relationship between export-growth and economic growth

Study	Data Set	Methodology			Major findings	
		Economic growth	Export growth	Estimation Technique		Other explanatory variables
Michaely (1977)	Cross-section, 41 countries Ave of 1950-73	Per capita GNP growth	Growth in export share	Rank correlation	None	Support for export led growth hypothesis.
Balassa (1978)	Cross-section, 10 countries Ave of 1956-67 and 1967-73	GNP growth	Export growth or real export growth	Rank correlation OLS Production function	Labour force growth. Domestic investment and foreign investment / output	Support for export led growth hypothesis.
Williamson (1978)	Cross-section 22 countries Ave of 1960-74	Change in GDP	Lagged exports	OLS linear models	Country dummies; Direct investment. Other foreign capital.	Support for export led growth hypothesis.
Fajana (1979)	Time series 1954-74 one country	GDP growth	Export shares or export change/output	OLS	Trade Balance.	Support for export led growth hypothesis.
Tyler (1981)	Cross-section 55 countries	GDP growth	Export growth	OLS Production function	Labour force growth. Investment growth	Support for export led growth hypothesis. Threshold effect.
Feder (1983)	Cross-section 31 countries	GDP growth	Export growth or export change / output	OLS production function.	Labour force growth and Investment output ratio	Support for export led growth hypothesis
Kavoussi (1984)	Cross-section 73 countries	GDP growth	Export growth	Rank correlation OLS	Labour force growth. Ratio to output of domestic investment.	Support for export led growth hypothesis. Threshold effect.
Balassa (1984)*	Cross-section 10 countries	GNP growth	Export growth	OLS Production function	Labour force growth, ratio of output to domestic investment.	Support for export led growth hypothesis.

continued table 2.6

Jung & Marshall (1985)	Time series 1950-81, 37 countries	Real GNP or GNP growth	Lagged real export growth	Maximum likelihood. Simultaneous linear functions Granger causality	Lagged GNP (GDP) growth	Little support for export led growth causing economic growth
Moschos (1989)	Cross section	Real GDP growth	Real export growth	OLS production function	Labour force growth and real domestic investment growth.	Support for export led growth hypothesis. Threshold effect
Salvatore and Hatcher (1991)	Time series 1963-73, 1973-85, 26 countries	Real GDP growth	Real export growth	OLS production function	Labour input growth. Capital input growth Growth in industrial production.	Support for export led growth hypothesis.
Ram (1985)	Cross section, 73 countries. Ave. of 1960-70 & 1970-77	Real GDP growth	Real export growth	OLS tests for heteroskedasticity and specification bias.	Labour force growth. Investment growth.	Support for export led growth hypothesis Threshold effect.
Daratt (1987)	Time series 4 countries 1955-82	Real GDP growth	Real export growth and lagged real export growth.	OLS, and white test for causality.	None	Rejection of export led growth hypothesis in 3 out of 4 cases.
Greenway & Sapasford (1993)	Cross section, 104 countries Ave. 1960-73 1973-90, 1980-88.	Real GDP growth	Growth in export - GDP ratio	OLS	None	Support for export led growth hypothesis. Indirect evidence; Threshold effect.

continued table 2.6

Greenway & Sapsford (1994)	Time series data from diff. period ranging from 1957-85, 13 countries	Real GDP growth	Growth in export - GDP ratio	OLS	None	No support for export led growth hypotheis.
Roy (1991)	Time series Bangla-desh 1975-88	Per capita GNP, GNP net of export.	Ratio of Export to GNP, Export.	Rank Correlation	-	Higholy positive and significant coefficient.
Satter (1993)	Time series Bangladesh 1979-1992	GDP growth.	Export growth.	OLS production function	-	Support from export led growth hypothesis.

Source : Greenway and Sapsford (1994) and addition

1

¹"Several researchers find evidence of a difference in the effect of export on economic growth between countires above and below some critical level of some variable, indicated in the table as threshold effect (Greenaway and Sapsford 1994). For example Tyler (1981), Kavoussi (1984) concluded that 'growth is affected by export performance only once countries achieved a minimum level of development. But Balassa (1984), Moschos (1989), Ram (1983) come to the different conclusion that 'given increment of capital, labour and exports, the rate of economic growth will be higher, the lower the level of development."

Chapter 3 : The Nature of Bangladesh Economy

3.1 Introduction

This chapter primarily presents the economic features of Bangladesh with a brief discussion on physical features and climate. Bangladesh is a small deltaic region of South-Asia covering an area of 143,998 square kilometre. The land is enclosed by Indian territory, except for a short South-Eastern frontier with Myanmar and a Southern deltaic coast fronting the Bay of Bengal, with territorial waters of 12 nautical miles. As the eastern part of the historic region of Bengal, it was under British rule for long 200 years from the mid-eighteenth century. Before 1947, Bangladesh was a part of undivided India; during 1947-1971 it was a province of Pakistan, known as East Pakistan. Bangladesh emerged as an independent nation in December 1971. Before independence the living standard in Bangladesh (then East-Pakistan) steadily fell behind that of West Pakistan because of economic exploitation of the former by the latter.

This chapter is organised as follows. In section 3.2 the physiography of Bangladesh is described briefly. Section 3.3 presents the characteristics of population and labour force. Macroeconomic characteristics of Bangladesh is presented in section 3.4. In section 3.5, foreign trade and balance of payments issues are discussed. The final section reviews the recent economic policy reforms in Bangladesh.

3.2 Physical Features and Climate

The physical features and climate are important determinants of the structure of GDP and the composition of export of an economy. The physiographic characteristics of Bangladesh are almost homogeneous with the dominance of the low, flat and fertile alluvial soil. These physical characteristics helped Bangladesh in gaining a competitive edge in the world market for raw jute. As a riverine country, the surface of Bangladesh consists of alluvial deposits of the Ganges, Brahmaputra, and the Meghna river systems. The major river systems are all notorious for causing annual floods. There are only 200 square miles of hilly area in the South. The coastal fringe is a huge expanse of marshy deltaic forest, Sunderban. The total forest area covers about 14 percent of the land area.

The economy of Bangladesh is often susceptible to natural disasters. As a tropical country it has a typical monsoon climate with maximum temperature in summer ranging from 21° to 40° celsius. Three main seasons are summer (March-June), monsoon (July-October) and winter (November-February). Average temperature in winter ranges from minimum 7°c to 31° c. Storms occur during March-July when cyclonic conditions in the Bay of Bengal tend to whip-up the waves and sometime cause widespread flooding in the low land coastal deltaic area. It is important to note that fluctuation in Bangladesh GDP over time primarily reflects the effects of natural calamities (and perhaps man-made political disasters), rather than external economic shocks.

3.3 Population and Labour Force

3.3.1 Population

Bangladesh is one of the most densely populated country in the world and eighth largest in population size. The average density of population was 755 per square kilometre in 1991 (BBS, 1993). Between 1951 and 1961 the population of Bangladesh has increased by about 2 percent annually but in 1970 the annual growth rate increased to 2.8 percent. The population continued to grow rapidly during the 1970s despite heavy loss of lives in the cyclone and tidal waves of 1970 and the liberation war of 1971. The population growth rate declined in 1980s. The intercensal (1981-91) average annual growth rate of population was 2.17 percent.

The factors contributing to high population growth over the period 1960-1992 are a decline in infant mortality rate, an increase in life expectancy and a negligible fall in crude birth rate in rural Bangladesh. Life expectancy at birth increased from 37.3 in 1960 to 57.1 in 1992 (BBS 1993). Assuming declining fertility and mortality rate, the country's population is expected to reach 140 million by the year 2000 from its present approximate size of 120 million (BBS 1993).

Table 3.1 presents a historical account of the size and growth of population in Bangladesh since 1901. Initially, Bangladesh had high birth and death rates which caused a very low growth rate of population. Over the period 1901-1931, the annual average growth rate of population was less than 1 percent. This was followed by an increase in the population growth rate due to a decline in the death rate. However, the annual average population growth rate reached a low rate of 0.50 percent during 1941-1951 because of the 'Bengal Famine of 1943'. Since 1951, the annual average

growth rate of population remained above 2 percent primarily because of a dramatic fall in the infant mortality rate and an improvement in life expectancy.

Table 3.1 The demographic transition of Bangladesh 1901-1991

Census	Population	Percentage change	Annual Average Growth Rate
1901	28,927,786	-	-
1911	31,555,056	9.08	0.94
1921	33,254,096	5.38	0.60
1931	35,604,170	7.07	0.74
1941	41,997,297	17.96	1.70
1951	44,165,740	5.16	0.50
1961	55,222,663	25.04	2.26
1974	76,398,000	38.35	2.48
1981	89,912,000	17.69	2.35
1991	111,455,185	23.96	2.17

Source : BBS 1993.

3.3.2 Labour force

In Bangladesh the natural growth of population is the main source of labour force growth because of very low rate of net immigration. We now focus on the composition of population based on their activity status in the labour market for the period 1961-1991. Table 3.2 presents the data on activity status. The labour force participating rate increased from 30.6 percent in 1961 to 46.9 percent in 1991. The official unemployment rate was below 1 percent over the period 1961-1991. Considering the extent of absolute poverty and population pressure in Bangladesh, the official estimate of the unemployment rate seems to be biased downward. It is widely believed that the unemployment rate, inclusive of disguised unemployed workers, is close to 30 percent. It may be noted that the labour force participation rate increased dramatically in 1989 compared to 1984-85, because of the inclusion of specific rural activities such as care of domestic animals, poultry, threshing, food processing, in the measurement of aggregate economic activity.

Table 3.2 - Economically active and inactive population by activity status 1961 - 1991

Activity Status		1961	1974	1981	1983-84	1984-85	1985-86	1989	1991
		Census	Census	Census	LFS				
Percentage									
Distribution									
1	Total civilian labour force	30.6	28.7	28.8	29.9	30.2	30.4	46.9	46.9
2	Employed population	30.4	28.0	28.1	29.4	29.7	30.1	46.3	46.0
3	Unemployed population	0.2	0.7	0.7	0.5	0.5	0.3	0.6	0.9
4	Not in civilian labour force	69.4	71.3	71.2	70.1	69.8	69.6	53.1	53.1
5	Housewives	25.5	23.3	25.0	25.0	25.4	24.5	16.8	8.8
6	Other inactive persons	6.9	12.7	13.1	13.2	13.2	14.2	1.8	11.7
7	Children (0 to 9 years)	37.0	35.3	32.3	31.8	31.2	30.9	34.5	32.6

Source: Bangladesh Bureau of Statistics, Labour Force Survey (LFS) and census.

Note : Row 1 + Row 4 = 100 percent, where Row 1 = Row 2 + Row 3 and
Row 4 = Row 5 + Row 6 + Row 7

The structure of employment for the period 1961-1991 is presented in Table 3.3. One of the best known characteristics of labour market in a LDC like Bangladesh is that most people work in agriculture. The share of agriculture (inclusive of forestry and fishing) in employment decreased from roughly 85 percent in 1961 to 66 percent in 1991. Over the same period, the shares of manufacturing and (non-personal) service employment increased. The observed composition of employment over time in Bangladesh is consistent with the well known study of Syrquin and Chenery (1989) on the relation between the level of development and the structure of employment. The changes in the domestic structure of employment /production contributed to dramatic changes in the composition of Bangladesh export. In the next chapter, we focus in the composition of export.

Table 3.3 : Structure of employment in Bangladesh

Major Economic Sector	Structure of employment in percent	
	1961	1991
Agriculture, Forestry, Fishing	84.61	66.0
Mining, Quarrying	0.005	0.029
Manufacturing	4.81	11.81
Electricity, Gas, Water	0.07	0.08
Construction	0.55	1.05
Trade, Hotels, Restaurants	3.67	8.54
Transportation, Storage, Communication	1.21	3.21
Finance, Business, Services	0.059	0.59
Community, Personal Services	4.60	3.81
Household Sector	0.40	4.48

Source: BBS 1973, 1993.

3.3.3 Labour policies and human resource development

Low labour productivity and poor industrial relations are important constraints on industrial development and export expansion. Labour unrest and the politicisation of labour disputes further compound the problems. There is an urgent need of labour market reforms in Bangladesh. In 1992, the government of Bangladesh awarded a pay increase to civil servants, which set of demands for a similar increase for workers in other sectors. The 'wages and productivity commission' was created to advise on the wage awards for public enterprises and to suggest a minimum wage for the economy as a whole. The increases in real wage in the last decade was not matched by comparable increase in the labour productivity. This has adversely affected the competitiveness of Bangladesh vis-a-vis the rest of the world. The tripartite consultative committee consisting of government, labour unions and management representative should play a more effective role in promoting the labour relationship issues and better functioning of the labour market.

According to the LFS, employment in formal the sector accounts only 9.5% of labour force (4.8 million) of which about 30% is in the public sector. The level of formal sector employment declined from 5.8 million in 1986 to 4.8 million 1990. To strengthen the external competitiveness, the formal sector employment must be raised, because the informal sector mainly produces non-traded goods and services utilising unskilled labour.

Availability of skilled human resources is an important precondition for rapid economic growth. The basic indicators of human development such as literacy rate and indices of health and nutrition are extremely low in Bangladesh. The human development index for Bangladesh India and Pakistan are respectively 0.309, 0.383, and 0.393 (UNDP 1994)

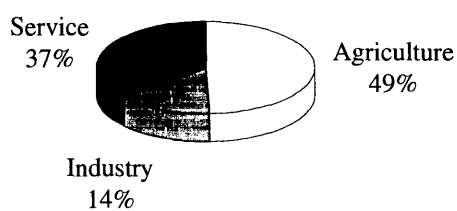
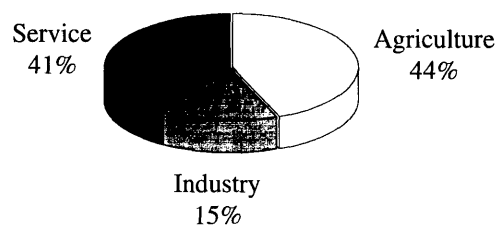
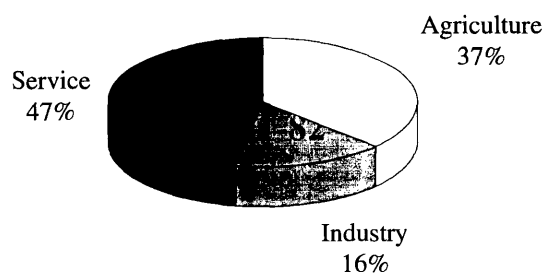
The ability of a country to effectively exploit non-human resources is dependent on, among other things, the managerial and technical skills of its people. Hence technical and vocational training scheme specially relating to the export oriented industries must be adopted in both the private and public sectors.

3.4 The Structure of Output

Bangladesh is one of the least developed countries in the world supporting a population of 114 million with per capita income of 220 US dollars in 1992 (World Bank 1994). In this section we focus on the performance of the economy with particular attention to the composition of GDP in Bangladesh. In addition an attempt has been made to relate the composition of GDP with the composition of exports and chart 3.1 present the the percentage share of GDP comprising the three sectors.

Chart 3.1 The structure of GDP

(at constant prices 1984-85)

1972-73**1981-82****1991-92**

Basic indicators of Bangladesh is provided in appendix A 1

3.4.1 Agriculture

Agriculture is the dominant sector of the economy, which is employing 66 percent of economically active population and contributing 37 percent to GDP in 1991. Agricultural technology is still heavily reliant on traditional technology. Labour productivity is low in agriculture because of the use of primitive technology and low land-man ratio (0.25 acre). The average annual agriculture growth rate was only 2.16 percent during 1972-73 to 1991-92 (BBS 1993). Agricultural export including jute, fish and prawns, tea, vegetable and leather contributed more than 35 percent of total exports in 1991-1992 (EPB 93). The agricultural sector consists of the following sub-sectors.

- **Crop**

The crop sector represents almost 79 percent of agricultural GDP of Bangladesh. There has been a significant increase in rice output which has made the country nearly self sufficient in food grain production. This has been made possible by the introduction of high yielding varieties (HYV) of seeds and expansion in coverage of areas under modern production technique.

- **Livestock, Forestry and Fishery**

Livestock sector plays a vital role in the economy of Bangladesh. More than 20 percent of total population depends on livestock directly or indirectly for their livelihood. Gross value added of livestock and poultry sector was 7.39 percent of total agricultural value added in 1991-92. Hides skin and leather have been the important exportable since 1947. The share of leather in total merchandise export was 7.25 percent in 1991-92.

Gross value added from the forestry sector in 1991-92 was Tk 13,147 million, in constant price of 1984-85, which is 6.65 percent of total agricultural value added.

Fish, an important part of the Bangladesh diet, is a growing export industry. In 1991-92 fisheries sector's contribution to agricultural GDP was 7 percent at constant price of 1984-85 (BBS, 1993). Frozen fish was one of the main items of export and it fetched 6.55 percent of export earnings in 1991-92.

3.4.2 Infrastructure

Inadequate physical infrastructure is a serious hindrance to economic development as well as export promotion in Bangladesh. Infrastructure is the key factor for proper and timely shipment of exportables, and its insufficiency acts as a major impediment as exporters, frequently report. Often vegetable and other agriculture items cannot be transported properly to the place of shipment. Exporters complain about the inadequacy of feeder road and the transport system. The combined share of construction, transport and communication in GDP has gone up to about 18 percent in 1992-93 from 13 percent in 1973-74.

3.4.3 Industry

Industrialisation in Bangladesh has been small in scale. However, quite a few of large scale industries based on both indigenous and imported raw materials have been set up. The notable ones are jute and cotton textile, paper and news-print, sugar, cement, chemicals, fertilisers and tanneries. Bangladesh is also known to have a tradition of cottage industries encompassing handlooms, carpet making and shoe-making. The average annual growth rates in the industrial sector was 9.2 percent in 1973-75 which was followed by a low growth rate of 2.3 percent, during 1975-80. The main reason behind the achievement of a higher growth during 1973-75 was the maximum utilisation of existing capital stock that resulted in continuous decline in the capital-output ratio (Economic Survey 1992-93). In 1980s, the annual average growth rate was around 4.5 percent.

The non traditional export- oriented industries have marked an impressive growth in recent years. The average annual growth rate of non-traditional export was more than 32 percent during 1983 to 1993 as against 6 percent for traditional export. The volatility in traditional export is high and this sub-sector has suffered negative growth rates in some years. The performance of non-traditional ready made garments (RMG) has been extraordinary. The garment industry is now the largest employer which provides jobs to one million workers (80 percent are female).

3.4.4 The service sector

The service sector includes services related to trade, catering, banking, insurance, owner occupied housing, public administration, defence and other miscellaneous services. The major structural change in the economy occurred when the contribution

of agriculture declined below 50 percent in the late 1970s from nearly 80 percent in the early 1970s. In 1981-82, the service sector's contribution to GDP was 41 percent while in 1991-92 its contribution increased to nearly 47 percent. The average annual real growth rate of the service sector was 4.4 percent during the period of 1980-89. The construction sector's contribution to GDP increased from 4 percent in 1980-81 to 6.1 percent in 1992-93. The transport and communication sector contributed 11.8 percent in GDP while trade services' contribution was 7.5 percent in GDP in 1992-93 at constant market price of 1984-85. During 1972 to 1992, the contribution of non-factor services in export fluctuates between 5 and 22 percent (World Bank 1994).

3.5 The Composition of Expenditure

This section analyses the composition of aggregate expenditure in Bangladesh economy and discusses the issues related to the balance of payment.

3.5.1 Consumption and investment expenditure

Historically, the investment rate in Bangladesh has been very low, averaging about 12 percent of GDP. This is the lowest domestic investment rate in South Asia. In 1992, domestic investment as a share of GDP was 10.3 percent in Bangladesh, 38.3 percent in Bhutan, 21.9 percent in India, 20.7 percent in Pakistan and 23.4 percent in Srilanka at 1987 constant market prices (World Bank 1994). For achieving the desired growth in the economy at 6 to 7 percent, overall investment rate in Bangladesh must be raised to at least 20 percent of GDP (Bhuyan and Khan 1995).

In the pre independence period of 1960 to 1970, it was observed that Bangladesh financed over 70 percent of total investment from its domestic resources¹ (Alamgir and Berlege 1972). Domestic saving and foreign capital inflow changed remarkably in the post-independence era. Although per capita income during 1981-1986 was only 5 percent higher than in the period 1966-1970, per capita consumption was 12percent higher in the former period than that of latter period. This represents a sharp decline in the domestic saving rate from more than 8 percent of GDP in the pre-independence period to less than 4 percent in the post independence period. Table 3.5 shows that the saving rate is very negligible at around 3% in Bangladesh.¹

¹Only in 1960-61, the dependence on foreign capital increased to 35percent of total investment.

Table 3.4: Consumption, investment and saving in Bangladesh

	1985	1986	1987	1988	1989	1990	1991	1992
Consumption	98.4	97.0	96.8	97.4	98.0	98.0	997.0	96.2
Investment	12.8	12.3	12.5	12.0	12.2	12.1	10.4	10.3
Private	7.4	6.7	6.3	5.6	5.7	5.7	4.6	4.7
Public	5.4	6.0	6.2	6.4	6.5	6.4	5.8	5.6
Domestic Savings	1.6	3.0	3.2	2.6	2.0	2.0	3.0	3.8

Source : Report No. 11569-BD, World Bank (1993)

The World Bank claims that political uncertainty and some government actions such as appreciation of real exchange rate are the main causes of low private investment during the later half of 1980s in Bangladesh. Soaring of government consumption and stagnating revenue were the causes of low public investment. The decline in investment was associated with continued sluggish growth. During 1980's Bangladesh's growth performance was similar to that of Sri Lanka (average 4%), but was lower than those observed in other South Asian countries.

3.5.2. Balance of payment

The two-gap analysis suggests that the foreign exchange gap is a mirror image of domestic saving-investment gap. From Table 3.5 it is evident that the saving-GDP ratio is very small relative to the investment-GDP ratio. Bangladesh has been suffering from balance of trade deficit since independence (1972-73). However, aggregate merchandise exports as a percentage of import has been increasing. The ratio of export to import in 1993-94 increased to 60.46 percent from 43.95 percent in 1973-74. in US dollar terms. Trade deficits were financed by foreign grants, loans and remittances of Bangladeshi national working abroad. Workers remittance from abroad have gradually become major source of financing the foreign exchange gap. Around 237,779 workers in 1992-93 remitted US \$ 944 million which was equivalent to 23.6 percent of total import payments in that year (Economic Survey, 1993-1994).²

3.6 Recent Economic Policy Reforms

Bangladesh experienced a period of nationalisation of industries after independence and a period of denationalisation since 1983. Nationalised industries as a whole suffered with large losses and inefficiency. Political instability, inadequacy of

infrastructure, demotivation, indiscipline, discrimination against small entrepreneurs are some of the identified causes of this dismal picture.

The government macro economic reform and liberalization policies (flexible interest rates, overdue loan classification, value added tax), were initiated in the early eighties but intensified in recent years. The most important reform has been the introduction of a value added tax (15 percent VAT) in 1991-92. Imposition of VAT raised the tax-GDP ratio which contributed to a reduction in the budget deficit. The import duties have been reduced from an average of 89 percent in 1990-91 to 40 percent in 1993-94. Many non-tariff barriers have been removed. Investment procedures have been simplified to open up private participation in energy, telecommunication and domestic air transport. The dual foreign exchange rate, till December 1991, has been unified in January 1992, and the currency has been made convertible in 1993.

The set up of a Privatization Board, a Securities Exchange Commission in 1989 and administrative and legal reforms have brightened the investment climate in Bangladesh. Flexible interest rate policy and subsidised rates have been instituted for increasing the flow of credit and mobilising private savings. The government has promulgated the Industrial Relations Act 1993 to turn the country's labour force into a disciplined force and for speedy disposal of labour issues (Reza, 1995). Foreign direct investment remains at a very negligible level of US \$ 2.1 million. Because of the recent liberalisation measures, including opening up the securities market for portfolio trade, the inflow of foreign private capital increased in recent years.

This chapter presents the basic characteristics of Bangladesh economy with particular attention to the foreign trade sector. Since 1980s Bangladesh has been pursuing an outward oriented development strategy together with certain structural reform programs. In a labour surplus economy like Bangladesh, the agricultural sector is unable to absorb the excess labour supply. So industrial sector is the only means to absorb surplus labour and achieve high growth rate. The strategy of export oriented industrialisation may suit this purpose.

Chapter 4 : Export Characteristics and Growth Scenario of Bangladesh.

4.1 Introduction

The purpose of this chapter is to analyse the major characteristics of the export sector in Bangladesh, identify the patterns of export and GDP growth over time, and assess the effects of alternative government policies on export performance and economic growth.

The current national policy of Bangladesh aims to increase foreign exchange reserve through the development of non-traditional export. The policy represents a shift from ISI to EOI. Outward looking strategies and the growth of non-traditional exports are possible ways to achieve a trade surplus and thus contribute to the foreign exchange reserve position and debt servicing capabilities. Both are crucial to support overall development objectives.

The present chapter is organised in the following way. Section 4.2 analyses the aggregate trend of exports, and economic growth of the country. Section 4.3 deals with the structure of commodity export. Section 4.4 discusses the direction or destination of exports. Section 4.5 assesses the effects of alternative policy regimes on export performance and economic growth. The final section presents the essence of this chapter.

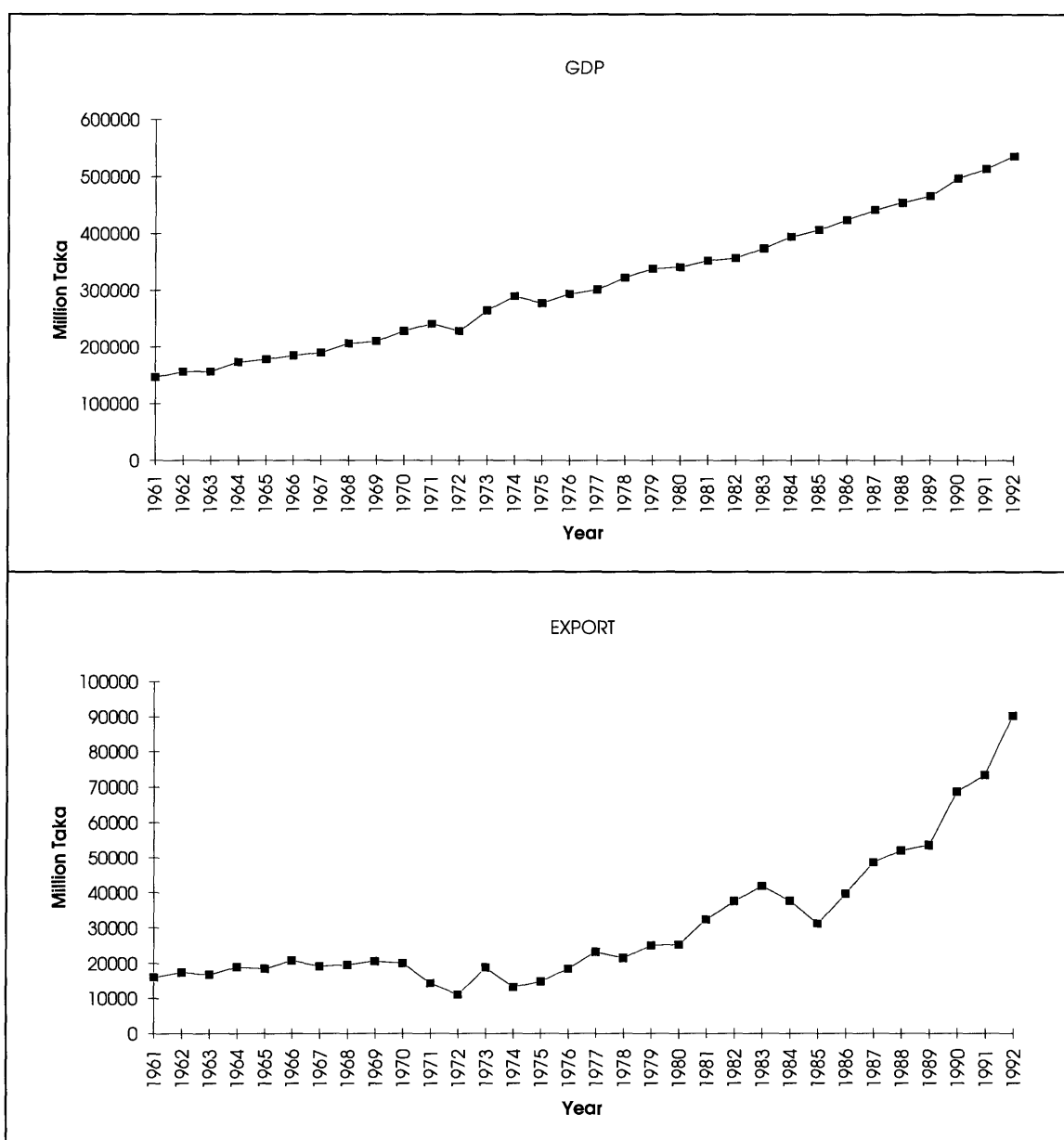
4.2 Export Performance and Economic Growth

This section presents the stylised facts on export performance and economic growth in Bangladesh over the period 1961-1992 and explain the observed patterns in a systematic way by sub-dividing the whole period into pre-liberation and post-liberation period and relating further we relate our discussion with different policy regimes.¹ The historical patterns of the data are presented in figures 4.1 to 4.7. The data on GDP, exports (include goods and non factor services), investment both public and private are measured at constant 1984-85 prices. Our data is on fiscal year basis (July to June).

¹ An econometric analysis of the data is presented in chapter 6.

For simplicity in the following figures we denote the fiscal year 1971-72 by 1972 and so on. Figure 4.1 shows the patterns of export and GDP over the period 1961 to 1992. The volume of export was more or less stable during the period 1961 to 1970, before

Figure 4.1 Gross domestic product (GDP) and export in million Taka at 1984-85 prices.



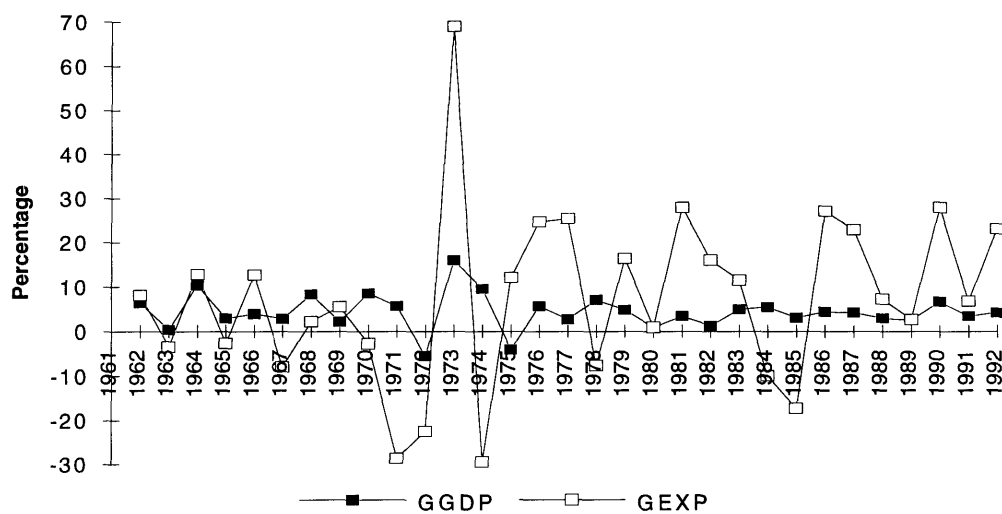
Source: Appendix 4

liberation. During 1970-71 and 1971-72, the quantum of export decreased sharply due to liberation war. Since 1974 a secular increase in export has been observed. Unlike OECD countries, GDP of Bangladesh did not exhibit any cyclical pattern over the sample period. It suggests that the volatilities in foreign economies over the period 1973-1992 were not transmitted to Bangladesh economy through its foreign trade sector. This can be partly explained by the inward oriented nature of the Bangladesh economy and its dependence on subsistence agriculture. The figure indicates a strong positive relationship between the levels of export and GDP. The increasing trend in the level of export was more prominent during 1985 to 1992.

Average annual export during 1961-62 to 1971-72 (preliberation period) was Taka 17936 million while in the post liberation periods of 1972-73 to 1981-82 and 1982-83 to 1991-92 mean exports were Taka 23,036 million and Taka 53,773 million respectively. The first regime in the post-liberation period pursued inward oriented trade policy, while the later regimes were more outward oriented. Significant increases in exports since the early 1980s can be partly explained by the changes in policy regimes.

Time series plots of the macro economic data in levels may not be useful to identify the true relationship among variables because of strong trend components in the data. Hence we compute the growth rates of the variables. Figure 4.2 shows that the export growth falls drastically in the liberation year 1971 and rises sharply in 1973. More volatility is found in export growth than GDP growth. Fluctuation in the export growth rate is higher in post liberation period than in the pre liberation period. There were negative export growth rates of -28.66 and -22.45 percent in 1970-71 and 1971-72 respectively. Due to inclusion of these two negative growth rates in the pre liberation period the country experienced an annual average export growth rate of -2.4% during 1961-62 to 1971-72. Export grows enormously in 1972-73, due to massive investment in the export sector financed by foreign funds. Again in 1973-74, the country faced a negative export growth of -29.4 percent as a result of natural calamities and famine coupled with political unrest. But in the post liberation period (1972-73 to 1991-92) the country achieved more than 12 percent real average annual growth rate of export. The average rate of growth of export was 7.5 percent during the whole sample period of 1961-62 to 1991-92 in real terms. With the exception of few years, the growth rate of GDP and the growth rate of export show a weak positive relationship.

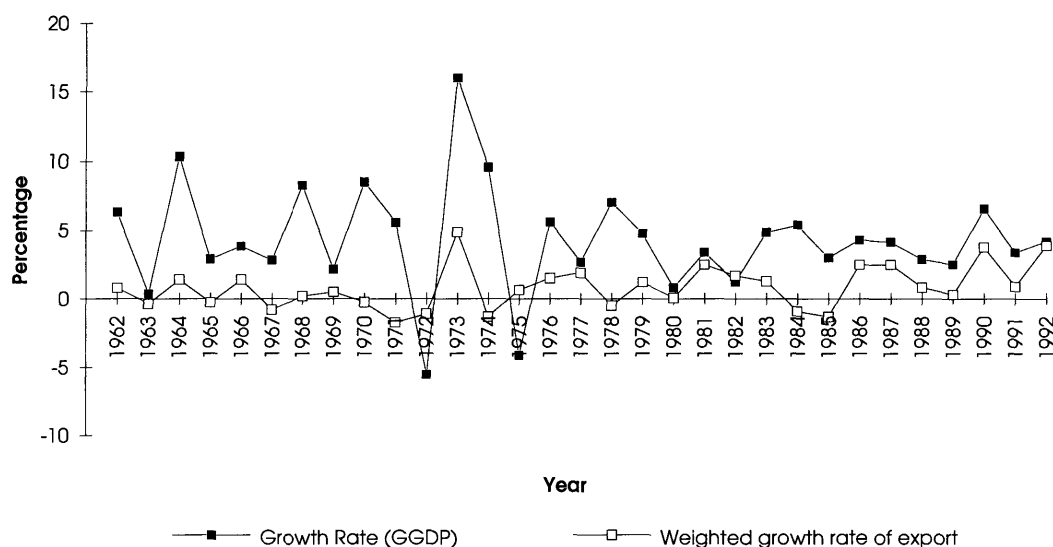
Figure 4.2 Growth rate of GDP and growth rate of export



Source : Appendix 4.

We also plot weighted growth rate of export and GDP growth rate in Figure 4.3. In our econometric model (see chapter 5), a key variable of interest is the weighted growth rate of export which is the product of the share of export in GDP and the growth rate of export.

Figure 4.3 Growth rate of GDP and weighted growth rate of export

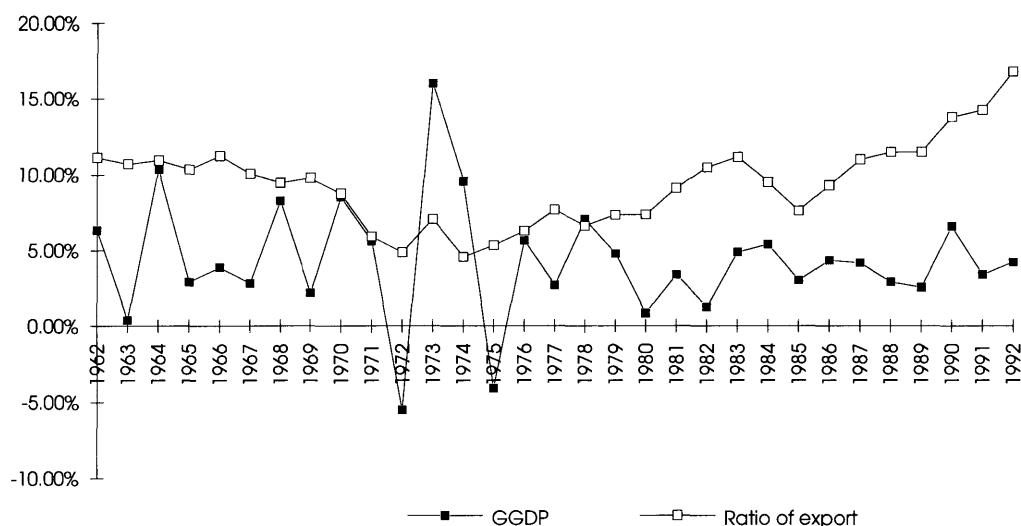


Source : Appendix 4

Figure 4.3 shows that the weighted growth rate of export follows more or less similar pattern as the GDP growth rate. In general, we observe a positive relationship between weighted export growth and GDP growth in Bangladesh.

Figure 4.4 shows that export as a percentage of GDP varies between 4.3 and 16.4 percent. The average percentage share of export in GDP was 9.3 during 1961-62 to 1971-72 and 9.4 during 1972-73 to 1991-92. But the average share of export was high in 1983 to 1992. During this period the share was 11.7 percent while during 1973 to 1982 it was 7.2 percent only.

Figure 4.4 Growth rate of GDP and ratio of export to GDP

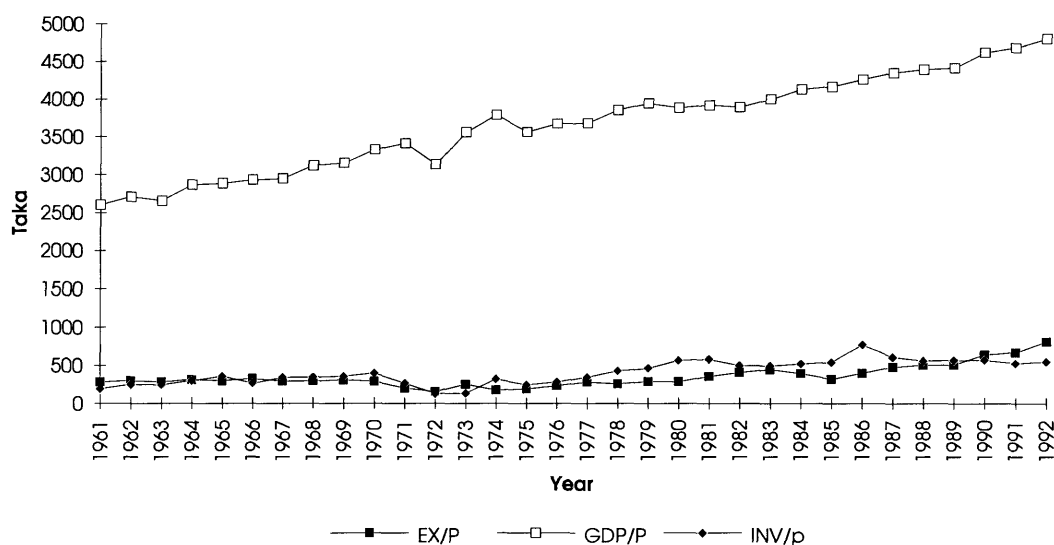


Source : Appendix 4.

From Figure 4.4, it is observed that during 1969-70 to 1971-72, there was a sharp decline in export performance due to natural calamities (tidal waves) and liberation war. The export share of GDP showed an increasing trend after 1974.

In Figure 4.5, we illustrate the patterns of per capita GDP, per capita export and per capita investment. All variables show moderate increasing trend with the exception of few years. The increasing trend of per-capita GDP and per-capita export is more prominent after 1985 indicating a strong positive relationship between the two variables. Mean per capita GDP, per capita export and per capita investment were Tk 4391, Tk 517, and Tk 572 respectively in post-liberation period.

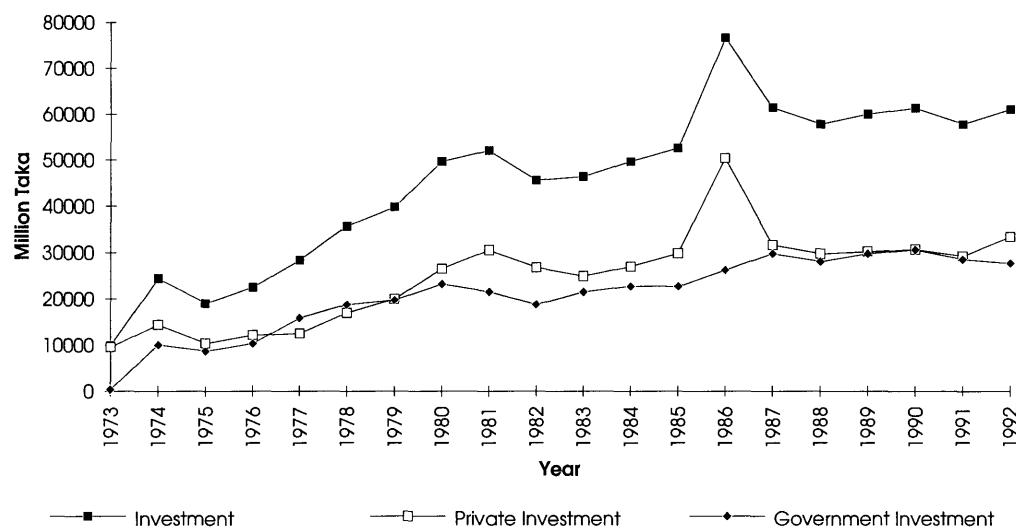
Figure 4.5 Per capita GDP, per capita export and per capita investment in constant 1984-85 price



Source : Appendix 5.

Figure 4.6 shows that the pattern of total investment closely follows the pattern of private rather than public investment. Both components of investment increased sharply during 1973-74 and 1985-86 due to increased domestic saving and foreign capital inflow. The average share of private investment is greater than public investment. The average investment during the pre-liberation period was Tk.19,048 million and in the post-liberation period was Tk.45,667 million in real terms.

Figure 4.6 Total, private and public investment in million Taka

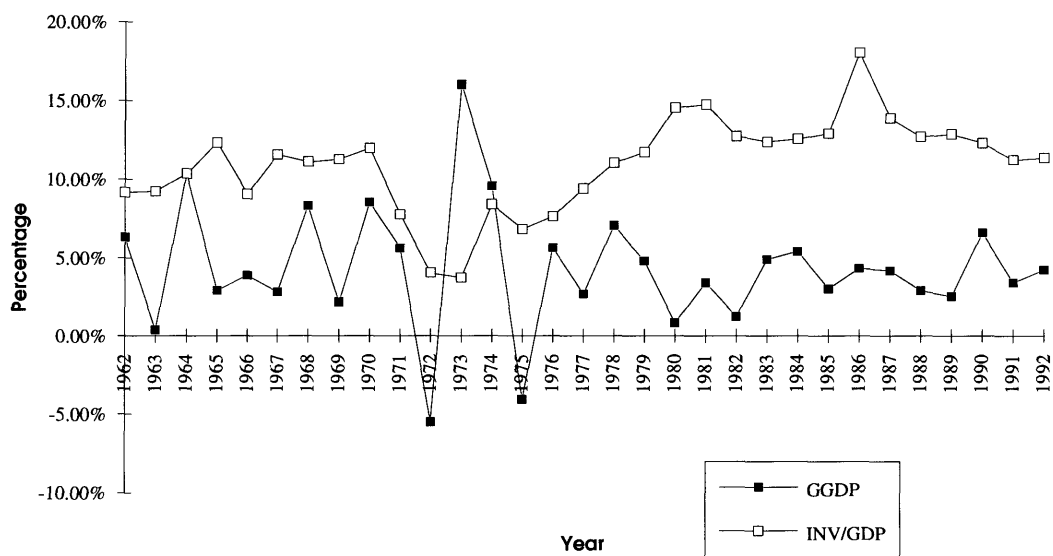


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Source : Appendix 4.

Figure 4.7 shows the relationship between the investment-GDP ratio and the growth rate of GDP. It is not possible to detect any systematic relationship between the two variables from the figure. The investment-GDP ratio varies from 4 to 18 percent. During 1975 to 1981, an increasing trend of the share of investment is observed. In 1985-86 due to heavy foreign capital inflow the share of investment had increased to 18 percent of GDP. The structural adjustment programs, particularly the financial sector reform has been started in mid-1980s. The investment-GDP ratio over the period 1978 to 1992 varies between 11 percent to 18 percent and the growth rate of GDP varies between 0.82 to 7 percent.

Figure 4.7 Growth rate of GDP and investment- GDP ratio



Source : Appendix 4.

4.2.1 Terms of Trade

The external terms of trade has not moved systematically against Bangladesh over the period 1973-1993. However, the commodity terms of trade index (Table 4.1) was never above 100 except in 3 out of the last 20 years. A fall in this index below 100 signifies a transfer of resources from Bangladesh in favour of its trading partners, even when the exchange involves equivalent values. The terms of trade effect have resulted in an average loss of more than 10 percent of export earnings per year in the last 20 years. Due to low price elasticity of export demand, export policies used to influence price, e.g. currency depreciation, would not facilitate export growth. The problem of boosting export growth to a desired rate is 'structural' in nature and hence, non-price commercial policies such as export bonus and other incentives would be more suitable policy instruments for accelerating export growth (Rahman 1990).

Table 4.1 Commodity terms of trade of Bangladesh

(Base: 1979-80 = 100)

Year	Export Price Index (Px)	Import Price Index (Pm)	Terms of Trade (Px/Pm*100)
1973-74	50	56	89
1974-75	62	73	81
1975-76	54	67	86
1976-77	60	66	97
1977-78	69	68	102
1978-79	86	79	110
1979-80	100	100	100
1980-81	86.8	113.5	76.5
1981-82	74.7	118.7	62.9
1982-83	76.1	112.5	69.6
1983-84	89.8	110.9	81.0
1984-85	108.8	110.8	98.2
1985-86	78.9	98.5	80.1
1986-87	81.8	89.9	91.0
1987-88	95.7	91.4	104.7
1988-89	92.6	97.2	95.3
1989-90	95.6	103	92.8
1990-91	101.9	107.4	98.9
1991-92	98.	104.4	93.9
1992-93	96.6	106.7	90.5

Source: Rahman 1990 and Annual Report 1992-93, Bangladesh Bank.

4.3 The Structure of Bangladesh Exports

Though our econometric analysis in chapter 6 and graphical portrait in section 4.2 is limited upto period of 1991-92, but in this section we include export data upto 1993-94 relating the structure of merchandise export. This section analyses the structure of export using three criteria :

- Method of transaction
- Commodity composition of exports and
- Spatial direction of exports

The first method classifies export into three categories based on the nature of export receipts. These are (i) cash transaction, (ii) barter and (iii) special trading arrangement. The second method focuses on the characteristics of exportables by analysing export at the disaggregated level. The third method classifies export according to its geographic destination. Due to lack of the data, the analysis of the structure of export is mostly restricted to the post-liberation period since 1972-73.

4.3.1 The Method of transaction

Overall export are broadly classified into 3 categories according to the method of exchange : cash foreign exchange, barter and special trading arrangement (STA). Barter and STA fall within the category of commodity exchange under the bilateral agreement between the two governments. Both countries exchange goods and services of equal values if not specified otherwise. Barter trade is usually conducted with the former socialist block of which Russia, China, Czechoslovakia and Romania were the major partners. Under STA, goods are exported to the countries like Germany, Switzerland, Egypt, Singapore, Belgium etc., under the commodity exchange agreement. The percentage of Barter and STA transaction is small relative to the share of cash transaction, and it has been decreasing since 1985 due to the transformation of the socialist economies into market economies. During 1977-78 and 1982-83, the share of merchandise export with Russia was above 6 percent of Bangladesh export which decreased to 1.10 percent in 1992-93. The share of Barter and STA in total export during 1991-92 were only 2.2 and 0.7 percent respectively.

Generally, export contracts in Bangladesh are based on FOB (Free on Board basis, where normally freight and insurance charges are excluded in the valuation).²

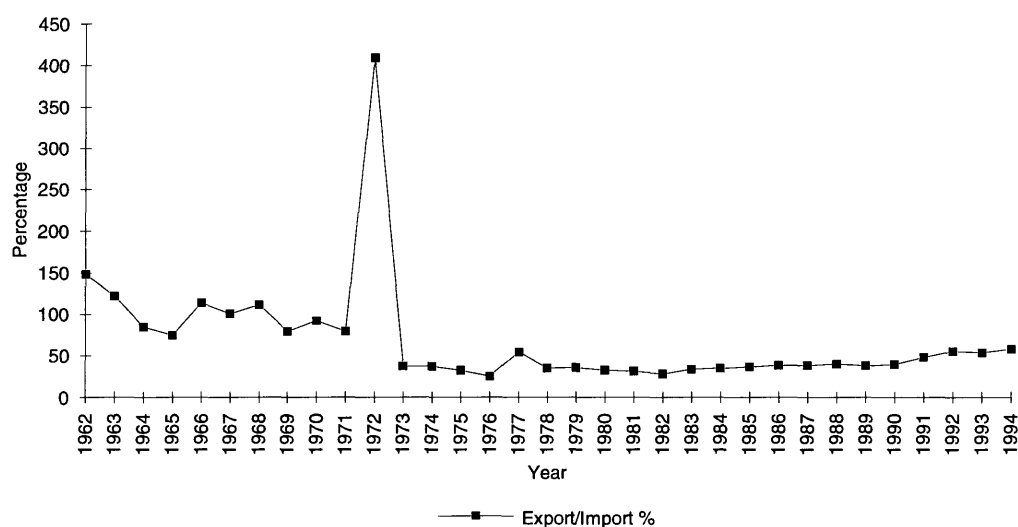
4.3.2 Composition of export

During the quarter century of its partnership with Pakistan (1947 -1971), trade of Bangladesh (former East Pakistan) was divided into two parts;³ trade with West Pakistan, and trade with the rest of the world. The export of Bangladesh was more than 50 percent of Pakistan's export with the exception of 5 years in 1948, 1949, 1951, 1953 and 1968 (Rahman, 1993).

Bangladesh used to export tea, jute manufactures, betel nuts, paper and plastic board, hides and skin , leather , etc. to West Pakistan. Tea was the major exportable item to West Pakistan. Bangladesh imports from Pakistan consisted of rice, wheat, raw cotton, cotton manufactures, chemicals, drugs, medicines, tobacco, metal and ores etc. During that period major international trading partners were USA, European Common Market, Eastern Europe, Middle East, Australia, Japan and Belgium.

Raw jute was the principal export item of Bangladesh (then East Pakistan). Jute manufacturing came in the scene in 1955-56. During the Korean war export receipt of Bangladesh and Pakistan dropped sharply. After the devaluation of Indian currency in 1949, trade between India and Pakistan declined. In the pre-liberation period, in most years Bangladesh experienced a favourable balance of trade.

²The data on export receipts reported in the Bangladesh Bank publications differ from those estimated from customs returns. The Export Promotion Bureau and the Bureau of Statistics, measure export as the shipment of goods recorded in the customs return. The Exchange Control Department of Bangladesh Bank records the export receipts when the actual payments are received.

Figure 4.8 Merchandise export as a percentage of import

Source : Appendix 6

Figure 4.8 shows that export as a percentage share of import lies between 150 and 60 percent during the pre liberation period (1962 to 1971). In the post-liberation period export as a percentage of import varies between 25 to 57 percent. In the 1990s export as a percentage of import showed an increasing trend.

In the pre-liberation period, there were few products in the export basket of Bangladesh, such as raw jute, jute goods, hides and skin, leather, fish, tea, cotton-spices, etc. Raw jute, jute goods, fish and tea covered almost 96 percent of total export in 1973-74. Since then the policy makers have recognised the need to promote export of non-traditional goods.

Traditional exports of Bangladesh include those which historically accounted for 90 percent of her export earnings until 1980. During that period such items as cotton textiles, frozen fish, newsprint, urea fertiliser, extract from oil and gas accounted for less than 10 percent of total exports. These items together with others were classified as non-traditional items and progressively become significant. Traditional primary products are raw jute and tea. Jute manufacturing is classified as traditional exports using the global market share test. But jute goods have a higher price elasticity of demand and it constituted nearly 30 percent of world export of jute goods. Bangladesh was well-known as a country of Golden Fibre (jute).

Non-traditional export items again may be subdivided into manufacturing and primary product. The former includes readymade garments, leather products, electronics,

chemical products, handicrafts etc., while the latter comprises of fish and fish products, vegetables, fruits, crude fertiliser, tobacco, spices, animal feed etc. Leather goods and certain jute products (e.g. carpet) display high foreign income and price elasticity of demand. Bangladesh as a small open economy faces infinitely elastic demand curves for those exportables. These are classified as non traditional exports. In late 1980s non-traditional items such as ready made garments, knit wear, frog legs, fish products, chemical products, paper and allied products, urea fertilisers, handicrafts, naphtha furnace oil and bitumen became predominant in the export basket.

According to the Export Promotion Bureau's classification currently most items fall under the category of non-traditional export. excepting raw jute, jute goods (excepting few) hides and skin and tea. The non-traditional commodities comprises 84 percent of commodity export in 1992-93 where as it was 31 percent in 1982-83. Non traditional export growth is higher than traditional ones. The level of non-traditional exports from the country increased from US\$ 196.83 million to US\$ 1582.73 million between 1981-82 and 1991-92. which shows over eightfold increase in non-traditional export earnings within a decade. It grows by 25.32 percent in 1992-93 while the growth rate of traditional commodities decreases by 2.88 percent in dollar terms (EPB 1993).

Export of consumer goods and material for consumer goods comprise major portion of merchandise export. In 1991-92 the share of capital goods and material for capital goods was only 4.12 percent (BBS, 1993).

4.3.3 Export characteristics of prime commodities

(i) Ready Made Garments (RMG) : Though the contribution of RMG is highest in export receipts presently, but it depends almost entirely on importation of fabrics and other accessories. This import dependence is acting as a great impediment on expansion of markets for garments. There is enough scope for diversifying the production of ready made garments in line with the requirement of the international market with Japan and Scandinavian countries. Currently, the main importing countries are USA, Canada and EC countries. The share of RMG including Knit wear was 57.36 percent in 1992-93.

(ii) Jute goods : Jute and Jute goods are the important traditional export item of Bangladesh. Before 1987, jute represented the highest share in total export. The share of jute goods decreased from 54 percent in 1973 to 12.54 percent in 1992-1993. The principal export market for these products are Pakistan, USA, CIS countries, Syria,

Sweden, Yemen, Egypt, China, Iraq and India. Owing to the recession in early 1990s, demand for jute and jute goods has slackened in these countries.

(iii) Hosiery products and knitwear : This is one of the important exportable occupying the third position in 1992-93 export earnings. Germany, USA. and UK., Japan, UAE., France, Denmark are some of the major export markets. Its share is included in RMG. But seperately it contributed more than 8 percent in 1992-93.

(iv) Frozen fish : In 1992-93, frozen fish was considered as the fourth largest export item. The principal importing countries are UK., Singapore, Saudi Arabia, Hongkong, Oman, USA, Japan, UAE, Qatar and Kuwait. Frozen fish contributed more than 7 percent while all frozen food including fish contributed 9.49 percent in 1992-93.

(v) Leather : Leather was the fifth largest export item in 1992-93. The export of leather has been showing an increasing trend in recent years. Principal markets are Hongkong, Italy, Brazil, Uruguay, Spain, France, Taiwan, Japan and Singapore. The contribution of leather was 7 percent in 1992-93.

(vii) Raw jute : In the pre liberation period the contribution of raw jute sector was the highest. During 1972-73 it contributed 35 percent of total export. Due to slakening of demand and instability of price its share came down to 3.48 percent in 1992-93. Singapore, Pakistan, Egypt, Thailand, Russia, India, Brazil, Turkey and Belgium are some of the major importers of raw jute.

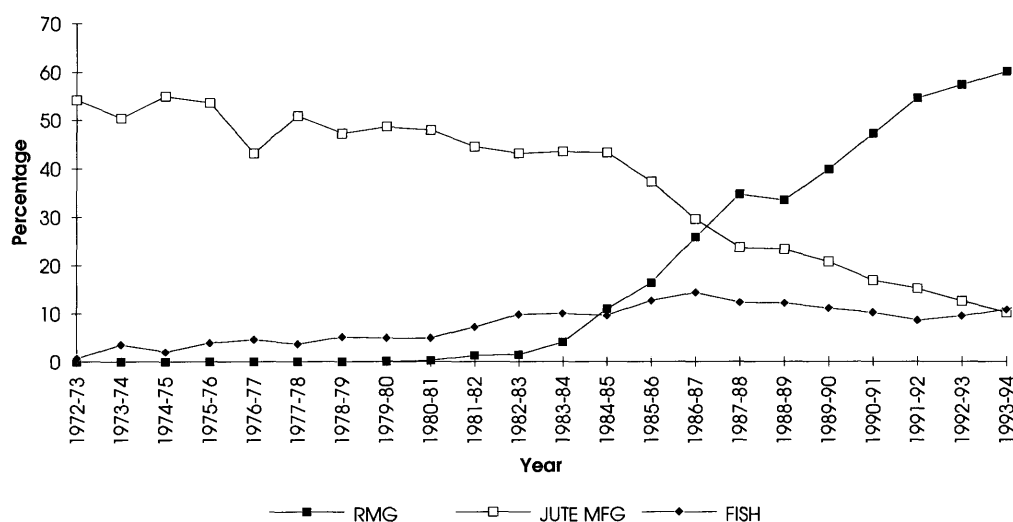
(vi) Chemical products (fertilisers) : The contribution of chemical products mainly fertilisers occupies a significant position. Namely, Jamuna Fertiliser Factory contributed to the expansion of overall export of fertilisers. India, Korea, Malaysia, Philippine, Pakistan, Srilanka, Thailand, Vietnam are some of the importers of Urea fertiliser and some other chemicals. Its contribution in 1992-93 was 2.17 percent.

(viii) Tea : Tea is an important export item of Bangladesh. There is a good prospect for increasing export through marketing of packet tea and thereby popularising the brand name of Bangladesh Tea. Major importing countries are Pakistan, UK., Poland, India, Germany, Iran and China. The contribution of tea was 1.75 percent in 1992-93. But its contribution was more than 9 percent in 1976-77.

(ix) Other important export items are agricultural products (fresh fruits, vegetables), engineering products, naphtha, furnace oil and bitumen (petroleum by-products) and handicrafts.⁴

Figure 4.9, 4.10, 4.11 show commodity specific pattern of exports. Due to lack of the data, the figure represents the pattern for the post-liberation period (1972-73 to 1993-94) Figure 4.9 shows the dominant position of jute manufacturing until 1987. After that its share drastically fall to 10 percent in 1993-94. The share of ready made garment dominated since 1987, and recently occupying more than 60 percent of total exports. Frozen fish is also a growing sector occupying 10.79 percent share in 1993-94. This non-traditional primary item is able to fetch a good value form overseas buyer. The growth rate of frogen food, such as frog legs, fish, shrimps, shark-fins and fishmaws, grow between 25 to 158 percent in dollar terms in 1992-93.

Figure 4.9 Share of readymade garments, jute manufactures and fish in percentage

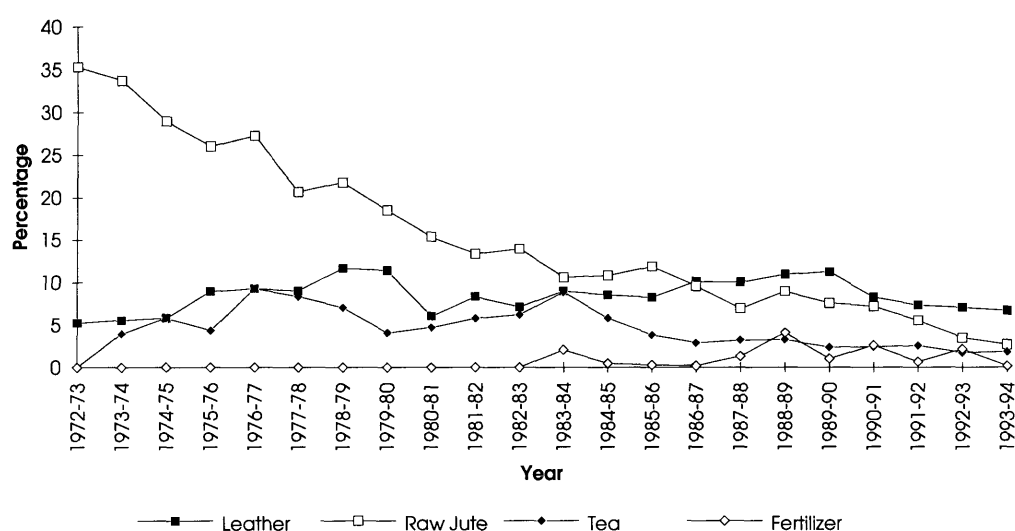


Source : Appendix 8.

⁴ It was decided in 1992-93 concerted effort should be made from exports of engineering consultancy in the area of construction and design work and computer software services.

In figure 4.10, we observe a sharp decreasing trend in the share of raw jute over time. Its share decreases from 35 percent in 1972-73 to 3.48 percent in 1993-94. This sharp decrease is due to some external and domestic factors, such as inelastic and decreasing demand, reduction in prices, disincentive to invest in primary sector etc. In addition to the long term decline in its share, jute export has been a major resource of fluctuation in foreign exchange earning. In view of the predominance of Bangladesh in the world market for raw jute, a more careful policy for stabilisation of prices and quantities through the operation of buffer stock should receive urgent attention (Khan and Hossain 1989). Jute sector has a huge employment and other domestic linkage impact. We also observe high volatility in the share of fertilizer export. The share of leather remains more or less stable while the share of tea shows a declining trend during 1984-1994.

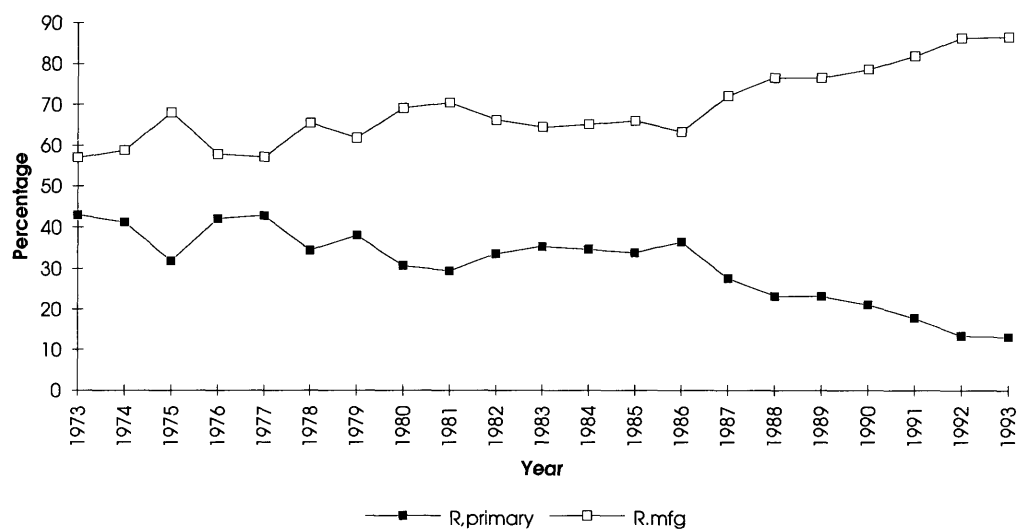
Figure 4.10 Percentage share of leather, raw jute, tea and fertilizer



Source : Appendix 8.

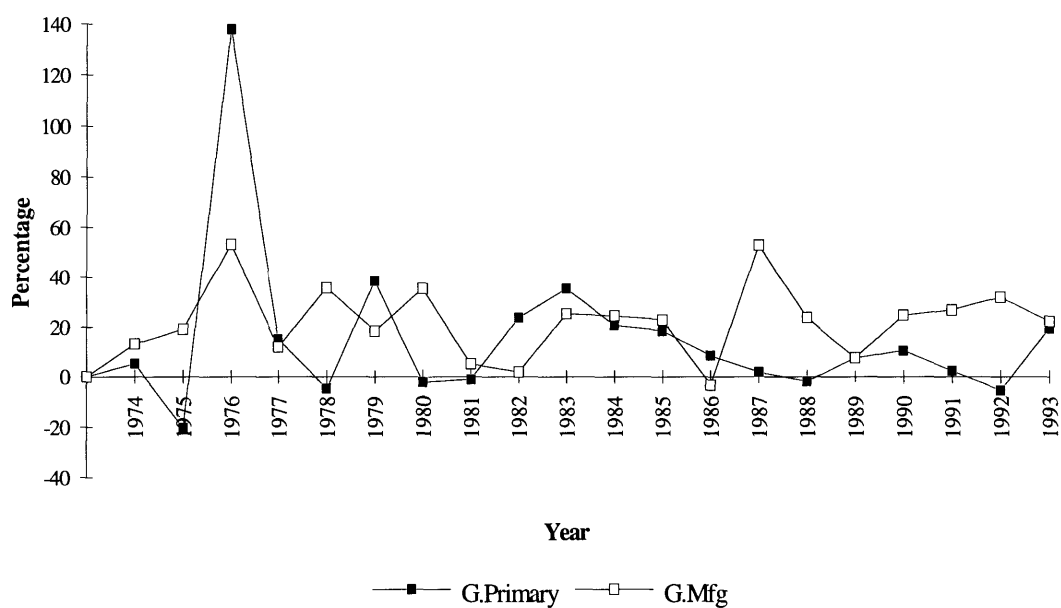
The shares of primary and manufacturing exports over time are shown in figure 4.11 and 4.12. The share of manufacturing shows a rising trends from 1986. While an opposite trend is observed for primary exports. during the same time. In 1993, share of primary exports was below 14 percent while manufacturing exports was above 86 percent. After liberation, in 1972-73, the share of primary export was more than 40 percent of merchandise export.

Figure 4.11 Percentage share of primary and manufactured exports



Source : Appendix 9.

Figure 4.12 Growth rate of primary and manufactured export



Source : Appendix 9

Figure 4.12 shows more volatility in case of primary export growth than that of manufacturing exports. The pattern shows that the growth rate of manufacturing export was higher than the growth rate of primary export after 1986. Primary export suffered from negative growth rate for several years.

4.3.4 Product diversification

Different export commodities will provide different stimuli, according to the technological characteristics of their production. The composition of export has an influence on the extent of other secondary changes elsewhere in the domestic economy beyond the primary increase in output of exportables (Meier 1984). All export commodities do not have same forward and backward linkages. The export-led growth involves some stimulus to other industries, which would not otherwise expand. For example when textile grows, it creates sufficient demand for inputs, such as cotton, dyestuffs, accessories etc., which may stimulate domestic production of those inputs which is named by Hirschman (1958) as backward or consumption linkage. Again for example mineral and timber exporters of Venezuela are trying to exploit forward linkages and divert part of their waste and raw materials into inputs for domestic industry (Gillis, et al 1983). Usually the linkage effects of primary goods on the other sectors of the economy are weaker than that of the manufacturing goods.

Diversifying the commodity composition of developing countries' exports is one of the main policy measures used in an attempt to reduce the instability of exports (Love 1992). The traditional hypothesis is that the export instability is detrimental to the process of economic growth. Export fluctuation in Bangladesh is partly demand induced. Primary export is price inelastic and creates more export instability than manufacturing ones. The greater the instability of export earnings, the lower will be the incentive to allocate resources in export sector. The uncertainty created by fluctuating export would mean unstable 'stop-go' policies in investment which will negatively affect capital formation and ultimately economic growth. Opposite opinion also stems regarding trade-off between stability and growth in order to attain stability and growth in export earnings, a country may need to diversify its export. The principle of diversification is incompatible with the principle of specialisation. The growth rate is expected to be higher if the country specialises in few commodities in which it has significant comparative advantage. However, specialisation in few primary products may lead to unstable export earnings. The diversification of exports, on the other hand, generates less unstable flow of export earnings at the expense of

lower GDP growth. Bangladesh experienced unstable export demand for jute. Bangladesh export earning depends on few products, most of which are subject to both domestic supply shocks and fluctuations in international demand and prices. It is widely recognised that export should be diversified. In the area of product diversification, some progress was made between 1972-73 and 1993-94. In 1972-73, the number of export products were 32 which increased to 115 in 1993-94. New export products include ready made garments, knitwear, specialised textile, frozen fish, salted and dehydrated fish, tobacco, chemical fertilisers, jute carpet, stainless steel, cutlery, silk fabrics, packet tea and sanitary ware, P.V.C. pipes, ceramic table ware, terry towels, audio-video cassette, artificial flower, footwear, electric bulbs, rice, toys, etc.

4.4 Direction of Export

This section analyses the direction of export based on major geographic destinations of Bangladesh exportables. The region distribution of export reveals that EC was the biggest buyer of Bangladeshi products followed by North America region. Other buyers, in order of importance, are Asia, Middle-East, Africa, Eastern Europe and Oceania.

Table 4.2 shows the direction of exports by countries. The table reveals heavy dependence of Bangladesh export on the US market. In 1993-94, Bangladesh products were exported to 107 different markets, but the US market alone accounted for 29 percent of total exports which was followed by Germany, UK, Italy, France, Netherlands, Belgium, Hongkong, Japan and Canada. Pakistan and Russia also contributed significantly in our export earnings. Second categories of another 10 markets are Singapore, Denmark, Iran, Russia, Spain, Australia, Pakistan, Turkey, Brazil and Syria. Percentage share of merchandise export to India, Nepal, Pakistan and Srilanka were only 0.41, 0.12, 1.21, and 0.36 respectively in 1991-92. In 1992-93, export of Bangladesh to all these South Asian nations was only 2.10 percent of aggregate exports despite low transport cost of trading with these countries. Bangladeshi exporters are possibly unable to penetrate into the markets of neighbours because they have also comparative advantages in labour-intensive products such as garments, leather, tea etc.

Table 4.2 Major destination of Bangladesh exportables (percentage share)

	1972-73	1982-83	1993-94
	% share	% share	% share
U.S.A.	20.49	11.49	29.00
Germany	3.03	2.00	10.86
U.K.	7.62	4.51	10.23
Italy	4.12	4.68	6.73
France	2.51	1.06	6.22
Netherlands	2.34	1.86	4.14
Belgium	6.60	4.41	3.88
Hongkong	0.25	0.66	2.85
Japan	1.92	6.56	2.41
Canada	2.02	0.91	2.26
Subtotal	50.89	38.19	78.59

Source :Export Promotion Bureau (1994)

ource :Export Promotion Bureau (1994)

4.5 Government Export Policy

4.5.1 Objectives

The biennial export policy of the government of Bangladesh incorporates export objectives, targets and strategies. The government attempts to implement the policy and programs pertaining to export, such as diversification of products, improvement of quality, expanding of market penetration as well as requisite structural

transformation and technology transfer for backward orientation in the export oriented sectors.

The main objectives as outlined in the Export Policy Order of 1991-93, 1993-95 are summarised as follows.

- (i) To narrow down the gap between export earning and import payment by target increase of export nearly, 25 percent yearly.
- (ii) To develop marketability of exportable through product diversification and quality improvement.
- (iii) To establish backward linkage with the export-oriented industries and service sector for utilisation of more local contents.

In order to achieve above objectives the government adopted following strategies:

- (i) Simplification of export procedures and strengthening support services through reducing regulatory role of the government.
- (ii) Rationalisation of the value of Taka to make the export trade more attractive.
- (iii) Creation of Export Promotion Fund (EPF) for strengthening the export development activities.
- (iv) Encouraging establishment of backward linkage industries through reactivating the process of utilisation of locally available raw materials.
- (v) Participation in the international trade fairs, single country exhibitions, specialised fairs, and sending businessmen's delegations abroad for expansion and consolidation of existing markets and creation of new markets.
- (vi) Expediting the process of balancing, modernisation, replacement and expansion (BMRE) of existing wet-blue producing tanneries and switching them over to finished leather producing and exporting units.
- (vii) Quickening the process of improved traditional/semi-intensive method of shrimp cultivation.
- (viii) Allowing import of high quality foundation tea for blending and the brand name of Bangladesh tea through marketing overseas.

- (ix) Strengthening measures to improve quality, increase production and expand market for agricultural produces.
- (x) Undertaking activities for increasing export of computer software, engineering consultancy and services.
- (xi) Expediting steps for export of labour intensive electronic and engineering products, keeping in view the market requirements in USA and other developed countries.

4.5.2 Export incentives

To achieve the export target, the government provides a set of incentives. Some of the major incentives are export-finance, export-credit guarantee scheme, concessional interest rate for credit, income tax rebate, back to back letter of credit for importation of raw materials for export oriented industries, foreign exchange for business travel, duty-drawback, cash-assistance, bonded ware-house facilities, rebate on insurance premium, freight rebates, tax holidays etc.

Though these incentives have benefited exporters, but it has not led to a broad based development of export (Roy, 1993). Some evidence shows that incentives have gone enough to encourage sustainable development of manufacturing exports of a broad range of commodities. Government policy shows a consistent improvements in the incentives to exporters, specially after the new industrial policy of 1982 and 1986.

The study by Rahman (1993), reveals that incentive structure provided to the exporters is less lucrative than India and Pakistan. For example, both in India and Pakistan export income is fully exempted from income taxes, where as in Bangladesh 50 percent income is deductible from income tax payment. Pakistan and India got special banks to cater specific needs of export credit and exporters get incentive like importation of machinery for export oriented industries without any duty.

4.6 Human Resource Export and Economic Development

Human resource export of Bangladesh is a major source of foreign exchange earning which finances economic development and trade deficit. Human resource exports can help Bangladesh in the following ways: (i) to solve the problem of unemployment (ii) to increase foreign exchange reserve (iii) finance imports payments (iv) to improve human skills (v) to accelerate the rate of capital formation.

Beginning with a relatively small amount of remittance of US\$ 11.8 million in 1974-75, the size of foreign remittance reached a total of US\$ 848 million in 1991-92. Most of the workers remittances come from the oil rich Middle Eastern Countries, as they are requiring both skilled and unskilled workers in all conceivable social and economic fields covering agriculture, communication, health, housing and industries.

Table 4.3 Number of persons leaving for abroad on employment and their remittances under Wage Earners Scheme.

Year	No.of Persons	Remittances	
		Millon US\$	Million Taka
1977-78	16908	102	1542
1978-79	24610	124	1888
1979-80	27610	249	3855
1980-81	38456	379	6197
1981-82	68362	412	8397
1982-83	63551	617	14802
1983-84	50122	596	14910
1984-85	69046	439	11465
1985-86	78422	555	16611
1986-87	60545	596	21363
1987-88	73677	737	23039
1988-89	86475	771	24774
1989-90	110014	761	24961
1990-91	96691	764	27256
1991-92	185106	848	32415
1992-93	237779	944	36969

Source: 1. Economic Trend, Bangladesh Bank 1994

2. Bangladesh Economic Survey 1993-94

Table 4.3 shows a decline of the number emigrants in 1982-83, 1983-84, 1986-87 and 1990-91 due to leak of job opportunities in OPEC countries following a fall in oil prices, fall in wages, Iran-Iraq war and Kuwait-Iraq war. From a small base of 16,908 overseas jobs in 1977-78, the level of foriegn employment continued to grow

unabated to a peak of 2,37,779 in 1992-93 with a remittance of US\$ 944 million. More than 47 percent of imports in Bangladesh was financed by remittances in 1991-92.

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Source: 1. Economic Trend, Bangladesh Bank 1994

2. Bangladesh Economic Survey 1993-94

These wage earners are provided with a set of incentives. These incentives comprise duty free import of some items under baggage rules, income tax exemption, payments of interest on foreign currency accounts, various saving certificates, special development bonds etc. They were also provided with higher exchange rate than the official rate which was called the secondary market rate or the wage earners' rate until

December 1991. The earnings from human resource export is vulnerable to political and economic conditions in Middle Eastern countries. Hence Bangladesh cannot rely heavily on this Wage Earners Scheme as the long term source of foreign exchange.

4.7 Foreign Exchange Regime and Export Performance

Criticism has been focused by the analysts on the phenomenon of overvalued exchange rates and quantitative restriction on imports in developing countries. The analysts argue that those policies discriminate against exports, they inevitably promote non-uniform protection for different products which in turn encourages a misallocation of resources, which ultimately constitutes an obstacle to industrial growth and efficiency.

The real effective exchange rate (REER) in taka per US dollar is generally estimated by Bangladesh Bank by adjusting the nominal exchange rate for:

- Price changes in Bangladesh relative to the weighted average of price changes in trading partners.
- Export duties and receipts from export subsidy scheme etc.
- Import tax and premium paid on wage earners rate.

In calculating the REER adjustments have however not been made for the value of certain incentives (tax, holidays, access to bonded warehouse, interest rate subsidies and several other benefits). Thus the REER for exports especially for non-traditional exports is somewhat understated. The REER for non-traditional export during 1973-86 is about 6 percent to 10 percent more favourable than for traditional exports. The traditional exports still are subject to discrimination as compared to non-traditional export. But before independence, in the late 1960's jute manufacturing and other exports qualified for bonus received and real exchange rate was more than twice as favourable as the rate for raw jute (Khan and Hossain, 1989). Discriminatory attitude towards the traditional sector may be one of the causes of its chronic declining share in export after liberation. But the system has greatly improved over the years. Overvaluation of the exchange rate has become small, the multiple exchange rate system has been abolished, discrimination against export has declined sharply and the level of protection has fallen sharply. From 1992 and onwards government is pursuing the liberalization policy. Further research is needed for a proper evaluation of this policy after certain span of time. Maintaining a favourable exchange rate for exports is critical to retain incentives in export production.

The depreciation of real exchange rate in Bangladesh was less than Pakistan and India during 1985-91 which reduced the competitiveness of Bangladesh. India has increased its share of jute export to EC and USA at the expense of Bangladesh (World Bank 1993).

Government of Bangladesh pursued a fairly flexible exchange rate policy since mid-eighties, aimed at achieving macro equilibrium and maintaining a stable real exchange rate with its main trading partners. Bangladesh's trade weighted effective exchange rate depreciated by around 19 percent between 1985 and 1991 (World Bank, 1993). However this depreciation was insufficient to maintain competitiveness in the export market, because other neighbours were pursuing more aggressive exchange rate policies. Rather its purchasing power parity rate appreciated significantly in relation to Indonesia (52%), Pakistan (29%), India (21%), and Thailand (50%). In India there was major devaluation in 1991. Bangladesh is still less competitive today than it was seven years ago when compared to Pakistan (World Bank 1993). Cross country experience indicates that a depreciation of the real exchange rate is also required for successful trade liberalization.

- **Reduction of anti-export bias**

Bangladesh is trying to offer a variety of investment incentives, including export incentives, tax holidays and other tax concession to promote export oriented and other industrialisation. But both public and private manufacturing investment and value added virtually stagnated in absolute and relative terms during the eighties (Bakht and Bhattacharya 1991). Haque and Sahota (1989) find that for 1975-88 import substituting industries were getting higher effective rate of assistance than export oriented industries. Rahman (1992) computed Effective Rate of Assistance (ERA) for 21 industrial sectors using Input-Output table of 1986-87 for Bangladesh. It shows that average ERA for ISI group is 0.78, where as it is only 0.09 for the export industries. It shows therefore ISI group enjoyed ERA several times higher than export oriented industries. Effective rate of assistance (incentives and others) and various demand and supply factors such as world demand, exchange rate, efficiency index, and other non-price factors (market penetration, learning process) and diversification of commodities seem to affect the export performance of Bangladesh.

4.8 Comparison with other South Asian Countries

In South Asian countries external sector development is gaining importance and the export sector is gradually becoming prominent to achieve sustained economic growth.

The main exportable items of these countries are more or less similar in nature. Textile clothing sector occupies a significant position textile and clothing sector contributed more than 50 percent of total exports in Bangladesh, Nepal, Pakistan and Sri Lanka in 1992. The share of primary export declined substantially during 1970 to 1992.

Table 4.4 South Asian Countries' structure of merchandise exports

	Percentage Share of Merchandise Exports									
	Fuels, Minerals		Other Primary		Machinery &		Other Manufac		Textiles	
	metals		commodities		transport equip		tured			
	1970	1992	1970	1992	1970	1992	1970	1992	1970	1992
Bangladesh	1	1	35	18	1	0	64	81	49	72
India	13	8	35	21	5	7	47	64	25	25
Myanmar	7	6	91	92	0	0	2	3	0	0
Nepal	0	0	65	6	0	0	35	94	25	85
Pakistan	2	1	41	20	0	0	57	79	47	69
Sri Lanka	1	1	98	27	0	2	1	71	0	52

Source: World Development Report. World Bank (1994).

The Table 4.5 presents the characteristics of foreign trade of Bangladesh with its South Asian neighbouring countries.

Table 4.6 shows the export performance of Bangladesh and its South Asian neighbouring countries according to Asian development Bank. Sri Lanka and Pakistan have higher percentage export share than Bangladesh, Nepal and India. The average share of ratios of merchandise export in GDP for Bangladesh, Nepal and India are 6.5, 5.5 and 6.2 percent respectively during 1985-1991 in real term. Pakistan and Sri Lanka appear to be more outward oriented than others.

Table 4.5 The Nature of trade between Bangladesh and the South Asian Countries

	Exportables	Importables
Bhutan	Textiles and textile articles	Fruits, textiles and mechanical appliances
India	Vegetable and animal products, mineral and chemical products, hides and skin, leather, textiles, base metals, mechanical appliances, transport equipment, antiques,	Live animals, vegetable products, prepared food stuff, mineral and chemical products, plastic products and rubber, textiles, articles of stones, ceramic products and glass, base metals, mechanised apparatus and antiques.
Nepal	Prepared food stuff, chemical and allied products, textile, transport equipment.	Vegetable products, mechanical appliances, antiques.
Pakistan	Vegetable products, hides and skin, leather, textiles, transport equipment, antiques miscellaneous, manufactured articles	Vegetable products, prepared food stuffs, mineral and chemical products, textiles, base metals, machinery and transport equipment, antiques, plastics & rubber articles.
Sri Lanka	Live animals and vegetables' products, chemical and allied products, textiles, machinery and mechanical appliance, antiques.	Live animals and vegetable products, oils and vegetable tests, plastic and chemical products textiles, articles and precious stones, base metals, machinery and mechanical appliance antiques.

Source: BBS (1993).

Table 4.6 South Asian merchandise exports (as per cent of GDP)

	1985	1986	1987	1988	1989	1990	1991	Ave.
Bangladesh	6.9	5.7	6.2	6.9	6.4	6.6	7.2	6.5
India	4.5	4.4	4.3	5.0	5.9	6.6	7.7	5.4
Myanmar	4.7	4.1	2.7	2.9	3.5	4.1	4.6	3.8
Nepal	6.6	6.0	6.0	6.5	5.5	6.0	6.8	6.2
Pakistan	9.2	11.4	10.5	11.4	11.5	12.2	13.3	11.3
Sri Lanka	22.6	19.7	21.8	21.5	22.6	24.0	24.1	22.3

Source: Asian Development Bank 1993.

From Table 4.7 and 4.8 it is observed that with some exceptions the export growth rate is positively linked with GDP growth, across South Asian LDCs. Most of these countries experienced higher growth rates of export.

Table 4.7 Growth Rate of GDP

(per cent per annum)

	1987	1988	1989	1990	1991	1992
Bangladesh	4.2	2.9	2.5	6.6	3.4	4.0
Bhutan	17.8	1.0	4.7	4.9	4.5	5.0
India	4.3	10.9	5.6	5.2	1.2	4.2
Myanmar	-4.1	-11.4	3.7	2.7	1.3	1.2
Nepal	3.9	7.3	4.2	6.1	5.5	3.1
Pakistan	6.5	7.6	5.0	4.5	5.5	7.8
Sri Lanka	1.5	2.7	2.3	6.2	4.8	4.6

Source : Asian Development Bank 1993

Table 4.8: Growth rate of merchandise exports

(percent per annum)

	1987	1988	1989	1990	1991	1992
Bangladesh	22.4	19.9	1.1	28.2	1.0	14.3
Bhutan	62.2	36.2	-2.0	0.9	-11.2	9.7
India	16.0	13.7	19.5	12.2	0.6	2.1
Myanmar	-19.3	13.8	32.5	15.6	6.9	26.5
Nepal	13.7	19.5	-19.4	39.5	26.0	27.6
Pakistan	23.4	11.9	8.9	12.2	18.1	13.8
Sri Lanka	15.3	6.0	1.9	23.1	8.4	13.9

Source : Asian Development Bank 1993

Though these countries are trying to pursue export promotion strategy, their market share in world export is very meagre. The table 4.9 shows that India's share in total world export is only 0.55 percent, and other countries' shares vary from .04 percent to .07 percent.

There is a considerable scope to enhance exports and foreign investment in these countries. The average growth rates of exports in these countries are moderately on the higher side. The strategy of using trade and foreign investment as a vehicle for regional cooperation and development is gradually getting importance. Asian developing countries absorb nearly 15 percent of Bangladesh exports while contributing nearly 30 percent of its imports; the possibility of expanding trade with Asian and Pacific region is high.

Table 4.9 South Asia's shares of world exports (percentage)

	1985	1986	1987	1988	1989	1990
Bangladesh	0.054	0.044	0.045	0.047	0.044	0.045
India	0.503	0.472	0.475	0.485	0.537	0.552
Myanmar	0.017	0.014	0.009	0.005	0.008	0.010
Nepal	0.007	0.007	0.006	0.008	0.008	0.008
Pakistan	0.149	0.168	0.174	0.164	0.156	0.154
Sri Lanka	0.069	0.058	0.056	0.054	0.052	0.054

Source : Asian Development Bank 1991

4.9 Summary and Concluding Remarks

The graphical representation of the data indicates a strong positive relation between the level of export and GDP. Volatility is more prominent in export growth, rather than in GDP growth. The patterns of GDP growth rate and the weighted growth rate of export show a positive relationship between the two variables. Mean export, export share, per capita export, and export growth are higher in post liberation period. Also mean investment, investment-GDP ratio exhibit the same pattern. Mean per capita GDP, per capita export and per capita investment were higher in 1983-1992 period while the government was pursuing a more open trade and privatisation policy.

Bangladesh significantly increased its manufacturing and non-traditional exports after liberation. Manufacturing exports comprise more than 86 percent of total export in 1993-94. If we divide export into traditional and non-traditional items, non-traditional export comprises 84 percent.

Jute sector had the overwhelming share of export before 1980. The composition changed rapidly. Manufactured item like ready made garments including knit-wear had a share of 61.4 percent in 1993-94 whereas jute sectors share was about 13 percent. Such a quick shift in the structure of exports visibly points out that Bangladesh has the capacity to respond positively to opportunities which may emerge in international market. Such success can be repeated by availing of other similar opportunities. This export success is partly attributed to the macro-economic reforms and export led growth policy of the government. After the success of ready made

garments, attention has been focused on knit products, frozen food and leather. In addition, some high potential products, such as leather goods including footwear, toys, cut and artificial flowers and luggage have also been brought under crash program for development. Again the fast growing demand for import of raw materials and capital for economic development has made the export sector a vital one. The paramount need to fill up the deficit of food resulting from rapidly growing population and slow increase of food production also sharpen the crucial role of export. Given the high dependence on imports of manufactured capital goods and intermediate components, Bangladesh breakthrough in the garments industry has a narrow base for raising the rate of growth.

The UNCTAD (1994) report indicates how the global opportunities have shrunk for the LDCs. It states that 20 of 24 industrialised countries are more protectionist than they were 10 years ago, when the level of average protectionism in developing countries is beginning to come down, partly as a result of structural adjustment programs, the protectionist trade in the industrialised nations is gaining ground. Bangladesh being a marginal participant in the global market, in terms of value of trade(.05%) will be adversely affected by this trade protection.

Despite worldwide economic recession and sluggish economic recovery export earning had increased US\$ 1292 million in 1988-89 to US\$ 2534 million in 1993-94 nearly 96 percent increase in current market price over five years. It is thought that quota restriction for garments on East Asian countries has created an opportunity for Bangladesh and argued that phasing out of quota restriction on East Asian countries under Multi-Fibre Agreement (MFA) after 2005 may create problems for Bangladesh garment export.