Bangladesh Policy Notes

Enabling Export Diversification

Key issues and challenges

Bangladesh’s export growth has been remarkable. Bangladesh aims to generate $54.1 billion in export earnings by FY2020, a significant increase over the $35 billion earned in FY2015-16. The leading sector, textiles and apparel, usually referred to as ready-made garments (RMG), has created 4 million jobs overall and accounts for 82 percent of Bangladesh’s exports. RMG exports have shown signs of deceleration in the recent past but the momentum has picked up in FY2018. At the same time, several other less dominant but promising sectors are showing a positive export growth trend and could possibly drive export diversification and job creation in the future.

However, the composition of the export basket has not changed much over the past two decades. Bangladesh’s HHI (Herfindahl-Hirschmann Index), that measures the level of sectoral concentration in exports is about five times that of other export-driven economies such as Thailand, China and Vietnam. During the last two decades, Vietnam expanded its export basket from agriculture to include machinery, footwear and electronics through national-level strategies and policy reforms to support specific sectors. However, Bangladesh continues to be primarily an RMG exporter.

Nearly 80 percent of exports are destined to North America and Europe and product sophistication has remained almost static. Bangladesh’s export destinations have also not changed much and it has not tapped into other large and emerging markets in the world. Also, over the years, the country continued to produce and export RMG basics in progressively larger quantities while fashion garments and higher value-added items remained a small portion of total exports. An opportunity exists for Bangladesh to increase its market share as rising wages in China is forcing firms to look for alternatives. According to a World Bank study, a 1 percent apparel price increase in China would create 1.36 percent additional demand for Bangladeshi products in its largest export market, the USA. However, countries such as Vietnam, Cambodia, Myanmar, India and Pakistan also have the advantage of low wages, and Bangladesh, so far, has not demonstrated much success in securing the declining share of Chinese apparel exports.

Several factors constrain export growth. A large number of sectors are identified by the Government for export diversification, resulting in diffused effectiveness of resources. Absence of a comprehensive and long-term strategic approach to support the export of these potential sectors has resulted in a fragmented and dispersed strategy framework. Unequal access to incentives/facilities such as duty-free import of raw materials and export-friendly financial products in sectors other than RMG have created a greater incentive to invest in RMG than in other potential export sectors. Adherence to various technical and process quality standards, testing and accreditation mechanisms, and most importantly, social and environmental standards have emerged as critical success factors to export products while local producers are unable to adhere to these standards. High costs of modern machinery and lack of knowledge of modern management and production practices constrain many entrepreneurs, and impede technology adoption. In addition, there are infrastructure constraints like dysfunctional common effluent treatment plants (CETPs) and restricted access to transport and power which impacts export competitiveness. Trade policy reforms like tariff rationalization and strengthening of the bonded warehouse regime have also been sluggish.

Policy Recommendations

To address these issues, in the short term, the government needs to:

- Remove policy, coordination and market failures in select sectors that demonstrate high-growth potential in export markets.
• Extend the existing incentives packages and facilities to non-RMG sectors with export growth potential, which will include expanding access to the Export Development Fund (EDF), rationalizing import duties for raw material and safety equipment, and allowing industry associations to facilitate the loan application process on behalf of the manufacturers.

• Adopt a national level compliance framework for the export sector and develop the institutional capacity to support firms to implement such a framework.

To address these issues, in the medium to long term, the government needs to:

• Identify gaps in national product standards and testing parameters as required in international markets and take necessary actions to harmonize those.

• Increase allocation in the Green Transformation Fund (GTF) provided to banks for non-RMG export sectors and incentivize banks to consider good proposals to increase uptake of the fund to be used to enhance environmental standards of the manufacturing units.

• Introduce a national guideline/framework for CETP management and operations.

• Incentivize the establishment of private sector run technology and service centers to provide necessary technology and skills for exports by allocating appropriate land and resources.

• Allow Special Bonded Warehouse facility for all export oriented manufacturers to minimize higher cost of imported inputs and eliminate the difficulty in claiming duty drawback on imported raw materials.