Why export diversification is not happening?

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With over two million jobs and 76 percent of export earnings from the RMG sector, there is little doubt that too much of the nation's fortune is riding on this one sector. Export concentration in readymade garments makes the economy, jobs and income, extremely vulnerable. Therefore, the government's focus on export diversification as a cornerstone of its export policy for several years running is appropriate. The problem lies in the lack of its fulfilment. Why is it not happening?

For starters, it is not because Bangladesh has no other products in which it has a competitive advantage. There are numerous exportable products lurking in the background. For instance, the world market for agro-processing industry is significantly larger than that of apparel. Bangladesh has already made inroads into this market.

Moreover it is a myth that to export, a country must have substantial locally available raw materials and other inputs to be fabricated into the final product. This is the age of globalized supply chains. Taking advantage of this system, it should be possible to source any industrial input from any part of the world, though transportation costs will vary according to the distance of the sourcing location.

To take advantage of globalized supply chains the country's trading system must be smooth both for imports and exports. Countries with high tariffs, high protection, and inept customs administration cannot take advantage of globalized supply chains.

South Korean entrepreneurs brought this lesson to Bangladesh in the 1970s. They not only demonstrated to our garment producers that there was a huge market for Bangladeshi garments under MFA quotas, but they also showed how to ensure the supply of world-priced inputs within the country's high-tariff regime. Thus came a policy innovation for Bangladesh the duty free import of inputs through the bonded warehouse system.

Those who argue that Bangladesh RMG sector thrived only because of quotas fail to recognize the other part of story, the creation of a free trade channel for RMG inputs and outputs within a highly protected trade regime. Without this policy in place and its credit supplement, back-to-back LC —, the RMG sector could not have reached the heights it has achieved today.

After long resistance, the government finally yielded to demands for similar facilities to be given to the export-oriented footwear manufacturers. Footwear exports have boomed, and the prospects remain bright.

What about other exports and potential exports? Tough luck, I would have to say. To obtain world-priced inputs, they remain at the mercy of the corruption-ridden and largely ineffective Duty Drawback office. When you add up all duties and levies, average import taxes on raw materials and intermediates are upward of 25 percent. These need to be paid by manufacturers upfront only to be reimbursed after much hassle once production and export are completed.

Failure to ensure world-priced (duty-free) inputs undermines export competitiveness. New exporters and potential exporters must not only pay duties on inputs but also face cumbersome import procedures. When I asked Kihuk Sung, the Korean entrepreneur who employs 30,000 Bangladeshi RMG workers and has factories in countries like China, Vietnam and Cambodia, how he rates Bangladesh's import regime compared to that of these countries, "terrible" was his reply. Most industrial and business houses hire personnel who function as intermediaries to get the import job done at a cost of course. We seem to be years away from the modern day practice of DTI (direct trader input) and post-audit customs processing.

To promote exports in general, and export diversification in particular, the cornerstone of our export strategy should be to make export production costs competitive. So how do we create the free trade channel for other exports in a manner that has been done for garment exports?

Since government revenues will remain tariff dependent in the foreseeable future (implying that import tariffs are not expected to come down any time soon), imported inputs specifically for export production must be allowed a duty-free regime through special bonded warehouses or a duty suspension scheme.

The National Board of Revenue already runs a large office for the management of the bonded system. This facility needs to be extended to exporters of non-RMG products, no matter how many extra personnel that might entail. This opportunity cannot be lost on the pretext of revenue leakage.

The idea of preparing a list of 'thrust' sectors described as a policy of picking winners and offering generous export subsidies is hardly the way to promote export diversification, though that is what the recipient of export subsidies would have us believe. For export diversification to succeed we need to create a replica of the free trade channel rightfully given to the RMG industries. I hope someone is listening.

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