Political smokescreen and economic reality

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WHILE watching TV talk shows and reading press reports on various local seminars, we come out with the impression that the real economy in Bangladesh has collapsed and tens of millions of families have been pushed below the level of absolute poverty.

Some reports also mention that the garment industry has virtually collapsed and millions of Bangladeshi workers are about to be expelled from various host countries.

Some economists have also come up with mind boggling numbers that say 40 million additional people have been pushed below the absolute poverty level in recent months because of the surge in food prices recorded in recent months, and many commentators have coined the term “silent famine” to describe the prevailing situation. These are serious statements and deserve to be analysed objectively.

Certainly, in the aftermath of the two rounds of major flood and cyclone Sidr and the sharp decline in exports experienced in mid-2007, such an outcome could not be ruled out.

The significant shortfall in aman crop and the surge in rice prices globally had even given rise to the prospect of mass starvation.

Industrial unrest coupled with the anti-corruption drive launched by the government led to a serious loss of business confidence. The outlook, indeed, looked grim.

Now that the fiscal year 2007-08 is almost over, we certainly know that the Bangladesh economy has not at all collapsed and the doomsday scenarios painted earlier did not materialise. The real economy is estimated to be growing at 6 percent or more, supported by strong domestic demand and a strong rebound in manufacturing, agriculture, transport and communications, and other service related activities.

Even the recent IMF mission, generally comprising conservative economists, has revised upward its real GDP projection to 5.5-6.0 percent despite the initial setbacks. Like in my previous articles, let’s take a panaromic tour of the macroeconomics.

All financial indicators, for which monthly and quarterly data are available, clearly demonstrate how dramatically the economic picture has changed in recent months.

Reflecting strong external demand for Bangladeshi products, average export growth during January-March 2008 was phenomenally high at 37.5 percent over the corresponding period last year. Export growth is broad-based, supported by both traditional and wide-ranging new products (pharmaceuticals, agricultural products, etc.). Despite the economic slowdown in the industrialised countries, Bangladeshi exports became more competitive and gained larger market shares during this period.

The outlook for exports appears to be even more promising, with large numbers of foreign firms considering relocation to Bangladesh.

If we look at the indicators of domestic demand, we certainly do not find any sign of weakness. Imports surged by more than 30 percent during January-March 2008. Private sector credit expanded at a healthy pace (17.5 percent).

In particular, credit expansion to the agriculture sector (73 percent) and term lending to the industrial sector (65 percent) are particularly noteworthy. The expansion in domestic demand is sustainable since, despite the surge in imports, Bangladesh is the only country in South Asia with a surplus current account position.

The story of economic rebound can't be complete without noting the phenomenal supply response from the farmers in the aftermath of Sidr, and in response to the sharp increase in food prices.

The country has never recorded the level of boro output we are observing now (20 percent above the 2007 level of 15.5 million tons), which also followed bumper crops of potato and wheat.

Government initiatives to boost agricultural output have yielded handsome dividends, and the country may end the fiscal year by doubling the level of official rice stock through the ongoing boro procurement program. If this trend continues, Bangladesh will become a food surplus country within a short time.

The strong rebound in domestic activity has certainly been complemented by the ongoing surge in inflow of remittances. During the first four months of 2008 through April, remittances averaged at $800 million per month, pointing to the possibility that remittances may even reach $10 billion in 2008.

To understand how strong our performance is, we need to look at the contribution of remittances to the Bangladesh economy (10 percent of GDP) relative to remittance contribution to GDP in India (3-4 percent) and Pakistan (4-5 percent).

If growth in remittances continues at the current 30-40 percent rate, growth in gross national income should be 8-9 percent in real terms in 2007-08, since it would add an additional 2-3 percentage points to the estimated 6 percent of GDP growth in 2008.

Against this strong economic expansion, and a further expansion of domestic purchasing power, is it even conceivable that 40 million additional Bangladeshis could fall below the poverty line? The argument appears to be based on the increase in food prices, the high share of food in household budgets, and the consequent substantial loss of real purchasing power, pushing families below the poverty line.

This analysis, however, is seriously flawed, since it fails to capture the domestic redistribution effect of higher food prices (particularly rice), impacts of government interventions, and the very large positive income effect generated through remittances and economic expansion. The increase in rice price is a gain for the farmers (constituting 60-70 percent of population) at the expense of non-farm families.

Furthermore, many poor rural families (about 5 million households or 20 million individuals) received food from the government under the Vulnerable Group Feeding (VGF) and food for work programs. The negative impact on the urban poor families was partly alleviated by subsidised open market sales of rice and sale of essential products through BDR shops.

Certainly, government interventions alone could not have been enough to offset the real income loss for the non-farm poor families. But, if we include the effect of income gains being received by the farmers through higher prices, we are not sure whether the overall poverty situation in the country would deteriorate.

In addition, we must take into account the income effect on household budgets resulting from a more than 30 percent growth in remittances (about Tk 14,000 crore or Tk 1,000 per person more than the amount received last year), much of which go to low income families all across the country, and the growth in nominal GDP which would be about 16-17 percent (equivalent to more than Tk 6,000 per person in additional income).

Various groups with vested interests may create smokescreens to paint scenarios consistent with their political or other objectives. But, as professional economists, we must analyse the issues more objectively and disseminate the correct analysis for public consumption.

When the pace of economic expansion in the second half of the fiscal year is running at about 6.5 percent (since the first half growth was much slower), which matched the highest growth rate that Bangladesh ever experienced in recent decades, how can we characterise the economy as one on the brink of collapse?

When the growth is originating from labour-intensive activities like manufacturing (garments and textiles), farming (boro, wheat, and potato), transport and communications, how could we conclude that it would not help reduce poverty?

When Bangladeshi workers are going abroad in record numbers (100,000 per month), and they are sending $800 million every month (equivalent to half the foreign aid we receive annually), why do we constantly complain about market loss for our labour and spread fear about mass deportation from host countries?

Bangladesh receives much more remittance in dollar terms, and at a faster rate, than Pakistan, and much more than India relative to its population and size of the economy, although we were a late starter in this field.

Since January 2008, Bangladesh is the only country where inflation (point-to-point) is on a declining trend while it is still rising globally, including in Pakistan and India. It may sound unbelievable, but rice price today in Bangladesh is the lowest in the world, and BDR is talking about ways to prevent smuggling of rice to India.

The financial market and market participants are certainly not fooled by the smokescreen. The stock price index and market capitalisation are hovering at record high levels, and market turnover is reaching new frontiers almost every week.

Foreign direct investment in Bangladesh has surged, and international investors are arriving in Dhaka at a pace not seen before. New domestic airlines are being floated and expanded, and foreign airlines are also crowding in to get a bigger piece of the pie of the growing Bangladesh market.

Bangladesh’s strong export and remittance performance and the strength of its economy have not gone unnoticed: since January 2008, the taka has strengthened significantly relative to Pakistani and Indian rupee, both of which depreciated markedly against the dollar.