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Chapter 2

Reflections on Bangladesh in Comparison to East Asia

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A comparison of Bangladesh with East Asia can be viewed in terms of the proverbial story of the Tortoise and the Hare. The performance of Bangladesh is often compared to the high-flyers of East Asia in an unfavourable way. But this may well be a case of the well-established race between the Tortoise and the Hare. Around 1990 Bangladesh, very much like India, turned a major corner, began to liberalise its economy, resulting in an acceleration of the rate of growth, just at the time the East Asian hares were beginning to settle down from their 8-9 per cent growth rates, down to 6 per cent and 5 per cent. I am not speaking of East Asia's problems during their financial crisis which, I believe, was more of a blip from which they recovered quite quickly. What I have in mind is that, as the East Asians begin to approach mature economy status, we can expect growth rates to decline to the level of the mature economies, most of which would be quite satisfied with 3 or 4 per cent. In the meantime, Bangladesh was converging towards 5 per cent and can do even better if spared natural disasters and able to effectuate some additional policy changes which are still lacking (see below).

Any explanation of a country's growth performance usually combines neoclassical growth theory with political economy dimensions. Such growth theories customarily deploy a kitchen sink of variables, from culture to governance, from trade and industrial policies to research and development (R&D), education and health, geography, etc. But the question still remains: why policymakers in East Asia, compared to Bangladesh, chose a somewhat different path at the end of the early easy import substitution epoch, given that all countries apparently start with such a policy package, the difference being how long it is carried on, and how severe the regime. While cultural differences are often cited, I've never found them very satisfactory and prefer to focus on differing initial conditions which affect countries' subsequent behaviour. One of these is the extent of organic nationalism, the second is the initial natural resource endowment, and the third is the extent of easy access to foreign capital.

As Simon Kuznets pointed out long ago, if there is organic nationalism, assisted by ethnic homogeneity, i.e. a homogeneous population, and/or a perceived external threat which seems to unify people, there is no need to have to try to create synthetic nationalism. East Asia generally could call on such organic nationalism, Bangladesh less so. This means that a government may have to devote a lot of effort just to create an economy out of disparate factors, often leading to over-promising and over-commitment, trying to control too many things, given the limited number of fingers available. Consequently, the credibility of government, falling from its early honeymoon period, diminishes rapidly. It also means that Bangladesh suffered from a longer and more severe import substitution phase, as did India, compared to the Korea's and Taiwan's of the earlier East Asia case. As a result, Bangladesh, as well as India, initiated its gradual liberalisation focusing on the liberalisation of trade, exchange rate flexibility, some reforms of state enterprises, some privatisation, etc. in the 1990s instead of the 1960s—with latecomer China's reforms initiated in the early 1980s.

Turning to natural resource endowments and easy access to foreign capital, such flows provide an incentive for rent-seeking and corruption. As welcome as resource bonanzas may seem to be on the surface, Bangladesh had to worry about the impact of Dutch Disease, both in terms of such flows strengthening the exchange rate, and, to my mind, more importantly, via an extension of the Dutch Disease in terms of their negative impact on governance. Clearly, Bangladesh experienced better development performance once its primary exports—mainly jute—disappeared from the scene and total primary exports fell from 20 per cent of the total down to 5 per cent. The shift to garments, quite spectacular, also meant that Bangladesh was now less buffeted by terms of trade shocks. In a sense, the country was moving towards the East Asia case which had little natural resources to speak of from the beginning and was therefore forced to focus attention on human capital early on.

Easy access to foreign capital, moreover, reinforces these twin impacts of the Dutch Disease. In the Bangladesh case it was foreign aid since foreign private capital is still not a major feature of the scene. Large inflows of foreign aid have undoubtedly been helpful, especially in times of natural disasters. But, in general, even though aid is advertised as a major tool for promoting reforms, the income effect, taking the pressure off, and thus permitting Bangladesh to continue what it has been doing,

has, in my opinion, generally been able to swamp the substitution effect of policy change. It therefore seems quite clear to me that the relatively easy access to foreign aid has affected governance adversely, i.e. permitted rent-seeking, corruption and capital flight.

However, Bangladesh, like India, clearly shifted toward a reform mode in the early 1990s, given the delay due to a lack of organic nationalism at the outset. While the East Asian hares meanwhile met diminishing returns to their high investment rates as they approached mature economy status, convergence was beginning to become a real possibility. Another reason, of course, is the demographic gift which leads to slower growth in aging societies than in societies like Bangladesh where there is still a large and increasing working-age population. What used to be a real demerit, a large population, is thus beginning to turn to an advantage for the tortoise. Moreover, the tortoise has accomplished much which is to its credit: inflation has been generally tamed; quantitative restrictions (QRs) eliminated; trade liberalisation in terms of tariffs has been achieved, i.e. maximum tariff rates have declined from 350 per cent in 1991 to 37 per cent in 2000 (even though we must remember that the early rates contained a lot of water); interest rates have been deregulated and the exchange rate rendered flexible; agriculture has been given a good deal of attention, and, what is even more impressive, rural non-agricultural activities now comprise as much as 40 per cent of rural families' income; remittances have become important, up to $6 billion per year; labour markets have become less rigid, in comparison, for example, with India, in spite of the occasional hartals called by the politicians on both sides; fertility has been falling substantially as a consequence of increased female labour force participation rates and agricultural productivity change; and foreign aid,—while still important—has declined from 59 per cent of central government expenditures in 1989 to only 20 per cent at the turn of the century.

But perhaps one of the major achievements is in the area of human development, which, in fact, makes "basket case" Bangladesh compare favourably with the average developing country. Progress on infant mortality reduction, increases in life expectancy and educational enrolment (especially of females) have been quite spectacular, all way above the increase in growth itself, which is by no means to be sneezed at. Thus, in contrast to India, Bangladesh has a better chance, given its strong human development base, to move into the promised land of a virtuous cycle characterised by continued advances in human development being fed by growth and feeding growth, in turn.

Nevertheless, the tortoise still has some serious problems on its way to catching the hare. First and foremost, to my mind, is the fact that the spectacular success of garments, which now comprises 75 per cent of exports and is the mainstay of industrial activity, also constitutes a grave potential vulnerability in case either Chinese or Sub-Saharan African competition begins to bite seriously. It is remarkable that leather goods, footwear, light engineering, pharmaceuticals and other potential exports, some of which presumably could compete internationally, seem to have withered away; apparently liberalisation has focused very much on garments only, while the overall environment still reflects an anti-export bias.

Second, I would put the well-known problem of economic governance and continued political confrontation between the two parties, leading to an inability to maintain any sustained policy direction. Third, I would put the worsening of the distribution of income which, while bad in and of itself, also implies that, even at 5 per cent growth rates, while poverty has declined, it has not declined by as much as it should have. Fourth, I would put the well-recognised inadequacy of economic overheads, congested ports, transport and power problems which impede industrial activity. Fifth, it strikes me as passing strange that a country of NGOs co-exists with a heavily centralised government. A more devolved government, leaning more heavily on local bodies, would likely be much more effective in working with NGOs and civil society generally. Some gradual devolution from the union down to the village level would thus be extremely helpful. Lastly, wage bargains are still centrally determined and unions are still tied to political parties, which contribute to the aforementioned policy uncertainty and occasional gridlock.

If one were to conclude with a few priority suggestions for further policy change, in order to encourage full convergence between the tortoise and the hare, high on the list would be an attack on the overall generally accepted atmosphere of corruption, leading to a level of cynicism one can literally cut with a knife. One way of tackling this might be to substantially increase the emoluments of Class I government officials, while shifting many Class III and IV public sector employees to nation-building activities. Moreover, in order to tackle the avid pursuit of rents I would suggest that Bangladesh changes its stance towards aid donors, using its currently underestimated bargaining power by insisting that it is now fully capable of setting its own reform priorities and only then approach the international donor community. The poverty reduction strategy paper (PRSP) approach was supposed to reduce the number of conditions and provide for real ownership by recipients, but, in fact, there has been relatively little change from the days of structural adjustment lending (SAL) since the guidelines as to how to prepare a PRSP are still issued by the International Monetary Fund (IMF). A real change in the modus operandi, of course, requires the donor community to be willing to open a different kind of aid window which is not the normal country-assistance "business as usual" programme but one which would be responsive to a recipient determining precisely what is in its own interest to try to accomplish over the next five years, complete with self-conditionality and the understanding that non-compliance with such self-conditionality would lead to the cessation of aid, one way to ensure the recapture of credibility for the entire, fatigued process.

Needless to add, but nevertheless central, is the threat Bangladesh faces in terms of continued global warming. Some estimates claim that as much as a third of the country could eventually be under water if current international efforts to arrest global warming prove unsuccessful or too slow. Since affecting the environment is an international public good, the tortoise by itself cannot materially affect the outcome. However, Bangladesh must lobby as hard as it possibly can in all international venues to ensure that Kyoto and its successor post-Bali arrangements lead to a consensus by both rich and poor countries to act in time to avert major disasters. A corollary would be to also plan ahead for the possible necessary relocation of populations, including some in Bangladesh, in the eventuality that actions of the international community prove insufficient and/or too tardy.