

GENERAL AGREEMENT ON TARIFFS AND TRADE

RESTRICTED
BOP/W/98
7 April 1986
Limited Distribution

Committee on Balance-of-Payments Restrictions

1986 CONSULTATION WITH BANGLADESH
(SIMPLIFIED PROCEDURES)

Background Paper by the Secretariat

1. This paper has been prepared in accordance with paragraph 7 of the Declaration on Trade Measures Taken for Balance-of-Payments Purposes (BISD 26S/205-209) to assist the Committee on Balance-of-Payments Restrictions in taking the decision referred to in paragraph 8 of the Declaration.

I. Bangladesh's previous consultations

2. Bangladesh first consulted following the introduction of simplified procedures in 1973 (C/W/216). Subsequent simplified consultations were held in 1976, 1978, 1980, 1982 and 1984. No full consultations have been held.

II. Recent changes in trade policy

3. As noted in the background note for the 1984 consultation (BOP/W/85) a new "negative list" system of import authorization was adopted with effect from 1 July 1985.¹ Two lists of restricted products are established: a "Negative" list, imports of goods on which are prohibited, and a "Restricted" list which comprises goods that can be imported under specific conditions. Certain products are banned for religious, social or moral reasons or because they are of substandard quality.

4. The Negative list closely reflects the structure of the import-substituting elements in Bangladesh's industry, as well as that of agricultural production. Its purpose appears to be to encourage or safeguard new or existing foreign or local investment in infant industries. Most products which are locally manufactured for domestic sale are thus prohibited for import.

5. The Restricted list is divided into two parts. Part 1 contains goods importable for three main purposes: products for use by foreign-exchange-earning hotels, goods imported as supplies for export-oriented industries, and imports of controlled items such as drugs or pesticides. Thus, a wide variety of foreign foodstuffs are importable only by tourist hotels. Certain textile materials and accessories may be imported by recognized industrial

¹A copy of the Import Policy Order, 1985-86 has been supplied to the secretariat and may be consulted in the Technical and Other Barriers to Trade Division (Room 1064).

units up to specified entitlements (based on past performance and an agreed assessment of import needs). Others may be imported for export-oriented garment factories working entirely under "back-to-back" letters of credit. Tea for blending, and such items as tea chests, may only be imported with the authorization of the Tea Board. Drugs, medicaments, disinfectants, herbicides, insecticides and fungicides are only importable under strict conditions with the approval of the Drugs Administration or of the Agriculture and Forest Division. In this connection it may be noted that Bangladesh has pioneered the application of the World Health Organization's recommended list of generic drugs for import and sale.

6. The second part of the Restricted list covers, firstly, conditions for import of industrial raw and packing materials and spares by industrial consumers: these are linked strictly to the quantity agreed as necessary for the industry's expected requirements for the year. Other items on the list, which are mainly consumer goods or office supplies, may be imported only by registered commercial importers with funds made available under the Wage Earners' Scheme.

7. Items not included in the Negative or Restricted lists may be freely imported. Imports may be made against cash, external economic aid, barter or other commodity exchange arrangements, or under the Wage Earner's Scheme. With effect from 1 July 1985, no import licences are required for any item. Control is exercised through letter of credit applications. Normally all imports, irrespective of the source of finance, may only be made by irrevocable letter of credit, obtainable by application to authorized banks. Thus, the general import control is strictly related to availability of foreign exchange.

8. The introduction of the "negative list" system represents, in the context of the structural payments imbalance of Bangladesh, a major change in import policy from one basically subject to administrative clearance and approval to one where, unless stated otherwise, goods may be imported relatively freely without recourse to import authorization. It has made the import system considerably more clear and transparent in operation. It was coupled with an expansion in the scope of the "secondary" foreign exchange market system and a revision of incentives available to exporters which, together, moved in the direction of a more market-oriented external sector. These changes are as follows.

9. Until March 1985, only workers' remittances under the Wage Earners' Scheme (WES), and earnings from non-traditional exports (those other than raw jute, jute goods other than carpets, loose tea, and wet-blue leather) covered by the Export Performance Licensing (XPL) scheme could benefit from premium rates available on the secondary foreign-exchange market. Exchange purchased in the secondary market could be used for imports of most permissible products, as well as for certain invisible transactions such as travel; import entitlement certificates (IEC's), allocated to exporters of non-traditional goods in proportion to the domestic value-added content of the export product, could also be used for imports and traded in the secondary market.

10. In late February 1985, tourist receipts were also made negotiable in the secondary market. Since July 1985, under a new Export Performance Benefit

(XPB) Scheme, which replaces the XPL scheme, a proportion ranging between 40 and 100 per cent of all export earnings except for those of raw jute, loose tea and wet-blue leather may be sold on the secondary foreign-exchange market; and from the same date all receipts from consultancy and technical fees have also been sold in the secondary market. From 1 December 1985, XPB rates on a number of jute goods were raised and certain commissions were included in the secondary market. The IMF estimates that in 1985/86 some 50 per cent of Bangladesh's imports may be made through the secondary market.

Action in other GATT fora

11. The economic and trade situation of Bangladesh has been analysed in the Sub-Committee on Trade of Least-Developed Countries, where consultations were held in November 1983, with follow-up review in October 1984. In these consultations, proposals for trade-policy measures which would assist the export prospects of Bangladesh in its principal markets were examined and priority areas were identified. These included jute and jute goods, including carpets; frozen fish and shrimps; leather and leather goods; ready-made garments; handicrafts; household linen and specialized textiles. A certain number of actions in favour of either Bangladesh specifically or least-developed countries in general have been noted in the relevant meetings of the Sub-Committee (see COM.TD/LLDC/6, 7 and 9 in particular).

III. Economic trends and foreign trade

12. Bangladesh is one of the least-developed economies in the world, and it faces severe resource constraints in raising living standards from their current, extremely low, level. It is highly vulnerable to balance of payments difficulties because of its large structural trade deficit (Chart 1) and its heavy dependence on foreign assistance.

13. Agricultural production accounts for around 50 per cent of GDP, and generates directly and indirectly practically all merchandise export earnings. A certain amount of export diversification has taken place since the early 1970s; jute and jute products, leather and leather products, and tea have fallen from around 90 per cent of exports to 75-80 per cent, while fish and fish products and cotton garments have increased their share, particularly in the past five years, to around 15-20 per cent. Nevertheless, the export base remains narrow and small, accounting for around 6-7 per cent of GDP, and it has shown only a slight tendency to increase its share over the past fifteen years. Export earnings are sensitive to climatic conditions for agricultural production as well as world commodity price movements. They have grown at an annual average rate of about 9 per cent in US dollar terms since 1974, but with considerable year-to-year variation from as much as plus 25 per cent to minus 12 per cent.

14. Imports accounted, on average, for 13 per cent of GDP in the 1970s, but increased sharply to around 18 per cent in the 1980s. This increase was financed by higher foreign aid disbursements and, more importantly, by remittances from migrant workers (the WES scheme) largely from the Gulf countries. These developed into a large source of foreign exchange from the late 1970s worth, at their peak in 1982/83, 95 per cent of total merchandise export earnings. Although such remittances fell sharply between 1983 and 1985, reflecting the fall in demand for migrant workers in the Middle East,

the WES scheme remains a major source of finance for private sector imports. In 1984/85, some 43 per cent of imports were financed through official loans and grants. Of the remaining 57 per cent, nearly half (46 per cent) was financed through earnings from the WES scheme. Its importance for Bangladesh's import capacity can therefore hardly be overstated.

15. Imports increased at an annual average rate of 16 per cent in US dollar terms in the 1970s, but with massive year-to-year variations from as much as plus 54 per cent to minus 32 per cent. An important volatile component was imports of foodgrains. These are required every year to supplement domestic production and they rise sharply at times of crop failure due either to flooding or drought, to both of which the country is particularly vulnerable. Bad weather can also affect export crops at the same time. As a result, Bangladesh's trade deficit fluctuated substantially in the 1970s, from 6 to 10 per cent of GDP, but it was regularly financed almost entirely by highly concessional capital inflows. Gross foreign exchange reserves were maintained on average at the equivalent of 2.6 months' import cover.

16. In the 1980s, the rate of growth of imports decelerated sharply to an annual average of 3 per cent. Annual fluctuations in the rate of growth became less pronounced than in the 1970s, but they remain nevertheless sizeable. This has reflected mainly year-to-year volatility in the value of imports of consumer goods and certain intermediate goods for use particularly in the industrial sector. These are sensitive to domestic economic conditions and to the availability of foreign exchange, particularly from the secondary foreign exchange market.

17. Bangladesh suffered a deterioration in its balance of payments in 1984/85, after two favourable years in which gross foreign exchange reserves accumulated to the equivalent of 2.8 months' import cover. Export earnings are estimated to have increased by 13 per cent in 1984/85. Although the jute crop was adversely affected by weather conditions and production fell by 13 per cent, world jute prices rose sharply and large sales of jute stocks were made, so that export earnings from jute and jute products increased by 14 per cent. Export prices for the first few months of the 1985/86 season, however, show a decline to previous levels. Exports of ready-made garments more than tripled in value in 1984/85 to account for over 12 per cent of total export earnings. At present, about 55 per cent of ready-made garment exports are to the EC countries, 27 per cent to the United States and 13 per cent to Sweden. The rapid increase of exports of garments, particularly shirts and jackets from Bangladesh to the EC and United States markets led to the introduction in 1985 of MFA quotas, under bilateral agreements, on exports of shirts to France and the United Kingdom within the EC, and on exports of shirts and jackets to the United States (see documents COM.TEX/SB/1093 and 1113). Development and diversification of the export-oriented garment industry, under the conditions for import, value added and export laid down in the Import Policy Order (which reflect the conditions laid down under MFA rules of origin for "substantial transformation"), is a major priority of export policy.

18. Total imports are estimated to have increased by 15 per cent in 1984/85. About a third of the increase was due to higher foodgrain imports, but most of the remainder reflected increased imports of consumer goods and

intermediate industrial inputs, which had already risen by 22 per cent in 1983/84 and grew by an estimated 35 per cent in 1984/85. This has been directly attributed to strong domestic monetary expansion, reflecting high credit growth to both the private and the public sector.

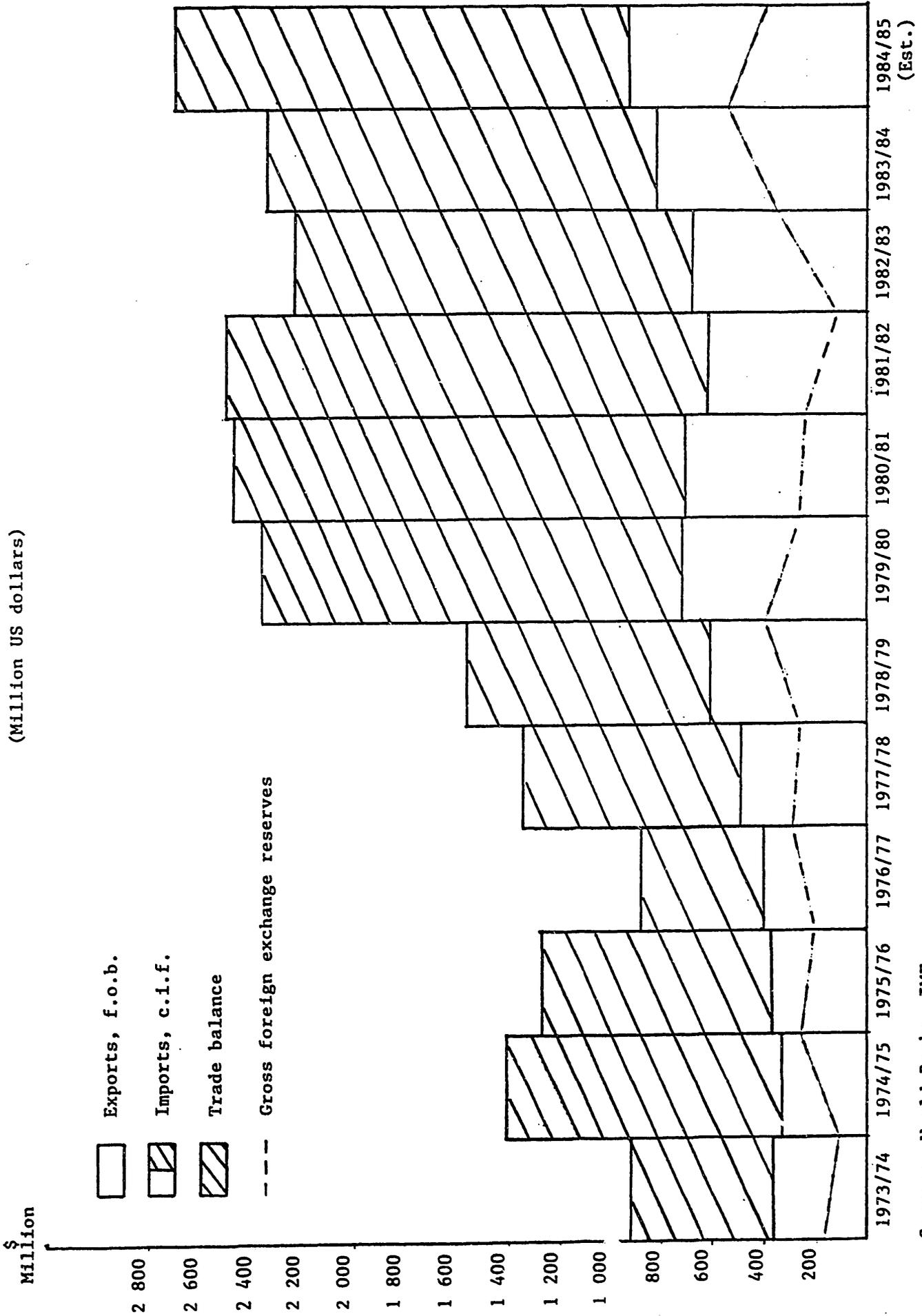
19. Notwithstanding the increase in export earnings, therefore, Bangladesh's trade deficit rose substantially in 1984/85. At the same time, workers' remittances are estimated to have fallen sharply with the result that the current account deficit rose to 9 per cent of GDP. Gross foreign exchange reserves fell to stand at 1.8 months' of imports in mid-1985.

20. Preliminary data for the first quarter of financial year 1985/86 show an increased trade deficit in local currency terms, with higher exports and imports, compared to the same period of the previous year: however, higher levels of private and official transfers led to improvements in the current balance and the overall balance. Receipts from the Wage Earner's Scheme were more than double the figure for the first quarter of 1984/85. Exports of readymade garments, fish, and miscellaneous items increased most rapidly.

21. The high and rising density of population, particularly in relation to available arable land, has emphasized the need for economic diversification over the medium to long term. The government has encouraged the private sector to play an active rôle in developing manufacturing activity, and has aimed in its New Industrial Policy of June 1982 inter alia to foster the development of efficient export-oriented and import-substituting industries. Industrial production is likely to continue to be based largely on export markets, both because of limited domestic effective demand and because of the need to generate foreign exchange for the purchase of imported raw materials and intermediate inputs. A high premium is attached to open access to export markets for the success of an outward-looking industrial development strategy. While clothing remains the largest non-traditional export development sector, leather goods, ceramics (both tableware and sanitary equipment) and more sophisticated jute manufactures such as carpets, wall hangings and tapestries, are sectors where export development is being actively promoted. At the same time, Bangladesh's trade policy will need to be carefully designed to promote economic diversification without adversely affecting the profitability of export activities. In particular, the pattern of import restrictions introduced in the overall context of the balance-of-payments situation should avoid upsetting the desired medium-term structure of relative prices in the economy.

BANGLADESH

Imports, Exports, and Foreign Exchange Reserves, 1973/74 - 1984/85



Source: World Bank; IMF.