TRADE REFORM AND PERFORMANCE IN SELECTED LEAST DEVELOPED COUNTRIES IN ASIA

Srinivasa Madhur*

May 1993

*The author is Economic Adviser in Planning Commission, Government of India, New Delhi. The views expressed in the paper are those of the author and not necessarily of the organisation to which he belongs.

Table of contents

List of Tables

Tables

TRADE REFORM AND PERFORMANCE IN SELECTED LEAST DEVELOPED COUNTRIES IN ASIA

The objectives of this paper are two fold:(i) to trace the trade policy reforms which have been initiated over the last decade by a few selected least developed countries in Asia and the main impulses and imperatives behind these reforms, and (ii) to examine the extent to which these reforms have been accompanied by export expansion and export diversification in these countries.

The Asian least developed countries selected for the study are Bangaladesh, Nepal, Myanmar and Lao. The selection of these countries is done based mainly on one criterion, namely, the availability of published information on the country's trade policy changes. Many other least developed countries in the region are equally important and would have been included in the study but for the lack of published information on their trade policy regimes. Even among the four countries which have been selected for the study, our emphasis will be mainly on Bangaladesh especially because information on Bangladesh's trade policy measures are more readily available than for the other three countries.

The Importance of Stable Export Earnings for LDCs:

The importance of stable export earnings for least developed countries hardly needs emphasis. In recent years, the flow of aid, i.e., concessional loans and grants to least developed countries has more or less stagnated at about $15 billion per year. The likely prospects for large increases in aid flows to least developed countries also do not appear very encouraging, especially in view of the fact that the number of prospective claimants to foreign aid is increasing. (See UNCTAD, 1992). Secondly, due to the tightening of fiscal situations in many developed countries, the supply of aid flows also may not show significant increase in the future. In such an environment, developing countries including the least developed countries may have to find alternative sources of earning the foreign exchange required to sustain a reasonable level of imports and growth. Accelerated growth in exports is one such alternative which the least developed countries may have to exploit.

It is not only important for least developed countries to export more but it is also important that their export basket gets more diversified both in terms of the composition of what they export and in terms of where they export to. Hence, in addition to stepping up exports, exporting a more diversified basket of goods should be the target of least developed countries. A more diversified export basket renders greater stability to the export earnings of a country by reducing year-to-year fluctuations in export earnings.

First, if exports are more diversified in terms of its commodity composition, specific shocks to the demand supply conditions of a particular commodity/commodity group cause less fluctuations to export earnings than if the export basket is highly concentrated in a few commodities. Secondly, a more regionally diversified export basket helps to lessen the adverse impact of region-specific recession in external markets of least developed countries. Thirdly, even if the number of commodities/products of a country's exports remain the same, if the composition of its exports changes in favour of higher value-added goods, this can also result in stabler export earnings. This is because the prices of higher value-added goods are more stable in the international market than traditional, lower-value added goods like, say, primary commodities. In other words, a diversified export basket helps countries to adjust to commodity- specific and region-specific shocks more smoothly than if the export basket is highly concentrated.

Role of Trade Policy in Export Expansion and Diversification

Rapid expansion and diversification of exports are a culmination of many factors, both economic and non-economic. Empirical evidence from large number of developing countries indicates that among the economic factors, the trade policy regime of a country is extremely important in fostering rapid growth and diversification of exports(See World Bank(1987)). In general, an outward-oriented trade regime - a regime in which the economic incentives for domestic sales and exports are more or less equal - has been found to be more conducive to export expansion and diversification than an inward-oriented trade regime, which biases the incentives in favour of domestic sales and against exports.

There are many ways in which an outward-oriented trade regime helps promote and diversify exports. First, an outward-oriented trade regime better aligns domestic prices with international prices and hence helps countries to allocate domestic resources more or less in line with their comparative advantage. Since most developing countries are endowed with abundant labour, it helps them to promote labour intensive exports. Secondly, in addition to this resource-allocational effect, an outward-oriented trade regime enhances total factor productivity of the domestic industry. Thirdly, an outward - oriented trade regime also helps to eliminate X-inefficiency which is rampant in an economy with inward - oriented trade regime. Fourthly, moving a country's trade regime towards greater outward-orientation releases resources, which are otherwise deployed to rent-seeking activities, for more productive uses and hence reduces the overall cost of production of an economy.(See World Bank(1987).

Moving a country's trade regime towards greater outward-orientation means lessening the anti-export bias of the trade regime. This can be done by a combination of policies: by relaxing quantitative restrictions on trade, reducing import tariffs, adjusting the exchange rate and strengthening export incentives. Broadly, therefore, in the present paper by trade policy reforms we mean any of these policy measures.

National trade policy regime is not the only determinant of export expansion and diversification. In addition to a nation's trade policy orientation, there are other factors which affect export expansion and diversification. These other factors which play an important role in determining the extent of export expansion and diversification of a country are:i) the overall macroeconomic environment of a country ii) the quality of economic governance in a country and iii) the trade policies of the rest of the world, especially those of developed countries.(See UNCTAD, (1991) and Madeley(1992)). It is, therefore, possible that even if a country's trade policy regime is highly outward-oriented and hence conducive for export expansion and diversification, the country may fail to accelerate and diversify its exports if these other factors are not favourable. In this sense, the role of a country's trade policy in export expansion and diversification is contingent on a favourable configuration of these other factors. This should be constantly kept in mind in assessing the extent to which trade policy reforms have helped export expansion and diversification among the Asian least developed countries selected for the present study.

The Implications of Trade Policy Reforms in Asia for LDCs

The trade policy regimes of the least developed countries in Asia are closely linked to the economic policy regimes of the other bigger, developing countries in the region. It is, therefore, difficult to discuss the trade policy reforms of the four least developed countries selected for the present study in isolation from the trade policy of the region as a whole.

At present, developing Asia perhaps has the most outward-oriented trade regime among the various developing regions in the world. These movements towards greater outward-orientation in trade and industrial policies and associated economic dynamism in the region have several implications for the formulation of economic policy in general and trade policy in particular for the least developed countries in Asia. First, there is bound to be what can be called the "demonstration effect". When a least developed country is located in such an outward-oriented and economically vibrant region of the developing world, it cannot resist changing its own economic policies towards greater outward-orientation. In fact, when the region as a whole is moving towards outward-orientation, the least developed countries in the region face the threat of being left out of the rapid development process if they themselves do not reform their economic policy regimes. Hence, by sheer necessity not to lag behind in the process of reforms the least developed countries may have to undertake economic reforms. In fact, Bangladesh and to a lesser extent Nepal had initiated significant trade reforms beginning almost from the middle of the 1980s coinciding with the trade reforms of their bigger neighbours in the region.

Secondly, the opening up of the region as a whole for foreign trade also throws up opportunities for rapid expansion of intra-regional trade. From the experience of the 1980s, there are indications that this is already happening in Asia. In 1980, intra-Asian trade was less than $ 50 billion (constituting about 12% of Asia's total trade) but has increased to over $200 billion (constituting about 18% of Asia's total trade) by 1992. In fact, intra-Asian trade has grown so fast in the 1980s that it now exceeds Asia's trade with America and is strong enough to have offset the West's recently sluggish demand. To reap the benefits of such expansion of intra-regional trade, least developed countries need to open up their own economies for greater foreign trade and capital flows. These spin-offs of trade reforms for least developed countries in a region which is growing rapidly could be substantial.

Thirdly, for some of the least developed countries trade reforms in the bigger developing countries of the region could ease the constraints on moving their own trade regimes towards greater outward orientation. The clearest example in this context is that of Nepal. Nepal is a small country and relatively less developed compared to India. The two share a long and open border across which people, goods and capital move almost freely in spite of legal and administrative restrictions.

Nepal being a small country, it is optimal for Nepal to follow an open trade policy with the rest of the world. Yet, for a long time now, since its large neighbour, India had a trade policy which was highly inward-oriented, Nepal had constraints in opening up its own economy.(See Blejer and Gyargyszapary(1991)). The key problem for Nepal had been that if it followed a free trade policy, goods imported into Nepal on low tariffs became a source of illegal re-exports over the open border to India. Besides causing concern to India, such illegal re-exports from Nepal to India entail a loss of international reserves for Nepal in exchange for non-convertable Indian rupee. Hence, Nepal could have pursued a freer trade policy and comparative advantage but only at the cost of reserve losses and a worsening relations with India. Consequently, Nepal was constrained to align its trade policy with that of India but at the cost of severe loss of efficiency in its production structure. Now that Nepal's big neighbour, India itself has started moving towards greater outward-orientation, the external constraint on Nepal's trade policy regime, sometimes refered to as the "Gulliver effect" has eased substantially.

A fourth implication of Asia's movement towards greater outward orientation for the least developed countries is that they can benefit by sharing experiences in formulating and implementing economic reform measures from the next door neighbours. These external economies of experience sharing for the least developed countries can be substantial in that they can avoid some of the pitfalls involved in the transition of moving from an inward-oriented trade policy regime towards an outward-oriented one. Overall, just the fact that the least developed countries in Asia are a part of a region which is rapidly moving towards outward-orientation in trade policy and greater integration with the world economy could, therefore, work as a major impulse for these countries to undertake substantial reforms in their own trade and external sector policies.

The Plan of the Paper:

The plan of the rest of the paper is as follows: Section 2 presents an overview of the trade policy measures undertaken by the four least developed countries over the last decade. Section 3 correlates the trends in export expansion and diversification in these countries over the last decade with their trade policy reforms. Finally, Section 4 besides summarising the main conclusions highlights the key challenges of export expansion and diversification for these least developed countries.

SECTION 2 : TRADE POLICY REFORMS IN THE LDCs

Among the four countries selected for the present study, Myanmar is the richest with per capita income of over $500 whereas Nepal with a per capita income of little over $150 is the poorest(see table 2.1). During the 1980s except for Myanmar, per capita income for these countries have grown at close to 2% per annum -- a significantly higher rate of growth than for all the least developed countries put together. In terms of the overall growth rate in the 1980s, except for Myanmar the other three countries had an above-average rate of growth.

A crucial feature of the countries selected is that Bangaladesh and Nepal are mixed economies whereas Myanmar and Lao have been socialist-type, centrally planned economies. Because of this difference, the issues of trade policy reforms facing both Myanmar and Lao are somewhat different in nature than the ones facing Bangladesh and Nepal. The institutions and the legal framework relevant for a market economy, however, imperfect, are already in place both in Bangladesh and Nepal whereas in Myanmar and Lao these are in the process of being instituted and developed. In spite of these differences, in recent years all these economies have shared one common feature: all of them have initiated policy changes to move their economic policy regime in general and trade policy regime in particular towards greater outward-orientation.

Bangladesh:

For about a decade after independence in 1971, Bangladesh followed an import substituting development strategy based on extensive state control and ownership. But by the beginning of the 1980s,it was increasingly realised that the inward-oriented trade regimes and the bureaucratic

TABLE 2.1

MACROECONOMIC CHARACTERISTICS OF THE FOUR ASIAN LDCs

	Bangladesh	Nepal	Myanmar	Lao	All LDCs	All Developing Countries
Per capita GDP(in US $) 964	200	159		548	206	311
Annual Average rate of per capita GDP(1980-90)	1.7	1.9	-1.4	1.7	-0.4	0.6
Merchandise Exports as % of GDP in 1991	7.0	7.0	1.0	9.0	8.0	27.0
Merchandise Imports of % of GdP in 1991	14.0	22.0	1.0	18.0	15.0	27.0
Annual Average growth rate of merchandise exports in US $						
1970-80	6.3	9.8	14.3	19.1	10.2	25.9
1980-90	9.0	8.9	-5.3	12.6	0.7	3.2
Annual Average growth rate of merchandise Imports in US $						
1970-80	16.4	18.6	8.8	2.4	15.0	23.8
1980-90	5.9	7.3	-1.0	3.9	1.4	4.1
External Debt to GDP ratio: 1990	54.0	55.0	21.0	186.0	72.0	--
Debt service to exports ratio:1990	31.0	17.0	23.0	15.0	25.0	--

Source: United Nations, The Least Developed Countries 1992 Report, 1993, New York.

regulatory apparatus governing domestic enterprises had not only led to sluggish export growth but also to widespread inefficiency in the domestic economy in general and the industrial sector in particular. The structural problems got worse following the two oil shocks.

By about 1980 the Bangladesh Government initiated an adjustment programme supported by the International Monetary Fund, principally aimed at stabilising the economy. The stabilisation programme succeeded in substantially reducing the inflation rate. But this reduction in the inflation rate was brough about at the cost of a lower economic growth. The challenge for Bangladesh in the second half of the 1980s was, therefore, to restrain aggragate demand and at the same time employ structural policy changes to promote export growth. In response, starting from 1985, the Bangladesh Government embarked on a structural adjustment programme. A key component of this adjustment programme was a substantial reform of the trade policy regime.

As a part of trade reforms, tariffs were reduced and rationalised, import licensing and quantitative restrictions on trade were gradually relaxed and trade-related administrative procedures were simplified and streamlined. At the same time, new export incentive measures were introduced alongwith strengthening the existing ones. (See GATT(1992).

In 1986 the quantitative restrictions on imports were substantially relaxed with a large number of importables taken out of the fold of import licensing. In an important departure from the past, the Bangladesh Government shifted from the then existing "positive list" sytem of import licensing to a "negative list" system of import licensing. In the subsequent years, the negative list of imports itself was substantially pruned. In the mid 1980s, customs duties in Bangladesh ranged from 0 to 300 percent. As part of the trade reform programme, not only was the average customs duty lowered but also that the dispersion of tariffs was reduced.

A dual exchange rate system with an official exchange rate and a secondary exchange market rate (SEM) was introduced. The secondary exchange market consisted of two schemes - wage earners scheme (WES) and export performance benefit scheme (XPB). Under the wage earners scheme, foreign exchange remitted by workers abroad, tourist receipts and most service receipts were sold at a rate determined by a Committee of Authorised Foreign Exchange Dealers constituted by the Bangladesh Bank. Under the export performance benefit scheme, exporters were eligible to receive exchange rate premium, which was set to equal the difference between the WES rate and the official rate. Most public sector imports were at the official exchange rate and were subject to foreign exchange allocation on the basis of foreign exchange availability whereas for most commercial imports, the secondary exchange market rate were used. More recently, the dual exchange rate system has been abolished and the exchange rates unified.

Since the initiation of trade reforms in the mid-80s, all industrial machinery and raw materials are free from import licensing and the import procedures have been vastly simplified with the increasing replacement of administrative approval by credit authorisation. Both the level and dispersion of tariffs have been significantly reduced. At present, the import duty on basic raw materials ranges from 0 to 20 percent, on intermediate products 30 percent, and on finished products 50 percent, with the exception of certain items, such as motor vehicles, alcohol, cigarettes, airconditioners which attract duties ranging from 100 to 200 percent.

To mitigate the anti-export bias of the remaining quantitative restrictions and tariffs on imports, Bangladesh has a number of export incentive measures. These include a duty draw back scheme, a duty exemption scheme through bonded warehouses for exporters, a compensatory cash subsidy scheme for exports, concessional finance for exports and rebate of income-tax on income earned through exports. In addition, exporters can also have access to banned or restricted items of imports, if considered necessary. These export incentive measures have created a virtual tax-free environment for exporters.

The movement towards greater outward orientation in the trade policy regime has also been accompanied by a freer foreign investment policy. Since June 1993, foreign companies are allowed to borrow from local banks and foreign investors can now repatriate capital, profit and dividend with minimal restrictions. Bangladesh has also recently entered into a bilateral investment exchange treaty with the United States of America.

Nepal:

In the first half of the 1980s, the Nepalese economy had grown at a respectable rate of about 5 per cent per year, with the agricultural sector spearheading this growth. Although this represented a substantial improvement on the growth performance of the economy during the 1970s, Nepal's economy was facing major macroeconomic problems by the mid-1980s. First, Nepal had experienced quite high inflation, of about 9 per cent per annum, during the first half of the 1980s. Secondly, Nepal's per capita income was lower than that of most South Asian countries. Thirdly, Nepal's industrial sector was still insignificant, with the economy being dominated by the agricultural sector.

To address these problems, the Nepalese Government implemented a stabilisation programme in 1985-86, which was supported by an IMF Standby Arrangement. Realising that macroeconomic stability by itself would not lead to increased growth, the Government embarked on a structural adjustment programme supported by the IMF and the World Bank(See World Bank(1990)). The abrupt elapse of trade and transit treaty between India and Nepal in March 1989, however, adversely affected the adjustment programme and the growth momentum of Nepal. Rate of growth of GDP, which was about 5.5 per cent per year during the period 1985 to 1988 slumped to about 2 per cent between 1989-90. Exports also suffered as a result of the trade and transit impasse. With the removal of the duty-free status of Nepal's exports to India and the application of the MFN tariffs that were typically in the 100-150 per cent range, Nepal's exports to India vertually disappeared. Although the impasse ended by the middle of 1990, the Nepalese economy continued to be faced with slow growth, high inflation and large payments imbalance. To address these economic problems, the new Government which assumed office in 1991 initiated wide ranging trade reform measures(See Government of Nepal(1991)).

Following the devaluation of the Indian rupee, the Nepalese rupee was devalued in early July, 1991. This was followed by significant macroeconomic policy changes. The major thrust of the policy changes were on opening up the Nepalese economy to greater competition. Towards this end, tariffs on many primary commodities have been either discontinued or lowered. The basic customs duty on raw materials has been reduced by 25 per cent. Import licensing has been relaxed substantially in that industries requiring imported raw materials with less than 50 per cent of the total value of raw materials, are eligible for the necessary foreign exchange without import licenses.

As a result of these liberalisation measures, which have more or less kept pace with Indian reforms, there has been a substantial reduction in the quantitative restrictions on Nepal's imports. Tariffs have also come down substantially. The maximum tariff rate at present is 100%. Since July 1992 tariffs on raw materials and chemicals for the manufacture of pharmaceuticals have been reduced to zero and since March 1993 the Nepalese Government has substantially reduced the duty on certain capital goods. Import liberalisation has also been accompanied by strengthening of various export incentive schemes. A duty drawback scheme refunds the import duty paid on raw materials and intermediate goods required for export production. This is also supplemented by an export promotion fund and cash incentives for the export of certain products. On exchange rate, the Nepalese Government after experimenting with dual exchange system for about a year in 1992 has made the Nepalese rupee convertible on the trade account in February 1993.

These trade reform measures have also been supplemented by a more liberal foreign investment policy. The Nepalese Govt. has introduced a "One window" service for granting licences, facilities and other services for foreign investments. Foreign investors are allowed to repatriate foreign loans, interests on these loans, dividends and proceeds from the sale of equity. All in all, the 1992 foreign investment and technology act of the Nepalese Government offers services and facilities to the foreign investors which are designed to be comparable to those offered by the neighbouring countries.

Myanmar:

Although a socialist country, Myanmar's socialism never evolved Soviet-style nor was Myanmar formally integrated into the CMEA trading bloc. Yet, the system was highly autarkic with a high degree of Government controls.

In many respects, it had features more in common with the different dirigiste nationalist regimes that emerged in other parts of Asia and Africa in the 1960s than with the Soviet-type centrally planned industrialising system. Although non-agricultural enterprises were nationalised, important segments of the economy remained in private hands even during the peak of state ownership: retail trade, small industry and parts of the road and river transport system were privately owned.

In recent years, Myanmar has carried out economic reforms under the State Law and order Restoration Council Regime(SLORC). (See ADB, 1993). The SLORC Government after it came to power in 1988 decontrolled agricultural commodity prices and raised wages. It also increased the price of gasoline, raised electricity, telephone and water rates and allowed State enterprises to charge market prices for their products. The reform process has given a larger role for private sector. A number of restrictions on trade were removed. Private individuals were allowed to serve as commission agents for foreign companies and private entrepreneurs are allowed to export. Private trading with China, India and Thailand is also legalised. Foreign investment Law was passed and Foreign Investment Commission was constituted to consider foreign investment proposals.

As part of economic reforms to move the highly State controlled system towards a market economy, Myanmar is attaching great importance to trade reforms(Government of Myanmar(1993)). Until recently, foreign trade was strictly controlled by the Government. The primary objective of trade policy in the past was self-sufficiency in as many commodities as possible and for achieving this import substitution was emphasised. When the last Government took over in 1988, it had inherited a system of state monopolies in both exports and imports. Since 1988, the Government has gradually opened up export and import trade to the private sector, while allowing state enterprises to continue trading and allowing a growing number of joint ventures with private enterprises to engage in international trade. Private enterprises and joint ventures trade at the free market exchange rate while the Government and State enterprises continue to trade at the official rate of exchange. The private sector's share in total exports increased from 38% in 1989 to 67% in 1990 and its share in total imports rose from 42% in 1989 to 46% in 1990. The tariff rates in Myanmar range from 10-35% on basic raw materials to 500% on consumer goods. Imports of items such as grains, chemicals, fertilizers, pesticides raw cotton are allowed duty free entry.

Lao:

From 1975 to 1986 economic development policy of Lao was based on central planning and the development of public enterprises. Like many other countries, most of the State owned enterprises were operating inefficiently, Government resources were insufficient to provide capital and managerial as well as technical expertise needed to upgrade their performance. The internal as well as the external economic disequiliprium were rapidly worsening. In response, in the party Congress held in December 1986, it was decided to undertake a series of economic reform measures designated collectively as new economic mechanisms (NEM). The main objective of NEM is to rejenuvate the economic and social situation by a transformation of centrally controlled economy to a more liberal market-oriented one. The policy objective of the NEM include the increasing of productivity and competitiveness, to a greater reliance on market forces in determining prices and resource allocation and a greater role for private sector and foreign trade.(See ADB, 1993).

As part of the NEM, Lao has initiated a number of far reaching reform measures in its trade regime. Most exports from Lao except for the items mentioned in a controlled list of exports do not require any licence. The controlled list of items, which require a licence are coffee, sawn timber, parqeet and cattle. This licensing regulation has been introduced in order to protect the excessive outflow of national resources from the country.

Imports to Lao are conducted by state trading companies, mixed companies, cooperatives, and public enterprises. Import licenses, which are issued by the Ministry of Commerce and provincial government authorities, are required only for a select number of goods. Goods requiring import licenses inlcude motorcycles, cars, rice, petroleum products, cement, steel, and imported products which compete with domestically produced goods of high quality. These goods are also subject to individual enterprise quota restrictions.

A national import-export plan is a key element of the trading system. This plan is formulated by the Department of Foreign Trade in the Ministry of Commerce and takes into account the plans of individual enterprises and the requests furnished by each ministry and the provincial governments.

Import duties in Lao now range from 2 per cent to 80 per cent, although tariffs on most items range between 20 per cent and 30 per cent. Some goods may qualify for duty exemption or reduction under certain conditions. For instance, imported raw materials, meant for the production of necessary consumer goods may be exempted from duty or subject to concessional import duties.

Until 1988, all investment in Lao was either funded by state or foreign assistance. In 1988, the government began a drive to attract foreign investment and released a foreign investment code in July 1988. The code authorised both joint ventures and wholly owned foreign investment projects and guaranteed the remittance of profits and protection against nationalisation. An investment oversight board, staffed by the Ministries of Commerce and Foreign Relations and chaired by the Prime Minister, has been established to consider and approve investment proposals.

Section:3 EXPORT EXPANSION AND DIVERSIFICATION

It is difficult to quantify the effect of the trade policy reforms by the least developed countries on export expansion and diversification. First, such a quantification would require macroeconometric models of these economies, which can be used to simulate the effects of trade policy. Secondly, even if such macro models are available, since export expansion and diversification is the result of the culmination of many factors, it would be extremely difficult to disentangle the effect of trade policy from those of other factors. Given these constraints on a quantitative evaluation of the effect of trade reform, all that can be done is a much more qualitative assessment of the contribution of trade reforms to export expansion and diversification. One way of doing such a qualitative assessment is to look at trends in export expansion and diversification in the 1980s, a decade in which the four least developed countries initiated substantial trade reforms.

Export Expansion

The trade policy reforms of the 1980s appear to have been accompanied by reasonable export expansion in Bangladesh and Nepal whereas the export performance of Myanmar and Lao in the 1980s has been highly volatile. During the decade of the 1980s, dollar value of exports grew at an annual average rate of about 9 per cent in Bangladesh and Nepal, which is much higher than the average growth of exports achieved by all the LDCs (See Table 3.1). Myanmar's exports after having declined consistantly for most part of the 1980s, have started growing at impressive rates since 1988-89 whereas the trends in Lao's export growth is just the opposite: reasonably good growth during most part of the 1980s but a sharp deceleration since 1988-89.

It is difficult to arrive at any strong links between trade reforms and export growth based on these highly agggregative data. But it appears that the two LDCs - Bangladesh and Nepal - which have carried out extensive trade reforms have also achieved rates of growth of exports much higher than the average export growth of all the LDCs. Also, in the case of Myanmar, the trade reform measures appear to be leading to significant step up in export growth in the last three to four years, although the trends are much more mixed in the case of Lao.

Commodity-wise Export Diversification

If one considers the conventional aggregative measures of trade diversification such as the export concentration index, the export diversification index or the percentage share of top three export products, there does not seem to be any substantial improvement in export diversification for most of these LDCs. (See Table 3.2). Aggregative measures of export diversification have remained virtually unchanged during the 1980s in the case of Bangladesh and Myanmar, whereas there has been some reduction in the share of the top three export products in the case of Lao. In contrast to these, exports, if any thing, have become much more concentrated in the case of Nepal: the export concentration index more than doubling from 0.26 in 1980 to 0.59 in 1990 and the share of the top three export products increasing from about 48 per cent in 1980 to about 82 per cent in 1990. These aggregate measures of diversification, however, conceal an important change that has taken place in the export basket of Bangladesh and Nepal: the increasing importance of higher value-added items in the export basket.

Since the introduction of the reforms, Bangladesh has witnessed a striking change in the composition of exports. The share of higher value-added items like clothing has grown rapidly, whereas the share of raw materials and lower value-added items such as textiles, jute, leather and tea has declined or stagnated. For example, the share of clothing which constituted only about 2.6 percent of Bangladesh's exports in 1983 has gone upto 37 per cent by 1988. In contrast the share of textiles has come down from 45 per cent in 1983 to about 21 percent in 1988 and that of raw materials from over 15 percent in 1983 to less than 8 percent in 1988 (See Table 3.3). This shift in the composition of exports does indicate a very encouraging feature: that is the replacement of lower-value added goods by higher value added goods in the export basket of Bangladesh. In fact, over the last decade Bangladesh has emerged as a major exporter of garments. Garment exports which was about $ 7 million per year in the early 1980s had increased to over $ 600 million by 1989-90, now constitutes about 40 percent of Bangladesh's export earnings. About 55 per cent of garments exports go to the United States, about 35 percent to Europe and the remaining 10 percent mainly to Canada, Sweeden and Norway. In terms of quantity, Bangladesh is the tenth largest supplier of garments to the European Community and the seventh largest to the United States. Bangladesh's success in diversifying its export basket in favour of higher value-added goods was partly attributed to the international trading environment and partly to the economic policy reforms undertaken since the mid-1980s(See GATT(1992)). In terms of the international trading environment, the Multi-Fibre Arrangements (MFA) ensured market access for Bangladesh at a time when other exporters faced quota restrictions on their exports of garments. Many of these developing countries, therefore, relocated part of their production in Bangladesh. The international technology required for the entry into the trade was simple and labour intensive, and therefore well

Table 3.1

Growth Rate of Exports in US $(per cent per annum)

	1980-91	1986-87	1987-88	1988-89	1989-90	1990-91
Bangladesh	9.0	25.0	12.6	5.4	6.7	0.5
Nepal	8.9	5.7	28.9	-17.2	31.4	19.6
Myanmar	-5.3	-26.8	-37.0	55.8	51.2	32.3
Lao	12.6	3.3	30.6	-1.2	0.0	0.0
All LDCs	0.7	10.2	3.8	4.1	-8.7	5.2

Source, UNCTAD, The Least Developed Countries' 1992 Report.

Table 3.2
Measures of Export Diversification

	Bangladesh	Nepal	Myanmar	Lao
Export Diversification Index				
1980	0.915	0.874	0.850	-
1990	0.914	0.973	0.893	-
Export Concentration Index				
1980	0.400	0.255	0.326	-
1990	0.397	0.593	0.337	-
No. of commodities Exported				
1980	56	55	60	-
1990	72	12	55	-
% share of top three products in exports				
1980	74.9	47.9	67.8	95.6
1990	75.5	82.3	68.4	71.4

Notes: The top three products are as follows:

Bangaladesh: Jute goods(50.2%), raw jute(16.7%) and leather(8.0%) in 1980 garments(50.6%), jute goods(16.6%) and fish and crustaceans(8.3%) in 1990.

Nepal: Goat and Kid skins, (21.1%), timber (13.6%), and raw jute (13.2%) in 1980, wool carpets (47.7%), dresses (28.8%) and goat and kid skins (5.8%) in 1990.

Myanmar: Rice (39%), Teak (24.5) and pulses (4.3%) in 1980, teak (35.9%), pulses (26.9%) and rice (5.6%) in 1990

Lao: Electricity(47.8%), sawlogs (34.8%), and coffee (13.0%) in 1980, Sawlogs (33.3%), non-coniferous (23.8%), and electricity (14.3%) in 1990.

Sources: 1) United Nations, Handbook of International Trade and Development Statistics for 1992, New York 1993. For definition of export diversification and export concentration indices see p.244
2) UNCTAD,The Least Developed Countries 1992 Report, United Nations, New York, 1993.

suited to Bangladesh's factor-endowment. Government policy contributed to this process of diversification by creating an environment in which garment exports could take advantage of the available opportunities without being fettered by import restrictions or taxes. Besides providing an overall liberal import regime, the government also provided certain specific facilities such as bonded warehouses, back-to-back letters of credit for raw material imports, and until recently export performance benefit entitlements.

Like in the case of Bangladesh, the trends indicated by the aggregative measures are somewhat misleading in the case of Nepal too. For example, even though the share of the top three products in the export basket has gone up from about 48% in 1980 to about 82% in 1990, the composition of Nepal's exports seems to have changed in favour of somewhat higher value added items. In 1980, the top three products accounted for about 48% of Nepal's exports. These three products were goats and skins(21.1%), timber(13.6%) and raw jute(13.2%). By 1990, the composition of Nepal's exports had changed dramatically in favour of higher value-added goods like wool carpets(47.7%) and dresses(28.8%). These two items accounted for three-fourth of Nepal's exports. In contrast, the share of traditional, low value added exports such as goats and skins, timber and raw jute have become negligible. It, therefore, appears that like Bangladesh, Nepal has been successful in diversifying its export basket away from lower value added primary articles to higher value added, labour intensive manufactured products.

Unlike Bangladesh and Nepal, neither Myanmar nor Lao appears to have been successful in changing the composition of their export basket in favour of higher value added products. It is, however, important to mention here that both these countries started economic reforms somewhat later than both Bangladesh and Nepal. In addition, having been under centrally planned systems, the extent of reforms have also been much less in comparison to Bangladesh and Nepal. For example, in spite of their recent reform efforts, both Myanmar and Lao continue to have much more restrictions on trade than Bangladesh and Nepal. It is, therefore, not surprising that both Myanmar and Lao have been less successful in diversifying their export baskets. Rice, tea and pulses which contributed about 68% to Myanmar's export earnings in 1980 still continue to account for about the same extent even now. In Lao, timber and timber-related exports accounted for about 35% of exports in 1980; its share in exports has gone up to over 50% in 1990.

Geographical Diversification of Exports

In terms of geographical diversification of exports, the share of exports going towards industrial countries has increased significantly in all the four LDCs.(See table 3.4). In the case of Bangladesh and Nepal, this trend towards greater concentration towards industrial countries appears to have been closely related to the commodity-wise changes in the export composition - change in the export basket in favour of higher value-added exports. In the case of Lao, the reduction in the importance of electricity as an export item and the increase in the share of timber and timber-related exports seems to have contributed to the sharp increase in the share of exports going towards industrialised countries.

Table 3.3

Bangladesh's Merchandise Exports by Product Group, 1978-88
(US $ million and percentage)

	1978	1983	1988
	(Percentage share)		
Clothing	0.0	2.6	37.2
Textiles	49.6	44.9	20.9
Food	13.7	19.3	19.8
Other semi-manufactures	10.7	9.5	10.8
Raw materials	22.4	15.5	7.8
Fuels	1.2	3.7	1.3
Residual	1.2	0.5	1.1
Chemicals	0.4	1.3	0.4
Other consumer goods	0.2	0.3	0.3
Power generating machinery	0.0	0.0	0.1
Other non-electric machinery	0.0	1.0	0.1
Electric machinery & apparatus	0.1	0.6	0.0
Automotive products	0.0	0.1	0.0
Other transport equipment	0.3	0.7	0.0
Office machinery and telecommunications	0.1	0.0	0.0
Iron and steel	0.0	0.0	0.0
Ores and minerals	0.0	0.1	0.0
Non-ferrous metals	0.0	0.0	0.0
Total merchandise exports	100.0	100.0	100.0
Memorandum:		US$ Million (f.o.b.)	
Total merchandise exports	553	789	1,347

Source: GATT, Trade Policy Review - Bangladesh 1992, Volume I.

Table 3.4

Geographical Distribution of Exports
Percentage Distribution

		Industrial Countries	Developing Countries	Developing Asian Countries
Exports from				
Bangla-desh:	1986	59.6	35.1	13.2
	1992	78.7	19.7	9.7
Nepal:	1986	56.3	43.7	42.2
	1992	90.8	9.2	9.1
Myanmar:	1986	19.6	74.5	47.1
	1992	20.9	76.1	63.0
Lao:	1986	14.2	78.4	72.1
	1992	51.8	48.2	47.3

Source: IMF, Direction of Trade Statistics Yearbook, 1993.

SECTION 4: SUMMARY AND CONCLUSIONS

All the four least developed countries have effected significant trade reforms over the last decade. The timing of these reforms have varied somewhat across countries. Bangladesh and Nepal began the reforms somewhere in the early 80s, whereas Myanmar and Lao have initiated the reforms in more recent years. All the four countries, therefore, have joined in developing Asia's movement towards greater outward-orientation in trade and external sector policies.

To what extent these trade reforms have affected export expansion and diversification of these countries is difficult to pin point. For, export expansion and diversification is a multi-faceted phenomenon which depends on a number of factors. The trade policy regime of a country is only one such factor. This has been clearly demonstrated by the experience of Bangladesh where the international environment, especially the multi-fibre agreement, played a significant role in helping Bangladesh to diversify its exports in favour of higher value added products. Yet, it appears reasonable to conclude that without significant trade policy reforms, it would have have been difficult for Bangladesh to take advantage of the international environment and diversify its exports. Similarly, the positive correlation between greater outward-orientation and the share of carpets and garments in Nepal's exports in the 80s, is unlikely to have been just coincidental. Trade reforms must have helped Nepal to diversify its exports away from traditional primary articles like goats and skins, timber and raw jute, towards woollen carpets and garments.

Myanmar and Lao have been less successful than Bangladesh and Nepal in diversifying their exports towards higher value added products. It may not be a coincidence that the degree of outward-orientation in trade and external sector policies effected by these countries have also been less than that effected by both Bangladesh and Nepal. Overall, therefore, it appears that there has been a positive correlation between the degree of outward-orientation in trade policy and the share of higher value-added items in the export basket.

The increased share of higher value-added products in the export basket has also been generally associated with an increase in the share of exports going towards industrial countries. Hence, "what" these countries exported and "where they exported to" appears to have been highly inter-linked. The greater the share of higher value-added items in the export basket of a country, the higher has been the proportion of its exports going towards industrial countries.

The four least developed countries that have been selected for this study at present are at different stages in terms of the outward-orientation of their trade policies and the extent of export diversification. Quite obviously, therefore, the challenges facing these countries are bound to be somewhat different from one another. Yet it may be useful to identify a set of common factors that would be important for most of these countries. The key challenge facing most of these countries is to move their trade policy regimes towards greater outward-orientation in the future and at the same time maintain the viability of their fragile balance of payments. Further trade reforms would, therefore, have to be complemented by efforts at maintaining macroeconomic stability. As experience elsewhere shows, trade liberalisation without macroeconomic stability could worsen the already fragile balance of payments of least developed countries.

Broadly, there are two alternative ways of moving the trade regimes of these countries towards greater outward-orientation: one with a substantial reduction in the barriers to trade including tariffs coupled with fewer and lower export incentives and the other with a significant increase in the export incentives but not accompanied by major reduction in the barriers to imports. It is difficult to prescribe the precise combination of these two types of measures which would be best suited for the four least developed countries as a whole. But one general observation appears to be in order. A reform programme in which import restrictions are high but the anti-export bias of these restrictions are compensated by higher export incentives involves greater State intervention in the implementation of the trade policy. In contrast, implementing a trade regime with fewer quantitative restrictions and low tariffs on trade (and hence fewer and lower export incentives) requires less State intervention. From the point of view of the least developed countries, it appears that the former alternative of less interventionist trade regime with fewer restrictions on trade including a lower and more uniform tariff structure, accompanied by fewer export incentives would be better suited for a number of reasons.

First, the least developed countries in general have inadequate administrative personnel and are short of technically trained manpower. Administering a trade regime which requires detailed and discretionary administrative decisions, therefore, would put undue strain on the least developed countries. Second, a less interventionist trade policy regime is less susceptible to mis-judgement and abuse to which a more interventionist policy regime is prone. Finally, the more interventionist trade regime and the accompanying export incentive measures involving large subsidies would also invite retaliatory action by other countries (like countervening duties) under the GATT. Overall, therefore, it appears that it is advisable to the least developed countries to effect greater outward-orientation in their trade policy regime through fewer and lower trade barriers and hence lesser state intervention than through a combination of greater trade barriers and liberal export incentives. This also appears to be the general trend in trade policy among the developing countries in Asia such as Thailand, Indonesia, India, Pakistan and Sri Lanka.

Judging by the geographical composition of exports of the least developed countries, it appears that except for Myanmar and Lao, both Bangladesh and Nepal have extremely high concentration of exports towards industrial countries. The rapid growth in intra-Asian trade during the last decade seems to have more or less bypassed both Bangladesh and Nepal. Whether it happened in spite of best efforts by these countries or because of some fundamental flow in their trade strategy is difficult to answer precisely. Yet, developing Asia as a whole is now rich enough to be on the edge of an enormous consumer boom. There is a general consensus that unlike in the past when Japan and the East Asian NICs grew rapidly, intra-Asian trade is going to be a key source of exports and growth for the Asian developing countries in future. It is increasingly argued that in China, India, Thailand, Malaysia and Indonesia there is going to be little of the artificial repression of consumer demand that Japan and South Korea resorted to in their early development. It may, therefore, be well worth the effort for the least developed countries in the region to formulate policies and strategies which could take advantage of the likely intra-Asian trade boom in the future years.

As for Lao, it is located next door to one of the fastest growing countries in the Asian region at present - Thailand. In fact, the whole region of Yunan-Thailand-Lao-Cambodia and Vietnam is being increasingly recognised as an emerging "growth pole" in Asia. Lao, therefore, is situated in a region with great potential and there is no reason why it should not benefit from the dynamism of this newly emerging "growth pole".

Despite significant reforms in recent years, Myanmar's economy is at cross roads at present. In particular, reform measures to transform the economy toward market-oriented economy and to free foreign trade from the grip of State controls have been fragmentary and far from comprehensive. Despite reforms, Myanmar's import tariffs and export taxes has changed surprisingly little. The trade regime remains highly restrictive with registration and numerous licenses required to trade and State monopolies persisting in the provision of key trading services such as insurance and freight booking. The adverse effects of all these have been compounded by Myanmar's exchange rate management. Myanmar has been one of the very few countries in developing Asia whose real effective exchange rate appreciated substantially in the last decade. Hence, the task of trade reforms and trade diversification is the most challenging for Myanmar among the four countries studied in this paper.

Bangladesh and Nepal perhaps have the most outward-oriented trade regimes among the four LDCs considered here. However, even for these countries, there is considerable scope for further trade reforms. Consider, for example, Bangladesh. Although over time quantitative restrictions on imports have been substantially relaxed in Bangladesh, about 16 per cent of 4-digit HS categories are still affected by bans and restrictions. These include many items which compete with domestic production such as tobacco production, sanitary ware, news-print, stationery, carpets and floor coverings. There are also quantitative restrictions on the import of some industrial inputs.(See GATT 1992).

Secondly, in spite of considerable freeing of exports in recent years, Bangladesh imposes minimum price restrictions on exports of raw jute and jute products, ostensibly to take advantage of its market power for this commodity. In the private sector the minimum price restriction has often been circumvented by over-invoicing of exports. In the public sector, it has frequently led to accumulation of stocks and the under-utilisation of capacity, further undermining the financial viability of the public sector. Simultaneously, the imposition of a 30 percent local-content requirements on the exports of garments may prevent the diversification of this industry into higher quality products.

Thirdly, since the initiation of the trade reforms in the mid-80s by Bangladesh, tariffs have been substantially reduced and made more uniform; but even now the average tariff rate is as high as 70 percent. Moreover, there are a variety of tariff exemptions which are commodity- specific as well as end-use specific. As is well known, such exemptions have the effect of increasing the level and dispersion of effective rates of protection on the industrial sector.

Finally, even though trade-related administrative procedures have been gradually simplified over the years, many importers still face a cumbersome process. For instance, to obtain access to foreign exchange an industrial importer requires, among other things, a trade licence from local authority, a pass-book and import registration certificate from the Chief Controller of Imports and Exports, permission to import specific item from the sponsoring authority (e.g. The Board of Investment) and a completed letter of credit authorisation form. These trade related administrative procedures needs to be gradually simplified, if Bangladesh has to step up and diversify its exports in the future years. On a balance of considerations, therefore, the scope of further trade reforms for even the most outward-oriented of the four LDCs is indeed vast.

....

References

Asian Development Bank(1993), Asian Development Outlook, Manila.

Blejer, M.I. and Gyorgyszapary(1991), "The Gulliver Effect" and the 'Optimal Divergence' Approach to Trade Policies: The case of Nepal', World Development Vol.19, pp. 255-262.

GATT(1992), Trade Policy Review: Bangladesh Vol.1. Geneva.

Government of Myanmar(1993), Review of The Financial and Social Conditions For 1993-94, Ministry of National Planning and Economic Development.

Government of Nepal(1991), Economic Survey for Fiscal Year 1990-91, Ministry of Finance.

Madeley, John(1992), Trade and the Poor: The Impact of International Trade on Developing Countries, Intermediate Technology Publications, London.

Thomas, V. and World Bank(1987), World Development Report: Industrialisation and Foreign Trade, Oxford University Press.

World Bank(1990), Nepal: Maintaining Structural Reforms and Managing Public Resources, Asia Country Department, March.

UNCTAD(1991) The Least Developed Countries 1991 Report, Geneva.

UNCTAD(1992) The Least Developed Countries 1992 Report, Geneva.