How well founded are the devaluation worries?

ZAHID HUSSAIN

IN an interview published in this newspaper on January 3, the finance minister stated unequivocally "no currency devaluation". Is such a sweeping stance compatible with the government's own economic policy objectives?

Exports have been declining recently. Exporters argue this happened partly because our main competitors such as Vietnam allowed its currency to devalue more than us. As a result, its exports became more price competitive relative to ours. Vietnam's exports increased 9.6 percent in July-October while ours declined by 6.8 percent during the same period.

The finance minister is justifiably concerned about the effect of devaluation on the cost of imports. He does not want to devalue because the Bangladesh economy is highly import-dependent. The increased cost of imports will increase inflation. "We will die," he said.

Let's check the facts. Vietnam's annual import is about $225 billion, constituting over 92 percent of its GDP. Bangladesh's annual import is $66 billion, constituting about 23 percent of GDP. Clearly, Vietnam's economy is more import-intensive than the Bangladesh economy.

Since November 2018, Vietnam has allowed 1.6 percent devaluation of its currency, while Bangladesh allowed 1 percent. Inflation in Vietnam rose from 2.98 percent in December 2018 to 3.52 percent in November 2019 whereas in Bangladesh it increased from 5.35 percent to 6.05 percent during the same period. Vietnam devalued more with less inflation while Bangladesh devalued less with more inflation.

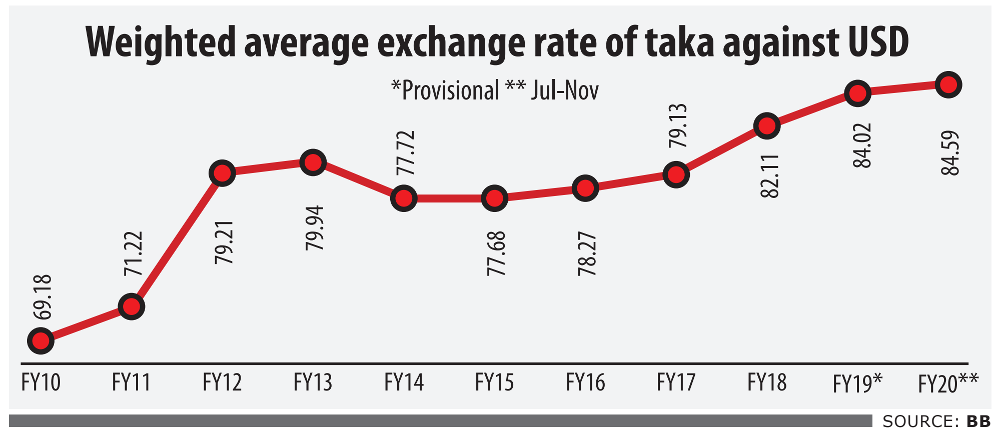
Import prices are not the only determinant of inflation. Also, the impact of devaluation on the cost of imports can be mitigated through compensatory adjustment in import duties.

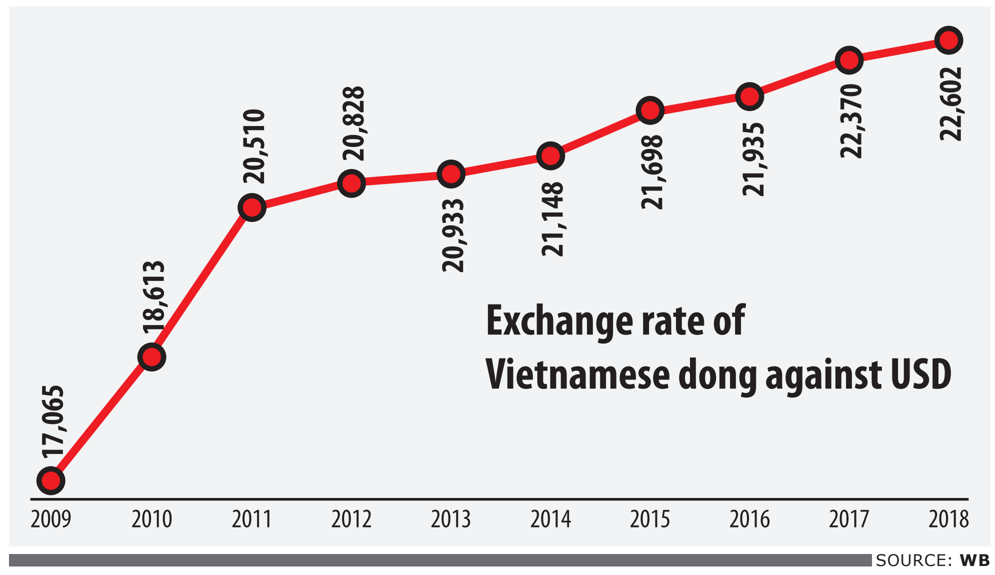
On other occasions, the finance minister expressed worry about the negative impact of devaluation on foreign direct investment (FDI). Let's check the facts again.

Vietnam attracted $29.11 billion in the first 10 months of 2019 while Bangladesh attracted $2.5 billion during the same period. Vietnam devalued more with more FDI while Bangladesh devalued less with less FDI. It is generally accepted that a devaluation increases foreign direct investment flows.

The finance minister worries that devaluation would escalate the cost of development projects. There are numerous factors that increase project cost. In Bangladesh, delays are a major factor. The exchange rate is relevant when contracting services or other elements of the project are purchased from abroad. If exchange rates change beyond the level predicted by the project sponsor, the cost of the project can increase. An extra element—contingency—provides cover against cost over-runs due to exchange rate changes. The impact of devaluation is, therefore, never as large as appears at first sight.

Another worry is devaluation makes foreign currency denominated loan servicing more costly. This is true when we calculate foreign debt servicing in the taka. The case for keeping the exchange rate unchanged on this ground depends on the impact of the devaluation on revenues and the cost of servicing domestic debt. Devaluation can increase revenues if the value of imports in local currency increases and by boosting production of exports as well as import substitutes. Interventions to stem currency depreciation deplete banks' taka liquidity. Interest rates rise, increasing the default risk and the cost of servicing domestic debt. Thus, on balance the fiscal impact of devaluation may be either a wash or even favourable despite increase in the local currency cost of foreign debt servicing. Because of these mixed effects, empirical studies internationally find no perceptible influence of devaluation on fiscal deficits.





In general, when markets are allowed free play, foreign exchange rates are determined by the supply and demand of foreign currency. However, foreign exchange markets are rarely allowed complete free play in any country. Central banks often intervene to smoothen volatility and provide uniform protection to domestic industries. Macroeconomic policy makers in Bangladesh deserve kudos for not doing anything to trigger disruptive volatility in the exchange rate. The practical question facing our policy makers is whether, through exchange market intervention, you want to take your chances on the side of under-valuing or over-valuing our currency.

Undervaluation of the exchange rate is, in fact, an industrial policy to promote growth in sectors producing internationally tradable goods and services. Undervaluation provides a subsidy to exports directly and automatically while protecting the domestic producers of import substitutes by increasing the cost of imports. It does not require a bureaucrat to select possible beneficiaries. Several Asian countries have used such strategic exchange rate policy to promote domestic manufacturing.

This non-selective industrial policy promoting tradable seems to be quite efficient, especially in countries with high levels of corruption and poor-quality institutions. Selective policies rarely work in developing countries where the quality of bureaucracy is far from perfect. The finance minister appears to have reawakened to the latter when he lamented "does anything happen according to timeframe in Bangladesh?"

Paradoxically, industry leaders in Bangladesh have revealed a preference for selective policies time and again. If correcting the overvaluation of the exchange rate through devaluation can produce the same industry specific result as a direct cash subsidy, should they not opt for the former than latter? Do not expect the industry to say yes, because it is in their self-interest to get both. However, when choosing between the two, they insist more on the latter because they do not have to compete with all others to benefit from the devaluation whereas the targeted subsidy is a lock-in for the insiders.

The finance minister is willing to provide Tk 5 cash subsidy per dollar of value added over imports to garments to compensate them for the overvaluation of the taka. What about non-garment exports? Won't this policy deepen our over-dependence on garments? Since the subsidy will be based on value added over imports, will this not encourage garments to under-invoice their imports when claiming subsidies, thus making corruption more profitable than it already is?

Our policy stance on the exchange rate has so far favoured taking chances with the overvaluation of the taka. This policy is inconsistent with the strategy of diversified tradable production-based industrialisation.

The author is an economist.

Rains give hope for record tea production

MINTU DESHWARA

Recent rains naturally spelt misery amidst the winter chill but have brought smiles all around for tea production, giving hopes of an early start to the plucking season.

Water gets scarce in winter, especially in the hilly Sylhet division where groundwater levels drop, making extraction difficult even from deep tube wells, and natural streams are reduced to a trickle.

Not all tea plants can bear with this limitation while just around 5 percent of the 166 tea gardens around the country are capable of going for artificial irrigation, which is spraying water using pipes.

While rains in Sylhet in December amounted to 3 millimetres, way below the 9mm average, it has already gone past the January average of 9.4mm to reach 12mm.

This moisture will be held by the soil for around a month, which producers believe will give rise to early buds and subsequently a week's head start to the plucking season that runs from March to October.

Moreover, rainwater contains high levels of nitrogen which aids the nitrogenation of the soil while the showers help dislodge any infestation of red spider mites, which feed on the sap and cause leaves to fall off.

This gives rise to possibilities of a continuation of record-breaking production.

Production in 2018 was a two-year high of around 82.13 million kilogrammes and Bangladesh Tea Board expects the final tally of 2019 to reach around 95 million kilogrammes.

Another bumper yield will come in 2020, expects Shah Alam, chairman of Bangladeshiyo Cha Sangsad, an organisation of the tea garden owners.

STAR/FILE

The government recommends garden owners increase plantation area by 2.5 percent each year by incorporating unused land.

"Plus, if we can get the price as good as last year, we might be able to secure a hefty profit margin," he added.

Bangladesh exported tea worth $1,470,311 in the July-November period of 2019-20, a 4.26 percent rise from the same period in 2018-19. Moreover, the country's annual consumption has reached 95.2 million kilogrammes, as per the tea board.

Hopes also come from a government recommendation for garden owners to increase plantation area by 2.5 percent each year by incorporating unused land, says Mohammad Ali, director of Bangladesh Tea Research Institute.

Tea cultivation first started on a commercial basis in 1854 in Sylhet's Malinichara tea garden, as per the tea board. Currently around 279,439 acres of land are under cultivation.

Of the gardens, 91 are in Moulvibazar, 25 in Habiganj, 19 in Sylhet, 22 in Chattogram, seven in Panchagarh, two in Rangamati and one in Thakurgaon.

Daimler recalls 744,000 Mercedes-Benz vehicles in US for faulty sunroofs

REUTERS, *Washington*

GERMAN automaker Daimler AG said on Saturday it will recall 744,000 Mercedes-Benz vehicles in the United States from the 2001 through 2011 model years because the sunroof glass panel could detach and pose a hazard.

The large recall covers more two dozen vehicles from C-Class, CLK-Class, CLS-Class and E-Class model lines. The automaker said the bonding between the glass panel and the sliding room frame might not meet specifications and could lead to sunroofs detaching.

Owners who paid for repairs for the issue will be able to seek reimbursements from Daimler. A Mercedes-Benz USA spokesman said on Saturday he did not have a worldwide vehicle total for the recall.

Dealers will inspect the glass panel bonding and replace the sliding roof if necessary, the company said.

Last month, Mercedes-Benz USA agreed to a $20 million civil penalty over its handling of U.S. vehicle recalls after a year-long U.S. government investigation into 1.4 million recalled vehicles.

Under the terms of the settlement, the automaker will pay $13 million and faces another $7 million fine if it does not comply with the agreement. The U.S. National Highway Traffic Safety Administration said the company failed to notify owners in a timely fashion in some recalls, did not submit all reports and did not launch at least two recalls in a timely fashion.

REUTERS/FILE

The Mercedes-Benz logo is seen before the company's annual news conference in Stuttgart, Germany.

Confidence crisis brings DSE back to red

STAR BUSINESS REPORT

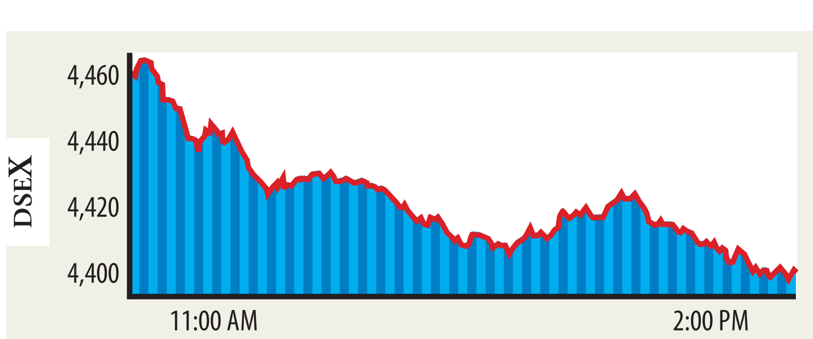
A confidence crisis has wiped off all the gain the Dhaka bourse has witnessed in the last six trading days as the benchmark index fell 1.32 percent yesterday.

Moreover, foreign investors sold more shares than what they purchased at a time when participation of institutional investors was thin, causing the DSEX to lose 59.15 points to end the day at 4,400.14.

United Power, Square Pharmaceuticals, Brac Bank, Renata and Olympic hit the index hard, taking away around 20 points from DSEX.

Turnover, another important indicator of the market, decreased by 24.39 percent to Tk 292.46 crore from the previous day.

Khulna Power Company dominated the turnover chart with transaction of shares worth Tk 19 crore, followed by LafargeHolcim Bangladesh, Bank Asia, National Tubes and City Bank.



Emerald Oil was the day's best performer with a 9.70 percent gain whereas Generation Next Fashion was the worst loser that shed 7.14 percent.

Among the major sectors, textile dropped 2.44 percent, life insurance 2.29 percent and fuel and power 1.79 percent.

Losers beat gainers as 269 issues declined, 52 advanced and 33 finished unchanged on the premier bourse.

The benchmark index of Chittagong Stock Exchange—CSCX—also dropped. It fell 99.16 points, or 1.20 percent, to finish the day at 8,109.28.

Losers beat gainers as 163 declined, 37 advanced and 20 finished unchanged on the port city bourse.

The stock exchange traded shares and mutual fund units worth Tk 9.14 crore.

Samsung Electronics to unveil 'innovative devices' on Feb 11

REUTERS, *Seoul*

SAMSUNG Electronics said on Sunday that it will introduce new, innovative devices in San Francisco on Feb. 11, with the electronics giant widely expected to unveil its new foldable phone and a new version of its flagship S model.

The move comes as the world's top smartphone maker seeks to maintain its lead in the foldable phone and 5G phone markets, with rivals plotting a catch-up in the nascent, but growing segments.

"Samsung Electronics will unveil new, innovative devices that will shape the next decade of mobile experiences," the South Korean firm said at an invitation letter. It said the event at 11 a.m. Pacific time will be live-streamed.

In a teaser image, Samsung hinted at two phones - one shaped like a square and another with a rectangular form.

In October, Samsung Electronics unveiled its new foldable phone concept that folds vertically like an old flip phone. Its first foldable phone, which folds horizontally, was launched in September after delays caused by screen problems.

Samsung Electronics has traditionally unveiled new versions of its flagship Galaxy S phones ahead of the Mobile World Congress which takes places in February.

A Samsung spokeswoman declined to comment on which models it will unveiled at the upcoming event.

REUTERS/FILE

The logo of Samsung Electronics is pictured at the company's factory in Tijuana, Mexico.