

# Higher growth a must to raise income status

FAARIA TASIN

THE recent reclassification of Bangladesh to a lower middle income country (LMIC) has been a highlight in its long voyage towards economic development. But what does it really imply? Is it reason enough for us to relax for the time being?

In order to progress to an LMIC, a country's gross national income (GNI) per head needs to be higher than \$1,045. Bangladesh's GNI in 2014 stood at 1,080 and as such it was promoted to an LMIC.

This is, no doubt, the fruits of the country's resilience over the years. We know that Bangladesh has been able to maintain an economic growth rate of 6 percent and above despite the dreadful global economic slumps.

For Bangladesh, joining the league of LMICs is just the first step towards further economic growth. The country now envisages becoming an upper middle income country (UMIC) for which it needs to churn out an annual GNI per head of at least \$4,126.

Simple calculations can tell us that if the Bangladesh economy can grow by 8 percent annually, this can be achieved by the early 2030s. However, at the current growth rates of 6 percent, the country may not be able to achieve its target even in the next 30 years.

It is important to note that Bangladesh has climbed the minimum threshold level by a narrow margin to get promoted as an LMIC and still is at the bottom of that echelon. The country still has

COUNTRY	GNI per capita (current \$) in 2014
Bangladesh	1,080
Pakistan	1,410
India	1,610
Vietnam	1,890
Thailand	5,410
China	7,380
United States	55,200

SOURCE: WORLD BANK

not been able to achieve its growth rate target of 7 percent.

East Asian economies have shown that transformational changes in the economy came about when these countries were growing at a rate of 7 percent or higher annually.

For Bangladesh, achieving the growth rates of 7-8 percent per year would require going the extra mile. Let us look at the investment scenario in Bangladesh.

Investment as a proportion of GDP has been hovering around 28 percent for the last five years.

Though public investment has been on the rise in recent years, private investment (which is instrumental in attaining higher growth rates) seems to be more or less static.

In order to achieve growth rate of 8 percent, investment to GDP ratio needs to increase from 29

percent to 35 percent.

Turning to foreign direct investment (FDI), Bangladesh managed to rake in only \$1.5 billion in 2013 as compared to India (\$28 billion), Vietnam (\$9 billion), Malaysia (\$11.5 billion), Indonesia (\$23 billion), and China (\$347 billion).

Despite having advantages of cheap labour and large market size, investment is arrested by problems in enforcing contracts, getting electricity and registering property (Doing Business Report, 2015).

Other major barriers to investment include a lack of energy, inadequate infrastructure and political instability.

Growth has been stalled by insufficient energy. Investment is required in the energy sector to keep up with the rising demand. All these factors can hinder economic growth and discourage foreign investments.

Exports have hugely contributed to higher growth rates over the decades. However, the country's export basket is largely concentrated on garments that made up 82 percent of the total exports in fiscal 2015.

This makes the industry vulnerable to shocks that may stem from domestic inadequacies and rival countries. A way to lower dependency on garments and to increase exports is through adding new products into the export basket and finding new markets.

Also the protection system that currently exists in Bangladesh creates an anti-export bias which makes domestically produced import competing goods more

profitable to sell in the country rather than exporting.

Investment in human capital needs to be increased. Government expenditure allocation for education is only 1.8 percent of GDP compared to India (3.8 percent), Indonesia (3.6 percent) and Vietnam (6.3 percent).

The problems of dropout rates in primary (21.4 percent) and secondary education (44.4 percent) still persist. Moreover, public spending on health is only 0.7 percent of GDP.

Remittances have also been a major contributor to the economy, generating a total of \$15 billion in fiscal 2015. Increasing education of migrants and improving their skills can help raise the average remittance per worker.

Promotion to LMIC status can also lead Bangladesh to lose the advantages that it used to get as a low income country. For instance, the terms and conditions may get stricter for getting funds from development agencies.

On the other hand, the country can now take out loans relatively easily from international financial institutions due to its higher credibility.

It is also important to remember that becoming an LMIC does not necessarily mean greater income equality. We must note that a quarter of the population still remains below the national poverty line.

For Bangladesh, growth should be sustainable and inclusive to achieve its targets.

The writer is the head of research at The Daily Star and can be reached at faaria.ts@gmail.com.

# Automakers buckle up for more China woe after stock crash saps sales

REUTERS, Beijing

Automakers in China may be forced to come up with more drastic mitigation measures when July sales results released from this week likely reveal a fourth month of contraction after a stock market crash sapped consumer sentiment.

Many Chinese who put money in the mainland bull market in the first half of 2015 had to delay big-ticket purchases like cars, analysts said. But a crash from mid-June erased as much as \$4 trillion in share value in under a month. What is left of their money is now locked in stocks as many try to avoid losses.

Sales in the world's biggest auto market have been hit by declining sentiment as the economy grows at its slowest in 25 years, prompting cost-cutting and discounts. But the crash likely left July sales falling more than June's 2.3 percent, analysts said.

"Car manufacturers are biting their nails as they wait to see July sales and the full impact the stock market crash really had," said a Shanghai-based executive at a major U.S. carmaker.

China's auto manufacturing body said

it more than halved its 2015 sales forecast because of the crash's impact on sentiment, while consultancy Automotive Foresight last week demonstrated a correlation between money locked in stocks and falling sales.

Audi AG sales chief Christian Klingler in a conference call on Thursday, said China will turn "into a bumpy road in the next few months".

The government took several measures to stabilise share prices, but they continue to fluctuate wildly with last week seeing the steepest single-day fall since 2007.

Analysts expect car sales will continue to be weak at least until stocks stabilise as fear of another tumble cloud consumers' future finances in uncertainty.

Automakers, many of whom have already flagged slowing sales, start reporting China figures on Monday, beginning with Japan's Toyota Motor Corp. The China Association of Automobile Manufacturers releases overall market data next week.

Toyota and compatriots like Honda Motor Co Ltd look likely to lead the pack due to strong sales of new sports utility vehicles (SUVs) as many middle-class Chinese trade up from sedans.



New vehicles are seen at a parking area of an automobile factory in China.



A man walks past a Banco Bradesco branch in downtown Rio de Janeiro.

# HSBC selling unprofitable Brazil unit to Bradesco for \$5.2b

REUTERS, Sao Paulo

HSBC Holdings Plc agreed to sell its Brazilian unit to Banco Bradesco SA for \$5.2 billion, retreating from the second-largest emerging market economy after years of disappointing performance.

Europe's No. 1 bank said in a statement on Monday that the accord with Bradesco includes the disposal of the HSBC Bank Brasil SA Banco Múltiplo and the HSBC Serviços e Participações Ltda units. The sale, which still requires regulatory approval and was sealed on July 31, could be completed by June next year.

The purchase price, which could undergo adjustments to reflect the net asset value of both businesses and is equivalent to 1.8 times book value, was way above what analysts expected. Reuters reported on July 20 that Bradesco had entered exclusive talks with HSBC after offering to pay about 12 billion reais, or 1.2 times book value, for HSBC Brasil.

Other sources had told Reuters in June that fellow suitor Itaú Unibanco Holding SA had placed a bid below book value for HSBC's Brazilian business. Bradesco, Brazil's second-largest private-sector bank, is currently trading at about 1.5 times book value. The acquisition will allow Osasco, Brazil-based Bradesco to close the asset gap with larger rivals Itaú and state-controlled banks Banco do Brasil SA and Caixa Econômica Federal. HSBC Brasil's focus on high-income customers fits well into Bradesco's plan to ramp up sales of specialized financial services for the wealthy and larger corporations.

"The acquisition will create scale gains and the optimal use of business platforms,

leading to bigger nationwide coverage ... and reinforcing the bank's presence in the high-end income segment," Bradesco said in a securities filing.

HSBC, which arrived in Brazil late in the 1990s, never gained enough size to pose a real threat to Itaú, Bradesco or Banco do Brasil, the nation's top lender by assets. HSBC Brasil has 854 branches, 21,000 employees and assets of about 170 billion reais, representing about 2.3 percent of Brazil's banking system assets.

Strategy missteps coupled with rising competition turned the unit into a problem for HSBC Chief Executive Officer Stuart Gulliver, who in June laid out plans to slash nearly one in five jobs worldwide and fix operations which, like in Brazil, were grappling with operational underperformance, high compliance costs and fierce competition.

Slow asset growth prevented HSBC Brasil from gaining scale to win market share, and return on equity was a negative 4.2 percent last year. ROE, as the gauge is known, reached about 16 percent four years ago.

The disposal of the Brazilian business will help HSBC reduce risk-weighted assets by about \$37 billion. Gulliver set a target of \$290 billion in planned asset reductions to take advantage of potential growth opportunities elsewhere.

"I am pleased to be able to announce today a transaction which achieves both a solid financial outcome and swift delivery of one of our stated actions," Gulliver said in the HSBC statement.

HSBC was advised on the deal by Goldman Sachs Group Inc. Bradesco was advised on the transaction by its own investment banking unit Bradesco BBI, JPMorgan Chase & Co and NM Rothschild & Sons Ltd.

# Factory growth bucks Asia trend, speeds to six-month high

REUTERS

Indian manufacturing activity expanded at its fastest pace in six months in July as new export orders accelerated, a business survey showed on Monday.

The Nikkei Manufacturing Purchasing Managers' Index, compiled by Markit, rose to 52.7 in July from June's 51.3, bucking weakness seen across much of the rest of Asia. The 50-mark demarcates contraction from expansion.

"This reflects stronger increases of new orders and output. Furthermore, the sector was also boosted by the quickest expansion in export orders since February," said Pollyanna De Lima, economist at Markit.

A Reuters poll last week predicted the PMI would dip slightly to 51.0.

Firms resisted passing on higher raw material costs to customers, which will be good news for the Reserve Bank of India ahead of its next policy review on Tuesday. It is expected to leave interest rates on hold.

Retail inflation in June crept to an eight-month high but remains far from the double-digit levels less than two years ago and within the RBI's target of 2 to 6 percent.

The new export orders sub-index jumped to 54.5 from 51.8, the highest reading in five months, which coupled with a similar increase in domestic orders suggests renewed demand for Indian goods both home and abroad.

But a Reuters poll last month suggested India's economic growth prospects have dimmed due to delays in passing reforms through parliament.

"Although the latest data suggest that the manufacturing upturn gained traction, worries regarding the labour market persist," De Lima said.

# Western companies look hard at China as growth slows

REUTERS, London

THE Chinese slowdown is forcing many Western companies to take a hard look at their businesses there, leading many to reduce investments, costs and product lines and to tackle increasing bad debts.

Double digit growth rates during the first decade of the millennium lured scores of Western companies to invest heavily in China. But in recent years growth has slowed sharply, hitting demand and raising doubts about the financial health of Chinese companies.

A recent equities market rout has dashed hopes China will, in the coming years, return to the robust growth it saw in the past.

"We had five fabulous years in China, of course, where we grew strong double-digit, and it has been gradually slowing down. Currently, in China we had negative order intake," said Frans van Houten, chief executive of Dutch electronics group Philips NV, on a call with analysts on Monday.

"Going forward, we need to be much more modest on expectations with regard to China growth; that's just being realistic," he said.

The size of China's economy means executives are not talking about withdrawing from the market but they say business cannot continue as normal.

"I'm optimistic long-term and medium-term that China will come back. Short-term, we need to manage through the drought that we see," said Ullrich Spiesshofer, CEO of Swiss-based industrial conglomerate ABB.

ABB is carefully managing costs and working hard to convince customers its products offer value despite premium prices. Stuart Rowley, vice president at Ford Motor Company, said his company had responded to the softening market by cutting production.

Such actions have knock-on impacts on suppliers, which are also often Western. French auto components group Valeo said slackening demand from Chinese car factories was forcing it to review its growth plans.

"We see the growth rate slowing down. And in the summertime, some of our customers are extending their summer holidays ... Of course, we adapt hiring and CapEx (capital expenditure) to current market conditions," said CEO Jacques

Aschenbroich.

Will Hallyer, partner with Strategy Consultants OC&C, said the toughening conditions were prompting companies to shift their focus from boosting market share to ensuring their operations were profitable or at least reducing any losses.

"It had been more of a land grab mentality -- buy a position, invest heavily in growth and have confidence that at some point you'll be able to make money," he said.

"As the market slows down, it accelerates the shift toward people thinking hard about making sure they have a business that makes money," he added.

Strategies vary across companies and sectors. Some have focused on cost reductions -- General Motors flagged "material cost performance"



Dumex milk powder products of Danone are seen on display on shelves at a supermarket in Beijing.

in China to investors. Acting CEO of Sweden's Volvo AB Jan Gurander said this was easier to achieve in China than in Europe, where workers enjoy more protections and factory shutdowns can be politically sensitive.

Others, including BMW and eyewear manufacturing Luxottica, are trying to attract increasingly cautious Chinese consumers with price cuts.

Some companies are rethinking their product lines. French dairy group Danone told investors it was offloading its Chinese business, Dumex, which operates in a highly competitive, commoditized market, to a joint venture partner to allow it focus on marketing its international brands which offer the potential for higher margins.

The deteriorating Chinese environment is also forcing companies to think harder about credit risks.

Swedish lockmaker Assa Abloy Ab's Chinese unit is heavily exposed to the hard-hit construction industry. Chief Financial Officer Carolina Happe said the time it took for Assa's Chinese customers to pay had increased by a month in the past year, to 99 days. That compares to a group average of 55 days. The change could lead to increased bad debt provisions, she said.

Volvo issued a warning to investors last year that it would have to take a 650 million Swedish Crown (\$75 million) charge for expected credit losses in China. Gurander told investors in mid July his company was having tough discussions with dealers about outstanding debts but

it was hard to know if the situation was stabilizing or not.

Growing credit risks are also prompting some Western banks to rethink their exposure to China. Sergio Ermotti, CEO of Swiss-based UBS AG, said it had stopped lending money to onshore clients in China.

But even as they moderate their ambitions in China, companies retain an eye for growth opportunities. Some are hoping the stock market drop could help them snap up local companies cheaply.

But with many Chinese companies still supported by government interventions like cheap credit, bargains are few, executives said.

"There are many, many companies for sale, and we are looking to many of those. Still they haven't felt the heat of the downturn in full yet.