

Embrace diversity or accept divorce



TWO major divorces are in the making in March. The obvious one is Brexit, which officially occurs on March 29. The other is the deadline for the US-China trade negotiations on March 1, when US tariffs on

USD 200 billion worth of Chinese imports will increase from 10 percent to 25 percent. Even though a trade deal is likely, as both sides want to have a deal and the market is expecting one, this will come down to the wire as the gap in what can be achieved in the deal is still daunting.

Both negotiations have profound implications for years to come. Like all divorces, the disagreements are acrimonious, with second and third-order costs on everyone else involved.

So far, Britain seems to be bracing for a major slowdown, deal or no deal. The British statistics office reported that the British economy grew only 0.2 percent during the fourth quarter of 2018, with growth falling in December.

As Bank of England Governor Mark Carney warned in his global outlook this week, the global expansion is now weakening and risks are intensifying, because global monetary policy has been tightening, trade tensions increasing and China is also slowing. The more important risk he identified is the reversal of globalisation, caused by growing imbalance on the trade side due to the continued US current account deficit, in a situation when the US dollar has been more dominant than ever. Interesting enough, the Chinese are no longer major buyers of dollars, as their foreign exchange reserves have remained flat, whereas going forward the US current account deficit will be funded more than ever by the Japanese (through their quantitative easing) and also the Eurozone. Expect US trade pressure also on Japan and the Eurozone.

The second globalisation risk is social, with greater imbalance in income and wealth in many countries, because the benefits of free trade are shared unequally. Consumers



Containers are seen at a port in Lianyungang in China's eastern Jiangsu province.

PHOTO: AFP

overall benefit from global trade, but many workers in advanced countries have either lost their jobs or seen a fall in real wages.

The third globalisation risk is the loss of control and trust in democracy and sovereignty in many countries. Part of the problem is that barriers to trade have increased three times higher for services than for products. And this hurts countries that are strong in the services trade, such as the United States and the United Kingdom.

This is where the growing protectionism is going to hurt everyone. The Bank of England estimates that an increase in tariffs of 10 percentage points between US and its trading partners would take 2.5 percent of US output and 1 percent off global output through just the trade channel alone. If non-trade factors are taken into account, such as tighter financial conditions, greater uncertainty and permanent tariff increases, the output losses

could double to 5 percent for US GDP and half that for global GDP.

It is thus not surprising that despite the recovery in the advanced economies, business sector investments have not increased commensurately. Indeed, UK business investments growth has fallen by 3.7 percent in the last year despite a recovery in growth, profits and accommodative monetary policy.

Carney's conclusion is that "it isn't easy to win a trade war."

What is true for Brexit is also true for US-China trade disputes.

The barriers to reconciliation are huge, because there are now fundamental differences in outlook, approaches and territorial sovereignty on both sides of the Atlantic, English Channel and the Pacific.

Business confidence cannot be good, because in the case of investors in Britain, no one can predict with any certainty what deal

is going to be struck, including the possibility of a no-deal.

Either way, investors will take on a low-risk approach by avoiding long-term investments and sticking to cash. There is little doubt that in the short-run, Britain will be the loser, but with a flexible exchange rate, she will be able to cushion any long-term trade shocks with a competitive sterling.

At the same time, the Eurozone which sells a large portion of its cars and other products to Britain would also have to deal with a trade shock, on top of the internal complexities of keeping the Union intact. The Yellow Vest protests in France has weakened the ability of the French government to negotiate strongly with the Germans on European fiscal discipline issues, at a time when the Italians are now making very different noises from the other partners on austerity, immigration and

foreign policy issues.

In the Pacific zone, the longer the US-China trade tensions persist, the worse will be the investment climate overall. The major trading partners of both nations do not wish to make clear partnership choices, given the huge potential size of the China market and limits to the growth in the mature US market.

What is unspoken at the present moment is that if no deal is made, exchange rate flexibility of the RMB cannot be ruled out. No one wants to go this route, because a competitive devaluation as the solution to a trade war can only lead to another global recession that is reminiscent of the 1930s.

So even though the West worries, like Carney, about the risk of China's debt overhang, the reality is that if China truly undertakes the structural reforms that almost everyone agrees on, she will emerge more productive and competitive than before even in the face of higher trade tariffs. With a balanced current account situation, China has both the fiscal space and the monetary policy potential to undertake the necessary structural reforms and reflate domestic consumption at the same time.

This is because even if China buys more from the US, the rest of the world would worry if that increase in imports comes at their expense. All this means that not only is the trade war negative directly for US consumers, it will hurt trade and jobs for the rest of the world.

This is why feuding parties need to be realistic and come to terms that cannot be ideologically pure on either side. For the US hawks to expect that the US can enforce standards on China is as realistic as China enforcing ideas on US hawks. Even for the mightiest military force in the world, to sit down with the Taliban is to admit that the US wins by losing wars.

Negotiations are now down to the wire, without any illusion as anything will be solved in the medium term. As that is the negotiation style in Washington, expect nothing but higher political risks in the near future.

Andrew Sheng writes on global issues from an Asian perspective. Copyright: ANN

Some pre-emptive measures to avoid the middle-income trap

TAHMEED RIFA

GRADUATION from a low-income to a middle-income country has long been coming for Bangladesh as it has been performing extremely well among developing countries over the last few years. Robust economic growth supported by an export intensive industry and a burgeoning service sector has pushed the country into the limelight as a beacon of inspiration for most LDCs. While superficially the country might seem to be gliding along, internal deterrents like a lacklustre banking sector, high youth unemployment, lack of export diversification and the gradual deterioration of its agro-economy are dragging the country back.

But, focusing only on short term problems can sometimes blind a country from seeing the true problems ahead. And anticipating the bigger, more obstinate issue of falling into the "The Middle-Income Trap" is a possibility that Bangladesh is not entertaining.

Bangladesh has created for itself a self-sustained brand image in the global market as one of the finest apparel processors around today. Boasting around 5,000 factories and employing around 4 million people, mostly women, the RMG industry is one that is leading from the front in the quest for economic glory. Since the 1970's, the country's dependence on export has exponentially increased with RMG taking up 80 percent share of total exports. The RMG industry's success is highly dependent on cheap labour and quality processing, making it an attractive investment for foreign buyers, and propelling it into being the second largest exporter of clothing goods. But this feat is not unique to Bangladesh. This initial growth boom is a textbook example. Most developing countries have shared a fairly similar storyline; running past the low-



ILLUSTRATION: JOHN TOMAS

income group only to be stuck at the middle-income bubble.

One of the primary criteria for graduation is a Gross National Income (GNI) per capita of USD 1,230 and Human Asset Index (HAI) of 66 or above. This quite strikingly indicates a considerable rise in the overall living standard of people. The minimum salary grade for RMG workers is currently set at Tk 8,000 per month or USD 4 a day, with more and more revisions of the provision coming up in the future. With each passing day, Bangladesh is gradually losing its core competency in cheap labour.

This in turn is biting into the profitability of RMG manufacturers by raising Selling, General and Administrative expenses. With foreign buyers' reluctance to raise final retail prices, this has come up as a major concern for the RMG factories, forcing some of them to even incur losses.

Beyond that, poor port logistics and rising transportation costs have compelled some US and EU buyers to opt for nearshoring. So, lack of export diversification and over-reliance on the labour intensive RMG industry might come back to haunt Bangladesh, as has been the case for most middle-income trapped countries.

While the status of graduation is comparatively paramount, there are certain drawbacks that come with it. One such obstacle is losing preferential duty. Bangladesh currently enjoys duty free access to the EU market in accordance with the "Everything but Arms" initiative along with preferences in China and India. After graduation, Bangladesh will face 15.62 percent tariff on average in the EU along with the existing 10 percent in the US. This is likely to lose the country USD 2.7 billion in export earnings. Another impediment is ineligibility

for concessional loans from the World Bank. All these, coupled with an unskilled labour population are likely to limit economic growth from 2024.

Now is a better time than any to wisen up in order to minimise the damage. The country should underline what adjustments it needs to make as well as derive empirical initiatives from similar stories.

Competitive edges are more often than not features that set you apart, and what better way to establish an advantage than through continuous innovation? Bangladesh sits on the lowest position in South Asia in terms of innovation along with consistently scoring low in ranked institutes, research papers and citations. One salvation in this regard is research and development. The country needs to make firms more research intensive through incentivising R&D expenses. And in order to draw in more private and public investment towards R&D.

The government along with the help of NGOs must also utilise foreign aid sitting idle in the pipeline to incorporate a culture of research in the educational institutes in the country in the form of upgraded labs, better instruments and more relevant facilities. Developed countries spend on average about 5 percent of their GDP on R&D. Expenditure of 1 percent of total GDP for Bangladesh should suffice for the next 5 years. Prioritising research is at the forefront of Malaysia's "New Economic Model" (NEM), formed to help the country graduate to a developed one.

Industrial Revolution 4.0 comes hand in hand with innovation. Dealing with the tech revolution to come is tricky for Bangladesh which has been raking in jobless growth over the last few years. Of the 109.1 million working age population, only 63.5 have been participating in the labour force, with

Bangladesh having to cope with 2 million young people entering the market each year. With the introduction of AI, the RMG, leather and agro-processing industries would lose a further 5.4 million jobs in the future. But there is no way to circumvent this other than sustainably espousing the insurgency.

Sustainably striving through this change requires heavy investment in social capital. This would entail a core structural change in education as demonstrated by Malaysia formulating "The New Education Blueprint 2013-2025". An educational shift in primary, secondary and tertiary, focusing on training children from the start to be fluent in technology is a must to overcome economic myopia. Furthermore, encouraging a new generation of entrepreneurs through easier fundraising facilities like accessible financing instruments and start-up funding platforms should be undertaken. Another sector that needs dire attention is on the skills frontier. Currently, the mismatch in industry requirements and employee skills is being tackled by the government through the introduction of Industry Skills Councils (ISCs). But they are completely negligent in training people for future changes in skills requirements.

Only, through more strengthened cooperation among the private and public sector can the country hope to avoid the imminent problems that are to come. The country should immediately deploy resources in order to assess the impacts of the problems that come with graduation and form committees to articulate possible steps that should be implemented in order to avoid the "Middle-income trap".

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ON THIS DAY IN HISTORY



February 16, 1959

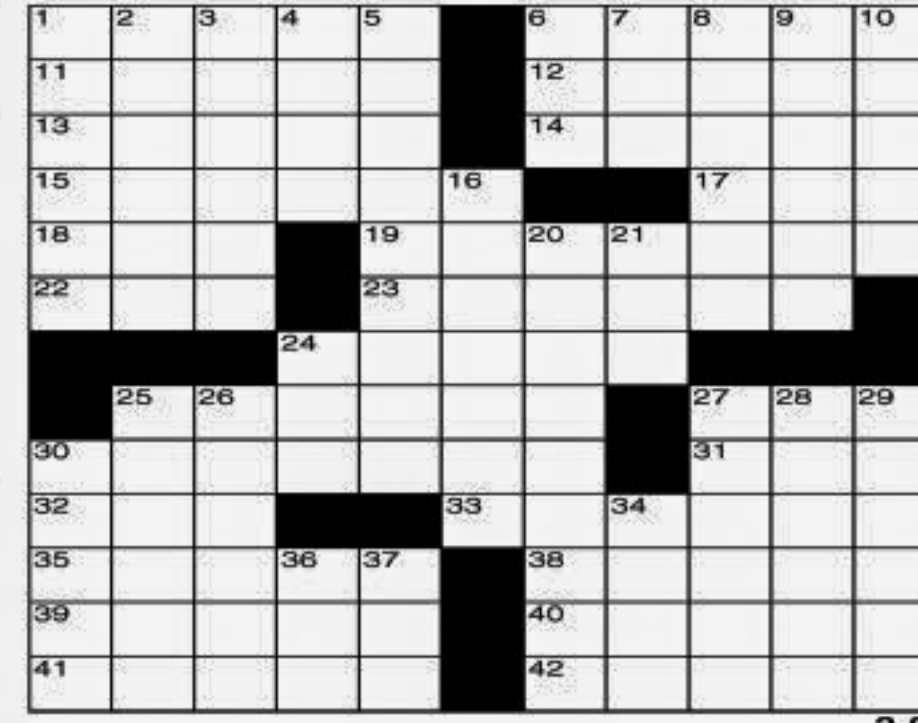
CASTRO BECOMES PRIME MINISTER

Cuba's revolutionary leader Fidel Castro becomes the country's 16th and youngest ever premier.

CROSSWORD BY THOMAS JOSEPH

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|-------------------------|----------------------|------------------------|
| ACROSS | 31 P look-alike | 8 Neatnik's no-nos |
| 1 Satchel part | 32 Curator's concern | 9 Concert bonus |
| 6 Toy store section | 33 Trembling | 10 Declare |
| 11 Sweet liqueur | 35 Intended | 16 Copier features |
| 12 Bond, e.g. | 38 In debt | 20 Observatory feature |
| 13 Critic, at times | 39 Earlier | 21 Cow chow |
| 14 Puccini opera | 40 Pound parts | 24 Center |
| 15 Venus' love | 41 Boxer Liston | 25 Corrida star |
| 17 Lush | 42 Borders | 26 Get |
| 18 Foreach | | 27 Going awry |
| 19 "Suits you right!" | DOWN | 28 From that place |
| 22 Id— | 1 Tough situation | 29 Avoids |
| 23 Iron's target | 2 Market events | 30 Highway exits |
| 24 With fervor | 3 Snappy answer | 34 Blown away |
| 25 Pat cover | 4 Church reply | 36 Opposite of oui |
| 27 Airport sched. abbr. | 5 Sub feature | 37 Take a stab at |
| 30 Cops' foes | 6 Heater | |
| | 7 Previously | |

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YESTERDAY'S ANSWER

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