

# RMG sector: Challenges versus portunities

**M Shahidul Islam**

The raging controversy over wage hike in the readymade garments (RMG) sector continues. This is happening at a time when the industrial structure in China, the world's largest exporter of apparel products and one of the major competitors of Bangladesh, is undergoing rapid transformations. While the China shift could benefit Bangladesh's RMG in the medium to long run, the industry faces some short-term challenges largely owing to economic problems in the advanced economies.

While the emerging markets returned to the high growth path following the great recession of 2008-09, the advanced countries' economic outlook remains gloomy. The hope of economic recovery is overshadowed by continuous job losses in the United States (US) and the sovereign debt problem on the both shores of the Atlantic.

Further, most countries in Europe are announcing a series of austerity measures that could slash their demand for imported goods and services significantly. Both Europe and the US remain Bangladesh's major exports markets.

Amidst the global financial crisis Bangladesh's apparel exports have not had much impact largely owing to the massive fiscal stimulus packages in the advanced world. However, the recent austerity measures and a less than rosy outlook of advanced economies could affect Bangladesh's apparel sector adversely. This indeed limits the RMG owners in Bangladesh revising labour cost upward, particularly at the scale the workers have been demanding.

However, there is also a silver lining as far as the industry's prospects are concerned. China is increasingly focusing on the development of high-end manufacturing and services, given the structural needs of its economy. Beijing has also decided to allow a gradual appreciation of its currency in the wake of relentless pressure from the

US and Europe. China's undervalued exchange-rate policy is believed to be a cause of strain in the global economy.

The rising unit labour cost and upward adjustment in its currency mean that a plethora of low-end manufacturing jobs will eventually be moving out from China. Indeed, many jobs have already moved inland from China's coastal areas and some low-end manufacturing units are relocating to Vietnam.

Economic Observer

The shortage of workers is particularly acute in the country's two major manufacturing hubs – the Pearl River Delta and the Yangtze River Delta. In Guangdong province there was a shortage of half a million workers in 2009. Following this development, of late, the minimum wage in Beijing has increased to 960 Yuan (142 dollar, Tk. 9,800). There is no unique minimum wage in China. It is set locally according to standards laid out by the central government.

Moreover, following the recent financial crisis, there is a realisation in China that the country's current growth model that relies excessively on exports and investment needs to be rebalanced, with a greater emphasis on consumption. Development of high-end manufacturing and service sectors is the key in this regard.

China's move towards a vertical economy could create much room for Bangladesh, given the latter's abundant supply of labour. Bangladesh's other competitors in the neighbourhood, India and Pakistan, are not in a good shape owing to the former's dilemma with its economic openness and the latter's overwhelming political problems.

India's economic openness bars its apparel sector taking the currency advantage – undervalued exchange rate – that the Bangladeshi RMG sector enjoys, given the huge capital inflows in the country that makes the Rupee exchange rate highly volatile. Moreover, India's labour market is highly inflexible, a major problem in its industrial structure. This leaves Bangladesh, Indonesia and Vietnam to augment their market shares in the wake of the China shift.

Given the structural shift in China and a bleak economic outlook of the advanced countries, the authorities in Bangladesh must understand the changes clearly before taking ad hoc decisions. There are three stakeholders as far as the RMG sector is concerned – the plant owners, the workers and the government.

The workers' fight against unsustainably lower wages in RMG is understandable given the growing cost of living in Dhaka. Nevertheless, they must accept the fact that it is the cheap labour cost that has made Bangladesh a competitive place for apparel manufacturing. Nonetheless, the recent hike in China's minimum wage will help Bangladesh to maintain its low cost advantage despite the likely upward wage adjustment in the RMG sector.

The government cannot escape its responsibility by merely announcing a minimum wage and letting the law enforcers go after the protesters. The successive governments in Bangladesh have failed to provide the required infrastructure and uninterrupted energy supply, making per unit production cost in Bangladesh more expensive than most of its competitors, if one isolates the wage cost effects.

The high energy cost and the poor infrastructure are neutralising Bangladesh's cheap labour advantage – leaving a squeezed margin for the producers. Unfortunately, the deadweight loss arising from the government's poor service delivery is mostly shared by the workers.

The situation in the global economy should be researched carefully. The owners and the government should explore new markets for apparel products, particularly focusing on emerging markets. More than half of global economic growth is now driven by emerging markets. However, Bangladesh's PR skills are relatively underdeveloped. This is reflected by the fact that it has failed to showcase the country in the 2010 Shanghai Expo, the largest business gathering ever.

The emerging markets may not substitute the advanced world as the consumer of last resort, at least in the short run, but in the medium to long run they could become significant markets for Bangladesh's RMG products. Many emerging markets including China are developing domestic markets offering various incentives. The expansion of the auto market in China in 2008-2009 is the prime example.

Moreover, as we observed in the case of China, an economy cannot suppress the prices of its non-tradables (housing, for instance) for long if the concerned economy undergoes a steady growth for decades. So, the exchange rates in China, Brazil and other emerging markets will gradually appreciate with their strong economic growth. The real exchange rate is nothing but the ratio of the goods and services that can be traded in international markets (e.g. an iPod) and those that cannot be traded (e.g. a haircut).

Bangladesh's autarkic financial system can continue to afford offering the exchange rate advantage to its exporters. Economic literature suggests that undervaluation is a second-best mechanism for alleviating institutional weakness and market failures that tax the tradables. Market failure in Bangladesh is rampant and its institutions remain weak.

This also means that owing to high opportunity costs, China, Brazil, South Africa and even India will increasingly abandon low-end manufacturing plants and start buying such products, including apparel, from Bangladesh, Indonesia and similar low cost producers. Such a scenario is not very unlikely in the near future. Bangladesh is one of the few countries that stand to benefit from such changes if the respective stakeholders act prudently.

---

***M Shahidul Islam is a Research Associate at the Institute of South Asian Studies, National University of Singapore.***

