Pitfalls of Export-Led Growth*

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After Sri Lanka and Pakistan, Bangladesh has become the third country in our neighbourhood to become afflicted by a serious economic crisis. It has asked for a $4.5 billion loan from the IMF, apart from $1 billion from the World Bank and $2.5-3 billion from multilateral agencies and donor nations. Though the government has put on a brave face, Bangladesh is facing a growing trade deficit, shrinking foreign exchange reserves, a rapidly depreciating currency, a record inflation and an energy crisis that has necessitated massive power cuts.

Ironically, Bangladesh was being hailed just a few months ago as a success story of "development", and indeed, according to many development indicators, it had made remarkable progress. Female literacy had reportedly increased to 73 per cent, infant mortality rate had become half that of Pakistan from which it had seceded in 1971, and its "Human Development Index" was higher than that of India, Pakistan and several other countries of the region. Many called it an "economic miracle" and not without some justification: a country that had been considered a "basket case" at independence, had pulled itself up quite remarkably to outperform all its neighbours, which is why the sudden emergence of economic difficulties for it has come as a big surprise to many.

As in the case of Sri Lanka, there is a tendency to blame "corruption" for the crisis; but, though corruption itself is reprehensible, this is an utterly facile explanation. More plausible is the view that the rise in international prices of a number of commodities in the wake of the Ukraine War has increased the import bill of Bangladesh to a point where it has simply run out of foreign exchange to pay for imports; for an import dependent country this has created domestic shortages that have pushed up the inflation rate. And the shortage of foreign exchange, primarily dollars, also explains the depreciating exchange rate, despite the using up of foreign exchange reserves for stabilising it. The problem with this explanation however is that it focuses only on imports and makes no reference to Bangladesh's reduced export earnings from garments that account for 83 per cent of its total exports.

Some Bangladeshi economists have blamed the country's monetary policy for the crisis: Bangladesh kept its interest rate unchanged for a long time instead of raising it. Had it done so, it would have been able to attract adequate private financial flows for financing its trade deficit; and in such a case the exchange rate would not have depreciated and remittances would not have dried up in expectation of such a depreciation. But this again is a superficial explanation; the problem lies much deeper, in the very nature of the strategy of export-led growth that Bangladesh, together with most other countries, has been following in the era of neo-liberalism.

The wisdom of pursuing a strategy of export-led growth has been discussed among development economists for at least half a century, ever since the so-called East Asian "miracle" started being contrasted with the comparatively sluggish growth experience of countries like India that were pursuing, in the World Bank's language, an "inward looking" development strategy. This entire discussion however has missed an important element that plays a role in real life.

Among the various expenditures that constitute aggregate demand in an economy, some are autonomous while others are induced by the growth of aggregate demand itself. Exports and government expenditure are generally considered to be the two main autonomous items: consumption, for any given distribution of income, is supposed to be dependent on the level of income itself. There is no doubt an autonomous element in consumption too that is independent of income, but that becomes pronounced only in certain situations, for instance when goods hitherto unavailable to consumers suddenly become available.

The growth of demand and hence of output in an economy depends on the growth of the autonomous element of demand. And in a neo-liberal economy where being open to cross-border financial flows imposes limits on the fiscal deficit relative to GDP and also practical constraints on the government's ability to tax the rich and stimulate demand without raising the fiscal deficit, exports become the main stimulus for growth. A neo-liberal economy in short is characterised by primary reliance upon export-led growth.

But the export-led growth strategy is not confined only to a neo-liberal setting. The government can deliberately encourage exports, rather than expanding the home market by enlarging its own expenditure, in which case we can have export-led rather than government expenditure-led growth, but with the government still being pivotal to growth; indeed many argue that this was the case with East Asian countries.

We must distinguish between two cases among countries pursuing an export-led growth strategy: one where the countries earn systematically large current account surpluses and thereby build up their foreign exchange reserves, China being a prime example. In the case of such an economy, any adverse development in the world economic situation makes a difference only to the magnitude of the current account surplus, which affects the magnitude of accumulated foreign exchange reserves only marginally. The country therefore, can ride out such an adverse development without experiencing any crisis.

Many other countries however belong to the second category, where they run more or less perennial current account deficits, balance their payments through private financial inflows, and even when they build up foreign exchange reserves these are financed through borrowings, including from private financiers. India belongs to this category, as do the countries of South Asia in general, and indeed most countries of the global south.

In the case of this second group of countries, if there is a widening of the current account deficit because of some exogenous reason, whether a pandemic induced reduction in tourist earnings (as in the case of Sri Lanka), or a Ukraine War-induced increase in import prices, or a world recession-induced fall in export earnings (both of which have happened in the case of Bangladesh), its impact on the economy gets exaggerated because of the behaviour of private agents in general, and of private financiers in particular. This is because, when there is a widening of the current account deficit, and hence a greater need for private financial inflow, this very widening causes a greater financial outflow.

Private financiers expect the currency of the country that has seen a widening of its current deficit to depreciate, and hence, concerned exclusively with their own interest,

take funds out of the country, thereby intensifying the foreign exchange problem for it. In fact, if things were left exclusively "to the market", it is not clear that the country would ever reach an equilibrium in the foreign exchange market; but that is when the country approaches the IMF, and a loan from it creates expectations among private financiers that the depreciation of the exchange rate would be arrested, so that the foreign exchange market can come to some sort of an equilibrium. But the IMF demands a heavy price for giving a loan, in the form of a reduction in welfare spending, a winding down of the public distribution system, a handing over of the nation's assets to foreigners (sometimes called "denationalisation" of assets) and so on.

It is this exaggeration of an initial shortfall in foreign exchange to a huge shortfall because of the behaviour of private finance, that occurs over an extremely brief period and pushes the country to the steely embrace of the IMF, which explains why countries suddenly go from being "miracles" to mendicants. The problem with export-led growth is precisely this: its apparent success can evaporate in a jiffy; and this happens when the pursuit of export-led growth makes the country dependent on the whims and caprices of globalised finance.

We have seen this happen in our neighbourhood, even to countries like Sri Lanka and Bangladesh which had notched up impressive human development achievements. With the world economy stagnating, and exports of several third world countries being hit by such stagnation, the list of mendicant countries is likely to grow in the coming days; and India despite its economic size and the large size of its foreign exchange reserves (though these are built up not from current account surpluses but from financial inflows) is by no means immune from it. The only saving grace in India's case is its foodgrain self-sufficiency (though at very low levels of consumption) and external relations that would allow oil imports from countries "sanctioned" by imperialism. Even foodgrain self-sufficiency however would have disappeared if the Modi government's three farm laws had been implemented; but the kisans saved the day for the country.

The idea of export-led growth had become discredited by the inter-war crisis of capitalism before it made a reappearance through neo-liberalism; with world capitalism confronting a new crisis, a change away from it is once again on the horizon.

*** This article was originally published in the Peoples Democracy on June 18, 2023.**