

Tahir Jahangir

Faltering exports

The textile exports are faltering since July 2022. They have been growing rapidly for the previous two years, but we have now come to a barrier to further growth. While it lasted, the growth rate was exceptional — at over 20% per annum. This was remarkable by itself, but achieved in a period when the world was afflicted with Covid and people all over the world were embroiled in a grim struggle just to keep their jobs or businesses going it was truly exceptional.

The cause for this exceptional growth was a correction of the exchange rate policy of the past. As the dollar-rupee parity was adjusted to reflect market conditions it provided a strong impetus to exports. Then followed a six-month period when the new government under IMF (International Monetary Fund) conditionalities imposed a 17% sales tax on all manufactured items.

The FBR (Federal Board of Revenue) was unable to evolve a sales tax refund mechanism for six months and the industry almost came to a complete halt. Once the refunds were smoothed out and the back-dues paid, exporters were able to win back most of the markets lost to India and Bangladesh over the last 10 years, and performed magnificently.

What that spurt in exports demonstrates is clearly the ability of the exporting industry to respond to opportunities and stimulus. All the old arguments used to deter export promotion like; “where is the export surplus?”

“Our industry is not capable of competing with the world.”

Were negated. Exports boomed despite Covid, despite soaring transport costs and despite the lock downs in the developed world.

What does the future hold? Another export surge? Or a stagger back into the depressed years before that?

For sure, if the FBR and the government do not correct their policies exports will falter and even go down. The current emergency measures are surely based on our current difficulties and cannot be a long-term policy. The most glaring of these measures is:

a. Suspension of sales tax refunds to the exporters; the refunds for November applications have still not been paid. This is a fast-acting poison.

b. Cessation of permissions to import spare-parts and machinery, which is a slower acting poison.

c. The huge gap between the exchange rate at which exporters get their foreign exchange earnings translated into Pakistan Rupees (currently Rs225 to the US dollar) to the real rate of exchange in the open market (currently over Rs250 to the dollar).

If these poisons are not remedied fast exporters will see their working capital depleted as their Sales Tax refunds are stuck, and whether they want to or not, their export performance will start faltering. The huge difference that has opened up in the exporters rate of exchange and the real rate is effectively subsidising imports by taxing exports.

A de facto reintroduction of the old economic policies to keep imports cheap. A lot of the immigrant remittances will slip from the official channels to the hundi system, thereby reducing the official remittances rapidly. There is also a danger of seeing the smaller exporters dealing with individual importers, and not corporates, getting their exports paid through the hundi system.

Water flows from higher ground to lower ones and there is no one who can stand against the laws of gravity. Similarly, supply goes to the highest bidder and the hundi system will win out. What's more important, this will reverse all the gains made in moving towards a recorded official economy.

There are a number of other measures which are a deterrent to the exporting industry.

The rupee-dollar parity has moved by over a hundred percent in the last three years. The export refinance limits fixed by the State Bank of Pakistan (SBP) have been revised by a mere 25%.

The exporting industry has to either make do without adequate credit, or finance it at the current exorbitant rates. There are frequent electric and gas outages and these are a serious threat to cost of production. All these factors can be managed by a confident and capable government.

There is no doubt that the looming recession in the developed world as well as the improvement in the supply chain has also affected our export performance in the last six months. The retailers in the developed world are seeing a slowdown in their sales as the world reels over the high energy costs unleashed by the Ukraine war. The effects will wear off as the winter recedes and prices of energy decline, the central banks will also ease off anti-inflationary measures over this year.

The supply chain factor is a little more complex. During the Covid period, there was a shortage of port handling facilities as workers were not turning up for work as normal. This started snowballing and long queues were built up outside major US ports. All this led to ships taking twice as long as they normally did to deliver cargo to their destination.

A typical container moving from Karachi to the East Coast of the USA which normally delivered cargo in less than four weeks was taking as long as six to eight weeks. The retailers therefore started ordering well in advance, and fearing Covid disruptions to the supply chain were also over ordering as a precaution. To them having empty supply shelves is suicidal.

As Covid receded and conditions began to normalise, the stores were left with a lot of excess stocks on their hands. To add to all this was the slowing down of demand as consumers struggled with higher energy bills. So, the stores panicked and instructed their suppliers to suspend deliveries even for the orders placed and confirmed for shipments through the autumn of 2022. A substantial part of the orders placed for shipments in the last quarter are still on hold and will start moving in a few months.

All these are the short-term factors leading to a fall in exports. They are short lived, and most are in the hands of the Government, and can be rectified. Market conditions will improve over the summer, tourism will boom and so will spending. Our exports will also pick up. However, there are longer term factors which I will define in another article, and these are more difficult to tackle.

These factors are the results of our exporting industry growing to maturity. In whatever field we are involved in, we are no longer babies scratching at the surface of a large world. We are substantial players in those fields. I can give an example from my own field which is terry towels from cotton.

Here we were exporting about 300 million dollars' worth or about 6 % of the world trade in value a decade ago. Today we are approaching a billion dollars' worth of exports in a world trade of six billion dollars. So roughly 16 % of the world trade by value. In terms of volume we are about 25 % of the world trade! Not an insignificant figure. One of the obvious conclusions that we come to is how to improve our value with current volumes?

There is after all a limit to how many cheap towels, or for that matter bedsheets, garments, etc. the world will consume. We are approaching those limits and further growth in exports has to come through greater sophistication of our existing industries; and developing more exporting industries where we have a competitive advantage.