

## Trade Performance of the Garments Sector of Bangladesh: A Critical Appraisal

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*Abstract: The economy have been affected by various natural disasters like severe floods, cyclones and thus the gross domestic product (GDP) growth is estimated to be below 6% in fiscal year (FY) 2008. But an economic turn around is expected in the second half of FY2008. Due to this, international trade is gradually improving with an up trend in ready-made garments exports. As the economy depends heavily on the garments industry for employment, income generation, and foreign exchange earnings, the country cannot afford to give up its current position. From this point of view, this study focuses on trade performance of the garments sector of Bangladesh. It is revealed that despite pressures on the current account and foreign exchange reserves, balance of payment situation remain stable. However; continuing severe inflation and devaluation of taka against United States dollar (US\$) remains a major challenge. We know that the lions share of garments product of Bangladesh is exported to United States (US) and European Union (EU) markets for competitive price and low production cost. The study also attempts to discuss direction of export and import, terms of trade, position of international reserves and tries to clarify the contribution of garments sector on trade performance of our country. At present, the total export revenue from ready-made garments (RMG) industry is almost \$ 8 billion. Bangladesh earns that amount in a year by exporting textile products, mainly to EU and the US. Whenever the country is criticized for its high level of corruption and confrontational politics, its garment industry is held up as a success story.*

### Introduction:

Garments industry is the largest foreign exchange earning sector of Bangladesh. At present, the industry is responsible for earning 76 % of the country's gross foreign currency income, and is vitally important for the country. However, it is certain that it will be very hard for the RMG sector to maintain today's high profit margin, as prices will fall

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and shortage of fabrics will increase the production cost. To maintain the profit trend in this sector, the industry have to reduce production cost. The major problems of our garments sector are absence of backward linkages that create further obstacles like unavailability and inadequacy of inputs which consequently raise production cost. It is shown that today customers consider quality and compliance for selecting the vendor. The RMG industry has around 4,000 units across the country. The key advantage of Bangladesh over other Asian producers is still confined to low labor cost and comparatively low price. But this is gradually eroding with differences in other costs, quality, design, delivery times, and other non-price factors. Thus, by considering the advantages of garments product and ensuring quality we can expand our market share to other countries as well. This paper seeks to identify contribution of garments sector of our economy in international trade. The specific objectives are to show distribution and composition of exports, explain trade and industrial policy towards textile and clothing sector, discuss dynamics of comparative advantage in clothing, clarify the international trade situation of Bangladesh. The suggestions based on findings of the study will help to improve overall performance of our garments sector.

#### Materials and Methods:

The methods of this study include empirical field observation and data collection through a questionnaire survey. Primary data have been collected from 30 readymade garments industrial units of Dhaka city. The sample size of the data have been fixed on the basis of stratified random sampling. From all the industrial units, every 10th has been surveyed through structured questionnaire. Secondary data are also used to make conceptual framework and discuss trade performance of garments sector. The data have been analysed through general statistical methods. Secondary data about direction of export and import, total volume of exported ready-made garments are collected from government and non-government organizations such as ministry of finance (MoF).

### Distribution and Composition of Exports:

This section examines the trade performance of Bangladesh in textiles and clothing based on several criteria. First, it is instructive to examine the geographical distribution of clothing exports from Bangladesh. The market shares of Bangladesh have made a good progression in the mid-nineties in the US and EU respectively. A relevant question arises whether competition is more intense in those markets.

One way to explore this is to ascertain volatility of ranks of leading clothing exporters with the help of the Kendall coefficient of concordance (KCC) in major two markets defined below (Siegel, 1986).

We know,

$$KCC = \frac{\sum_{i=1}^N (\bar{R}_i - \bar{R})^2 / [N(N^2 - 1) / 12]}$$

Where,

$\bar{R}_i$  = average of the ranks assigned of the i-th exporting country. The number of sets of ranking associated with this average in this number of years for which data are available.

$\bar{R}$  = the average (or grand mean) of the ranks assigned across all exporting countries being ranked.

N = Number of exporting countries being ranked.

The concordance coefficient lies between zero to unity. If the ranks of leading exporters change little over time, the coefficient will be close to unity. On the other hand, if ranks of leading exporters change substantially, the coefficient will be close to zero, suggesting the existence of volatile comparative advantage or what Bhagwati and Dehejia (1994) called "Kaleidoscope comparative advantage" in clothing. The KCC is computed for 1980-1997 period i.e. for 18 years. The number of leading exporting countries are the US, EU and rest of world market.

Greater competition in the European market can be attributed to the facts that (i) this market is relatively less restricted by multi-fibre

agreement (MFA) quantitative measure, compared to the US market and (ii) the presence of several clothing exporting member countries, for instance, Spain, Portugal and Italy, which are competitors of developing countries. Note that the KCC values are higher for the total world market than either for the US or EU. This implies that ranking of leading exporting countries of clothing are more stable in the world market but less stable in the two regional markets. It has been represented in Table 1.

Table 1. Kendall Coefficient of Concordance (KCC) of Leading Clothing Exporters

SITC codes	United States (%)	European Union (%)
8421	.75	.59
8422	.62	.59
8423	.63	.65
8429	.77	.70
8431	.63	.66
8432	.57	.61
8433	.70	.72
8434	.62	.69
8441	.72	.66
8442	.58	.57
8451	.69	.66
8452	.60	.58
8459	.74	.63
8461	.65	.56
8462	.59	.63
8471	.85	.81
8472	.76	.76
8481	.72	.84
8482	.61	.72
8483	.45	.63
8484	.74	.81

Source: The world Trade Analyzer; The Textile and Clothing Industry of Bangladesh in a Changing World Economy, page no. 52

Table 1 represents the value of KCC for various clothing categories at the 4-digit level. The figures reveal a mixed picture. The EU has higher KCC for 10 categories, and lowers for 10 categories, and equal for 01 category, compared to the US. It is striking to note that for the three categories (8429, 8441, and 8461), which are dominant in clothing exports from Bangladesh, the EU has lower KCC. This suggests that for categories of clothing in which our economy now specialize; the EU market is more competitive and volatile, compared to the US market.

It is note that the KCC values are higher for the total world market than either for the US or EU market. This implies that rankings of leading exporting countries of clothing are more stable in the world market but less stable in two regional markets. It is apparent that 03 categories (8429, 8441 and 8461) of clothing account for about 65 % of total clothing exports from Bangladesh. The share of categories 8429 and 8441 in total world trade, however, has declined in recent years. Accordingly, we need to shift toward high value added categories whose demand is increasing. It is observed that the concentration index declined for our country during 1980-97. However, the index for Bangladesh is higher, compared to that for India and China.

#### Dynamics of Comparative Advantage in Clothing:

Clothing includes a variety of products, which differ substantially in terms of quality, unit prices, degree of standardization and types of major inputs embodied. The comparative advantage of a country in clothing change as factor endowments, technology, factor price, and level of income change. Accordingly, it is necessary to pay attention to change in comparative advantages in clothing categories of exporting countries. In this section this is done by examining the Revealed Comparative Advantage (RCA) in clothing at 4 digit level. The RCA is defined as below:

$$[RCA=(X_{ib} / X_b) / (X_{iw} / X_w)]^*$$

Where,

$X_{ib}$  = Export of i-th category of clothing from Bangladesh

$X_b$  = Total export from Bangladesh

$X_{iw}$  = Export of i-th category from all countries

$X_w$  = Total export from all countries

\* The equation of RCA has been mentioned in the book *"The Textile and Clothing Industry of Bangladesh in a Changing World Economy"*, page no.63

If the RCA is greater than 1, the relevant country is considered to have a comparative advantage in the product concerned, while an RCA is less than 1 implies a comparative disadvantage in the product. The data on RCA for the selected countries reveal the pattern that when a country becomes economically advanced, its comparative advantage change. Countries such as Bangladesh and Sri Lanka, which did not have comparative advantage in most of the categories of clothing in 1980, managed to achieve comparative advantage for most categories by 1997. However, the comparative advantage of these countries are still concentrated on low-value added categories.

#### Trade and Industrial Policy towards Textile and Clothing Sector:

During the last decade, Bangladesh has substantially liberalized its trade regime, moving away from costly protectionist policy toward a more export- friendly trade regime. Industrial policy, 1999 and export policy, 1999-2002 have identified the textile and clothing sector as one of the 'thrust' sectors of Bangladesh. The patterns of comparative **advantage** and hence the structure of exports and imports involving textile and clothing, as stated before, depend on stages of economic development in Bangladesh and other countries. Formulation of trade and industrial policy for the textiles clothing sector must be based on a dynamic and broader perspective covering all the major components of the 'textile cluster'. The components are natural and synthetic fibers, yarns, grey and finished fabrics, garments and other made up products, textile machinery and parts, chemicals for textile, marketing services, research, skill formation, training services, financial, administrative and physical infrastructure.

A country does not need to have comparative advantages in all the components. Similarly, a factory does not have to produce or export all the components. An industrially advanced country like Japan may specialize in a few high value added components like fabrics, chemicals and textile machinery. Because of extensive outsourcing activities by factories in developed countries, there has been a significant increase in 'vertical de-integration' or what has been called 'slicing the value chain' (Feenstra, 1998 and Hummels *et. al.*, 1999) in

many products including textiles and clothing. Similarly, for a country like Bangladesh, it is logical to follow the traditional road to industrialization by concentrating on the labor intensive components such as garments. The experiences of textile and clothing producing countries seem to suggest that there is inverted 'U- shaped' relationship between the degree of integration of the textile complex (that is, the number of components of the textile cluster being produced) and the stage of industrial development of the relevant country. A labor abundant country, which is an early stage of industrial development, is likely to specialize in only one component of the cluster, for instance, clothing. As the country moves into higher stages of development, it acquires the capacity to develop other components such as yarns, fabrics, synthetic fibers, chemicals and textile machinery. However, as the country becomes industrially advanced, it loses comparative advantage in labor intensive components such as clothing. Accordingly, the degree of textile cluster declines at a very advanced stage of industrial development. This does not imply that all textile and clothing producing countries move through all the stage in a deterministic pattern. It is possible for a country to leapfrog a stage and also to make the transition from one stage to another. Furthermore, the literature on 'spatial agglomeration' (Fujita, et. al., 1999.) suggest that industrialization does not spread uniformly to countries which have similar factor endowments. Proximity to markets, transport network, proximity to suppliers and increasing returns play an important role in location of industries. Bangladesh is one of the few developing countries, which have emerged as significant exporters of clothing within a short period of time. Yet, in recent years, concerns have been raised about the viability of the clothing sector of Bangladesh. Because of the heavy dependence-on-imported inputs, the contribution of the clothing sector in total manufacturing value added is far from spectacular. The share of manufacturing value added at GDP increased only from 9.8% in 1980 to 10.3% in 1995. Given the current structure of government incentives, a 'new dualism' has emerged in Bangladesh, with domestic market oriented sectors in our country. It has been argued that may Bangladesh lose its competitive position relative to other South-East Asian countries in a liberalized

trade environment, because the clothing sector of this economy lacks 'backward linkages'. Promotion of industrial linkage is one of the major features of export, industrial, and textile policies of our government. The textile and garments manufacturers and exporters associations of also support the policy of promoting industrial linkages.

The questions of backward linkage or more broadly industrial linkages involving linkages raise many theoretical and policy related issues. Several theoretical arguments for industrial linkages can be stated below:

Firstly, rationale for industrial linkages is that for sustained international competitiveness in high value added products, a cluster of upstream and downstream industries is essential (Porter, 1999 and Christerson 1994).

Secondly, industrial linkages, especially involving firms and suppliers of inputs are consistent with the flexible specialization paradigm (Piore and Sable, 1984). Inter-firm co-operation involving a firm and suppliers are likely to emerge when the firm and suppliers are closely complementary but dissimilar in capabilities.

Thirdly, export of high quality and value added products require shifts from mere assembly of imported inputs to a more domestically integrated full-package supply system (Gereffi, 1999).

Finally, industrial linkages can facilitate by endogenous products differentiation, incremental secondary innovations, as emphasized in the literature on new trade theories (Grossman and Helpman, 1991.) Furthermore, development of linkages is likely to promote international trade in machinery, equipment, and specialized inputs with greater learning effects (Lee, 1995).

The view that development of a cluster of industries is essential for maintaining or improving the competitive position of the clothing industry is not free from criticism. It can be argued that for a variety of reasons, Bangladesh does not have a comparative advantage in



textiles such as yarn and fabrics. The reasons include substantial economies of scale and high capital intensity in textiles, the comparative disadvantages of Bangladesh are shortage of raw cotton and low production capacity compare to other textiles exporting countries. Accordingly, for the clothing industry of Bangladesh, it may be optimal to procure intermediate inputs such as fabrics and yarn from cheaper sources such as India, China and East Asian countries. Another argument is that if profitable, market forces will induce the private sector to develop industrial linkages. Alternatively, vertically integrated firms may emerge to minimize transaction costs. According to this argument, any government intervention is unnecessary or counter productive. This laissez-faire approach however, ignores the presence of externalities and imperfections in financial markets in industrial linkages. In the presence of market failures, trade liberalization could induce a technologically less advanced country to specialize in product groups in which the potential for learning is limited (Young, 1991). In the presence of inter-locking externalities in many developing countries including Bangladesh, government can and should play some role in promoting relationships between upstream and downstream industries through a coherent trade and industrial policy. Government policy instruments take the form of "input-related incentives," "output-related incentives" and other incentives such as infrastructure provision and credit for research-and development. The list of government incentives may vary little across developing countries. The critical issues are the timing and duration of government incentives, coherence among policy instruments underlying government incentives. Often in many developing countries, textile industries are promoted through costly protectionist policies, which hurt rather than help clothing industries.

Results:

### *International Trade Situation of Bangladesh*

Terms of trade means the ratio of an index of a country's export prices to an index of its import prices. The Terms of trade are said to be declined if the ratio decreases as table 2 suggests from the year 2000-

2006 so that each unit of exports buys fewer imports.

Table 2. Terms of Trade Situation (Period averages)

Item\Year	1990	1995	2000	2005	2006	2007
Export price indices	269.0	120.8	178.5	206.6	215.0	145.94
Import price indices	270.0	120.7	180.1	248.1	257.8	183.81
Terms of trade	99.6	100.1	99.1	83.3	83.4	79.40

Source: Planning Commission (up to FY95) & Bangladesh Bank (since FY96).  
Base Year 1995-96 = 100

Moreover, terms of trade is proportionately related to countrys export and import price indices as the above table 2 signifies. From the year through 2000-2005, export as well as import price indices are increasing sharply but terms of trade seems to decline from 99.1 to 83.3. then after a little improvement it declines again to 79.40 in the year 2007 and both the price indices change simultaneously.

An overall statement of country's economic transactions with the rest of the world over some period of time can be regarded as balance of payments. The current account includes visible trade like export and import. The overall balance of payment recorded a significant surplus of US\$ 365 million in FY 06, which was much higher than surplus of US\$ 67 million of FY 05, reflecting a notable improvement in current account balance and a larger surplus in capital account, despite impacted mainly by large net outflows in trade credit and other short term loans, the financial account swung into a deficit from a large surplus of FY 05.

Table 3. Balance of Payment Picture ( in million US\$)

Item\Year	1990	1995	2000	2005	2006
Current account	-436	<b>-664</b>	<b>-418</b>	<b>-557</b>	<b>572</b>
Capital account		489	561	163	242
Overall balance	<b>138</b>	<b>452</b>	<b>179</b>	<b>67</b>	<b>365</b>

Source: Bangladesh Bureau of Statistics.

(Data based on 1995/96 benchmark and prices; fiscal year ending June 30)

The above table represents that we are in a state of current account deficit i.e. spending exceeds receipts since 1990-2005. Except in the year 2006, we are in current account surplus situation. The capital account includes inward and outward foreign direct investment. As the foreign exchange reserves are increasing, the balance of payment situation is sustainable in our economy at the present situation.

Foreign trade means buying and selling abroad. A country's balance of trade is the excess of value of its exports of its goods over its imports. Trade barriers are obstructions to international trade, such as tariffs and quotas. Trade preferences are differences in the rules applied to trade with different foreign countries.

Table 4. Direction of Export from Bangladesh (in million US\$)

Exporting Countries/Year	1990	1995	2000	2005	2006	2007
United states	<b>510</b>	<b>999</b>	<b>1779</b>	<b>2003</b>	<b>3179</b>	<b>3441.02</b>
<b>Germany</b>	<b>108</b>	<b>294</b>	<b>608</b>	<b>1144</b>	<b>1610</b>	<b>1955.38</b>
United kingdom	<b>119</b>	<b>317</b>	<b>440</b>	<b>795</b>	<b>1249</b>	<b>1173.95</b>
Italy	<b>107</b>	<b>195</b>	<b>228</b>	<b>326</b>	<b>486</b>	<b>515.66</b>

Source: Bangladesh Bank, Statistics Department.

Bangladesh earn highest amount of foreign currencies in every year through export to the United States. Table 4 clearly signifies that the amount of export is US\$ 510 million in 1990 while in 2006 this amount goes up to US\$ 3179 million. From revenue earning point of view, Germany is in the second position. We earned US\$ 108 million in year 1990 compared to US\$ 1610 in 2006.

The biggest market for Bangladesh to import was India. Surprisingly, the data presented above suggests that Bangladesh imported highest amount of US\$ 2571 million in the year 2006-07 from china.

Table 5. Country-wise Import Payments (in million US\$)

Importing Countries/Year	1990	1995	2000	2005	2006	2007
India	<b>170</b>	<b>994</b>	<b>945</b>	1951	<b>2145</b>	<b>2268</b>
Japan	482	598	850	571	660	690
China	133	707	709	1642	2079	2571
Singapore	407	396	761	852	989	1035

Source: Bangladesh Bank, Statistics Department.

The amount of import from India is increased sharply at about US\$ 170 million in 1990 to US\$ 2145 million in the year 2006 and continued to increase US\$ 2268 million in 2007. China stands just next to India in terms of as an importing country of Bangladesh. We spend US\$ 407 million in the year 1990 compared to US\$ 989 million in 2006 to Singapore for import purposes.

From table 6, we can comment that Bangladesh earn a total of US\$ 4084 million in the year 2005-06 by exporting RMG compared to US\$ 3364 million in the year 2000-01 clearly signifies an upward trend in case of revenue earning.

Table 6. Contribution of RMG in Comparison to Total Exports

Item/Year	2000/01	2001/02	2002/03	2004/05	2005/06
RMG (Million of USS)	<b>3364</b>	<b>3125</b>	<b>3258</b>	<b>3598</b>	<b>4084</b>
Volume (million of dozens)	<b>71</b>	<b>77</b>	<b>83</b>	<b>92</b>	<b>109</b>
Average unit value index	<b>47</b>	41	<b>39</b>	<b>39</b>	<b>38</b>
Total exports (Million of USS)*	<b>6419</b>	<b>5929</b>	<b>6492</b>	<b>8655</b>	<b>10526</b>

Sources: Bangladesh Bank, Statistics Department; Export Promotion Bureau.

\* Excludes goods procured in ports and repairs on goods.

A recent study estimates that duty-free access could result in exports to the US increasing by US\$500 million to US\$1,000 million. The total volume of exports is 109 millions of dozens in the fiscal year 2005-06. While the total earning from exports is US\$ 10526 million,

the ready-made garments comprised a significant portion of it (more than 40% of total export earning).

#### Discussions:

It is indeed difficult to recommend some measures which can bring dramatic changes on trade performances in a country like Bangladesh. But one thing is clear that policies adopted by government cannot be implemented without proper monitoring. The following measures may be helpful to increase the revenue earning by garments sector.

Proper foreign policy is necessary to expand existing foreign markets and to identify new potential markets and gain access to these markets. Simultaneously participation in specialized trade displays in various potential markets will help exporters to promote their products. To be cost competitive and to produce quality items, modern technology and training to develop skill at all levels of RMG are essential.

To sustain our competitive edge, diversification of market is essential. Liberalized trade and investment presents opportunities and challenges for the textile and clothing industry of Bangladesh. At the same time, we need to develop the product quality and design, as change fashion and taste chsnge frequently all over the world.

Bangladesh is located far away from major markets such as EU and US. Existence and possible expansions of free trade blocs such as the EU and North American Free Trade Area (NAFTA) provide opportunities through increased trade and investment relationships to Central American countries but it is a challenge for us to face it. Furthermore, the country are in a disadvantageous position compared to several other Asian countries such as China, India which have large domestic markets with a higher degree of integration in the textile cluster.

Labor cost in Bangladesh is still lower than in most apparel exporting countries. In the post-Uruguay Round period the country must continuously upgrade its comparative advantage in high value added

products. In this process, the government has to play the role of a catalytic agent.

Industrial and trade policy concerning the textile and clothing sectors must be formulated from a dynamic perspective. The policy measures such as the bonded warehouse system and the back-to-back Letter of Credit (L/C) have helped Bangladesh to become a significant supplier of apparel within a short period of time.

Bangladesh must develop backward linkages in the textiles and clothing industry. For Bangladesh, this implies development of efficient spinning and weaving industries, which are generally capital intensive. Private companies in Bangladesh lack financial resources to establish large-scale textile operations or vertically integrated operations.

The government of Bangladesh must play an important role in providing financial resources at low interest rates. Governments in India and China, for instance, are already involved in massive modernization of their textile sectors. Any government support to the private sector in Bangladesh however, must be performance based. Bangladesh can also encourage foreign investment, especially from East Asian countries. In order to attract foreign capital Bangladesh needs to develop the physical and administrative infrastructure for the textile and clothing industry. Liberalization of rules and fiscal incentives alone should be inadequate.

#### Conclusions:

In the last decade of the twentieth century, Bangladesh has emerged as the twelfth largest garment-manufacturing nation of the world. The macro economic indicators such as balance of payment, foreign exchange reserves, terms of trade clearly signifies the upwarding tendency of the economy to stay in a balanced situation. Garments sector play a significant part to improve the overall economic balance as well as the trade in international market in this age of globalization. While the government has declared this sector as "thrust", the policy instruments are not quite consistent with the objectives. Fiscal

incentives and financial support to the relevance of tariffs as an instrument to improve the competitive position of any sector or subsector is limited. In recent year, import-intensiveness of textiles and clothing sectors has received a great deal of attention. Any policy of imports substitution of inputs requires a careful analysis of the cost or input structure of the relevant sectors. As the level of industrial development increases in our country, it will have to diversify its exports away from ready-made garments towards high value added products for which demand is more income-elastic. Accordingly, organisations and think-tanks must play a dominant role to ensure the better production and distribution of those products to stay competitive.

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