The Wake-up Call

The coronavirus (COVID-19) has brought many underlying vulnerabilities of the global economy to the surface. The virus has already claimed 3,123 lives worldwide, with over 90,441 infected cases. Although the infection and death rate have appeased to some extent in China, the birthplace of the outbreak, the rapid spread outside China has crippled all hopes of a speedy recovery from the pandemic.

Protracted factory shutdown in China, the manufacturing superpower that has tightly held grip of 30% of the global manufacturing output, has jeopardized the global supply chain. Although the Chinese authorities are trying to usher workers back to their workplaces, a month after announcing the unprecedented quarantine, the manufacturing activity is slowly normalizing with production currently running at ~60-70% of the pre-outbreak levels.

Like many other countries, Bangladesh has not been spared from the repercussions of an interruption in business as usual in China. Chinese goods comprise 26.1% of imports in Bangladesh, worth USD 56 bn, creating susceptibility for the supply chain of major industries owing to disruption in production activities in the world's largest exporting country. Moreover, not only does Bangladesh's RMG sector procure a significant portion of its raw materials (more than 50%) from China, it also exports ~USD 506 million to the latter (as of FY 2018-19). Apparel makers such as H&M, GAP, and Uniqlo that source their products from Bangladesh are also experiencing lower demand as many retail outlets are being kept shut or operating on reduced hours with lower traffic in China. The adverse demand side impact in United States and Europe is unknown but Goldman Sachs revised its earnings estimate for the year for U.S. companies to $165 per share, representing 0% growth in 2020, which is a dramatic move from the consensus.

Additionally, given that high spending Chinese consumers account for approximately 46% of global luxury brand sales, that the majority of Chinese citizens are currently trapped indoors is leading to subdued demand within and beyond China's borders. Hence, while import volume from China has plunged 21% in volume in the first one and half months of 2020, both Bangladesh's ability to export as well as demand for Bangladesh's exports at both supplier and consumer end will likely take a beating.

Furthermore, the RMG sector is already handcuffed by lack of negotiation power, which means its trade partners may turn its head towards other countries if local garment owners want to ask for a higher price due to possible increase in production costs stemming from the smothered supply chain.

Other sectors such as leather, pharmaceuticals, consumer electronics, cement, steel, jute, among others, may also be impacted due to their high reliance on China for export and/or imports. As such, banks are likely to experience a spillover effect if overall industrial activity slows down in the country.

Bangladesh's mega infrastructure projects, that are to be a major driving force for expediting industrialization in the country, are also in danger of losing their pace as Chinese capital and manpower are highly involved in their construction process. Alongside this, a majority of the suppliers of important construction materials and equipment are China-based, which is worrying. The disbursement of China's fund commitment to Bangladesh may be delayed as well due to the outbreak.

In the global commodities market, oil and other basic materials such as coal, copper, aluminum, and iron ore, have witnessed significant downturn (S&P GSCI index for commodities lost 8.39% in February 2020 alone) due to the outbreak. Tumbling manufacturing activity in China and fear of significant global economic slowdown has resulted in weak demand for commodities. While the dip in energy and materials prices might create a breathing space for Bangladesh to curb inflation, it will also create significant balance sheet challenges for the businesses that purchased materials for their inventories at comparatively higher prices before the slump occurred.

According to the results from a survey conducted by Morgan Stanley, China's analysts expect the production levels in China to reach 80-100% by late March, 2020. Production in some sectors such as staple food and beverages, coal, industrial truck machinery and electronics are likely to resume faster than the automotive, cement, and apparel equipment manufacturing industries, as per the opinion of the investment bank. If these predictions stand, then the overall impact may remain within a tolerable level. While a certain portion of the demand may be permanently lost, the remaining demand may later bounce back in the form of a J-curve. At present, central banks in affected countries are considering accommodative policies to help their respective economies prevent a downturn. The US Federal Reserve has cut 50 bps to ease the economic impact of the escalating health crisis, a move that was also undertaken during the US financial crisis.

The implications of the coronavirus outbreak have sent us a strong message about how vulnerable we can be in the face of storms. Now is the time to proactively develop backward integration and reduce dependencies on a single geographic region so as to minimize volatility from external shocks. Other countries that also have a high concentration of their factories in China may currently or soon be rushing to seek alternate destinations for their production processes. While Bangladesh's name may appear in their list of options due to its low labor costs, the lack of high-skilled workers and product diversification may ultimately deter prospective foreign countries from stepping foot in Bangladesh. As such, proper training needs to be provided to close this gap.

Also, considering the high population density of Bangladesh in general as well as the cramped working conditions within the premises of RMG factories, the infection of a single person or a factory worker may lead to the virus inadvertently spreading like wildfire. The manner in which the COVID-19 rapidly infected people in cruise ships such as the Diamond Princess or the prisons in China stands testament to this.

Finally, even though Bangladesh is yet to detect any COVID-19 cases, the healthcare sector needs to adopt more stringent and thorough measures to ensure that the country does not face any hiccups in its growth trajectory due to any ugly contingencies given its weak healthcare infrastructure. The COVID-19 is a wake-up call for all of us. At this point, rather than being complacent about not being among the 62 affected countries that are currently battling with the coronavirus outbreak, we need to maintain a cautious stance and take all necessary steps across private and public sectors before it is too late.

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