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# Trade in Textiles & Clothing

*Exploring Cooperation between ASEAN and SAARC*

## Introduction

The global textiles & clothing (T&C) industry has grown exponentially to meet the demands of an increasing population as well as to maintain the standards of living worldwide. In 1950, for example, the consumption of fibre by the world's textile mills was seven million tonnes which increased to more than 50 million tonnes in early 2000. In addition, this sector has developed as a major activity in many countries that previously had little or no manufacturing activity. This is definitely the case with Cambodia where there was no garment-manufacturing unit ten years ago (Sok Hach, *Cambodia's Garment Industry in 2005 and Beyond*, EIC Economic Review, September 2005). Further, changing demand and supply patterns have resulted in a sharp increase in foreign trade in garments from US$108bn in 1990 to US$201bn in 2002 in Cambodia.

A survey of United States Agency for International Development (USAID*) – Measuring Competitiveness and Labor Productivity in Cambodia's Garment Industry*, carried out by the Associates for International Resources and Development (AIRD), Economic Institute of Cambodia (EIC) and Werner International in June 2005, observes that the elimination of global textile and apparel trade quotas on January 1, 2005 has brought about a dramatic shift in the world market for these products. China, with its vast supply of labour, significant upstream capacity in manufacturing, efficient garment factories in coastal areas and well-developed logistics infrastructure, has achieved remarkable gains in exporting these products during the first few months of the quota-free trade regime.

In contrast, some other global suppliers have suffered in this competitive race. Mauritius, Mexico, South Africa and South Korea have been the leading losers. Downward pressure on world prices was strong in the first few months of this more competitive environment.

The World Trade Organisation (WTO) figures also show that about 85 percent of garment imports over the years have been consistently made to the European Union (EU), US, and Japan. There is every possibility that these three importers will continue to be the major markets for garments.

The cost competitiveness of garment supplying countries in the three major markets will change considerably with the ending of quotas. Until now, several countries have maintained their exports due to the quota regime. The cost of these quota premiums was passed on to the eventual buyers. Without quotas, producers will be able to reduce prices accordingly. Some countries in South and Southeast Asia, in particular, will also lose some of their advantages as quotas end and competing countries, especially China, will be able to adjust their prices and therefore, will gain.

Given these challenges, could the Association of Southeast Asian Nations (ASEAN) and the South Asian Association for Regional Cooperation (SAARC) countries cooperate to optimise their competitiveness in the global market and take advantage of generalised system of preferences (GSP) provided by the EU, US and Japan to some of them? The need for cooperation is more important because small and medium-sized enterprises (SMEs) have a major share in this sector, employing a large number of workers from marginalised and vulnerable sections. For example, in India, the T&C sector provides direct employment to more than 30 million and is the second largest employment provider after agriculture.

**Table 1: Share of SMEs in T&C Sector (US$bn)**

| | |
|---|---|
| Bangladesh | 357 |
| India | 136 |
| Indonesia | 208 |
| Malaysia | 88 |
| Pakistan | 132 |
| Philippines | 235 |
| Sri Lanka | 130 |
| Thailand | 193 |

*Source: Comparative Assessment of the Competitiveness of the Textiles and Apparel Sector in Selected Countries*, http://63.173.254.11/pub3671/chap3.pdf.

## GSP Benefits in T&C

In 2003, export of T&C from Southeast Asian countries to the EU, US and Japan was about US$15.3bn, while that of SAARC countries was US$17bn. The combined export share of South and Southeast Asian countries in the EU, US and Japan was 21.9 percent, whereas China accounted for 23.5 percent in the same markets. The combined value of exports of T&C of these two regions (US$32.3bn) was about seven percent less than that of China (US$34.7bn).

**Table 2: Exports of Garment Products to EU, US and Japan in 2003 (US$bn)**

| | EU | USA | Japan | Total | Percentage |
|---|---|---|---|---|---|
| **World** | **62.4** | **66.1** | **18.8** | **147.3** | **100** |
| **EU** | - | 4.1 | 1.7 | 5.8 | 3.9 |
| **USA** | 1.1 | - | 0.5 | 1.6 | 1.1 |
| **Japan** | 0.5 | 0.6 | - | 1.1 | 0.8 |
| **China** | 11.0 | 10.0 | 13.7 | 34.7 | 23.5 |
| **Hong Kong** | 1.8 | 3.1 | 0.0 | 5.0 | 3.4 |
| **South Korea** | 1.2 | 2.4 | 0.5 | 4.1 | 2.8 |
| **ASEAN** | 4.4 | 9.5 | 1.4 | 15.3 | 10.4 |
| **SAARC** | 8.9 | 7.8 | 0.3 | 17.0 | 11.5 |

*Sources: Compiled from EU-EUROSTAT/COMEXT, March 2005; US and Japan - COMTRADE, March 2005.*

South and Southeast Asian countries have benefited significantly from the GSP provided by the EU, US and Japan during the last 15 years. GSP is a system whereby rich countries grant preferential treatment to eligible products imported from poor countries. This helps poor countries to improve their economic conditions through exports. In effect, it provides duty-free (or low tariff) import of a wide range of products that would otherwise be subject to customs duty (tariffs).

Many South and Southeast Asian countries enjoy such benefits provided by the EU, US and other rich countries. Some Southeast Asian countries, such as Thailand, have 'graduated' (i.e. not receiving preferential treatment for their T&C exports). Singapore is excluded from the preferential treatment because of its advanced level of development. However, all South Asian countries continue to benefit from GSP. For instance, India remains a major GSP beneficiary and might also qualify for the new GSP plus, which gives tariff preferences to vulnerable countries that can meet some objective criteria for sustainable development and good governance. Furthermore, after September 11, 2001 terrorist attack in the US, Australia, Canada, EU, Japan, US and other rich countries have started giving preferences to Bangladesh, Indonesia, Malaysia, Pakistan and Philippines.

However, conditions related to the 'rules of origin' (RoO) still play an important role in implementing the GSP scheme. This is to ensure that the benefits of the preferential tariff treatment are exclusive to products genuinely produced or substantially transformed into a final product by the preference receiving countries.

## Competitiveness in ASEAN and SAARC

Following the removal of the quota system, the T&C sector of South and Southeast Asian countries is facing huge challenges. They have to improve their competitiveness. Business climate, proximity to markets, infrastructure, labour costs and availability of raw materials are some of the main factors determining the competitiveness of this sector.

***Business Climate***

Many Southeast Asian countries are concerned with high bureaucratic costs, and political and social unrests hampering the climate of doing business. Political and policy-related issues have been identified as major factors increasing the cost of doing business, especially manufacturing and transportation. For example, Cambodia faces corrupt practices on the political front, while Indonesia and Philippines experience social and political instability (*Comparative Assessment of the Competitiveness of the Textiles and Apparel Sector in Selected Countries*, http://63.173.254.11/pub3671/chap3.pdf).

South Asian countries are encountering similar problems, including lack of transparency in legal matters. For example, economic governance in India is perceived to be relatively weak. Transparency in legal matters, complex paperwork and red tape significantly affect the cost of production and increases the time for product delivery to the market. Bangladesh is facing political instability. Sri Lanka is the most attractive place in South Asia as far as business climate is concerned (good investment law, etc).

***Proximity to Markets***

Southeast Asian countries are located far away from the west coast of the US and, thus, are at a disadvantageous position as compared to the South American countries. It is estimated that on an average it takes 45 days to ship from Southeast Asia to the US (*Comparative Assessment of the Competitiveness of the Textiles and Apparel Sector in Selected Countries*, http://63.173.254.11/pub3671/chap3.pdf). However, it takes even more time (45 to 60 days) to ship from India to the east coast of the US. The geographical location of South and Southeast Asian countries is considered a disadvantage when compared to that of China, which has to spend only 12 to 18 days to ship to the US market.

***Infrastructure***

In terms of infrastructure, Southeast Asian countries like Singapore, Thailand, Malaysia and Indonesia are considered as advanced. Indeed, good infrastructure has a positive impact on a firm's ability to export on time. In addition, reliable electricity, water and telecommunications are very important to increase productivity.

South Asian countries face many infrastructure-related challenges to enhance their competitiveness. For example, it has been found that the T&C sector in India is plagued by communication bottlenecks (road and rail transport), lack of deep-water ports, port congestion and frequent power outages. A good infrastructure developed through physical connectivity between South and Southeast Asian countries by enhancing road, rail, sea, and air linkages will help increase the much-needed investment including foreign direct investment (FDI) in this sector, besides increasing the productivity of existing units.

***Labour Costs***

Southeast Asian countries except Cambodia, Laos, Indonesia and Vietnam, have high labour costs. While the labour costs in these countries average around US$50 per month, in other ASEAN countries it is more than US$100 per month *(US Department of Labour and Bureau of International Labour Affairs)*. Moreover, skills levels and productivity standards vary greatly among these countries. Thailand has skilled garment workers and small production lines, which are considered as favourable conditions for producing fashion apparel.

The T&C sector is believed to be one of the largest sources of employment in South Asia. Labour costs in South Asian countries are among the lowest in the world. India has a skilled workforce, low cost labour and design expertise. Both Bangladesh and Pakistan have large sources of labour at a low cost. But Sri Lanka has a small labour pool and experiences relatively high wage rate. According to the US Department of Labour and Bureau of International Labour Affairs, the average wage rates in India, Bangladesh and Sri Lanka range between US$40 and US$60 per month. India also has well-educated and professional managers and technicians. Bangladesh suffers from low literacy levels, frequent labour unrests and outdated technology. Labour productivity in T&C was indexed at 107 in India during 2000, according to United Nations calculations. This was much lower than that of Indonesia (158 for textiles and 148 for clothing), Malaysia (209 and 151) and Philippines (140 and 145).

***Availability of Raw Materials***

Raw materials like cotton and fibre are scarce in Southeast Asian countries. They are mostly imported from China, Taiwan, and Hong Kong (*Comparative Assessment of the Competitiveness of the Textiles and Apparel Sector in Selected Countries*, http://63.173.254.11/pub3671/chap3.pdf). For example, Cambodia imports virtually all the raw materials for its garment industry. In Philippines, fabrics are shipped from Taiwan. Thailand has locally produced raw materials, but its strong reliance on import of high quality raw material is considered a weakness. Indonesia is known for its quality fabrics and, hence, is at a competitive edge in cotton products.

Despite this, Southeast Asian countries, with the exception of Brunei, are net exporters of T&C. This sector constitutes a major portion of total exports of Indonesia, Philippines and Thailand (12.6, 13.1 and 11 percent, respectively and ranking as the second most important export sector in each country). For Malaysia, T&C accounts for only 3.7 percent of total exports while in Singapore, it stands at 2.6 percent. According to the ASEAN Federation of Textile Industries, in 1999, Malaysia also imported textiles and textile products from neighbouring countries such as Indonesia, Singapore, Philippines and Vietnam.

On the other hand, South Asian countries are considered to be the world's largest suppliers of raw materials after China. India is ranked as the world's third largest producer of cotton, cotton yarn, man-made fibres and filament yarns. Pakistan is ranked as the world's fourth largest producer of cotton after China, India, and the US. But Bangladesh mostly imports raw materials from India. The same is true for Sri Lanka.

## Prospects for Cooperation

The cooperation between and among South and Southeast Asian countries in producing and exporting T&C is expected to benefit them hugely. Countries in both these regions are trying to increase their market shares. A comparative study of the EU, US and Japanese textiles markets in 2003 shows that in the EU the share of Southeast Asian countries was seven percent and that of South Asian countries was 14 percent. In the US market, these shares were 14 and 12 percent and in the Japanese market they were seven and two percent respectively.

**Comparison of EU, US, and Japanese Trade – Textile Sector in 2003**

| Market | EU-15 Export US$ (in bn) | Share of EU market (Percent) | US Export) US$ (in bn) | Share of US market (percent) | Japan Export US$ (in bn) | Share of Japanese market (Percent) |
|---|---|---|---|---|---|---|
| ASEAN | 6.07 | 7 | 12.98 | 14 | 1.87 | 7 |
| SAARC | 12.08 | 14 | 10.63 | 12 | 0.44 | 2 |
| Other | 66.49 | 79 | 66.55 | 74 | 23.37 | 91 |
| Total World | 84.64 | 100 | 90.16 | 100 | 25.68 | 100 |

*Sources: Compiled from EU-EUROSTAT/COMEXT; 02/03/05 US and Japan - COMTRADE, 02/03/05.*

The data is obvious. South and Southeast Asian countries have a small share of the world market *vis-à-vis* other regions. If cooperation is accomplished and GSP benefits are provided to these regions through cumulation of 'RoO,' these countries will surely increase their exports of T&C products to the world market. In addition, they will be able to increase their sale in the regional markets because duty-free exchange of raw materials and final products will be the cornerstone of such cooperation.

As per a proposal made by Sri Lanka, the Council of Ministers, at their meeting at the 12th SAARC Summit held in Islamabad in January 2005, decided to ask the SAARC Committee on Economic Cooperation to study how South and Southeast Asian countries can jointly work to enhance their market share in the highly competitive European market in the aftermath of the phasing out of quotas. The following factors need to be taken into consideration while developing cooperation in trade in T&C between and among South and South Asian countries.

### *Raw Materials*

The cost of raw materials for T&C has an important bearing on the competitiveness and exports of these products. Some South Asian countries are among the largest suppliers of these raw materials, especially India and Pakistan, and at a relatively low cost. One area of cooperation is that with the cumulation of GSP benefits Southeast Asian countries can source these raw materials from India and Pakistan.

If such cooperation is established under aegis of a cumulative GSP, Southeast Asian countries will gain immensely but for that they have to provide duty-free or low tariff access for these products. Moreover, India and Pakistan will also be able to enlarge their market share of raw materials and can replace China as the main supplier of raw materials to Southeast Asian countries.

### *Design Exchange*

Design is one of the important factors for enhancing competitiveness (particularly for niche products) and cooperation in this respect can assist South and Southeast Asian countries to cope with variable demand in the world market, especially in rich countries. By exchanging and incorporating innovative designs and styles, these countries can compete jointly and effectively. While South Asian countries are good at creating innovative designs (including ethnic designs), Southeast Asian countries have considerable presence in the fashion market. Together, these countries can satisfy continuously changing consumer demands in the western as well as local markets and, thus, create a better and more secured market for their niche products.

### *Transfer of Technology*

Technology is crucial to improve productivity. It can scale down fabric waste in the production process, gain production time, etc. Technological innovations have helped countries to cope with increased costs of labour and other competitive disadvantages. Together, they can better afford the cost of technological innovations to face challenges from other regions of the world, including China. Both the regional blocs have shown a strong sense of collective commitment to regional collaboration in science and technology.

The challenge is to exchange technology between and among these countries. Technology transfer could include know-how, do-how, labour and management skills. According to one estimate, the productivity of South and Southeast Asian countries is lower than that of China because of the use of advanced technology such as computer-aided cutting and design.

## Conclusion

Many South and Southeast Asian countries are exploring ways and means of cooperation, bilaterally as well as regionally. For example, India has signed a free trade agreement with Thailand while discussions are on to establish Indo-ASEAN free trade agreement (FTA). Besides making trade freer, cooperation in T&C could be an important element of these initiatives, as this sector is a significant source of livelihood for many.

Cooperation should be established in such a manner that these countries together benefit from schemes like GSP and issues like ‘RoO’ should not come in the way of providing such benefits to the producers and exporters of T&C in these countries.

The nature and functioning of this sector demonstrates that South and Southeast Asian countries can achieve complementarities in the production and export of T&C. Together, and by exploring avenues of cooperation, they can be more competitive in the global market. Given the widely prevalent scepticism about international trade and its impact on poverty, innovative cooperation is required for securing and enhancing livelihoods. Cooperation is not an end, but a means to make trade work better for the people, especially the poor.

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