CHAPTER 3: COMPARATIVE ASSESSMENT OF THE COMPETITIVENESS OF THE TEXTILE AND APPAREL SECTOR IN SELECTED COUNTRIES

This chapter is divided into two parts: (1) a discussion of the analytical framework used in the study to assess the competitiveness of the textile and apparel industries of the selected countries, which are listed in table 1-1 of chapter 1 of this report; and (2) a comparative assessment of the competitive strengths and weaknesses of these countries' textile and apparel industries.

To better understand the key factors underpinning a country's competitiveness in textiles and apparel, Commission staff conducted interviews in the United States and abroad with buying managers of major U.S. importers of apparel and home textiles--namely, the large apparel and home textile companies and retailers--regarding their current sourcing strategies, likely changes to their sourcing strategies following quota elimination in 2005, and reasons for the expected changes. Staff also conducted interviews with representatives of East Asian firms that produce or purchase textiles and apparel worldwide and that are major sources of investment in the production of such goods in many countries covered by the study; representatives of textile and apparel producers in India, which is considered by many U.S. apparel companies and retailers as the major low-cost alternative to China as a source for apparel and home textiles; and representatives of textile and apparel producers in sub-Saharan Africa, Mexico, and Central America.[1] The analytical framework and competitive assessment presented in this chapter are also based on information obtained from a wide range of sources, including a review of the literature (discussed in chapter 2 of this report) and testimony presented to the Commission at the hearing and in written statements (a summary of the views of interested parties is presented in chapter 4).

Several caveats should be noted about the Commission assessment. First, as requested by USTR, the Commission analysis focuses on likely changes in trade and production among certain developing-country suppliers, and does not consider likely changes in trade and production among developed-country suppliers, particularly the United States and the

[1] In interviews with USITC staff, representatives of both U.S. and foreign firms stressed that the information provided was "confidential business information" and that they did not want their own names or their firm names connected to specific information in the USITC report to USTR because of the "sensitive economic and political nature" of the information. A list of U.S. and foreign firms interviewed by USITC staff appears in appendix D.

European Union (EU), or the impact of such changes on global production and trade patterns. Second, the assessment focuses primarily on likely changes in sourcing strategies of U.S. apparel companies and retailers, and not the likely effects of the elimination of EU quotas. Third, the assessment looks primarily at static, rather than dynamic, effects of quota removal on the competitiveness of the textile and apparel sector in selected countries.[2] In particular, the study does not fully consider the possible long-term effects of economic growth in key developing-country markets, particularly China and India, and how it might affect global trade patterns.

In the long term, continued economic growth in Asian countries, particularly China and India, may spur their domestic demand for goods, including textiles and apparel, and lessen their propensity to export.[3] Economic growth in China and India likely will lead to rising incomes and an increase in domestic consumption of textiles and apparel, which might provide opportunities for other exporting countries to expand sales. As wages and domestic demand for textiles and apparel increase, the possibility exists that China and India could become less cost competitive in the production of textiles and especially apparel, compared with other low-cost producers. Although it is difficult to predict when such a development might occur, some analysts have noted that the shift to new suppliers might simply be part of a natural evolution of the comparative advantage from high-cost to low-cost suppliers.[4] During the past three decades, for example, Japan and then the newly industrialized economies (NIEs) of East Asia (Hong Kong, Korea, Singapore, and Taiwan) have lost their comparative advantage in labor-intensive apparel production and have been shifting from these products into other sectors, while China and other low-wage economies have emerged as major suppliers.[5]

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[2] As requested by the USTR, this study provides a qualitative assessment of the relative competitiveness of the textile and apparel sectors in selected countries. For a quantitative assessment of the likely effects of the removal U.S. textile and apparel quotas, see U.S. International Trade Commission, *The Economic Effects of Significant U.S. Import Restraints* (inv. No. 332-325), USITC Pub. 3519, June 2002.

[3] In the past 10 years, real economic growth in China was 142 percent (more than five times as fast as that of the United States) and India's was 77 percent (more than three times as fast as that of United States).

[4] See, for example, Gary Gereffi, "The International Competitiveness of Asian Economies in the Apparel Commodity Chain," Asian Development Bank, ERD Working Paper Series No. 5, Feb. 2002.

[5] The relative decline of the NIEs in the global apparel market has been attributed to the sector's high labor intensity. As real wages increase and labor skills upgrade, they lose most of their comparative advantage in apparel (while maintaining it in textiles). Rapid growth in other sectors may also be enough to divert resources (both labor and investment flows) away from the apparel sector.

Analytical Framework

During the past two decades, the availability and cost of quotas have influenced sourcing strategies of U.S. apparel companies and retailers, and investment and production strategies of Asian producers and trading companies. Many of the U.S. firms stated that quota availability and cost largely explain why they import apparel from as many as 50 or more countries, especially for heavily traded items such as tops and pants. The cost of quotas can be quite high and thus serve as deterrent to sourcing. For example, in 2002, the estimated export tax equivalent on the quota for Chinese knit cotton shirts was about 27 percent ad valorem and for cotton trousers it was 64 percent ad valorem.[6] With the elimination of quotas and related quota costs, other factors will grow in importance in the sourcing decisions of U.S. apparel companies and retailers; it is likely that some countries will have the capability to meet these factors but many others will not. U.S. apparel companies and retailers plan to consolidate their post-quota sourcing among many fewer countries as part of their strategy "to reduce the merchandise cost structure, reduce the timeline to get product into the stores, and increase the flexibility of their supply chains."[7]

The analytical framework used in this study to assess the competitiveness of selected countries' textile and apparel industries comprises factors that affect sourcing strategies of U.S. apparel companies and retailers. As shown in figure 3-1, the factors include a country's business climate, infrastructure conditions, proximity and preferential access to major world markets, availability of low-cost skilled workers and effective management, access to a reliable supply of competitively priced raw materials, and the level of supplier service and reliability. Although the relative importance of each factor can vary by firm, depending on its corporate philosophy, import volume and product mix, risk tolerance, and existing supplier relationships, the key criteria likely to affect sourcing decisions in a post-quota world are cost and availability of labor; cost, quality and availability of raw materials (including fabric, trim, and findings); and the efficiency and flexibility of suppliers to meet changing fashions and retailer demands. The competitive factors are discussed below.

Business Climate

An assessment of a country's business climate is an important element of evaluating the risk of doing business there. According to the American Apparel & Footwear Association (AAFA), numerous factors enter into this assessment, including compliance with human

[6] See discussion on China in appendix E of this report for additional information on export tax equivalents of quotas on U.S. apparel imports from China.

[7] Peter McGrath, Senior Vice President and Director, JCPenney Product Development & Sourcing, and Chairman, Board of Directors, USA-ITA, transcript of public hearing, pp. 62-63.

Figure 3-1
Textiles and Apparel: Factors of Competitiveness

Business climate
- Political stability
- Safety of personnel
- Security of production and shipping
- Transparent and predictable legal, commercial, and regulatory system
- Minimal administrative burden and corruption
- Compliance with internationally recognized health and labor standards
- Subsidies and tax credits
- Free trade zones
- Real exchange rates
- Market demand and economic growth

Infrastructure and proximity to markets
- Roads, ports, rail, and airports for moving goods into and out of the country
- Shipping and other transportation times and costs
- Proximity to major markets
- Access to reliable sources of energy, water, and telecommunications

Market access
- Preferential access in major markets

Labor and management
- Availability of workers and competition for workers from other sectors
- Compensation rates
- Labor skills and productivity
- Availability of qualified managers, including middle management

Raw-material inputs
- Access to quality and cost-competitive domestic or regional yarn and fabric production
- Tariffs on imports of raw materials
- Rules of origin for trade preferences
- Cost and availability of capital to invest in new machinery and purchase raw materials

Level of service provided and reliability of supplier
- Reputation for quality and on-time delivery
- Existing business networks (supply chain linkages, relationship with customers)
- Level of service provided (e.g., full-package versus assembly)
- Flexibility and variety in styles or products and lot sizes offered
- Lead time and flexibility to respond to quick turnaround orders

rights requirements in the country and ensuring the security of shipments from the factory through the country's infrastructure.[8] Some firms cited the lack of internationally recognized labor standards as a reason for not sourcing from certain countries. For example, many firms said they would not source apparel from Myanmar (Burma) because of human rights concerns. Several firms cited security as a reason for not sourcing garments from a country at all, while some firms said they would use buying agents to source from a country where there was a safety concern, rather than set up their own office there.

AAFA stated that firms also examine factors affecting the movement of inputs into, and final goods out of, a country, including compliance with applicable local and U.S. customs requirements; the level of U.S. customs enforcement activities related to that country; transparency in the foreign country's political system; and transparency and predictability in the foreign country's commercial, regulatory, and legal system. U.S. firms can incur significant costs to ensure that a foreign supplier complies with local laws and regulations, U.S. import regulations, and policies of the individual U.S. firms. Further, the lack of transparency in laws and regulations can lead to disruptions in sources of supply and shipments of goods. These overhead costs are among the reasons U.S. apparel companies and retailers are planning to consolidate sources of supply following quota elimination and strengthen strategic relationships with their suppliers.

Infrastructure and Proximity to Market

A country's infrastructure affects a firm's ability to produce goods and move them into and out of the country in a timely manner. Access to ports having frequent shipping traffic to and from the United States can make even geographically distant locations competitive from a shipping standpoint. Shipping times largely depend on the frequency of shipping from a port and the volume of business conducted. According to U.S. retailers, shipping times to the west coast of the United States generally average from 12 to 18 days from Taiwan, Hong Kong, and China, but as much as 45 days from some member countries of the Association of South East Asian Nations (ASEAN). The geographic proximity to a market can also be an advantage for goods needed on short notice. Shipping from the Caribbean Basin Economic Recovery Act (CBERA) countries to the United States can take as little as 2 to 7 days.

A country's telecommunications infrastructure has become very important for U.S. apparel companies and retailers in communicating with suppliers and handling supply chain logistics as they seek to reduce lead times and increase control over all elements of the supply chain. In addition, a reliable source of electricity is essential for all segments of the industry, as is access to reliable supplies of water for dyeing and finishing yarns, fabrics, and certain garments requiring special finishes, such as denim jeans.

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[8] Kevin M. Burke, President and CEO, AAFA, written submission to the Commission, Jan. 22, 2003.

Market Access

U.S. apparel companies and retailers indicated that the major benefit of U.S. trade preferences is the absence of quota restrictions, with duty-free access a secondary benefit. The firms claimed that the extent to which duty-free access is a competitive advantage depends on the rules of origin and the accompanying customs regulations to implement the trade preferences. According to the firms, preferential trade agreements permitting the use of third-country fabrics (e.g., the African Growth and Opportunity Act (AGOA), the U.S.-Israel Free Trade Agreement, and the qualified industrial zone (QIZ) program with Jordan) are more beneficial than agreements requiring U.S. content (e.g., the Caribbean Basin Trade Partnership Act (CBTPA)), because they allow for the use of less expensive Asian fabrics and for greater flexibility in the choice of fabrics. The U.S. firms stated that the benefit of trade preferences is diminished considerably or eliminated by U.S.-content rules because U.S. fabrics reportedly cost as much as 20 to 40 percent more than Asian fabrics. In addition, two large U.S. apparel companies claimed that it is more difficult to work with U.S. mills in the development of new products; one company said that U.S. mills' minimum lot sizes are too large. The allowance for the use of regional inputs was considered of some benefit, to the extent that regional fabrics are available in the quantities and styles required. ***

Other disincentives to sourcing apparel from CBTPA and the North American Free Trade Agreement (NAFTA) beneficiary countries are paperwork requirements and related compliance costs. Some U.S. apparel firms noted that the cost of complying with regulations under the CBTPA and NAFTA offset a large portion of the program benefits. A firm estimated that the paperwork associated with complying with CBTPA and NAFTA regulations adds 3 percent to 5 percent to the cost of the goods.

Labor and Management

U.S. apparel companies and retailers stated that a country will need to have an abundance of skilled, inexpensive, productive labor to remain competitive in a post-quota world. The cost and availability of a trained or trainable workforce will be critical. Low wage rates alone are not a good indicator of labor costs, as rates of productivity, which contribute to the cost of labor, vary among countries. Table 3-1 shows the hourly compensation rates of selected countries for spinning and weaving, and apparel operations. According to the U.S. firms, although wage rates are higher in China than in such countries as Bangladesh, India, and Vietnam, productivity is considered much higher in China, making its overall labor cost lower. Sewing skills of workers, along with factory setup, influence the type of product that U.S. importers would consider sourcing from a particular country or factory. For example, sewing skills are particularly important in the production of fashion items, for which styles change frequently. In general, sewing skills are considered to be very good in Asia, particularly in China, Hong Kong, Korea, Taiwan, and Thailand. U.S. apparel companies and retailers often import apparel from East Asia that requires more sewing and construction, complex operations, and detailed work.

Another important competitive factor is the effectiveness of middle management, which has the day-to-day responsibility for maintaining the reliability of product quality and supply

Table 3-1
Textiles and apparel: Hourly compensation[1] for selected countries, 2002

Region or country	Textile industry	Apparel industry
	U.S. dollars	
East Asia:		
China	[2]$0.41 [3]$0.69	$0.68 [4]$0.88
Hong Kong	6.15	([5])
Korea	5.73	([5])
Taiwan	7.15	([5])
South Asia:		
Bangladesh	0.25	0.39
India	0.57	0.38
Pakistan	0.34	0.41
Sri Lanka	0.40	0.48
ASEAN countries:		
Indonesia	0.50	0.27
Malaysia	1.16	1.41
Philippines	([5])	0.76
Thailand	1.24	0.91
Mexico	2.30	2.45
CBERA countries:		
Costa Rica	([5])	2.70
Dominican Republic	([5])	1.65
El Salvador	([5])	1.58
Guatemala	([5])	1.49
Haiti	([5])	0.49
Honduras	([5])	1.48
Nicaragua	([5])	0.92
Sub-Saharan Africa:		
Kenya	0.62	0.38
Madagascar	([5])	0.33
Mauritius	1.33	1.25
South Africa	2.17	1.38
Andean countries:		
Colombia	1.82	0.98
Peru	1.63	([5])
Other countries:		
Egypt	1.01	0.77
Israel	8.17	([5])
Jordan	([5])	0.81
Turkey	2.13	([5])

[1] Includes wages and fringe benefits.
[2] Represents hourly compensation for China, other than in coastal areas.
[3] Represents hourly compensation for coastal China.
[4] Reflects labor compensation for factories in China producing moderate to better apparel.
[5] Not available.

Source: Data for the textile industries compiled from Werner International Management Consultants, "Spinning and Weaving Labor Cost Comparisons 2002," Reston, VA; and data for the apparel industries compiled from Jassin-O'Rourke Group, "Global Competitiveness Report: Selling to Full Package Providers" (New York, NY), Nov. 2002.

and ensuring the flexibility to change orders as needed. Many importers contended that middle management is very good in many factories in China and other East Asian countries, but problematic in many factories in Mexico. In fact, weak middle management was cited as a major reason why U.S. importers have had problems sourcing from Mexico.

Raw-Material Inputs

The availability of cost-competitive, quality fabrics and trim in a country or region is expected to grow in importance in determining sourcing strategies for apparel in a post-quota world. Fabric availability affects lead times not only for production of goods for delivery, but also for production of samples prior to order placement. The availability of fabric, trim, and findings (e.g., zippers and buttons) is considered one of the many advantages of sourcing from China, because almost all the raw materials needed to make a garment are produced there.

If fabrics are not available locally, then shipping times and other logistics (such as customs issues) can affect lead times and costs. Shipping times and the frequency of shipping are important factors in determining the availability of fabrics in cases in which local fabrics are not available in the quantities or styles required. The Philippines, for example, does not have a local supply of export-quality fabrics, but several U.S. companies said they are able to obtain such fabrics in about 2 days from Taiwan for cut-and-sew operations in the Philippines. Preferential trade agreements that require use of certain yarns and fabrics in order to qualify for the trade preferences can deter sourcing if the yarns or fabrics are not available at the price, quality, or quantity needed.

Level of Service Provided and Reliability of Supplier

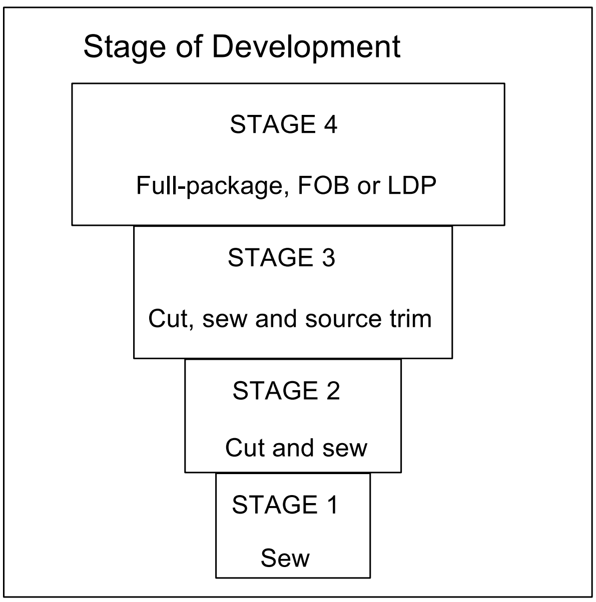
The enormous buying power of major U.S. retailers has challenged existing supplier-buyer relationships and compelled suppliers to be more responsive to retailer demands, as it tends to reduce the flexibility of suppliers in scheduling production and negotiating prices and other contract terms. As U.S. retailers consolidate their sourcing among fewer suppliers in a post-quota world, they are likely to use suppliers that offer not only competitively priced goods but also faster, more flexible service. With retailers reducing stocks and pushing inventory costs back up the supply chain, suppliers will need to be able to respond more quickly and efficiently to retailer demands for smaller, more frequent orders.

U.S. apparel companies and retailers said they prefer to source from foreign suppliers that can provide “full package” services. An established infrastructure exists in East Asia to provide such services to U.S. buyers, including product development, fabric sourcing and cutting, garment sewing, packaging, quality control, trade financing, and logistics arrangements. Retailers said they generally supply their own designs, but some suggested they are open to ideas from their suppliers and even solicit design and trend information. A certain skill level and knowledge base are required to translate a garment design into production patterns, which must be adapted to specific body types in the target markets. Another service sometimes supplied by manufacturers is point-of-sale replenishment, where the manufacturer ships store-ready products to the retailers on the basis of point-of-sale data at the retail level (see box 3-1 for information on the stages of development in apparel production).

Box 3-1
Stages of Development in Apparel Manufacturing

The figure below shows the different levels of service offered by manufacturers or vendors. At the first stage, the manufacturer sews the cut garment pieces as a contract service. This stage was common in the development of new offshore assembly operations in the Caribbean or Mexico in which fabric was cut into garment parts in the United States and sewn together offshore.[1]

The next level of garment industry development is cutting and sewing. At this stage, the factory still generally operates as contractor, and does not procure the raw materials needed to produce the garments. The production patterns are also provided by the apparel company. At the next stage, manufacturers will take the next step and source trim, particularly for basic products, for which the trim is standard, such as white buttons for a men's dress shirt.



At the final stage, a manufacturer becomes a full-package supplier, responsible for many aspects of the garment production from purchasing the fabric and trim, patternmaking, to full production and packaging, ready for retail sale.

The level of service for full-package producers can vary. Even though the manufacturer will purchase the fabric and trim, the retailer or apparel company importing the garments will often choose the actual fabrics, and the mill to produce the fabrics. The retailers and apparel companies then issue a letter of credit against which the apparel manufacturer issues a letter of credit to purchase the raw materials. Sometimes the full-package supplier will select the fabric and fabric suppliers, or suggest alternative suppliers that are able to meet the fabric specifications given by the customer. Full-package suppliers must be financially solvent in order to obtain financing for the purchase of raw materials. Generally the large importers purchase the products on a free-on-board (FOB) basis, taking responsibility for shipping and duty charges, because they can negotiate better shipping rates than smaller overseas apparel suppliers. However, some companies will purchase part of their product on a landed-duty-paid basis, allowing the foreign manufacturer to take care of shipping and payment of duties.

[1] Prior to legislation implementing NAFTA and the CBTPA, garments were required to be assembled from fabric formed and cut in the United States in order to qualify for preferential quota access and reduced duty treatment under the production sharing arrangements.

[2] For example, full package programs in the CBERA region generally refer to services ranging from procurement of materials to cutting and sewing, and to finishing and packaging of the final products. In the Far East, an established infrastructure exists to provide full package imports to U.S. buyers, including product development, fabric sourcing and cutting, garment sewing, packaging, quality control, trade financing, and logistics arrangements.

Country and Regional Assessment

The rest of this chapter provides a comparative assessment of the competitiveness of the textile and apparel sector in the selected countries, which are grouped by region.[9] In order to anticipate the possible implications of quota removal in 2005, it is useful to examine the changes in trade that have occurred for certain textile and apparel products that have been integrated into the General Agreement on Tariffs and Trade (GATT) and for which quotas have been removed for WTO members (table 3-2). For every product, the total volume of U.S. imports increased from 2001 to 2002, and China significantly increased its share of the U.S. import market for these products. For example, China's share of the U.S. import market for babies' apparel rose from 3 percent in 2001 to 27 percent in 2002, while that for robes (and dressing gowns) increased from 5 percent to 25 percent.

It is also helpful to examine the extent to which imports of textiles and apparel from the selected countries are concentrated in product categories that are highly constrained by quota for a large number of U.S. suppliers. Following quota elimination in 2005, countries whose shipments are concentrated in such product categories, likely will face significantly greater competition in the U.S. market than those countries whose shipments are diversified across a broader spectrum of products. As shown in table 3-3, U.S. textile and apparel imports from countries that benefit from preferential market access–particularly the CBERA countries, sub-Saharan African countries, Jordan, and, to a lesser extent, the Andean countries–are concentrated in a narrow range of highly import-sensitive product categories. By contrast, these same product categories make up only a small share of U.S. textile and apparel imports from China, India, and Pakistan, largely because all or a large share of the imports of such goods from these Asian countries are subject to binding quotas.

Table 3-4 summarizes the Commission assessment of key changes that are likely to occur in the global pattern of textile and apparel production and trade following quota elimination in 2005. Chief among the major beneficiaries will be China, which is expected to become the "supplier of choice" for most U.S. importers because of its ability to make almost any type of textile and apparel product at any quality level at competitive prices. China has proven its ability to compete in other developed country markets, particularly Australia and Japan, for which it accounted for 69 percent (2002) and 77 percent (2001) of their apparel import markets, respectively.[10] However, the extent to which China continues to expand its shipments to the United States and the EU following quota elimination in 2005 may be tempered by uncertainty over the use by the United States and other importing countries of the textile-specific safeguard provisions contained in China's protocol of accession to the World Trade Organization (WTO). In addition, as noted above, long-term economic growth in China may increase its domestic demand for textiles and apparel, as well as for labor and capital from competing sectors of the economy, possibly reducing the cost competitiveness of China vis-a-vis other developing country suppliers.

[9] The assessment is based on the detailed information presented in the individual profiles of each country's textile and apparel industries in appendixes E through L of this report. The information used in preparing this assessment came from many sources, as noted in the beginning of this chapter.

[10] Based on United Nations data.

Table 3-2
Selected textile and apparel products integrated into the GATT: U.S. imports, total and by selected countries, 2002, percentage change in imports from 2001 to 2002, and share of total U.S. imports, 2001 and 2002

Product and source	U.S. imports, 2002	Change in imports 2001 to 2002	Share of U.S. imports from the world-- 2001	2002
	1,000 units	*Percent*		
Babies' garments (category 239 in kilograms):				
World	109,446	10	100	100
China	29,941	826	3	27
Thailand	16,250	-7	17	15
CBERA	10,560	-14	12	10
Philippines	7,252	-17	9	7
Indonesia	5,716	-12	6	5
Bangladesh	5,518	-18	7	5
Mexico	4,514	-21	6	4
Hong Kong	4,299	-70.6	11	3
Brassieres (categories 349 and 649 in dozens):				
World	44,641	21	100	100
CBERA	13,297	15	31	30
China	10,580	232	9	24
Honduras	4,666	38	9	10
Mexico	4,322	-21	15	10
Indonesia	3,927	16	9	9
Thailand	3,536	10	9	8
Dominican Republic	3,662	-1	10	8
Costa Rica	2,286	2	6	5
Robes (categories 350 and 650 in dozens):				
World	8,538	28	100	100
China	2,172	540	5	25
CBERA	1,172	25	14	14
Turkey	1,072	20	13	13
Pakistan	826	15	11	10
Bangladesh	346	-6	6	4
Mexico	415	-14	7	5
Indonesia	208	5	3	2
Philippines	184	-36	4	2
Hong Kong	109	-57	4	1
Luggage and flat goods (category 670 in kilograms):				
World	276,735	39	100	100
China	181,812	536	14	66
Thailand	28,970	-43	25	10
Philippines	18,556	-49	18	7
Indonesia	12,876	-34	10	5

Table 3-2–Continued
Selected textile and apparel products integrated into the GATT: U.S. imports, total and by selected countries, 2002, percentage change in imports from 2001 to 2002, and share of total U.S. imports, 2001 and 2002

Product and source	U.S. imports, 2002	Change in imports 2001 to 2002	Share of U.S. imports from the world-- 2001	2002
	1,000 units	*Percent*		
Luggage and flat goods (category 670 in kilograms):–Continued				
Sri Lanka	10,570	-44	10	4
Vietnam	4,987	6,850	0	2
Taiwan	4,612	-72	8	2
Mexico	2,138	-52	2	1
Korea	2,053	-72	4	1
Knit fabrics (category 222 in kilograms):				
World	140,616	33	100	100
Canada	54,310	-6	55	39
Korea	33,199	212	10	24
Taiwan	21,619	120	9	15
China	7,011	21,976	0	5
Mexico	7,773	10	7	6
Thailand	2,102	-29	3	1
Hong Kong	1,729	-65	5	1

Source: Compiled from official statistics of the U.S. Department of Commerce.

Table 3-3
U.S. imports of selected apparel articles in highly constrained quota categories,[1] their share of total textile and apparel imports, and share subject to binding quotas, by selected countries and regions, 2002

	U.S. imports of selected apparel articles--		
Country or region	Total	Share of total textile and apparel imports in highly constrained categories	Share subject to binding quota
	Million SMEs	------------------*Percent*------------------	
Bangladesh	356.8	32	100
China	252.2	5	100
Egypt	97.8	37	0
Hong Kong	440.7	46	81
India	136.4	9	90
Indonesia	207.7	17	88
Israel	94.4	18	0
Jordan	62.5	69	0
Korea	124.6	6	98
Macau	204.1	64	51
Malaysia	88.0	27	51
Mexico	1,406.0	33	0
Pakistan	131.9	5	73
Philippines	235.1	29	100
Sri Lanka	130.1	23	90
Taiwan	223.8	16	23
Thailand	193.4	15	67
Turkey	215.2	20	96
Andean countries	104.5	54	0
CBERA countries	2,967.4	78	0
Sub-Saharan Africa	223.4	73	0

[1] The highly constrained quota categories are cotton and manmade-fiber knit tops (categories 338/339 and 638/639), pants and shorts (347/348 and 647/648), nightwear (351 and 651), and underwear (352 and 652). These categories, which accounted for 53 percent of total U.S. apparel imports in 2002, have a large number of supplying countries subject to binding quotas (individual country quotas with a “fill rate” of 90 percent or more in 2002).

Source: Compiled from official statistics of the U.S. Department of Commerce.

Table 3-4
Summary of anticipated effects of quota elimination in 2005 and key competitive factors, by selected regions and countries

Region/country	Likely effect of quota removal	Contributing factors
EAST ASIA	**Summary**: U.S. apparel companies and retailers are likely to expand sourcing from the region and continue close relationships with suppliers in the region, who are major sources of textile and apparel investment worldwide.	**Summary**: Labor - Sewing skills considered among the best in the world. Inputs - Substantial manufacturing base for raw materials. Transportation - Best shipping times to the U.S. west coast within Asia.
	China: Likely to be supplier of choice for most large U.S. apparel companies and retailers; uncertainty regarding textile-specific safeguards may temper export growth. Over the long term, competitiveness may diminish as strong economic growth leads to greater domestic demand for textiles and apparel, and for the labor and capital to make these goods. Showed tremendous growth in export of goods for which it became eligible for quota-free entry in 2002.	**China:** Labor - Per-unit labor costs very low due to low wages and high productivity. Inputs - Produces fabrics, trim, packaging, and most other components used to make apparel and made-up textile articles. Products - Considered by industry among the best in making most garments and made-up textile articles at any quality or price level. World's largest producer and exporter of textiles and apparel, notwithstanding tight quotas in major world import markets.
	Hong Kong and Macau: Initially, may continue to be suppliers of some apparel under outward processing arrangements (OPAs) with China because of uncertainty regarding textile-specific safeguards with China. There are no other compelling reasons to source most apparel from these relatively high-cost suppliers.	**Hong Kong and Macau**: Labor - High-cost suppliers compared with China. Special arrangements - OPAs allow for some of the labor intensive production steps to take place in China, but remain a product of Hong Kong or Macau for trade purposes. Will not be subject to China-specific safeguards after quotas are removed.
	Korea and Taiwan: Likely to continue as major suppliers of fabrics to global industry, including to China. However, U.S. firms are likely to move sourcing of apparel to lower-cost countries, particularly China; may continue to source certain garments from these suppliers (e.g., men's dress shirts, dresses, and other fashion apparel).	**Korea and Taiwan**: Labor - High per-unit labor costs; high labor productivity. Products - Small, flexible sewing lines advantageous for fashion apparel; highly automated sewing lines for dress shirts; offer full-package services.

Table 3-4--Continued
Summary of anticipated effects of quota elimination in 2005 and key competitive factors, by selected regions and countries

Region or country	Anticipated effects of quota removal	Key competitive factors
SOUTH ASIA	**Summary**: U.S. firms will likely expand sourcing from South Asia with the removal of quotas in 2005.	**Summary**: Inputs - Huge manufacturing base for yarns and fabrics. Competitive position - Most competitive alternative to China as a supplier, but competitiveness of each country varies widely.
	India: Likely to remain a competitive supplier to the United States when quotas are removed in 2005. Considered by many U.S. firms the primary alternative to China. Over the long term, competitiveness may diminish as strong economic growth leads to greater domestic demand for textiles and apparel, and for the labor and capital to make these goods.	**India:** Labor - Huge, relatively inexpensive, skilled workforce; has design expertise. Inputs - Among the world’s largest producers of yarns and fabrics; Products - Wide range of apparel; considered a competitive source for home textiles (e.g., bed linens and towels). Business climate - Personal safety, security of shipments between factories and ports and bureaucratic red tape and infrastructure are issues, with many U.S. firms using agents in lieu of dealing directly with producers.
	Pakistan: Likely to continue as a supplier to the U.S. market. Considered by many U.S. firms as a competitive alternative to China, particularly for men’s apparel. May continue to be a global supplier of cotton yarns and fabrics.	**Pakistan** Labor - Large, relatively inexpensive labor supply. Inputs - Access to local supplies of raw cotton. Business climate - The Government is taking steps to ensure the global competitiveness of the textile and apparel sector; personal safety and security of shipments between factories and ports are issues.
	Bangladesh: The status of Bangladesh as an overall supplier to U.S. market is uncertain. Considered by some U.S. firms to be competitive alternative to China for mass-produced, low-end apparel.	**Bangladesh**: Labor - Very low wage rates; productivity improving, but lags China; government is working to improve labor standards. Inputs - Relies heavily on imports for woven fabric requirements; becoming increasingly self-sufficient in knit fabrics. Special arrangements - Duty-free access to major world import markets, including the EU, Canada, and Norway. Products - Mass-produced basic garments, including knit cotton tops and woven cotton pants.

Table 3-4--Continued
Summary of anticipated effects of quota elimination in 2005 and key competitive factors, by selected regions and countries

Region or country	Anticipated effects of quota removal	Key competitive factors
	Sri Lanka: Likely to see its share of U.S. apparel imports fall, but expected to be a niche supplier for specialty or fashion goods, hosiery, and women's intimate apparel such as bras and underwear.	**Sri Lanka** Labor - Relatively small labor pool; relatively high wage rates. Inputs - Relies heavily on imported yarn and fabric.
ASEAN	**Summary**: Overall share of U.S. textile and apparel imports is likely to decline as U.S. firms reduce sourcing in all but a few countries.	**Summary**: Labor - Costs relatively high in all ASEAN countries except Indonesia and non-WTO members Vietnam and Cambodia, which are ineligible for quota liberalization. Transportation - Shipping times to the U.S. west coast average 45 days, compared with 12 to 18 days from China.
	Indonesia: Future status as a supplier to the U.S. market uncertain. Many U.S. firms consider Indonesia to be a competitive supplier, but indicated its political and social unrest may discourage future sourcing.	**Indonesia**: Labor - Abundant supply of low-cost, skilled labor. Inputs - Huge manufacturing base for raw materials, especially synthetic fibers, yarns, and fabrics. Business Climate - Frequent political and social unrest likely to deter growth in sourcing in the short term.
	Philippines: Share of U.S. apparel imports is likely to decline, as has already occurred in goods for which quotas were eliminated (e.g., babies' apparel).	**Philippines**: Labor - English-speaking, skilled labor force; high wage rates. Inputs - Relies heavily on imported yarn and fabric. Special arrangements - Foreign-trade zones on former U.S. military bases provide established modern infrastructure. Business Climate - Political and social unrest.
	Thailand: Share of U.S. imports is likely to decline, as has already occurred in goods for which quotas were eliminated (e.g., babies' apparel and luggage); may become a niche supplier of garments having complex construction or detailed sewing requirements.	**Thailand**: Labor - Highly-skilled workforce; high wages, partly because of a labor shortage. Inputs - Domestic supply of yarns and fabrics. Products - Strong needlework skills and small-scale factories enable intricately designed garments and flexibility in sourcing fashion apparel.

Table 3-4--Continued
Summary of anticipated effects of quota elimination in 2005 and key competitive factors, by selected regions and countries

Region or country	Anticipated effects of quota removal	Key competitive factors
	Malaysia: Share of U.S. apparel imports is likely to decline significantly.	**Malaysia**: Labor - Labor shortage; wages second-highest in the region after Singapore. Business climate - Although Government highlights importance of textile and apparel sector, investment is largely directed to other industries.
MEXICO	Share of U.S. apparel imports is likely to decline further, even with NAFTA preferences. May continue to be a niche supply for some basic apparel, particularly for goods needed on short-turnaround basis. Has the potential to expand yarn and fabric exports to other countries in the western hemisphere under a proposed Free Trade Area of the Americas or to Central America if the proposed U.S.-Central America FTA permits the use of Mexican inputs.	Labor - Costs are relatively high; product quality and production reliability problematic; middle management responsible for running the factories is considered weak; product design expertise limited. Inputs - Produces knit and woven fabrics. Cost is reportedly less than that for similar U.S.-produced fabrics, but higher than similar Asian fabrics. Products - Concentrates on mass-producing basic garments, particularly 5-pocket denim jeans, knit tops, and undergarments; limited capability for fashion apparel. Limited ability to offer full-package services. Business climate - Additional overhead costs in providing security for shipments from factories to the U.S. border and complying with paperwork requirements for preferential treatment under NAFTA.
CBERA	**Summary:** Most U.S. firms indicated they will reduce sourcing from the CBERA countries, especially if the proposed U.S.-Central America FTA does not permit the use of regional (e.g., Mexican) or third-country (e.g., Mexican or Asian) fabrics. However, even without a regional or third-country fabric provision in the proposed U.S.-Central America FTA, the region is likely to continue to mass-produce garments having minimal labor content and make apparel for quick-turn orders.	**Summary:** Products - Mass-produces basic garments, particularly those with low-labor content and few delicate sewing operations. Inputs - Relies heavily on imported yarn and fabric from the United States, largely reflecting U.S. content rules under the CBTPA to qualify for trade benefits; U.S. and regional fabrics required to qualify for CBTPA preferences cost more than similar fabrics made in Asia. Transportation - Benefits from proximity to U.S. market. Special arrangements - Duty-free access under CBERA.

Table 3-4--Continued
Summary of anticipated effects of quota elimination in 2005 and key competitive factors, by selected regions and countries

Region or country	Anticipated effects of quota removal	Key competitive factors
	Costa Rica: Share of U.S. apparel imports is likely to decline significantly.	**Costa Rica:** Labor - Highest labor costs in region; highly educated labor force. Business climate - Government trying to attract other, non-apparel investment.
	Dominican Republic: Share of U.S. apparel imports may decline, but likely to continue to supply apparel for quick-turn orders. Considered among the five most attractive suppliers from the region.	**Dominican Repbulic:** Labor - Shifted some assembly operations to Haiti to take advantage of Haiti's lower labor costs. Transportation - Benefits from proximity to U.S. market.
	El Salvador, Guatemala, Honduras, and Nicaragua: Future status as a supplier to the U.S. market uncertain, pending the outcome of regional or hemispheric free trade negotiations. Considered among the five most attractive suppliers from the region.	**El Salvador, Guatemala, Honduras, and Nicaragua:** Labor - Costs in most countries higher than China and other Asian countries. Inputs - Some regional knit fabric production.
	Haiti and Jamaica: Share of U.S. apparel imports is likely to decline significantly.	**Haiti and Jamaica:** Labor - Haiti has lowest hourly compensation costs in region. Business climate - Personal safety and security of shipments are issues.
ANDEAN	**Summary:** Share of U.S. imports likely to decline overall, but may continue to be a niche supplier to the U.S. market.	**Summary:** Special arrangements - U.S. legislation enacted in August 2002 providing for duty-free treatment of apparel imports from region using regional yarns and fabrics.
	Colombia: Colombia likely to become less cost competitive in the U.S. market with Asian suppliers following quota removal, but could still be competitive for garments in which lead times are critical.	**Colombia:** Inputs - Domestic supply of knit and woven fabrics. Products - Considered capable supplier of tailored clothing, sportswear, and only country in South and Central America skilled in fashion apparel. Business climate - Personal safety and security of shipments between factories and ports are issues.

Table 3-4--Continued
Summary of anticipated effects of quota elimination in 2005 and key competitive factors, by selected regions and countries

Region or country	Anticipated effects of quota removal	Key competitive factors
	Peru: May see its overall share of U.S. apparel imports decline, but expected to continue to be a niche supplier of high-end knit shirts.	**Peru:** Inputs - Domestic supply of high-quality cotton and fine-animal hair. Domestic production of yarns and fabrics. Products - Niche supplier of high quality, cotton knit shirts and related garments.
	Bolivia and Ecuador: Very small suppliers to the U.S. market; could become sources for specialty goods, such as those made of fine hairs from animals indigenous to these countries.	**Bolivia and Ecuador:** Inputs - Relies heavily on imports of fibers, yarns, fabrics, and findings. Has some supply of specialty animal fibers.
TURKEY	Future status as a supplier to the U.S. market uncertain. Several firms indicated Turkey would be an attractive supplier if it had a free-trade agreement with the United States. A few firms indicated they would continue or increase sourcing from Turkey, even without a free-trade agreement. May continue to be a global supplier of cotton fabrics.	Inputs - Domestic supplies of raw cotton, cotton yarns and fabrics. Special arrangements - Proximity and duty-free access to EU market. Products - Large cotton-based textile and export-oriented apparel industries; fast turnaround and fashion capabilities. Transportation - Shipping times to U.S. market similar to those for East Asia.
EGYPT	Likely to decline in importance as a supplier to the U.S. market, though a few industry sources indicated they will continue to source some products from Egypt following the removal of quotas. U.S. firms indicated Egypt would be an attractive supplier if a free trade agreement were negotiated with the United States.	Inputs - Largely government-owned textile industry characterized by excess employment, outdated technology and relatively low productivity. High raw material costs, owing to government -set minimum prices on cotton. Apparel manufacturers import yarn and fabric. Products - Industry largely cotton-based. Exports large quantities of its acclaimed “Egyptian cotton” in the form of yarns to the U.S. textile industry.

Table 3-4--Continued Summary of anticipated effects of quota elimination in 2005 and key competitive factors, by selected regions and countries		
Region or country	**Anticipated effects of quota removal**	**Key competitive factors**
ISRAEL AND JORDAN	Israel may continue to be a niche supplier for intimate apparel. Jordan may continue to be a niche supplier of apparel articles that are subject to high U.S. duty rates, such as manmade-fiber garments. However, sourcing from Jordan may be affected by the outcome of free-trade negotiations involving countries in the Western Hemisphere. If the proposed U.S.-Central America FTA or FTAA extends unlimited duty-free treatment to U.S. imports of apparel made in the region from third-country fabrics, U.S. firms are likely to shift sourcing to the region from distant sources such as Jordan.	Labor - Production in Israel highly automated and labor costs are high. Relatively low labor costs in Jordan. Special arrangements - Under the FTA with Israel, the United States established a "qualified industrial zone" program with Jordan and Israel that grants duty-free treatment to qualifying textile and apparel articles.
SUB-SAHARAN AFRICA	**Summary:** Industry sources indicated that this region's overall share of U.S. apparel imports will fall, notwithstanding AGOA preferences. AGOA preferences may spur U.S. firms to source products from the region that are subject to high U.S. duty rates, such as manmade-fiber and wool apparel, particularly if the provision allowing for the use of third-country fabrics is extended beyond 2004. Some sourcing of basic garments made in the region from local fabrics, such as pants and knit tops, may also continue.	**Summary:** Products - Produces basic, rather than fashion apparel. Most manufacturers do not offer full-package services. Many firms have limited capacity to offer large volumes that may be required by U.S. firms looking to consolidate sourcing following quota removal. Infrastructure - Infrastructure and logistics inferior to those in other regions of the world. Shipping time longer than that from East Asia.
	Kenya: Share of U.S. apparel imports is likely to decline.	**Kenya:** Business climate - Personal safety an issue for sourcing from country.
	Lesotho: Share of U.S. apparel imports is likely to decline.	**Lesotho:** Inputs - No domestic yarn or fabric supply. Planned investment in new yarn and knit fabric production capacity.
	Madagascar: Share of U.S. apparel imports is likely to decline.	**Madagascar:** Business climate - Political unrest in 2001 and 2002 resulted in large disinvestment in the industry. Government is trying to restart the industry, but future prospects are uncertain.

Table 3-4--Continued
Summary of anticipated effects of quota elimination in 2005 and key competitive factors, by selected regions and countries

Region or country	Anticipated effects of quota removal	Key competitive factors
	Mauritius: Share of U.S. apparel imports is likely to decline.	**Mauritius:** Labor- High labor costs owing to shortage of labor. Competition for workers from high-tech sectors. Inputs - Shortage of cotton yarn production for knit apparel. Planned investment in new yarn spinning capacity.
	South Africa: Share of U.S. apparel imports is likely to decline.	**South Africa:** Labor - Relatively high labor costs. Inputs - Domestic supply of yarns and fabrics. Only SSA country producing synthetic filament yarn.

Source: The Commission assessment is based on interviews with representatives of U.S. apparel and textile companies, U.S. retailers, foreign textile and apparel producers and investors, and foreign government officials; a review of the literature; and testimony presented to the Commission at the public hearing and in written statements.

To reduce the risk of sourcing from only one country, U.S. importers also plan to expand trade relationships with other low-cost countries as alternatives to China, particularly with India, which also, like China, has a very large manufacturing base to produce a wide range of textile and apparel goods at competitive prices and a large supply of relatively low-cost, skilled labor. One or two other low-cost exporting countries in South Asia–Bangladesh or Pakistan–are expected to emerge as major suppliers of a narrower but still significant range of goods, such as mass-produced basic knit cotton tops and woven cotton shirts and pants (Bangladesh) or men's and boys' cotton apparel (Pakistan). Some firms indicated they also would consider CBERA countries, particularly those located in Central America, as a major source of supply if a Central American or western hemisphere free-trade agreement is negotiated that permits the use of regional (e.g., Mexican) fabrics or third-country (e.g., Asian) fabrics. In the ASEAN region, the only countries considered competitive as major alternate suppliers to China or India are Vietnam and, to a lesser extent, Indonesia. Although both countries have an abundant supply of low-cost labor, Vietnam will not be eligible for quota elimination until it becomes a WTO member, while Indonesia is considered somewhat risky because of its political and social unrest.

There are likely to be exceptions to the overall trends, especially at the firm level, reflecting the importance of longstanding relationships that U.S. apparel companies and retailers have with foreign suppliers, and the efficiency, flexibility, and experience of foreign suppliers in producing certain articles. In addition, although many countries are likely to see their share of the U.S. market decline, a large number of them may become major "second-tier" suppliers to U.S. apparel companies and retailers for niche goods or services. As U.S. firms seek to balance cost, flexibility, speed, and risk in their sourcing strategies, they likely will look to the second-tier suppliers to meet the needs that are not met by the first-tier suppliers. For example, Mexico, currently a major supplier to some U.S. companies, is expected to decline in importance; however, it may still remain a significant supplier of some basic garments, particularly 5-pocket denim jeans, for which it is considered cost competitive. Regardless of the outcome of regional free-trade negotiations, the production of certain goods is likely to remain in the CBERA region and Mexico to service U.S. buyers' quick turnaround or mid-season order requirements. For quick-turn business, CBERA countries and Mexico primarily are used for replenishment of basics, particularly garments offered in a wide range of sizes, such as men's dress shirts and pants. Quick-turn orders sometimes also are needed for fashion goods, when retailers are "chasing" the latest trends, styles, or colors. Turkey is considered a capable supplier for quick-turn business. Industry sources believe that Colombia has the potential to become a source for quick-turn apparel once it resolves concerns about personal safety and the security of merchandise shipped into and out of the country. Firms also are looking for low-cost suppliers that have preferential access to the U.S. market to help contain costs for articles subject to relatively high duty rates.

China

China is the world's largest producer and exporter of textiles and apparel and it has invested in more spinning and weaving equipment than any other country during the last 5 years. Moreover, China's huge supply of inexpensive labor and skilled sewers, coupled with access to indigenous raw materials, has enabled the Chinese textile and apparel industries to remain highly price competitive and attract foreign direct investment (FDI) in facilities and technologies. The industries also are considered to have efficient management and the technical know-how to produce virtually any textile or apparel article. For U.S. retailers, buying more from China will also allow them to take advantage of the existing infrastructure and logistics they have in place there for buying and shipping non-textile products (e.g., housewares and toys), in addition to textiles and apparel.[11] Trade data reveal that China's share of the U.S. market has increased markedly in products for which quota restrictions have already been removed (table 3-2). Several retailers indicated that they have shifted sourcing of these products to China from such countries as the Philippines, Thailand, and Malaysia.

However, most firms indicated that the uncertainty of whether or not safeguard actions could be placed on U.S. imports from China likely will temper the amount of sourcing that firms dedicate to China, at least in the early years following quota elimination. To reduce the risk of sourcing from only one country, U.S. importers also plan to expand trade relationships with other low-cost countries as alternatives to China, particularly with India, which also has a very large manufacturing base to produce a wide range of textiles and apparel at competitive prices.

Prices are expected to decline following quota elimination. Several U.S. firms estimated that prices might fall by as much as *** percent; another said China likely will be the price leader in a post-quota world that other countries will need to match or beat. U.S. importers are concerned that the decline in prices, combined with stiff competition among supplying countries, could result in antidumping actions, particularly against China and possibly against India; however, it is not clear who in the U.S. apparel sector might initiate such actions.

Business Climate, Infrastructure, and Proximity and Access to Markets

U.S. apparel companies and retailers reportedly are finding China to be a much more business friendly place from which to source textiles and apparel as a result of changes China has made as part of joining the WTO. U.S. firms increasingly work directly with manufacturers in China rather than through buying agents, as was the common practice in the past. Industry sources described much of the Chinese industry as very business savvy and capable of meeting the needs of western buyers.

U.S. imports of most textile and apparel articles from China are highly constrained by quotas. In November 1999, the United States signed a market-access agreement with China that became part of China's WTO accession package and obligated the United States and other major import markets, such as the EU, to eliminate quotas on imports of Chinese textile and apparel as of January 1, 2005, the same date as that for other WTO members. However, the agreement allows for the United States and other importing countries to apply selective safeguards (quotas) on imports of textiles and apparel from China for 4 additional years beyond the termination of the textile and apparel quotas for WTO members–that is, from January 1, 2005 to December 31, 2008. The agreement also states that no textile-specific safeguards established during the 4-year period will remain in effect beyond 1 year without reapplication, unless both countries agree.

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[11] Retailers indicated they are able to negotiate better shipping rates with large volume loads. In addition, retailers will generally establish a buying office in countries with which they do a lot of business.

U.S. industry representatives noted that China, unlike India, its major competitor, is investing heavily in infrastructure throughout the country, including a major highway system linking western China with the more developed eastern part of the country. In terms of location, industry sources indicate that shipping times from China to the West Coast of the United States are relatively fast, particularly compared with many of the ASEAN countries or India. China is also investing in deep water port facilities that will further shorten shipping times.

Labor and Management

China has a very large pool of inexpensive skilled labor, and its management is considered very effective and relatively low cost. In the apparel sector, the workers are considered to have very good sewing skills. In fact, several U.S. importers said there is no garment that they would not make in China. China currently has high-level specialists that can be hired at low cost, which saves a firm from sending its own specialist to oversee production. One trading company representative asserted that it has even hired Chinese supervisors in its overseas (non-China) facilities.

China's abundant supply of labor helps keep wages relatively low. Those low wages, which are especially important for the labor-intensive garment industry, have led many companies to move or to plan to move at least some of their production to China in order to take advantage of abundant cheap and productive labor. Some retailers noted that because of rapid economic development, labor costs have started to rise in Chinese textile and apparel factories, especially in the eastern and coastal special economic zones (SEZs). However, even though China does not have the lowest wages in the region, it is considered competitive in terms of per unit costs.

Raw-Material Inputs

Many industry representatives in Hong Kong, Korea, and Taiwan reported in effect, that "China has everything" and, thus, will be in a good position to compete. China has a competitive local supply of raw materials, including fibers, yarns, fabrics, and trim. Although China is currently importing cotton, as its domestic supply is insufficient to meet domestic demand, it has abundant supplies of other natural fibers such as ramie, silk, and angora rabbit hair, and the government is encouraging the production of these fibers.

China is the world's largest producer of manmade fibers, even though it still imports some fibers. China's shift in development policy toward a market-friendly approach has led to upgraded technology in manmade fiber production, as well as for the production of yarns and fabrics. Numerous firms interviewed by Commission staff believe that China is in the process of becoming a competitive fabric supplier, and in 1 or 2 years, China will catch up to Taiwan and Korea in the manmade-fiber sector.

Some inefficiency has been noted in Chinese state-owned enterprises (SOEs), especially in the cotton textile industries. However, there has been major restructuring and market-oriented policies have led to diversified ownership as well as product diversification. Although the SOEs still experience lower productivity rates than private firms and foreign-invested enterprises, they account for less than a quarter of the total gross output value of Chinese textile and apparel production.

According to a number of companies, the Chinese dyeing and printing sector lags behind the rest of the world in terms of equipment, technology, expertise, product innovation, variety, and research and development. For these reasons, some Chinese grey fabric is exported to Hong Kong or Korea for finishing before being reimported for manufacture in the Chinese apparel sector.

Level of Service Provided and Reliability of Supplier

According to industry representatives interviewed by Commission staff, one of China's advantages is that it can make virtually all types of textile and apparel products, from basics to fashion. At the lower end of the retail market, one firm is expecting the bulk of its commodity (or basic) business (which is very price sensitive) to go to China. At the higher end, another firm asserts that Chinese factories are very flexible and good at producing fashion garments. One firm indicated that China is likely to capture most of its fashion business. One trading firm indicated that it makes sense to make China its manufacturing center because so much of what the firm sells is already being made there.

Currently, most Chinese apparel exports are manufactured in response to orders received, often with samples and materials supplied by clients. China has few internationally recognized brand names and few experienced apparel designers.

Other East Asia (Hong Kong, Macau, Korea, and Taiwan)

The industries in Hong Kong and Macau are largely platforms for outward processing arrangements (OPAs) with China, whereby a certain amount of sewing takes place in Hong Kong or Macau to confer origin for trade purposes, while the remainder of the sewing and packaging takes place across the border in China, where labor costs are much lower. In table 3-2, U.S. imports from Hong Kong show a substantial decline for several products that were integrated into the GATT regime and became quota free in 2002. However, discussions with U.S. retailers and apparel suppliers indicate that at least some of this sourcing may stay in Macau and especially Hong Kong, until there is a better sense as to whether safeguards will be placed on U.S. imports from China.

Korea and Taiwan are major world suppliers of fabrics, benefiting from their large manmade fiber industries. Both countries have large spinning and weaving sectors, and despite rising labor costs, it is generally believed that they will remain competitive in the relatively capital-intensive production of synthetic fibers and fabrics. According to some retailers, the best yarns for knit-to-shape garments are made in Korea and Taiwan. Industry sources stated that apparel manufacturers worldwide likely will continue to use Taiwan and Korean fabrics.

A number of U.S. retailers noted that wage rates in Korea and Taiwan are relatively high, and that following quota elimination in 2005, they will be too high for producing most labor-intensive garments. Also, rapid development in high tech sectors means that traditional sectors like textiles and apparel have more difficulty attracting skilled labor. Taiwan has had to recruit some workers from other countries to help offset the chronic labor shortage. Although these economies have high labor costs compared with China's, their workers are considered highly skilled in making dress shirts, production of which is relatively automated compared with that of other garments. Industry officials indicated that some of this production may remain in these countries. Many firms believe that East Asian workers offer much better sewing skills than those in Latin America or sub-Saharan Africa. Korea and Taiwan are also known for having excellent plant managers. These labor and management skills, along with the relatively small, flexible production lines, favor the production of fashion garments. Industry sources indicated that they likely will continue to source some dresses, which require highly skilled sewers and flexible production lines.

South Asia (Bangladesh, India, Pakistan, and Sri Lanka)

U.S. apparel companies and retailers generally indicated that they will expand their sourcing in South Asia after quota removal in 2005. However, sourcing decisions will vary significantly among the four countries in the region, in line with each country's competitive strengths in textiles and apparel. Industry sources cited a plentiful supply of low cost labor as a primary reason for sourcing in all four countries.

India is regarded as a major alternative source to China once quotas are removed for apparel and made-up textile products. Retailers and apparel suppliers acknowledged that India is likely to remain competitive after quota removal because of its large, relatively low-cost labor force, a large domestic supply of fabrics, and the industry's ability to manufacture a wide range of products. Retailers described Indian firms as innovative, particularly in design functions. Poor infrastructure and an inefficient bureaucracy were cited as concerns, but not as factors that will necessarily determine investment and sourcing decisions. Pakistan provides a more limited range of products than India, but is considered a competitive supplier of cotton goods, particularly men's apparel, home textile products, and fabrics.

U.S. firms presented a mixed picture when discussing the future of textile and apparel production in Bangladesh and Sri Lanka. Some buyers are confident that both countries will continue to manufacture large volumes of low-end apparel for Western markets once quotas are removed; others believe that sourcing will decline in Bangladesh and Sri Lanka if local producers are unable to provide full-service packaging and local inputs, such as fabric and trim. Several firms indicated that Sri Lanka will probably continue to be competitive in the production of intimate apparel, even if the country loses business in some other segments of its apparel industry.

Business Climate, Infrastructure, and Proximity and Access to Markets

The governments of the South Asian countries are taking steps to enhance the competitiveness of their textile and apparel sectors. Most of these efforts focus on encouraging new investment in the private sector, eliminating certain trade barriers to expand exports, and promoting industry quality standards. Nevertheless, a number of firms expressed difficulties in working in India and indicated that the lack of transparency in legal requirements and complicated paperwork increase producer costs and often necessitate the use of a broker rather than dealing directly with the manufacturers, particularly when many small manufacturers are involved. U.S. retailers noted that India's bureaucratic red tape required to move inputs and produce goods in a timely matter has also affected the time-to-market process for Indian-made goods.

Some industry sources considered Pakistan's business climate more difficult than India's. Some U.S. retailers indicated that they refuse to purchase from private mills in Pakistan not funded by World Bank loans for fear that financing has come from drug-money profits. ***.

Industry sources also expressed concern about the personal safety of their staff when examining factories and testing products prior to shipment. To encourage sales, some Pakistani firms are setting up showrooms in Dubai and other sites in the region.

Firms had mixed views on the ease of doing business in Bangladesh and Sri Lanka. One U.S. firm indicated that it thought manufacturers in Bangladesh had a more western approach to business than those in Pakistan, while another indicated that it is more difficult to work in Bangladesh than in India. In response to industry concerns regarding child labor, Bangladesh reportedly is working to get its factories certified for international labor standards. Some industry sources had concerns about working in Sri Lanka, in part because of its recent history of civil unrest. However, others described Sri Lanka as having a favorable business environment, including a functioning rule of law, corporate executives educated in the United States and the United Kingdom, and the use of English as the language of business.

South Asian countries face many challenges in upgrading infrastructure to enhance the competitiveness of their textile and apparel sector. U.S. firms indicated that India has poor infrastructure, including no deep-water ports and an antiquated railroad network. Bangladesh's poor physical infrastructure is reportedly less of a concern to business because most apparel production is in Dhaka or port regions, both easily accessible to the sea. However, communication networks in Bangladesh are described as substandard, and infrastructure is characterized by poor roads, port congestion, and frequent power outages.[12] Industry sources also described Sri Lanka as having poor infrastructure, in part because of the damage inflicted during the long period of civil unrest. Shipping times from South Asia reportedly are significantly longer than those from East Asia. One industry source said it takes about 45 to 60 days to ship from India to the east coast of the United States.

South Asian governments are beginning to focus on increased market access for their textile and apparel products both inside and outside the region to spur economic growth. In the aftermath of the September 11 terrorist attacks, Pakistan obtained additional quota access to the U.S. market for certain apparel and expanded trade preferences and market access from the EU. Sri Lanka obtained and currently enjoys quota-free and reduced-duty access to the EU and reduced-duty access to India, as well as duty-free access to large Asian markets as a member of the South Asian Association for Regional Cooperation.[13] Bangladesh also benefits from duty-free and quota-free treatment in the EU and trade preferences extended by Canada and Norway.

Labor and Management

The textile and apparel sector is believed to be the largest source of manufacturing jobs in South Asia. Labor costs for textile and apparel production in the region are among the lowest in the world. However, South Asia's relatively low labor costs are partially offset by lower

[12] The World Bank estimated that Bangladesh loses about $1 billion annually because of power outages and unreliability of power supply. See U.S. Department of Energy, Energy Information Agency, *Country Analysis Brief: Bangladesh*, Feb. 2002, p. 2.

[13] In return for EU market access, Sri Lanka reduced duties to 5 percent for yarns and fibers and 10 percent for textile items from the EU. Certain articles are subject to a double-checking system of export and import licensing.

productivity levels. U.S. retailers interviewed by Commission staff indicate that productivity rates in India, Pakistan, and Bangladesh are about 20 to 25 percent below those in China.

India has a very large pool of skilled and unskilled workers employed on a 48-hour, 6-day work week. Indian firms reportedly also have well-educated management and technicians. Bangladesh suffers from low literacy levels, frequent labor unrest, and outdated technology. In general, the quality of management in Bangladesh's factories is considered poor, though one industry source indicated that some factories there have very good managers. Sri Lanka reportedly has low industrial labor productivity resulting from relatively high employee absenteeism and turnover, and strict labor standards lead to a shorter workday than that for India and Bangladesh. Nevertheless, one U.S. firm stated that Sri Lanka benefits from well-educated middle managers.

Raw-Material Inputs

India ranks among the world's largest producers of cotton, cotton yarn, and manmade fibers and filament yarns; it also has a large domestic fabric supply. However, with the exception of yarn spinning, an area of competitive strength for Indian firms, India's textile industry is highly fragmented. The weaving, dyeing, finishing, and processing segments are considered the weakest links. The textile and apparel sector in Bangladesh relies heavily on imports for its production inputs, including fibers, yarns, fabrics, and findings. The sector is cotton based, with most of the cotton fiber coming from India and the United States. Cotton fiber imports are expected to rise from their current levels through 2005, reflecting the addition of new spinning capacity, increased demand for cotton yarn, and the substitution of lower priced cotton for polyester fibers. In 2002, Bangladesh's textile industry reportedly had the capability to supply about 70 percent of its apparel industry's yarn needs for knitwear production (e.g., T-shirts) and 20 percent of its woven fabric needs for production of casual apparel such as shirts and pants.

The availability of domestic cotton in Pakistan has been an important factor in the development of its cotton textile sector: it is the world's fourth-largest producer of cotton after China, the United States, and India.[14] In addition, Pakistani companies have begun purchasing more high-quality cotton to create better cotton yarns and fabrics.[15] Pakistan has the third-largest installed capacity for spun yarn in the world, after China and India. U.S. retailers believe that Pakistani firms will remain competitive in unfinished cotton fabrics owing to large installed capacity, continued investments, and consistent quality.

Level of Service Provided and Reliability of Supplier

The size and quality of Indian textile production has made Indian suppliers a major source for both woven and knit products. Several industry sources noted that India produces good-quality home textiles and maintains a full range of knit and woven apparel. Indian firms are considered innovative with designs, and are capable of manufacturing a multitude of different styles. With its large supply of relatively low-cost labor, India is known for its

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[14] U.S. Department of Agriculture, FAS, *Cotton: World Markets and Trade*, Dec. 2002, table 1.
[15] "Pakistan Shifts to Quality Cotton Textiles," *World Textile News*, June 4, 2001, found at *http://www.emergingtextiles.com*, retrieved June 8, 2001.

capability to provide relatively labor-intensive embellishments to apparel and home textile products, such as hand embroidery.

Pakistan provides a more limited range of products than India but is considered a competitive supplier for such cotton goods as men's apparel, bed linens, and fabrics. Pakistan is generally considered a competitive producer of knit tops. Bangladesh is considered a competitive low-cost supplier for large quantities of basic apparel items, including knit and woven shirts. Sri Lanka has developed a reputation as a niche supplier of intimate apparel. In addition, one U.S. firm described Sri Lankan firms as market savvy, and competitive in garment finishing and product development.

Association of South East Asian Nations (ASEAN Countries)[16]

A number of U.S. apparel companies and retailers expressed concern about the competitive position of most ASEAN countries following quota elimination in 2005. For example, although Indonesia has a huge textile and apparel infrastructure, from raw materials to finished goods, it faces political and social instability. Some firms contended that Thailand is likely to remain competitive in a post-quota world, because of its sophisticated textile industry; however, other firms claimed that Thailand may decline in importance because its costs are relatively high and its product quality is not high enough to compensate. Malaysia is considered an even higher cost supplier, and given its focus on more advanced manufacturing sectors, it is likely to see its share of the U.S. and global textile and apparel market diminish in a post-quota world. A number of firms interviewed claimed that the recent rapid growth in Vietnam's apparel shipments to the United States largely reflected its low labor costs and absence of quotas. However, the United States and Vietnam recently reached a bilateral agreement that establishes quotas on U.S. imports of apparel from Vietnam; because Vietnam is not a WTO member, those quotas will not be lifted in 2005.[17]

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[16] Includes Brunei, Myanmar, Cambodia, Indonesia, Laos, Malaysia, Philippines, Singapore, Thailand, and Vietnam. In this report, the focus is on Indonesia, Malaysia, Philippines, and Thailand.

[17] Committee for the Implementation of Textile Agreements, "Establishment of Import Limits for Certain Cotton, Wool, and Man-Made Fiber Textiles and Textile Products Produced or Manufactured in the Socialist Republic of Vietnam," *Federal Register*, May 16, 2003 (68 F.R. 26575).

Business Climate, Infrastructure, and Proximity and Access to Markets

A number of political and policy issues have been identified as increasing costs or exacerbating uncertainty regarding supply in some ASEAN countries. Many firms have raised concerns about political and social instability in Indonesia; for example, the concentration of wealth in the country's Chinese population has been cited as triggering social and racial tensions there. Similarly, FDI has declined significantly owing to concerns about the judicial system's ability to protect an investor's capital. In the Philippines, domestic security concerns are an issue. Some firms have complained that corruption in some countries, including Cambodia, has led to substantial cost increases.

The geographical location of some ASEAN countries was presented as a disadvantage. For instance, according to an industry source, shipping times from ASEAN countries to the west coast of the United States average 45 days. Cargo shipping from Indonesia to the United States reportedly takes about 55 days (with a transit in Singapore), while shipping from the Philippines can take as little as 20 days (through Taiwan). One firm has indicated that it takes 2 days to ship from Vietnam to Taiwan, and from there 12 days to the U.S. west coast.

Labor and Management

Industry representatives generally did not consider the ASEAN countries, particularly Thailand, the Philippines, and Malaysia, to be very competitive in terms of labor costs or labor abundance. According to one industry source, manufacturing costs in the Philippines are 11 cents per minute, compared with 5 cents per minute in China. In Malaysia, local labor is scarce and expensive, prompting some firms to bring in foreign workers (from Indonesia and Pakistan), a costly approach. Thailand faces a similar problem and has relatively high labor rates. The relatively high cost of labor has caused more than one firm to move production of babies' garments from Malaysia and Thailand to China following quota elimination for China in 2002.

Some ASEAN countries do have low labor costs. According to many retailers and apparel suppliers, Indonesia has a large labor force and much lower costs than the Philippines and Thailand. Similarly, although Vietnamese workers are not necessarily as productive as workers in China, their costs are low enough that Vietnam is considered by a number of companies to be competitive.

Skill levels and productivity vary greatly among ASEAN countries. According to one retailer, Cambodia is 40 percent less productive than China (manufacturing productivity) and yet their manufacturing costs are similar (5 cents per minute). The existence of an English-speaking, skilled and semiskilled workforce is considered an advantage for the Philippines. Thailand has skilled sewers and small production lines that favor the production of fashion apparel and embellished garments.

Raw-Material Inputs

ASEAN countries have ready access to raw materials in the region. However, ASEAN countries having a fabric industry are believed to be more competitive than those without one. For instance, the Philippines is at a disadvantage because it has no locally produced raw materials, and thus lead times are longer when sourcing from the country (though one industry source indicated that fabric can be shipped from Taiwan to the Philippines in as little as 2 days). Customs delays for importing fabrics into the Philippines, combined with high port and shipping costs, can greatly extend lead times and total costs.

Lead times are shorter in Thailand than in the Philippines because of the availability of locally produced materials, reflecting the vertically integrated structure of the textile and apparel sector in Thailand. A retailer asserted that it would consider Thailand second to China in a post-quota world, simply because it has a competitive textile industry. On the other hand, Thailand's strong reliance on imported high-quality raw materials has been considered a competitive weakness. Malaysia and Indonesia also have vertically integrated textile and apparel sectors through all phases of production ranging from yarn to apparel. Indonesia is known for its quality fabrics and is said to be competitive in both cotton and polyester goods.

Level of Service Provided and Reliability of Supplier

The quality of production in Thailand and the Philippines is considered good, but the cost is relatively high compared with that in China. Thailand, in particular, is considered a capable supplier of fashion garments. U.S. apparel companies and retailers noted that they produce high-volume basic tops and bottoms with few style changes in Cambodia and Vietnam, but it is difficult to produce high-end or fashion goods in either of these countries.

Mexico

U.S. apparel companies and retailers interviewed by Commission staff indicated that they have reduced or eliminated their sourcing in Mexico, or plan to reduce their sourcing when quotas are removed, because of a number of factors that make Mexico less competitive than other suppliers. Industry sources cited rising labor costs, inconsistent quality, and problems with the reliability of production as major reasons for moving sourcing, along with concerns for the security of shipments during transit. Most products being sewed in Mexico are basics, particularly 5-pocket denim jeans and knit shirts. Industry sources expressed concern that their Mexican suppliers were not able to diversify into fashion denim jeans. Industry sources also pointed to the limited availability of full-package services as an impediment to doing business in Mexico.

Business Climate, Infrastructure, and Proximity and Access to Markets

Proximity and preferential access to the U.S. market are Mexico's major competitive advantages as a source of supply for apparel and textile products. Companies indicated that the duty-free and quota-free preferences are what originally attracted U.S. companies to Mexico for sourcing purposes, but that Mexico has lost some of its competitive advantage and the administrative burdens of doing business in Mexico have not improved. U.S. firms also indicated that they must devote considerable resources to dealing with U.S. Customs and administrative matters when importing from Mexico, adding to the total cost of the product.

The time required to ship goods to the United States from Mexico's interior, where a substantial amount of Mexico's textiles and apparel are now made, is sometimes longer than the shipping time from the Caribbean because goods move by truck.[18] Security issues, particularly as they relate to truck hijackings and container security (to prevent problems with drug smuggling) are issues many firms listed as disincentives to sourcing from Mexico. According to Mexican industry sources, up to 5 percent of the cost of apparel from Mexico can be attributed to shipments being stolen or security measures taken to prevent such theft.[19] An Asian apparel supplier that has invested in Mexico indicated that Mexico is a difficult country in which to produce garments, but proximity to the U.S. market has made such production worthwhile.

Labor and Management

The cost of labor in Mexico is higher than that for most of the Caribbean countries, and much higher than that for China or India. U.S. firms indicated that labor productivity or efficiency is much lower in Mexico than in Asia. Several firms listed rising labor costs, which are partly associated with the appreciation of the Mexican peso, as one of the reasons they are shifting production out of Mexico to other regions, including to Central America and Africa. According to one retailer, Mexican factories do not have effective middle management–the decisionmaking power rests at the top, so it can be difficult to communicate with the factory if the top manager is away. Another concern expressed by an Asian apparel supplier is high absenteeism among Mexican workers.

Raw-Material Inputs

Mexico has a domestic textile industry producing both knitted and woven fabrics. However, Mexican fabrics tend to be priced higher than fabric from Asia, but lower than fabric from the United States.[20] Mexico specializes in basic fabrics,[21] and is reportedly the world's third-largest producer of denim.[22] However, according to the Mexican Apparel Chamber, fashion trends are moving toward the production of more fashion garments, using fabrics that the Mexican industry does not produce. While Mexico is considered competitive in the production of denim and certain wool fabrics, it is not considered competitive in the production of many other fabrics, particularly manmade-fiber fabrics. Under the NAFTA, the United States has tariff preference levels (TPLs) with Mexico that permit a certain volume of U.S. apparel imports from Mexico to consist of non-NAFTA fabrics. Mexico has fully utilized these TPLs over the last 5 years.

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[18] Some apparel is still made in the border region between the United States and Mexico, which reportedly has much faster transport times, and new apparel production is increasingly moving into the Yucatan Peninsula region, from which apparel is generally transported by ship.

[19] Representative of the Textile Industry Chamber, Mexico City, interview by USITC staff, Feb. 10, 2003.

[20] Representatives of the Fiber Articles and Synthetics Section of the National Association of the Chemicals Industry, Mexico City, interview by USITC staff, Feb. 10, 2003, and representative of the Textile and Apparel Industry Association, Guatemala City, interview by USITC staff, Feb. 26, 2003.

[21] Representative of the Apparel Chamber in Mexico, Mexico City, interview by USITC staff, Feb. 10, 2003.

[22] Representatives of the Fiber Articles and Synthetics Section of the National Association of the Chemicals Industry, Mexico City, interview by USITC staff, Feb. 10, 2003.

Level of Service Provided and Reliability of Supplier

Companies interviewed by the Commission said that most of the Mexican factories are able to handle production of only basic, commodity goods that they can produce in large volumes. One company interviewed by Commission staff indicated it pulled some of its business out of Mexico because of a lack of flexibility on the part of manufacturers to switch production to more fashion-oriented jeans that are currently in style. Only a few large apparel firms in Mexico are vertically integrated. Most of the Mexican firms continue to focus on basic apparel assembly rather than providing the full-package service requested by U.S. importers.

CBERA Region

According to U.S. apparel companies and retailers, the major competitive advantages of sourcing apparel from the CBERA region are its quota-free access and proximity to the U.S. market, which makes shipping to the U.S. market faster and relatively less expensive than it is from Asia. U.S. apparel imports from CBERA countries are concentrated in product categories for which imports from lower cost Asian suppliers are highly constrained by quotas. The CBERA region mostly supplies high-volume commodity garments that have reasonably predictable consumer demand, particularly basic knit shirts, pants, underwear, and nightwear. The production of these basic goods involves large and standardized runs, relatively simple sewing operations, and few styling changes, which together help offset the higher cost of labor in the region vis-a-vis Asia.

Several large U.S. apparel suppliers indicated that the CBERA countries have been an integral part of their sourcing strategy; however, most industry sources indicated that the benefits of the CBTPA preferences are becoming less attractive as production costs in the region increase vis a vis those in Asia, particularly when combined with the higher costs of using U.S. yarns and fabrics. Most U.S. apparel companies and retailers indicated that their decisions regarding sourcing from the CBERA region in 2005 will depend on the outcome of negotiations on the proposed U.S.- Central American Free Trade Agreement (CAFTA) and/or Free Trade Area of the Americas (FTAA), and what type of provisions are put in place regarding the use of non-U.S. fabrics. Among the CBERA countries considered most promising for sourcing are Honduras, Guatemala, the Dominican Republic, El Salvador, and Nicaragua. High costs in Costa Rica reportedly have priced the country out of the market for many U.S. importers, and the Government of Costa Rica is now trying to attract other, nonapparel investment to the country to utilize its highly educated labor force.

Business Climate, Infrastructure, and Proximity and Access to Markets

Importers reported shipping times from Central America to the United States ranging from 2 to 7 days, depending on the country from which they ship and the port of entry. One U.S. firm said it sources large quantities of apparel from the region because the short lead times allow it to adjust orders according to market demand.

U.S. firms indicated that they have developed strategic relationships with their suppliers in the CBERA region, and many import garments under the CBTPA provisions using either

U.S. or regional fabrics.[23] In 2002, 79 percent of the value of U.S. apparel imports from CBTPA-eligible countries entered under preferential duty provisions, though the shares for individual countries varied considerably. For example, 85 percent of imports from Honduras qualified for preferential access in 2002, while only 32 percent from Nicaragua and 49 percent from Guatemala qualified. Nevertheless, industry sources indicated that CBTPA requirements are complex and add an additional layer of administrative burden, which in turn adds to the cost of the product. According to industry sources, the CBTPA yarn and fabric provisions also limit firms' flexibility in their supply chains. A number of firms indicated that they have already reduced apparel sourcing from the region or are in the process of doing so because of cost considerations and other disruptions to supply resulting from CBTPA regulations.

U.S. industry sources cited safety and security concerns in doing business in Jamaica and Haiti. Drug smuggling in Jamaica, Haiti, and Guatemala was also cited as a concern.

Labor and Management

Labor costs in CBERA countries are lower than those in Mexico, but higher than those in most apparel exporting countries in Asia. As such, U.S. apparel imports from CBERA countries are concentrated in products having low labor content, particularly basic knit tops, pants, shorts, underwear, and nightwear. A large U.S. retailer indicated that it has found labor productivity in CBERA countries to be about 50 percent of that in China. Labor costs reportedly have been increasing in El Salvador and especially in Guatemala, making them less competitive from a cost perspective. Some Dominican Republic firms have reportedly shifted some assembly operations to Haiti, which has lower labor costs.

U.S. apparel companies and retailers indicated that they generally do not source fashion apparel from the CBERA region or garments that require many delicate sewing operations. One large U.S. apparel supplier indicated that most factories in the region do not have skill sets, management, or production lines to handle fashion goods or complex sewing operations. This supplier also indicated that middle management is one of the biggest challenges of working in the region.

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[23] See the "overview" in appendix I (CBERA countries) for information on CBTPA preferences.

Raw-Material Inputs

Most fabrics used in apparel production in the CBTPA countries are imported from either the United States, Mexico, or Asia. The Caribbean countries do not produce woven fabrics (except for some limited amounts believed to be for local consumption). The region does have a small knit fabric industry whose development was facilitated by the regional fabric provision under the CBTPA. Honduras has several integrated knit apparel facilities that produce fabric as well as finished garments, and in 2002, it was the largest supplier of regional knit fabric for U.S. apparel imports from the region qualifying for CBTPA benefits under the regional fabric provision. Nevertheless, U.S. imports of apparel using regional fabrics accounted for no more than 5 percent of total apparel imports from the region in 2002. In the same year, the TPL for goods using regional fabrics was fully utilized for T-shirts, but the TPL for other knit apparel, which accounted for most of the regional fabric provision, had a utilization rate of 51 percent.[24] A U.S. firm interviewed by Commission staff indicated that regional fabrics meet only one-half of its sourcing needs from the region.

One firm indicated that it rarely uses U.S. fabric in clothing produced in the region, except for some manmade-fiber products that have higher duty rates than cotton products. Several retailers and apparel suppliers indicated that they use some regional knit fabrics and forgo the preferential duty treatment under the CBTPA for the remainder, because U.S. fabrics cost 20 to 40 percent more than Asian fabrics. According to one retailer, apparel suppliers that sell under branded labels can charge a premium for their product and so can afford to pay more for their raw materials and are more likely to use U.S. fabrics than retailers sourcing for private label programs. Commission staff interviews with certain U.S. branded apparel suppliers indicated that they use U.S. fabric in their production in the region.

Level of Service Provided and Reliability of Supplier

According to companies interviewed by Commission staff, CBERA apparel factories generally are set up specifically to produce basic garments in long and standardized runs, rather than smaller and more flexible runs that are typical for making fashion apparel. To make fashion goods in the region would require a higher level of labor and managerial skills than currently exists in most factories and a redesign of production lines to accommodate the shorter, flexible runs. Moreover, while CBERA firms recognize the growing importance of offering full-package services to U.S. apparel companies and retailers, few currently offer it.[25] Among the firms offering full-package production in the region are some of the Asian investors that have links back to their parent companies in Korea or Taiwan. In the Dominican Republic, at least some apparel firms in the free zones reportedly offer full-package services. Honduras also has some companies capable of offering full-package

[24] TPL data were compiled from data of the U.S. Department of Commerce, Office of Textiles and Apparel, found at *http://otexa.ita.doc.gov/agoa-cbtpa/agoa-cbtpa_2002.htm*, retrieved Apr. 8, 2003.

[25] Full package programs in the CBERA region generally refer to services ranging from procurement of materials to cutting and sewing, and to finishing and packaging of the final products. In the Far East, an established infrastructure exists to provide full package imports to U.S. buyers, including product development, fabric sourcing and cutting, garment sewing, packaging, quality control, trade financing, and logistics arrangements.

production. Korean and Taiwanese producers have established spinning and knitting facilities in Honduras to supply apparel manufacturers in Central America.[26]

Andean Countries

The Andean countries (Bolivia, Colombia, Ecuador, and Peru) are a small source of U.S. imports of textiles and apparel, which became eligible for duty-free treatment for the first time with the enactment of the Andean Trade Promotion and Drug Eradication Act (ATPDEA, Division D of the Trade Act of 2002). Peru and Colombia, which account for most of U.S. textile and apparel imports from the Andean region, produce high-quality apparel products, such as combed cotton knit tops (Peru) and tailored clothing, fashion apparel, and jeans (Colombia). Both countries are considered cost competitive by some importers, in large part because quotas increase the cost of sourcing garments from certain lower cost producing countries. The allowance for regional yarns and fabrics in the ATPDEA is considered a factor that will help the region to compete with other suppliers, though some firms question whether the region will be able to be cost competitive once the quotas are removed. Some suppliers thought Peru may be able to compete in the supply of high-end knit shirts, and Colombia might be a good source for retailers and apparel suppliers looking to do quick-turn business, for which they might be willing to pay a premium.

Business Climate, Infrastructure, and Proximity and Access to Markets

During the past decade, the Andean countries have implemented numerous government incentives (substantial reduction of tariffs, the elimination of most import-license requirements, and simplified import and export procedures) to open their economies and attract foreign investment. Under the ATPDEA, qualifying textile and apparel articles have duty-free and quota-free access to the U.S. market. The trade preferences are limited to apparel made of U.S. fabric and to specified quantities of apparel made from regional fabrics (see the "overview" in appendix J, Andean countries, for information on the trade preferences).

Colombia has ports on both its coasts, but transportation inside the country can be difficult. One industry source noted that Colombia has a well-developed airfreight industry for its flower sector that could be used to transport fashion items that are needed on a quick-turn basis. However, one apparel supplier pointed out that it is difficult to ship fashion garments on hangers by air. Safety and security for both personnel and shipments are always a concern for importers. ***. Peru has problems with its infrastructure, which was severely damaged during the disruptive weather patterns of El Nino in 1997-98. In addition, its shipping and transportation costs reportedly are higher than those of its regional competitors.

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[26] Representative of textile producer, San Pedro Sula, Honduras, interview by USITC staff, Feb. 21, 2003.

Labor and Management

Colombia has an ample supply of highly skilled textile and apparel workers. Peru reportedly has an abundant labor force, but a shortage of skilled workers. From a cost perspective, one firm indicated its apparel vendor in Colombia is able to match China's prices. However, it indicated that once the quotas are removed (and the associated quota costs), its Colombia supplier may not be price competitive with China. Another firm indicated that Colombia is slightly more expensive than the Central American countries, but the Colombian workers have excellent needlework skills.

Raw-Material Inputs

Both Colombia and Peru have a local supply of fabrics for their domestic apparel industries. Peru's fabric capabilities are concentrated in knit fabric production, particularly cotton; it has developed a reputation for its ability to make high-quality cotton knit fabrics using long-staple cotton. One U.S. industry source said Peru also is competitive in polyester knit fabrics. Colombia's textile industry has vertically integrated firms that make a wide variety of cotton, manmade-fiber, and wool woven fabrics, as well as knit fabrics for use by its apparel sector.

Level of Service Provided and Reliability of Supplier

Colombia is an established supplier of tailored goods, jeans, and other sportswear. It is also recognized as a viable, though perhaps more expensive, alternative to Asian suppliers for fashion items, particularly for quick-turn items. By contrast, Peru supplies both knit and woven products to the U.S. market; it is known for its high-quality pima cotton knit tops. In an interview with Commission staff, a representative of the Peruvian government indicated that the high-end knit shirts will likely be the niche in which its industry will be most equipped to compete once quotas are removed, but he expressed some concern about the rest of the industry, including that which produces less expensive cotton T-shirts.[27]

Turkey and Egypt

Several U.S. retailers and apparel suppliers indicated that Turkey and Egypt would be more attractive suppliers from a cost standpoint if they had free-trade agreements with the United States. A few firms indicated that in the absence of a free-trade agreement they are likely to continue or increase their purchases of apparel from Turkey; other companies indicated that it probably would not be a significant supplier for them. However, Turkey is a member of the EU Customs Union and may continue to be a source of supply to that market, which accounted for nearly two-thirds of the value of Turkey's textile and apparel exports in 2001. Similarly, most U.S. firms indicated Egypt would decline in importance as a supplier to the U.S. market. However, at least one large retailer indicated that Egypt is likely to do well in a post-quota environment, and another large retailer stated that it will likely continue to source some products from Egypt because of its good relationship with the manufacturer and the fact that the products they purchase are competitive with other suppliers from a cost and quality standpoint.

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[27] Counselor, Embassy of Peru, interview by USITC staff, Washington, DC, Jan. 8, 2003.

A few retailers indicated that they are likely continue to source from Turkey after 2005. The Turkish workforce is flexible and highly skilled, even though labor costs are relatively high compared with those in China and India. Turkey also has an integrated and diversified textile and apparel sector, active in every segment of the supply chain, particularly cotton manufacturing. One retailer thinks that Turkey is and will remain competitive in cotton fabrics after 2005. According to industry sources, the Turkish industry is also skilled in making tailored clothing and has a good reputation for manufacturing apparel on a fast turnaround basis. However, another industry source indicated that the quality of apparel manufactured in Turkey is somewhat lower than that of similar goods from Hong Kong and China, and somewhat higher in price. Turkey caters mainly to the EU market, whose customers reportedly are demanding from the delivery standpoint, but are not as concerned with quality. According to industry sources, shipping time from Turkey to the United States is comparable with that from East Asia, at about 14 days.

Egypt has a relatively abundant labor supply, but its labor costs are higher than that for China. Egypt also has a well-established textile industry based on its production of high-quality cotton. However, owing to price floors set by the Government of Egypt, Egyptian cotton is relatively expensive, forcing downstream producers to import yarns and fabrics. According to some producers, imported inputs generally face high tariffs, but some firms are participating in a duty drawback program for exported final products. The textile sector in Egypt is largely under public-sector ownership and is characterized by excess employment, outdated technology, and relatively low productivity.

Israel and Jordan

Industry sources expressed uncertainty over the future of sourcing garments in Israel and Jordan. On the one hand, Israel and Jordan have preferential access–with advantageous rules of origin under free-trade agreements–to major import markets. On the other hand, U.S. apparel companies and retailers expressed concern about political instability and security matters in the region, which have greatly affected reliability of supply and inhibited the ability of firms to make long-term sourcing decisions and FDI in the region. Generally, U.S. firms indicated that any sourcing from Jordan is likely to be in apparel items that would normally be subject to high rates of duty, such as synthetic fleece tops and wool apparel. Given its high labor costs, the Israeli apparel sector tends to concentrate on the niche and high-end market segments. One firm told Commission staff that Israel is likely to remain competitive in those segments following 2005.

Both Israel and Jordan have free-trade agreements with the United States. In addition, their textile and apparel sectors have been significantly affected by the 1998 U.S. legislation on qualified industrial zones (QIZs), which allows U.S. imports of qualifying goods made in designated QIZs to enter free of duty and quota. For example, several firms reported that they buy synthetic fleece garments that are made in QIZs in Jordan from Asian fabrics, using the required minimum amount of content from Israel and enter the goods free of duty and quota into the United States (thereby avoiding payment of about 30 percent normal trade relations tariff rate). Shipping times from the region to the United States are also considered advantageous, with average shipping times from Israel (and Jordan via Israel) of about 2 weeks, which is better than that from many Asian countries.

Although Jordan and Israel are linked in terms of the QIZ program, they differ in terms of their cost competitiveness. Jordan has low manufacturing costs because of low wages, no income taxes, and inexpensive rents and electricity. Israel has high labor costs, which have pushed domestic firms to move production to more cost-competitive countries. Israel has a highly educated and trained workforce and it has been noted that high production costs in Israel are partially offset by the use of advanced technology and high product quality. The Israeli industry is highly automated, which keeps it competitive, and has a strong reputation for good service and fast turnaround.

The apparel industry in Jordan consists largely of assembly operations; lack of access to water prevents the development of a textile industry there. However, it has the advantage of being close to major regional fabric suppliers, including Egypt, Turkey, Israel, and Pakistan.

Sub-Saharan Africa

According to industry sources, sub-Saharan Africa (SSA) is not a particularly low-cost area for production of textiles and apparel, given the labor costs, low productivity, long lead times, and high cost of other inputs compared with those in Asia. Most companies located their production in SSA because of quotas on other suppliers. These quotas, combined with duty-free, quota-free access to the EU and, since October 2000, to the U.S. market, has led to increasing exports of mainly apparel items from SSA. Most companies interviewed indicated that because of the importance of quotas, it will be difficult for SSA to compete in a quota-free world. They indicated that EU and AGOA preferences will not be enough to keep the industry competitive except in the area of manmade-fiber and wool apparel, where SSA is competitive and U.S. duties are high. A number of SSA companies reported they are already losing sales in the EU market to countries such as Bangladesh, even with EU quotas in place. Most SSA firms view vertical integration as the means of survival in a quota-free world.

Business Climate, Infrastructure, and Proximity and Access to Markets

The political and business environment in the major SSA countries producing textiles and apparel is generally considered safe and secure. However, U.S. retailers have indicated that they will not send staff to countries where terrorism may be an issue, and this may affect countries such as Kenya. A benefit of AGOA is that the beneficiary SSA countries have had increased technical assistance and contact with U.S. Government agencies and companies. SSA countries exporting to the United States under AGOA have had to improve customs procedures and transparency, including adoption of procedures to prevent unlawful transshipments and the use of counterfeit documents. Many companies operating in the region believe that these changes have improved the business environment for textile and apparel exports.[28] A setback in SSA's attempts to improve the business environment in textiles and apparel occurred in Madagascar in 2002, when many foreign-owned textile and apparel companies pulled out of the country because of political unrest and refusal by the

[28] Indeed, one representative of a major company in South Africa noted that one of the big benefits of the AGOA was the technical assistance provided by the U.S. Customs Service in improving customs procedures in that country, particularly regarding the issue of under invoicing. Representative of textile/apparel company, interview by USITC staff in Durban, South Africa, Feb. 27, 2003.

Government of Madagascar to remit value-added taxes owed to businesses. Although the current government is attempting to restart the industry, to the extent that SSA countries experience the types of political problems, SSA will be at a disadvantage to other countries.

The United States and the EU provide preferential market access to qualifying textile and apparel articles from eligible SSA countries. Under the Cotonou Agreement, the EU grants duty-free and quota- free access to textile and apparel imports from African, Caribbean, and Pacific (ACP) countries, excluding South Africa,[29] subject to the use of ACP fabric with a double transformation rule.[30] In January 2000, the EU negotiated the EU-South Africa Trade, Development and Cooperation Agreement (TDCA) with South Africa under which the EU agreed to phase down its duties on textiles and apparel from South Africa over 6 years, while South Africa will phase down its tariffs on EU textiles and apparel to 50 percent of the MFN rate over 8 years.[31] The United States extends duty-free and quota free access to apparel from eligible SSA countries, including South Africa, under AGOA, which is described in more detail in appendix K of this report.

Companies in SSA indicated that both U.S. incentives under AGOA and the restrictiveness of U.S. quotas on imports of textiles and apparel from non-SSA suppliers have provided a significant impetus for expanded exports to the United States. However, most companies pointed out that the quotas on non-SSA suppliers were the most important policies making it economical to locate textile and apparel production in SSA and to export. Many companies indicated that retailers were increasing their purchases of apparel from SSA under AGOA because they do not have to pay duty, but without quotas on non-SSA suppliers, the absence of duties likely would not retain SSA's competitiveness, except in cases where U.S. duties are relatively high.

The importance of the U.S. market to SSA was stressed by a number of companies. These representatives noted that growth in EU imports of textiles and apparel from non-SSA suppliers, particularly Bangladesh, under the Everything But Arms initiative has made it difficult to compete in the EU market. The companies noted that the implementation of AGOA in 2000 served to provide a new outlet for SSA apparel exports at about the time export sales to the EU were starting to slump.

SSA has a number of disadvantages in terms of logistics and infrastructure. Buyers and companies in Mauritius cited the long shipping time to the U.S. market as a significant disadvantage. For example, one buyer in Mauritius noted that it can take up to 43 days to ship apparel to the U.S. market, (which travels via Durban and Capetown, South Africa). Long shipping times affect not only transportation to the final market, but also the time required to complete an order, because many inputs, including fabrics and yarns, have to be imported.

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[29] Although South Africa acceded to the Lome Convention as an ACP country, it was denied the trade preference benefits in favor of an FTA with the EU.

[30] Under the double transformation rule of the Cotonou Agreement, the fabric must be made in an ACP beneficiary country, and the fabric must be transformed into a new product, such as a shirt. Musa A. Rubin, "Effect of AGOA/Contonou Agreements on the Garment and Textile Industries in Southern Africa," prepared for IPM meeting, Maputo, Mozambique, Nov. 5, 2002.

[31] Textile Federation, *South African Textile Statistics & Economic Review 2001/2002* (Bruma, South Africa), p. 4.

Shipping is shorter in terms of time, and more frequent in occurrence, from southern Africa, about 21-30 days. Shipping times were not cited as a particular disadvantage by companies operating in South Africa, although one company in Lesotho noted that it was starting to lose orders for basic trousers to Mexico, which has much shorter shipping times. Longer lead times mean that SSA products will be largely confined to "basics" that do not depend on quick changes in fashion. These are also the types of products that can be produced in China, India, Bangladesh and other Asian countries very competitively.

Other logistical problems also confront SSA. For example, one integrated manufacturing firm indicated that the entire cost base in Mauritius is high; buildings, electricity, fabrics, and labor are cheaper in China. The same firm noted that although wages were cheaper in Madagascar, other costs were more expensive, including electricity and transportation. In Lesotho, utility costs, including water and electricity, are higher than in competitor countries,[32] and outages occur. One company operating in Mozambique indicated that operating a textile factory in that country would be extremely difficult owing to a lack of electricity and constant outages.

Labor and Management

With the exception of Mauritius, SSA has abundant labor for production of textiles and apparel. In SSA countries other than Mauritius and South Africa, factory ownership and most of the management are controlled by foreign interests, largely from Asia. Mauritius is labor constrained for expansion of textiles and apparel. It is reported that workers in Mauritius increasingly prefer to obtain jobs in high tech areas and that it is difficult to retain workers in the textiles and apparel industries. Approximately one-third of the workforce in textiles and apparel in Mauritius is foreign workers, largely from Asia.

Wages for textile and apparel workers in SSA are highest in South Africa and Mauritius, and tend to be much lower in other SSA countries. Workers in South Africa are highly unionized, resulting in the highest average wages for workers in this sector in SSA. Most companies interviewed indicated that workforce skill levels and labor productivity on average are lower in SSA than in Asia. For example, productivity in making basic trousers in Lesotho is estimated at 70 percent of that in Taiwan, and the rate falls to 50 percent or less if the style of the trouser is changed.[33] Most companies interviewed noted that SSA countries will have difficulty competing with Asia in global markets following quota elimination in 2005 either because their wages are high (South Africa and Mauritius) or because their low productivity, combined with the cost of other raw materials, offsets their low wages (for example, Lesotho, Madagascar, and Swaziland).

Raw-Material Inputs

Companies interviewed in SSA noted that the competitiveness of the region's apparel industry is undermined by the limited availability and high cost of regional inputs, compared with countries such as China and India. Although SSA has an important textile fiber base for the development of textile and apparel industries, many of the countries that produce fibers

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[32] Department of Industry, *Proposed Incentives for the Manufacturing Sector in Lesotho,* Oct. 2002.

[33] Representative of large apparel company, interview by USITC staff, Lesotho, Mar. 7, 2003.

have lacked the manufacturing investments required to use these fibers (mainly cotton and wool) locally. To improve utilization of SSA cotton within the region, a number of SSA countries are participating in the Cotton Pipeline Project, whose purpose is to assist cotton production, increase the number of ginning mills, and improve the distribution of SSA cotton so as to expand textile and apparel industries within SSA.[34]

SSA is a higher cost producer of cotton yarn and fabrics than China and India. As noted in Appendix K, U.S. imports of apparel made from third-country fabrics amounted to 75 percent of AGOA apparel imports in 2002. This reflects the high cost of U.S. fabrics in SSA, as well as the limited availability and relatively high cost of SSA yarns and fabrics. For example, one company estimated that the cost of a standard cotton chino fabric imported into Lesotho from China was 58 cents per square yard, compared with $1.57 per square yard for an identical fabric produced in South Africa. Some of this cost differential may be due to the appreciation of the rand against the U.S. dollar in 2002.[35]

In addition to cost differentials, concerns have been expressed about the small variety of fabrics that can be produced in SSA, compared with Asia. This is considered an important disadvantage for the region, as buyers and fashion dictate the type of fabrics used. In particular, SSA has a deficit in the production of knitwear fabric. Mauritius, an important SSA fabric producer, has a deficit in the production of cotton yarn for knitwear,[36] and Lesotho, a major exporter of knit shirts, does not produce yarn or fabric. Both countries have planned investments coming on line in the future, but these industries will take time to get into full-time operation. AGOA preferences have enabled SSA to become more competitive in manmade-fiber apparel due to the relatively high duties on such apparel. However, South Africa is the only country in SSA producing synthetic filament yarn, as this industry is highly capital intensive.

Another important disadvantage, particularly in Mauritius, is the lack of ability of SSA countries to produce the volume of apparel that can be produced in China and India. Many companies in SSA expressed concern that as buyers reduce the number of countries from which they source following the phaseout of the quotas, SSA will be left out as buyers work to eliminate sourcing costs by purchasing from larger suppliers.[37] The volume disadvantage was particularly cited in the context of the U.S. market, as the EU market generally demands smaller quantities on a flow basis.

Level of Service Provided and Reliability of Supplier

Companies operating in SSA recognize that to be competitive they need to become vertically integrated and to offer full service packages. Some companies in Mauritius and South Africa

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[34] Representative of the Department of Trade and Industry, interview by USITC staff, South Africa, Feb. 27, 2003.

[35] A representative of an integrated textile/apparel company in South Africa indicated that until the appreciation of the rand against the dollar, South African-produced denim was competitive with denim imported into Lesotho. In 2002, the rand appreciated 40 percent against the dollar.

[36] A number of planned investment is expected to come on line in the second quarter of 2003.

[37] For example, one large apparel company indicated that it has already begun to narrow its list of suppliers and that it does not like to account for more than 20-25 percent of a supplier's capacity.

produce high-value added products, such as fully fashioned sweaters in cotton, cashmere, lambswool, and various blends, and apparel from wool and manmade fibers. It is highly likely that these countries will be competitive in these high-value products in the future. However, most SSA exports are in basic products that will be vulnerable to lower cost Asian production once the quotas are phased out.

A number of investments are underway in SSA countries to increase the number of vertically integrated companies and to upgrade service packages, but these types of investments take time. Most companies cited vertical integration as a way to compete in a quota-free world because it will cut lead times, assure fabric availability, and give a company more control and flexibility over its output. There is recognition in Mauritius that due to the challenges the industry will face in a quota-free world, its industry may be better placed as a regional SSA center for textile and apparel services than as a producer of goods.[38]

[38] Joint Economic Council, *The Economic Transition of Mauritius: Report of the JEC Task Force,* Feb. 2001, and appendix K of the Commission report.