UNITED NATIONS CONFERENCE ON TRADE AND DEVELOPMENT

WEAVING A NEW WORLD: REALIZING DEVELOPMENT GAINS IN A POST-ATC TRADING SYSTEM

UNCTAD series on assuring development gains from the international trading system and trade negotiations

UNITED NATIONS

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Weaving a New World:
Realizing Development Gains in a Post-ATC Trading System

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United Nations

New York and Geneva, 2005

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UNCTAD/DITC/TNCD/2005/3

UNITED NATIONS PUBLICATION
ISSN 1816-2878

Preface

As the focal point of the United Nations for the integrated treatment of trade and development and interrelated issues, and in accordance with the São Paulo Consensus adopted at the eleventh session of UNCTAD, the UNCTAD secretariat supports member States in ensuring development gains from international trade, the trading system and trade negotiations, with a view to their beneficial and fuller integration into the world economy and to the achievement of the United Nations Millennium Development Goals. Through intergovernmental deliberations and consensus-building, policy research and analysis, and technical cooperation and capacity-building support, UNCTAD's work on trade negotiations and commercial diplomacy aims at enhancing human, institutional and regulatory capacities of developing countries to analyse, formulate and implement appropriate trade policies and strategies in multilateral, interregional and regional trade negotiations.

This paper is part of a new series on "Assuring Development Gains from the International Trading System and Trade Negotiations". It builds on the previous series on "Selected Issues in International Trade Negotiations". The targeted readership is government officials involved in trade negotiations, trade and trade-related policymakers, and other stakeholders involved in trade negotiations and policymaking, including non-governmental organizations, private sector representatives and the research community.

The objective of the series is to improve understanding and appreciation of key and emerging trade policy and negotiating issues facing developing countries in international trade, the trading system and trade negotiations. The series seeks to do so by providing a balanced, objective and sound analysis of technical issues involved, drawing implications for development and poverty reduction objectives, and exploring and assessing policy options and approaches to international trade negotiations in goods, services and trade-related issues. It seeks to contribute to international policy debate on innovative ideas in realizing development dimensions of the international trading system for the achievement of the Millennium Development Goals.

The series is produced by a team led by Mina Mashayekhi, Head, Trade Negotiations and Commercial Diplomacy Branch, DITC.

Abstract

The discriminatory trading system that restricted textiles and clothing exports from developing countries for over 40 years finally came to an end. Both developed and developing countries stand to gain substantially from the removal of quota restrictions and the full integration of textiles and clothing into normal WTO rules. While many quantitative studies were undertaken to examine the impact of the ATC termination, post-ATC analysis cannot be reduced to a single calculation of who will win or lose. There are economic, political and geographical factors which would affect trade in textiles and clothing in the post-ATC trading environment. This paper attempts to highlight these factors and to argue that the success of an exporter of textiles and clothing in the post-ATC phase depends on how it will take advantage of the opportunities, and overcome the challenges, that ATC expiration brings about. The first section discusses the historical perspective of trade in textiles and clothing and the recent new developments. This is followed by a review of the textiles and clothing trade patterns under the MFA and an ATC, and the analysis of the factors influencing post-ATC effects. The paper concludes with policy recommendations for ensuring and maximizing development gains in the post-ATC trading environment.

Acknowledgements

This paper was prepared for the Trade Negotiations and Commercial Diplomacy Branch, Division on International Trade in Goods and Services, and Commodities (DITC), UNCTAD, Geneva. The author wishes to thank Ms. Lakshmi Puri, Director of the Division, Mr. Sam Laird, Officer-in-Charge, Trade Analysis Branch, DITC, the Office of the Secretary-General and Mr. Sergio Delgado, formerly of the WTO secretariat, for their valuable comments on the study, and for the support provided by the UNCTAD Central Statistics and Information Retrieval Branch.

Contents

Introduction

During the last two decades, textiles and clothing were the second most dynamic products in world trade after electronic and electrical goods. Developing countries contributed significantly to this growth, and this sector continues to play a vital role in their economies on account of inherent and evolving comparative advantage. It is one sector that offers good prospects for diversification away from traditional commodity exports, for entry into the area of manufactures, for absorption of large pools of labour, for crossing the great divide between the rural and urban sectors, and for generating foreign exchange. Also, the economic performance of the sector has important implications for socioeconomic issues such as equitable distribution of income, employment opportunities for women, development of small- and medium-scale enterprises, spillover to the informal sector, integration of remote regions into the global economy, promotion of rural development and poverty alleviation.

Moreover, in many developing countries, textiles production is linked to traditional and cultural heritage, which points to the importance of maintaining the economic sustainability of the sector as a source of comparative advantage and economic vitality. Considerations of benefits from trade cannot be divorced from the larger issue, namely that there is an encompassing development dimension to the integration of textiles and clothing into the normal rules of the trading system. Certainly, the freeing of the textiles and clothing exports of developing countries from 40 years of restrictions by major developed countries has significant positive implications for trade and development. It can contribute to the realization of the Millennium Development Goals and the Monterrey Consensus objectives of ensuring that trade serves as an engine of growth and development, as well as the aim of the São Paulo Consensus, adopted at UNCTAD XI, to ensure that development gains from the international trading system and trade negotiations accrue to developing countries.

I. Historical perspective and recent developments

Historical perspective: Restrictions on developing-country exports

Exports of textiles and clothing from developing countries were the subject of special discriminatory and restrictive measures involving quotas that, although initially intended as temporary relief measures in favour of developed-country industries, were in force for over 40 years. In 1962 a Long-Term Agreement Regarding International Trade in Cotton Textiles (LTA) was signed, replacing the one-year Short-Term Agreement that existed at the time. The LTA was renewed several times until 1974, when it was replaced by the Multifibre Arrangement (MFA), which expanded its coverage to synthetic fibres and wool, thus affecting practically all fibres. While competitive developing countries gained an important share in the world trade of textiles and clothing, the full scope of opportunities for growth of their exports of these products was seriously constrained. The regime governed by the MFA lasted until 1994, when the Uruguay Round of Multilateral Trade Negotiations negotiated the Agreement on Textiles and Clothing (ATC). A timeline summarizing the historical development of trade regimes governing world textiles and clothing trade is provided in table 1 of the Annex.

The ATC replaced the MFA and established an integration programme to phase out all quota restrictions over a 10-year transition period. It set minimum thresholds for "integration" of textile and clothing products in four successive steps: an initial 16 per cent of these products were integrated by 1 January 1995, a further 17 per cent by 1 January 1998, a further 18 per cent by 1 January 2002 and the remaining 49 per cent by 1 January 2005, thereby completing the ATC integration programme.

Up to 1 January 2002, 51 per cent of the products in volume covered under the ATC were integrated. However, products of real interest to developing countries were still largely restricted until 1 January 2005, and therefore the commercial significance of the integration for these countries was very limited until the very end of the ATC phase-out period. The ATC integration programme included unrestricted textiles and clothing products (i.e. products which were not limited by quotas) as well as ones restricted by quotas, and, in the process of the negotiation of the ATC, the selection of products for integration was left to the discretion of the restricting countries. Those countries opted to integrate unrestricted products in the first three integration phases. As a result the majority of restricted products – 80 per cent of the products restricted by quotas in terms of volume – remained restricted until the final phase of the integration programme. The restricted products accounted for about half of the total textiles and clothing imports in the European Union and the United States. Earlier in 2004, restricting countries formally notified the WTO of their intention to meet commitments to eliminate all remaining quota restrictions as scheduled under the ATC. Subsequently, the ATC expired on 31 December 2004, and textiles and clothing were fully integrated into the normal rules and disciplines of the WTO. Hence, all the remaining quota restrictions were abolished.[1]

[1] However, countries that are not WTO members could be subject to quota restrictions.

Systemic implications of the ATC expiry

Textiles and clothing trade governed by the MFA and its predecessor arrangements derogated from the basic principles of the multilateral trading system. It represented a carve-out for developed countries at the expense of developing countries whose comparative advantage was superior in many of these manufactured products. It also constituted a reverse form of special and more favourable treatment for developed countries, providing their textiles industries with long-standing protection. Developing countries that had international competitiveness in textiles and clothing had borne the brunt of a restrictive, managed, discriminatory, discretionary and non-equitable trading system.[2] The end of the ATC thus contributes to the "upholding and safeguarding of an open, non-discriminatory, predictable, rule-based, and equitable multilateral trading system", an objective of the international community recently affirmed in the São Paulo Consensus adopted at UNCTAD XI in June 2004. It also contributes to the realization of the United Nations Millennium Development Goals.

As is noted below, some textiles industry trade associations that had been protected under the quota system pressured their Governments for an extension of the system. The ATC formed part of the Single Undertaking embodied in the Results of the Uruguay Round of Multilateral Trade Negotiations, which established the WTO. Developing countries had accepted the ATC Agreement in exchange for developed countries' acceptance of other agreements in this Uruguay Round. Changing the ATC would have required a reopening and unravelling of the Uruguay Round Agreements, with potentially serious implications for the multilateral trading system, including the Doha negotiations. Implementing fully the commitments of the restraining countries to eliminate all remaining quota restrictions, as scheduled under the ATC, was essential for maintaining a stable international trading system.

Recent developments in the WTO

Although the ATC expired, the legacy of textiles and clothing trade continues, and there have been new post-ATC developments in the WTO. In the summer of 2004, concerned by the possible negative impact on their economies of the removal of quotas that had given a protected share of major markets, some WTO member countries, namely Mauritius, Bangladesh and Nepal, requested the WTO to convene an "emergency" meeting of the Council on Trade in Goods (CTG) to consider "unintended negative consequences for vulnerable economies" from the impending phase-out of the textiles and clothing quotas on 1 January 2005. On 3 August 2004, the Director-General of the WTO convened a consultation meeting to discuss whether such a meeting would be necessary and concluded that there was no consensus regarding the need for the meeting. However, it was agreed that the meeting of the CTG on 1 October 2004, where the final review of the ATC would be on the agenda, could provide an opportunity to address this issue under the item "Post-ATC Adjustment-Related Issues".

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[2] On the other hand, some developing countries, particularly LDCs, that did not have competitiveness in the sector were able to develop exports of low-value-added apparel as manufacturers and retailers invested in these countries to overcome the quota limitations.

At the CTG meeting on 1 October 2004, the Governments of Bangladesh, the Dominican Republic, Fiji, Madagascar, Mauritius, Sri Lanka and Uganda (joined later by Jamaica, Nepal and Mongolia) jointly proposed that the WTO secretariat carry out a study on the post-ATC adjustment-related issues.[3] The 10 countries proposed that the study examine the global impact of the ATC expiry in a disaggregated manner at country level for the LDCs and other small and vulnerable economies that would be seriously impacted. Also, these countries proposed that the WTO establish a Work Programme on the post-ATC adjustment issues.[4] While some countries supported the proposal, many textiles and clothing exporting countries opposed it, particularly the idea of establishing a Work Programme specifically intended for textiles and clothing.[5] Their view was that the post-ATC adjustment issues should be dealt with in the context of the overall adjustment from trade liberalization.

Subsequently, at the informal CTG meeting of 26 October 2004, the Government of Turkey proposed that new WTO mechanisms urgently be developed to ensure a smooth transition to the post-ATC phase.[6] It suggested that such mechanisms could include a "monitoring system that would concentrate on the threat of market distortions and a unique safeguard mechanism that has a self-triggering structure and aiming at smooth functioning of trade in the major export markets and avoiding unfair practices". The Turkish Government argued that these measures would be necessary in order to protect the market share of developing countries in their export markets in the post-ATC phase. A number of countries firmly opposed the proposal, arguing that the proposed measures would cause distortions again in the international trading system. They recalled that the purpose of the integration of textiles and clothing into normal WTO rules was precisely to rectify the distortions caused by the quota system, and stressed that trade liberalization in any sector could cause pain and adjustments and that textiles and clothing should not be singled out. Furthermore, they argued that appropriate actions for easing the post-ATC impacts would be improving the effectiveness of the non-reciprocal preferential agreements with the major importing countries, increasing technical and financial assistance to enhance supply capacity, and promoting investments and South–South trade.[7]

The CTG meeting of 25 November 2004 discussed the agenda item on "Post-ATC Adjustment-Related Issues" again. Some major textiles and clothing exporting countries attempted to move this item to the Sub-Committee on LDCs, where concerns of LDCs were discussed. However, some non-LDC developing countries, as well as the United

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[3] WTO document, "Initial Submission on Post-ATC Adjustment-related Issues from Bangladesh, Dominican Republic, Fiji, Madagascar, Mauritius, Sri Lanka, and Uganda", G/C/W/496, 30 September 2004. Also, "WTO Members Deadlocked on Impact of Jan.1 Elimination of Textile Quotas", *International Trade Daily*, 27 October 2004.

[4] G/C/W/496, op. cit.

[5] Those that supported were: Haiti, Tunisia, Jordan, El Salvador, Nicaragua, Guatemala, Israel, Mexico, Kenya, Nigeria and Rwanda. Those economies that opposed were: Brazil, China, Colombia, Costa Rica, Cuba, the EU, Hong Kong (China), India, Indonesia, Pakistan, Taiwan Province of China and Thailand.

[6] WTO document "Turkey's Contribution to the Debate on Post-ATC Related-Issues", G/C/W/497, 25 October 2004.

[7] "Turkey for preserving clothing market shares after ATC", SUNS, 26 October 2004.

States, the EU and Turkey, demanded that the item remain under the auspices of the CTG. At present, the item is open in the CTG, but the Sub-Committee on LDCs decided in January 2005 that the WTO secretariat should prepare a study on issues relating to the termination of the ATC for the LDCs.[8] It is expected that this study will be completed around May 2005. Separately, in the CTG meeting of 11 March 2005, Tunisia proposed that the WTO undertake a post-ATC study addressing the concerns of developing countries that rely on exports of textiles and clothing and would be impacted by the ATC expiry.[9] The proposal is under consideration at present.

In the Committee on Trade and Development, too, the question of how to deal with textiles and clothing became a contentious issue. China opposed the proposal that the issue of textiles and clothing be included in the regional seminars to be organized under the technical assistance programme for 2005. Its view was that after the ATC's expiry these products should be dealt with in the context of market access like other goods. However, a compromise was reached, namely that textiles and clothing could be dealt with as part of national seminars in response to the request of beneficiaries.[10]

Recent developments in the private sector

The protectionist lobbying from the private sector played a significant role in shaping the current developments in the WTO on the post-ATC issues. Concerned over the negative impacts of ATC termination, in March 2004 a number of industry associations in the United States, Turkey and Mexico met in Istanbul and adopted the Istanbul Declaration Regarding Fair Trade for Textiles and Clothing, which called for the extension of the quota restrictions until 31 December 2007. In June 2004, a follow-up meeting held in Brussels resulted in the Brussels Communiqué by the Istanbul Declaration Partners in the Global Alliance for Fair Trade in Textiles and Clothing, which was signed by about 40 industry associations in some 20 countries. While continuously seeking the extension of the quotas, the Communiqué also requested the use of the safeguard mechanism to “prevent disruptive surges of textiles and clothing from a few countries, as well as to demand remedies to all types of unfair trading practices employed by certain major supplying countries, including currency manipulation, state-sponsored subsidies and state-provided non-performing loans”.[11]

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[8] The terms of reference of the study reads: "Fully respecting the basic principles and rules of the WTO and rights and obligations of the Members, the WTO Secretariat will prepare a paper that will look into options for LDCs to improve their competitiveness in the textiles and clothing business, namely coherence programmes of IMF and World Bank, more flexible rules of origin, technical assistance and capacity building, bilateral cooperation programmes and other means to tackle constraints affecting LDCs' exports".

[9] WTO document, "Post-ATC Adjustment-Related Issues, Communication from Tunisia, The Dismantling of Textile and Clothing Quotas: Impacts, Issues and Proposals for Action", JOB(05)/31, 11 March 2005.

[10] WTO document "Technical Assistance and Training Plan 2005", WT/COMTD/W/133/Rev.2, 16 December 2004.

[11] Not all private-sector groups favoured an extension of the ATC regime. Eighteen associations representing retailing and importing companies, collectively called the Group of 18, as well as consumer groups in the restricting countries, supported the scheduled elimination of quotas on textile and apparel products and attempted to counteract the protectionist lobbying campaign. They denounced the protectionist lobbying, arguing that “industries that have failed to use the 10-year phase-out to prepare for the end of quotas are now claiming they ‘need more time’ ”.

The campaign by the protectionist lobbyist did not succeed in securing the extension of the quotas; however, as discussed in the section of “Contingency measures” below, the pressures for protection continue, currently targeting China.[12]

[12] The US and the EU have initiated safeguard investigations for some textile products from China, and petitions for safeguard investigations for Chinese textile products continue to be filed.

II. Textiles and clothing trade patterns under the MFA and the ATC

Trade patterns of textiles and clothing

During the last two decades, trade in textiles and clothing has grown significantly, and developing countries have made a considerable contribution to this growth. In this period, clothing exports from developing countries increased by a factor of 7 and textile exports by a factor of 5, while the corresponding figures for developed countries were factors of 3 and 2 respectively.[13] Textiles and clothing were the second most dynamic products in world trade, with an annual export growth rate of 13 per cent, surpassed only by electronic and electrical goods, whose exports increased by 16 per cent annually.[14] In 2003, developing countries accounted for 76 per cent of total world clothing exports and 50 per cent of world textiles exports, while two decades ago the corresponding figures were only 8 and 9 per cent.

The leading exporters of textiles and clothing in 2003 are indicated in Tables 2 and 3 of the Annex. China, Hong Kong (China), India, Pakistan, Indonesia, Thailand, Mexico, Brazil Malaysia and the Islamic Republic of Iran were the developing economies among the top 20 world textile exporters, whereas for clothing exports, China, Hong Kong (China), Mexico, India, Indonesia, Thailand, Bangladesh, Pakistan, Morocco, Tunisia, Sri Lanka, Viet Nam, and the Philippines were among the top 20 economies. Many developing countries experienced very high rates of growth, particularly in clothing exports. The dynamism of developing-country exports of textiles and clothing in an era of ATC restraints masked the opportunities forgone. Also, although it is believed that textile trade is dominated by developing countries, tables 2 and 3 show a quite different picture. The United States and the EU continue to play leading roles in both textiles and clothing trade.

Securing the availability of quotas was a major concern of importers in the restricting countries under the MFA and ATC regimes. This factor led to the evolving structure of the exporting countries group, which is not necessarily or fully based on comparative advantage. Importers in the restricting countries engaged in "quota hopping" to overcome quota limitations, moving from one country to another searching for suppliers who could assemble garments cheaply – sometimes with minimal operations and relabelling – and export them to their countries without being restricted by quotas. The product range was also modified to move into sectors with unused quotas – for example, T-shirts were lengthened and exported as tunics under a different tariff line. Major retailers of textile products and intermediary contractors made investments in such countries to build factories. Eventually, helped by quotas, exports of textiles and clothing grew. As Table 4 in the Annex shows, in some developing countries, especially LDCs, they became a major source of foreign exchange earnings. The case of Bangladesh is an example of spectacular growth. Its clothing exports grew from $1 million[15] in 1978 to

[13] UNCTAD WITS-TRAINS database.
[14] UNDP, *Making Global Trade Work for People*, 2003, p. 174.
[15] All references here to dollars ($) are to US dollars, unless another currency is specified.

$4.5 billion in 2001 despite quotas and MFN tariffs in the US market. This growth was accompanied by a remarkable increase in female manufacturing employment.[16]

The phase-out period of the ATC leading to 2005 saw the emergence of regional trade agreements, including bilateral ones, between the two major trade partners on the one hand and their respective partner countries on the other. The Euro-Mediterranean Association Agreements, the North America Free Trade Agreement, the Caribbean Basin Trade Partnership Act, the Andean Trade Preferences Act and the United States–Jordan Free Trade Agreement are examples of regional trade agreements.

Observers have noted that regional trade agreements diminish the shares of major non-preferred suppliers. For example, in 1995, 64 per cent and 22 per cent of total imports of clothing into the United States came from Asia and Latin America, respectively; however, in 2000, the corresponding figures were 55 per cent and 30 per cent. Also, data from the International Textiles and Clothing Bureau show that non-preference-receiving countries' share of total US textile and clothing imports decreased from 79 to 69 per cent between 1990 and 2003. For the EU market, the market share of non-preference-receiving countries stagnated at around 41 per cent over the same period.

Diagrams 1 and 2 in the Annex clearly show that regional trade agreements contributed to the growth of clothing exports in preferred suppliers. Diagram 1 indicates that countries which were partners in the regional trade agreements with the United States, increased their shares of textiles and clothing exports to that country during the period from 1994 to 2003. These countries are Nicaragua, Peru, El Salvador, Mexico, Honduras, Guatemala and Canada. Meanwhile, the corresponding shares of Asian countries that are traditionally major exporters of these products diminished during the same period. Diagram 2 shows a similar picture for the EU market. Countries which had regional trade agreements with the EU, namely, Bulgaria, Lithuania, Romania, Ukraine, Latvia, Turkey, Egypt, Slovenia, Tunisia and Morocco, increased their export shares in respect of those products, whereas the major Asian exporters lost their shares.

Emerging trends in the 1990s

Three new trends in the 1990s — the emergence of transnational intermediaries, the concentration of retailers and "lean retailing" — had a significant impact on international production of and trade in textiles and clothing. Firstly, East Asian manufacturers moved up from assembly of cut fabric into more complex operations entailing coordination, supply of machinery and finance, and management of subcontractors. They are now full-package suppliers for international buyers and are operating as transnational intermediaries receiving orders from large retailers and subcontracting to their networks of producers, which are located in Asia, Latin America and Africa.

[16] UNDP, *Making Global Trade Work for People*, p. 171, and UBINIG, "Options for Women in the Textiles and Handloom Sector in Bangladesh", in *Trade, Globalisation and Gender: Evidence from South Asia*, edited by Veena Jha, UNIFEM and the United Nations, 2003, p. 231.

Secondly, the market has become more concentrated in the major importing countries.[17] In addition, high-volume discount chains in those countries have developed their own brands and outsource their clothing from suppliers. Major retailers have large distribution networks and considerable buying power, and they exert a great deal of control over prices and other conditions imposed on suppliers. These retailers and international intermediaries are developing close business relationships, and it is expected that the close ties between them will be a prominent feature of the international garment business in the post-ATC era.

Thirdly, "lean retailing" emerged in the 1990s. This is a business practice made possible by advances in information technology that allow retailers to hold small inventories and respond rapidly to fluctuations in consumer demand.[18] It is used particularly for seasonal apparel products, which are "rapid replenishment" goods, or items for which fashion changes rapidly, so that timeliness of shipment is crucial. Studies have found that proximity to suppliers is important for retailers as far as "rapid replenishment" goods are concerned, and nearby producers are increasingly specialized in such goods.[19]

[17] Apparel retailing in the major importing countries is dominated by large firms, which control major distribution channels. In the United States the 29 biggest retailers account for 98 per cent of apparel sales, and in the European Union retailing has been marked by substantial concentration in the last decade. Gereffi and Memedovic, (2003, p. 6).

[18] Evans and Harrigan, (May 2003, p. 1).

[19] For example, the sourcing of US apparel from Mexico and the Caribbean is disproportionately concentrated in "rapid replenishment". See Evans and Harrigan, op. cit.

III. Factors influencing post-ATC effects

Determining countries' performance in the textiles and clothing sector after ATC expiry cannot be reduced to a single calculation of who will win or lose, but rather involves the question of how countries will take advantage of the opportunities, and overcome the challenges, to which ATC expiration gives rise. In this context, a number of issues will be important, including gains, costs and adjustment, competitiveness, the role of tariffs in shaping sectoral trade, the trade policies of the major importing countries, and likely near-term changes in trade and investment patterns.

As the date of the ATC's expiry approached, press and media reports projected a somewhat gloomy picture of the impact of quota-lifting on some developing countries, or highly optimistic scenarios of gains for some other developing countries.[20] It was inevitable that positive and negative adjustments would take place in the post-ATC period, but the post-ATC picture has to be seen in its proper perspective as there are several factors that are likely to counterbalance, influence and modulate the post-ATC effects. The last section of this paper, "Strengthening participation of developing countries in the dynamic sectors of world trade", discusses the results of a recent UNCTAD Expert Meeting, which identified measures required at the enterprise, national and international levels to maintain competitiveness in the trade of textiles and clothing.

Welfare gains and market shares

Large welfare gains from increased GDP and productivity increment for both developed and developing nations are predicted to emerge from the integration of textiles and clothing into the normal WTO rules. The gains from the elimination of quotas are estimated to account for 42 per cent of the total gains of Uruguay Round liberalization in the static model and 65 per cent in the dynamic model.[21] The income gains accruing to the importing developed countries themselves could be as high, for example, as $18 billion a year in the United States[22] and ECU 25 billion a year in the European Union.[23] Another study estimated that freeing textile trade from quotas in 2005 could generate income gains for developing countries of $24 billion a year, export revenue gains of $40 billion and employment of about 27 million jobs.[24] Moreover, a study on protection in the textiles and clothing sector of the United States found that although textiles and apparel account for less than 2 per cent of total employment in the US economy, protecting them against import competition accounts for 83 per cent of the net cost to the

[20] For example, "From Riches to Rags: How Free Trade Can Wreck An Economy", *Far Eastern Economic Review*, 27 November 2003, and "The Financial Express", India, 9 August 2004. http://www.financialexpress.com/fe_full_story.php?content_id=65453

[21] Hildegunn Kyvik Nordas, "The Global Textile and Clothing Industry post the Agreement on Textiles and Clothing", WTO Discussion Papers, No.5, 2004, p. 25.

[22] World Bank, *World Development Report 1987*, 1987, p. 150.

[23] Francois, Glismann and Spinanger, (2000, p. 67).

[24] International Monetary Fund and World Bank, "Market Access for Developing Country Exports: Selected Issues", 26 September 2002, pp. 42–43.

US economy of all import restrictions.[25] The high administration costs of the complex customs systems under the ATC regime were eliminated when the quotas were abolished, thus producing considerable savings given the size of the sector.

Political and efficiency gains to be derived from the expiry of the ATC should not be neglected. These gains are related to the credibility of the multilateral trading system at a time when the system is experiencing considerable strains, as well as gains from elimination of highly distorting quotas that have led to an inefficient global allocation of resources.

A number of studies have been conducted to estimate the impact of post-ATC textiles and clothing trade on developing-country exporters using the Global Trade Analysis Project model (GTAP). Most model simulations conducted to date share the finding that some Asian countries are most likely to benefit from the ATC expiry, while many other countries that have gained market shares under regional trade agreement preferential schemes could be negatively affected. Results also suggest that countries specializing in assembly and export of low-value-added garments are likely to face particularly strong competition in the post-ATC period.

The latest statistics on US imports of textiles and clothing provide the data for January and February 2005. Comparison of the data for the period from January to February 2004 with the data for the same period in 2005 for the regional groups of APTA, ASEAN, CAFTA, CBI and sub-Saharan did not show Africa a reduction in their total exports of MFA products (in value terms) from these groups. For individual countries, the corresponding data for Bangladesh, Cambodia, Viet Nam, China, India, Mexico, Nepal, Pakistan and Sri Lanka were examined. Among these countries, Mexico and Nepal experienced a decrease in their exports, but it is too early to analyse the actual impact of the ATC's expiry, and continuous monitoring of trade data is required.

The challenge of adjustment

Because of the distorting effects of quota restrictions on international trade and production of textiles and clothing, industrial experts and scholars predict that significant adjustments will take place in the industry during the first few years after the ATC's expiry. One of the important features of the ATC was to provide a 10-year phase-out period for quota elimination to ease the impact of quota lifting. However, as discussed earlier in "Historical perspective: Restrictions on developing-country exporters", restricting countries chose not to use this transition period and backloaded liberalization of the restrained products until the last moment. Subsequently, about 80 per cent of the total restrained textiles and clothing imports were due to be quota-free on 1 January 2005. These accounted for about 50 per cent of the total textiles and clothing imports in the EU and the United States, representing about 30 per cent of total world imports of textiles

[25] Michael J. Finger and Anne Harrison, "Import Protection for US Textiles and Apparel Viewed from the Domestic Perspective: The Political Economy of Trade Protection", National Bureau of Economic Research Project Report Series, University of Chicago Press, 1996, pp. 43–49.

and clothing.[26] The opportunity for a soft landing was missed. Moreover, during the transition period itself, and with full knowledge of the impending complete elimination of the quota regime, new exporting countries emerged, mostly among the LDC group, to fill the supply gap produced by quota limitations on the established suppliers; in fact, their increasing participation in the garment export trade was actually based on the quota regime itself.

While some developing countries are expected to increase their exports of textiles and clothing significantly after the ATC's expiry, countries that enjoy quota- and duty-free treatment of their exports to the United States and the European Union through the AGOA, EBA and GSP schemes, and that rely heavily on exports of assembled garments, are particularly vulnerable to the expected increase in competition in the sector following ATC expiry. For many of them, textiles and clothing are extremely important sources of foreign exchange earnings; for example, in Asian LDCs such as Bangladesh, Cambodia, the Lao People's Democratic Republic and Nepal, the sector earns 50 to 90 per cent of the countries' international trade revenues. Clothing exports are significant for Kenya, Lesotho, Madagascar and Mauritius. Studies indicate that these preference-receiving countries would be adversely impacted by the elimination of quotas.

The countries discussed above have limited capabilities to adjust to the post-ATC impact, including the preference erosion that is likely to accompany the ATC's expiry. The international community should be sensitive to their needs and stand ready to extend appropriate assistance. Measures required for post-ATC adjustment are discussed below in "The need for adequate support measures".

Determinants of competitiveness

Competition in trade in textiles and clothing will be intensified in the post-ATC environment. To prepare for the competition, action needs to be taken by the industries whose trade has been sheltered by the quota regime to improve their competitiveness. Factors such as "quick-and-flexible response" systems, cost reduction, quality, investments in modern technologies, and product innovation are regarded as key ingredients for creating dynamic textiles and clothing industries. Also, when quotas disappear, importers of textiles and clothing in the major importing countries will continue to be influenced by such factors as speed, quality, compliance with legal requirements, logistics and production costs when selecting particular suppliers and countries.[27] One study predicts that, among developing countries, there will be a relocation of low-end operations to lower-cost countries, and that the apparel value chain will relocate to countries with the lowest wages.[28] A number of other studies have identified areas where national policy measures will be necessary in order to improve the

[26] WTO document, "Second Major Review of the Implementation of the Agreement of Textiles and Clothing by the Council for Trade in Goods, "G/C/W/325, 22 October 2001, p. 5.
[27] Dan Ikenson, "Threadbare Excuses: The Textile Industry's Campaign to Preserve Import Restraints", Cato Institute, Washington, DC, October 2003, pp. 14–15.
[28] Gary Gereffi and Olga Memedovic, op. cit., p. 9.

competitiveness of the textiles and clothing industries in developing countries.[29] These include consolidation of fragmented producers, revamping of national policies restricting competitiveness (e.g. policies to reserve handlooms production at the expense of modernizing the production facility), development of niche-based exports, support for technology upgrades, and streamlining of transport, shipping and customs clearance, including the aspect of trade facilitation. Also, an UNCTAD Expert Meeting held in February 2005 discussed opportunities and challenges for developing countries in enhancing the competitiveness of their textiles and clothing sectors. A summary of the Expert Meeting can be found in the Annex.

Costs for non-preferred developing countries

The issue of emerging regional trade agreements discussed above leads to the question of preferred countries' gains versus non-preferred countries' costs. Often referred to is the notion of "discriminatory trade liberalization" or "discriminatory free trade", terms that describe preferential trade arrangements within which countries permit duty-free and quota-free imports from subsets of countries, while maintaining barriers to imports from others. Lifting of quotas would restore the parity of quota-free treatment for non-preferred suppliers. At the same time, non-preferred suppliers would continue to be discriminated against by way of tariff treatment. Owing to tariff peaks on textile products discussed below in the section entitled "The role of tariffs", tariff preference margins will probably remain quite significant in the post-ATC phase. As a result of persisting high tariffs in the sector, preferred suppliers will continue to enjoy a preferential edge over non-preferred suppliers. This should cushion the impact of ATC expiry on preference-receiving countries to some extent, while reducing the potential benefits for non-preferred suppliers.

Substantial trade of textiles and clothing takes place between the United States and the European Union on the one hand and their respective preferred-country suppliers on the other hand, an indication of closed production chains. The high degree of inter-trade is attributable partly to business relations established in the past and partly to the increasing trend of "lean retailing". Also, rules of origin for regional trade agreements are likely to be an important factor influencing this trend, as they have been designed to encourage the use of preference-giving countries' inputs. Intermediate inputs such as cut fabric, thread and buttons are exported to offshore suppliers located in low-cost countries, often neighbouring ones, with reciprocal trade agreements that allow goods assembled offshore to be reimported duty-free or with a tariff charged only on the value added by foreign labour.[30] In other words, the beneficial impact of regional trade agreements is on

[29] For example, Indian, Bangladeshi and Philippine studies (Sanjay Kathuria, Will Martin and Anjali Bhardwaj, "Implications for South Asian Countries of Abolishing the Multifibre Arrangement", World Bank, November 2001; and Satinder Bhatia, "Indian Garments Industry in the Post-MFA Period", Indian Institute of Foreign Trade, February 1997).

[30] Gary Gereffi and Olga Memedovic, op. cit, p. 8. This international subcontracting system exists worldwide. In the United States, it is called the 807/9802 programme or "production sharing", with sourcing networks predominantly located in Mexico, Central America and the Caribbean. In Europe it is known as outward-processing trade, and the principal suppliers are in North Africa and Eastern Europe. In

textiles producers in the importing countries, a development that has permitted them to regain a competitive edge in the textiles sector, which is generally capital- and technology-intensive. In the process, the non-preferred countries have seen their shares in markets decline or stagnate, and the removal of quota restrictions will only partly restore the balance.

Closed investment and trade loops between the two major trade partners and their "preferred" countries are indicated in tables 5 and 6 in the Annex. The figures in these tables are import and export ratios of the United States and the EU with their "preferred" suppliers and non-"preferred" ones. As shown in the Tables, there is a stunningly high trade of textiles and clothing in the US and the EU with their respective "preferred" suppliers as compared with non-"preferred" ones. In the light of the lifting of quotas under the ATC, it seems unlikely that the close investment and trade loops would be disturbed unduly, let alone displaced. While this is so, it is also important to know that other factors such as lower-cost production could offset the advantage of preference.

Changes in investments and sources of supply

Concerns have been expressed about possible consolidation of investments as the result of quota lifting. However, as discussed, in addition to quota availability, factors such as proximity to markets, availability of preferential access and preferential rules of origin are very important for determining locations of foreign investments. Also, an industrial survey indicated that the five highly important factors in private-sector decisions on foreign investment locations are labour costs; policies affecting investment and international trade; politics and stability; policies affecting labour, health and environment; and quality of transportation infrastructure. Moreover, some developing countries that are situated near textile exporters have become important exporters of clothing promoting South–South trade.

Industry experts predict that large retailers will rationalize and consolidate their suppliers after the ATC expiry, while under the quota system suppliers had to be dispersed across different countries. Given the distorting effect of the quota system, some adjustments are likely in this respect, but again, other counterbalancing factors such as increasing demand for flexible production and shipment, as well as the search for preferential tariff access, which will continue in the post-ATC period for LDCs and other preferred countries, should not be discounted. Moreover, retailers, particularly in the United States, are increasingly leaning to intermediaries that could provide competitive "full-product packages". In order to meet the exigent and varying demands from retailers, intermediaries need to keep global networks of sub-contractors that could supply items of specialized product lines.

Asia, manufactures from relatively high-wage economies such as Hong Kong (China) have outward processing arrangements with China and other low-wage countries.

The impact of China's entry into the WTO

China's entry into the WTO has been seen as another major factor increasing competition in trade in textiles and clothing, and its impact has been debated. China acceded to the WTO on 11 December 2001. A surge of textiles and clothing exports from China after the ATC's expiry has often been predicted, but these exports would possibly be restricted by several conditions agreed to in China's WTO accession negotiations. First, Chinese textiles and clothing are subject to the special textiles safeguard provision until 31 December 2008, and the United States and the EU have already invoked this mechanism. Second, from 2009 to 2013, WTO members can apply a standard WTO safeguard mechanism selectively targeting only China. Third, application of the market economy principle to China in determining anti-dumping and countervailing measures is deferred for 15 years after the date of accession until December 2016.

There are other factors which are likely to affect Chinese textiles and clothing exports. It is not rational from a strategic point of view that retailers and intermediaries rely on a single source of supplies. The capacity of the Chinese textiles and clothing industry to respond to international demand has been questioned as well. Also, a revaluation of China's national currency — the Renminbi — may possibly reduce the cost advantage of China's exports. Moreover, costs of production are likely to increase as the Chinese economy progresses. In addition, it has been argued that other Asian countries such as India, Indonesia and Viet Nam are catching up with China in terms of favourable unit labour costs.[31] As discussed above, the growing trend of "lean retailing" requires a quick response from suppliers, but it has been reported that the lead-time for Chinese production is often a few months. Also, the Chinese industry is reported to be weak in design and fashion capabilities.[32] All these factors are constraining Chinese export growth, and caution needs to be exercised against overestimating the ability of China to go significantly beyond the strong position it has already built for itself.[33]

The role of tariffs

Tariffs on textiles and clothing remain the highest among industrial products in developed countries. The average post-Uruguay Round tariffs on textiles and clothing for the three major industrial country markets are 14.6 per cent for the United States, 9.1 per cent for the European Union and 7.6 per cent for Japan, while their average industrial tariffs are 3.5 per cent, 3.6 per cent and 1.7 per cent, respectively. Furthermore, as table 7 in the Annex indicates, disaggregated data reveal that remarkably high tariffs are imposed on textile products. As regards the post-Uruguay Round rates, 52 per cent of textiles and clothing imports in the United States have tariff rates of 15.7 per cent to 35 per cent, 54 per cent of EU imports have duties of 10.1 per cent to 15.0 per cent, and 55 per cent of Japanese imports have duties of 5.1 per cent to 10.0 per cent. Consequently, countries

[31] Nordas, op. cit., p. 23.
[32] Nordas, op. cit., p. 23.
[33] The United States has already imposed seven safeguard measures on Chinese textile imports, and on 10 June 2005, China and the EU agreed a deal that will manage the growth of Chinese textile imports to the EU until 2008.

benefiting from duty-free access under reciprocal and non-reciprocal preferential arrangements will continue to have significant tariff preference margins after the expiry of the ATC.

Implication of non-preferential rules of origin

Non-preferential rules of origin have a direct impact on trade in textiles and clothing. However, the WTO Dispute Settlement Case "United States – Rules of Origin for Textiles and Apparel Products" showed that it is difficult for affected countries to prove that they are impacted by such rules.[34] In July 1996, under Section 334 of the Uruguay Round Agreements Act, the United States modified its non-preferential rules of origin for textiles and clothing. The EU countries and India were affected and considered those changes inconsistent with the Agreement on Rules of Origin (ARO), which prohibits the use of non-preferential rules of origin for trade policy purposes, and they initiated dispute settlement proceedings against the United States.[35] The dispute between the European Union and the United States was settled through a *procès-verbal*, and the United States introduced legislation modifying the Section 334 to accommodate the European Union's particular export interests. However, India's problem remained, and the dispute settlement panel was established.

India argued that the structure of the changes, the circumstances under which they were adopted and their effect on the conditions of competition for textiles and apparel products suggested that they serve trade policy purposes. However, the panel ruled in favour of the United States, arguing that India had failed to show how the purported US measures undermined Indian textile exports. This ruling may have serious systemic implications from the point of view of developing countries that export textiles and clothing, and do not have preferential trade agreements with the major importing countries and hence are not covered by preferential rules of origin, because it permits the goalpost relating to non-preferential rules of origin to be shifted at will and act as an entry barrier.

GSP schemes of the major importing countries

In July 2004, the European Commission made a proposal for a new GSP system covering the period 2006–2015.[36] One of the objectives of the new GSP programme is to give benefits to countries that most need them, particularly LDCs and the most vulnerable developing countries, such as "small economies, land-locked, small islands and low-income countries". This objective is to be achieved by making the threshold of

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[34] WTO document, "United States – Rules of Origin for Textiles and Apparel Products",WT/DS243/R, 20 June 2003.

[35] The relevant WTO documents are (for the European Union) WT/DS85/1, WT/DS151/1 and WT/DS151/10, and (for India) WT/DS243/1 and WT/DS243/R.

[36] Communication from the Commission to the Council, the European Parliament and the European Economic and Social Committee, "Developing Countries, International Trade and Sustainable Development: The Function of the Community's Generalised System of Preferences (GSP) for the Ten-Year Period from 2006–2015", Commission of the European Communities. COM(2004)461 final, Brussels, 7 July 2004.

competitiveness determining graduation criteria lower. Also, the proposal recognized the need to ease the rules of origin in order to increase the utilization rate of the GSP and South–South cooperation, and it suggested simplifying the administrative rules and procedures as well as amending the origin criteria and cumulation rules.

The new GSP scheme has three types of arrangements, while the previous scheme had five. The three arrangements are: (i) a general arrangement (reduction of 3.5 per cent on the normal customs duty for sensitive products, and reduction of duties to zero for non-sensitive products); (ii) Everything but Arms initiative giving duty-free and quota-free access for all products for LDCs; and (iii) a new "GSP-plus" providing special benefits for vulnerable countries that meet the new objective criteria for sustainable development and good governance (reduction to zero duty for a total of 7,200 products). For the first category, nearly 300 additional products are included.

The new GSP replaces the current criteria for "graduation", namely share of preferential imports, development index and export specialization index, with a single, straightforward criterion. For textiles and clothing when a group of products ("section" of the EU customs code) from a particular country have exceeded 12.5 per cent of total EU imports of the same products under the GSP over the previous three consecutive years, and for other products, the corresponding threshold is 15 per cent. A prominent NGO has argued that the new mechanism of graduation would do more damage than good.[37] The criteria proposed for the graduation is EU imports under GSP instead of all EU imports, which could make a developing country graduate from the GSP just as it begins to get its foot on the ladder. Also, it was noted that the proposals for the rules of origin were disappointing as they hardly add any changes to its existing rules of origin for the GSP. On 10 February 2005 the European Commission proposed that the EU launch its new GSP scheme, which took into account the tsunami-affected countries, from 1 April 2005 until 31 December 2008.[38] No reference was made to the rules of origin in this proposal.

The GSP programme of the United States excludes textiles and clothing, except under the benefits granted to sub-Saharan African countries by the African Growth and Opportunity Act (AGOA). For the US GSP scheme to be highly effective, any future improvements of the programmes will have to extend preferential treatment to textiles and clothing products.[39]

Salience of duty- and quota-free access for LDCs

Although initiatives to provide duty- and quota-free access to LDCs' products have contributed to the notable growth of garment exports from LDCs, preferential rules

[37] "New trade preferences unfair to developing world", SUNS, 25 October 2004, and "EC Proposes Revisions to GSP Scheme for Developing Countries", *International Trade Daily*, 21 October 2004.
[38] EU Trade Issues, "Asia, GSP: The new EU preferential terms of trade for developing countries", Brussels, 10 February 2005, http://europa.eu.int/comm./trade/issues/bilateral/regions/asem/memo100205_en.htm
[39] "Trade Preferences for LDCs: An Early Assessment of Benefits and Possible Improvements", UNCTAD/ITCD/TSB/2003/8, UNCTAD, 2003, pp. 11–15.

of origin and complex administrative requirements have been identified as obstacles to making such initiatives fully effective.[40] In this regard, the recent development in the United States on rules of origin is welcome. The US has extended the special "third-country" fabric rule under AGOA until 30 September 2007. Flexible preferential rules of origin are an important factor in the development of local industries in beneficiary countries. They are also essential for promoting South–South trade and investment, as well as regional cooperation.

The importance of flexible preferential rules of origin for development is indisputable. However, experience so far suggests the necessity of other measures for the development of local industries. For example, many AGOA beneficiaries benefit from flexible rules of origin, which allow preferential access to garments made from domestic, regional and "third-country" inputs. The flexible rules of origin are supposed to encourage the development of local and regional cotton-based textile industries, but up to now local and regional content in the relevant countries' garment exports has remained very low. While preference-receiving countries benefit from exports of low-value-added garments, without measures to enhance supply capacity, they could be stuck at the low end of the production chain, which is vulnerable to international competition.

The United States does not provide preferential access for textiles and clothing from Asian LDCs, exports from these countries being subject to MFN rates. Given the tariff peaks on textiles and clothing and the high proportion of textile products in these countries' export basket, this leads to a perverse situation in which these countries are taxed disproportionately. For example, Cambodia's exports to the United States face a total of $152 million in tariff duties, while Norway's face just $24 million, even though the total value of Norway's exports is five times higher than that of Cambodia's.[41] Similarly, duties of $314 million were imposed on Bangladesh's $2 billion worth of textiles and clothing exports to the United States in 2001, while in the same year duties of only $330 million were imposed on France's entire exports to the same country, which amounted to $30 billion.

Recently, it was reported that a group of LDCs, including Bangladesh, Nepal, Cambodia, Afghanistan, Bhutan, Timor-Leste, and some Pacific island countries, is lobbying for duty-free access to the US market for their products, including textiles and clothing.[42] The group has dubbed itself the "Left Behind" coalition and is seeking preferential access to the United States in order to enhance their ability to compete in the country after the ATC's expiry. The removal of such tariff discrimination against Asian LDCs would considerably assist poverty alleviation through textiles-related production and trade revenues.

[40] For example, see *Trade Preferences for LDCs: An Early Assessment of Benefits and Possible Improvements,* UNCTAD/ITCD/TSB/2003/8, UNCTAD, 2003.
[41] "Stitched Up: How Rich-Country Protectionism in Textiles and Clothing Trade Prevents Poverty Alleviation", Oxfam Briefing Paper 60, April 2004, p. 12.
[42] "Developing Nations Seek Preferential Access to United States for Textiles, Other Products", *International Trade Daily*, 2 November 2004.

Contingency protection measures

Contingency protection measures have crucial importance for developing-country exporters of textiles and clothing. The restraining countries initiated numerous cases after the ATC took effect. For example, the European Union alone initiated 53 anti-dumping cases in the textiles and clothing sector between 1994 and 2001.[43] The United States had invoked 28 special safeguard measures under the ATC by October 2001.[44] The contingency measures were used for imports under quota restrictions and were targeted at individual enterprises, often small and medium-sized ones, which do not have adequate resources for defending their actions.

The damaging effects of anti-dumping actions are of particular concern. Many of the anti-dumping filings could be termed “process filers” that significantly hindered foreign exports during the investigation itself. A study found that anti-dumping duties on average have caused the value of imports to contract by 30 to 50 per cent.[45] Moreover, the potential threat of an anti-dumping action could force a firm to sell the product in question at a much higher price than it would have under normal circumstances. An exporting firm’s pricing behaviour to avoid an anti-dumping duty could result in suboptimal use of its competitive advantage.[46]

Against this background, the International Textiles and Clothing Bureau (ITCB) member countries have proposed to the WTO that developed Members implement a grace period of two years after the ATC expiry during which they do not initiate investigations into imports of textile and clothing products from developing countries.[47] This proposal was based on the Doha Ministerial Declaration and the Decision on Implementation-Related Issues and Concerns.[48] Given the distortions caused by the long-standing managed trade in this sector and the failure to use the transition period provided by the ATC to cushion the impact on protected industries, the restricting countries have a strong moral case in supporting the ITCB proposal and also refraining from using other contingency protection measures motivated by protectionist purposes.[49] Most recently,

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[43] WTO document “Anti-Dumping Actions in the Area of Textiles and Clothing: Developing Members’ Experiences and Concerns”, TN/RL/W/48/Rev.1, 5 February 2003, p. 2.
[44] WTO document G/C/W/325, p. 14.
[45] T. J. Prusa, “On the Spread and Impact of Antidumping”, Working Paper 7404, NBER Working Paper Series, 1999.
[46] B. A. Blonigen and T. J. Prusa, “Cost of Antidumping: Devil Is in the Details”, NBER Working Paper Series, 2002.
[47] WTO document "Anti-Dumping Actions in the Area of Textiles and Clothing: Proposal for a Specific Short-Term Dispensation in Favour of Developing Members
Following Full Integration of the Sector into GATT 1994 from January 2005", WT/GC/W/502, 14 July 2003.
[48] The former agreed to improve disciplines under the Agreements on Implementation of Article VI of the GATT 1994, and the latter calls for the examination of Article 15 of the Anti-Dumping Agreement relating to special and differential treatment of developing countries with a view to operationalizing it as a mandatory provision.
[49] The IMF/World Bank joint study echoed this concern, noting that "the back-loading of effective liberalization under the ATC is particularly unhelpful, as it turns out what could have been a gradual adjustment process into a shock at the end of the transition period…This raises concerns that political pressures might spark greater recourse to other forms of protection once quotas are phased out, with trade

concerns have been also expressed regarding a possible revival of voluntary export restraints (VERs), which are clearly prohibited by WTO rules and disciplines.

Market entry and non-tariff barriers

While tariffs do not block market entry – although they can make it prohibitive when duties are relatively high – market entry and non-tariff barriers can effectively block market entry for exporters that are unable to comply with often complex and stringent internal regulations and standards. Compliance with the latter is often difficult and costly for exporters. These barriers will remain significant constraints for developing-country exporters, and they need to be addressed adequately in order to reap the gains of ATC termination.

Regulatory measures comprise the major form of market entry and non-tariff barriers for textiles and clothing exports. They may include customs and other documentation formalities, non-uniform classification practices with respect to the same products, rules of origin (including stricter rules for eligibility to preferences), health and other sanitary and phytosanitary (SPS) prescriptions, technical barriers to trade (TBT) requirements, competition and social-condition-related requirements.[50] Importing countries often unilaterally impose these measures without consulting exporters that will be affected by them.

As just one example of an elaborate and complex trade-restrictive TBT/SPS non-tariff barrier, a new system called REACH (Registration, Evaluation and Authorization of Chemicals) has been proposed in the European Union. If adopted, the REACH legislation could make EU textiles and clothing firms subject to a procedure of registration, evaluation, authorization and restriction for a large number of chemical substances. In the Committee on Technical Barriers to Trade in the WTO, both developed and developing countries have expressed their concerns about the proposed EU initiative. A report from the US Department of Commerce noted that some 30,000 chemical substances would be subject to this measure and that the US textile industry would be widely affected, as technical requirements and testing procedures would be complex, time-consuming and costly.[51] Given that even the world's most industrialized country would encounter significant costs and difficulties in complying with REACH, the extent of the impact on developing-country industries could be severe.

In addition to technical market entry barriers, anti-competitive practices of dominant firms in the sector also give rise to significant market entry barriers. For example, developing-country clothing producers often experience great difficulties in

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remedy actions…becoming a new 'line of defence'", "Market Access for Developing Country Exports-Selected Issues", para. 68.

[50] ITCB document "New Non-Tariff Requirements", CR/37/EGY/7, 7 April 2003.

[51] US Department of Commerce, "Second Report to the Congressional Textile Caucus on the Administration's Efforts on Textile Issues", October 2003, p. 6.

entering developed-country markets unless they are accepted as suppliers by firms controlling major distribution networks.[52]

While apparel retailers in the major importing countries face intense competition in their domestic markets and seek low-cost producers globally, these actions are criticized by labour unions and NGOs, which claim that labour conditions in supplying developing countries are poor. Apparel retailers are thus pressured to impose tough labour conditions on their suppliers through private codes of conduct in order to avoid damaging publicity in their home countries. In fact, studies report cases of extremely poor working conditions in textiles and clothing factories in developing countries, and there is a danger that working conditions will deteriorate after the quota elimination as competition intensifies and pressures to cut prices increase.[53] Ensuring adequate labour conditions is a legitimate concern, and it is essential that Governments enforce the labour laws so as to gradually meet the norms of the ILO conventions.[54]

The problem for textiles and clothing factories in developing countries is that conditions imposed by buyers are often arbitrary, unpredictable and exceed the ILO labour standards, but these factories are forced to accept those conditions given the significant power that buyers possess. NGOs might have a genuine and legitimate concern; however, labour-standard issues can be inspired by protectionist motives of labour unions to hinder outsourcing of textiles manufacturing to developing countries by nullifying the cost advantage that these countries have.

In the post-ATC phase, the problems that developing-country exporters of textiles and clothing face regarding private codes of conduct can be aggravated. In the post-ATC environment, competition between domestic and foreign firms in the restricting countries will intensify, and industry analysts predict that international contractors will increase pressure on business partners in developing countries with respect to social conditions such as labour and environment. The challenge for developing countries is how to counter the problems of private codes of conduct. Individual exporters in developing countries have practically no bargaining power vis-à-vis the powerful large retailers, which may act at the behest of protectionist-minded labour unions interested in price equalization by imposing conditions going beyond the ILO norms. Also, there is no mechanism in the international organizations for addressing the systemic aspects and implications of such codes.

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[52] UNCTAD, "Report of the Expert Meeting on Market Entry Conditions Affecting Competitiveness and Exports of Goods and Services of Developing Countries: Large Distribution Networks, Taking into Account the Special Needs of LDCs", TD/B/COM.1/66, 19 January 2004.

[53] UBINIG, "Options for Women in the Textiles and Handloom Sector in Bangladesh", in *Trade, Globalisation and Gender: Evidence from South Asia*, edited by Veena Jha, UNIFEM and United Nations, 2003, pp. 244 and 248, and "Impact of the WTO on Women Workers in Sri Lanka" in *Trade, Globalisation and Gender: Evidence from South Asia*, p. 352.

[54] The ILO Declaration on Fundamental Principles and Rights at Work, adopted in June 1998, defines basic labour rights as (a) freedom of association and the effective recognition of the right to collective bargaining; (b) elimination of all forms of forced or compulsory labour; (c) effective abolition of child labour; and (d) elimination of discrimination in respect of employment and occupation.

Private codes of conduct are based on the concept of corporate social responsibility, and increasing emphasis has been placed on this concept for the textile and clothing industries. For example, in its report, the European Commission deemed corporate social responsibility to be a high priority for the EU textiles and clothing sector.[55] This responsibility largely pertains to the environment and labour conditions, and its importance is stressed owing to the sector's highly internationalized supply chain. The premise of corporate social responsibility is to be a good global-corporate citizen, but this responsibility should not be so onerous that it unfairly penalizes producers and exporters in developing countries and becomes a disincentive to invest there.

[55] European Commission, "The future of the textiles and clothing sector in the enlarged European Union", COM(2003) 649 final, Brussels, 29.10.2003

IV. Ensuring and maximizing development gains

Significant challenges lie ahead for textiles and clothing exporters in developing countries, and to ensure and maximize development gains after the ATC's expiry, the issues set out below need to be addressed.

Strengthening the participation of developing countries in the dynamic sector world trade

The textiles and clothing industry is a mature sector, but it will continue to be a dynamic sector driven by demand, change in demography, increasing living standard, and emerging opportunities arising from new trends in the international production and distribution of textiles and clothing. This is the area where developing countries have comparative advantage, but the competitiveness will depend on national and enterprise strategic engineering of dynamic products. The UNCTAD Expert Meeting on Strengthening Participation of Developing Countries in Dynamic and New Sectors of World Trade, held in Geneva in February 2005, stressed that in the post-ATC competition environment, developing countries that export textiles and clothing need to find niche products which are in increasing demand, contain higher value-added and generate wider profit margins. Opportunities for developing such products can be seized by tapping into the value chain of textiles and clothing production or by diversifying into technical textiles which are increasingly used in non-traditional areas such as medicine, environment, construction, civil engineering and agriculture. The advantage of developing niche products is that it does not necessarily require substantial investments.

To create a supportive environment for enhancing the competitiveness of the textiles and clothing sector, the Expert Meeting identified actions required at the national and international levels. At the national level, those include regulatory reform in the areas of energy, telecommunications, and transport, reform of domestic labour laws, enforcement of intellectual property right laws to protect ingenious products which are developed locally, and investments in infrastructure, including customs. At the international level, measures identified are improving market access for textiles and clothing through reduction of tariffs and non-tariff barriers, improving the effectiveness of the non-reciprocal preferential trade agreements, back-rolling protectionist measures and promotion of South–South cooperation. The detailed findings and recommendations of the Expert Meeting can be found in the Annex.

The need for adequate support measures

Support measures are necessary, especially for LDCs and small economies, in order to offset the impact of increased competition in the global market as quotas are removed. Intensified competition in the post-ATC period is expected to cause significant adjustments in the sector, and thus providing adequate assistance to enable affected workers to adjust, retrain and find alternative jobs will be a post-ATC priority issue. Sensitivity to the needs of women will be particularly important, as the textiles and clothing sector is traditionally a major employer of women, and studies find that they are likely to be the first affected.[56] The social and economic impact could be considerable, as women often provide vital financial support for their families, while their opportunities for alternative employment are limited.

Government measures are required in order to strengthen supply capacity in affected countries, as well as financial and technical assistance from industrialized countries and the international community. Other support measures recommended are building reserves through cooperation between retailers and suppliers and temporarily providing LDC-equivalent preferences for some small economies that are highly vulnerable owing to their greater dependency on textile products for their exports and GDP.[57] The Trade Integration Mechanism (TIM) introduced by the IMF in April 2004 is designed to assist member countries in meeting balance-of-payments shortfalls that might result from multilateral trade liberalization, including the ATC expiry.[58] Other donor-supported mechanisms such as the Trade Adjustment Fund recently proposed by the EU could also be considered forms of sectoral adjustment aid to affected developing countries. Moreover, as discussed below, improvement of non-reciprocal preferential access and preferential rules of origin would help to overcome the rigours of ATC expiry. At the Expert Meeting referred to above optimism was expressed that basic requirements for competitiveness exist in these countries and that competitiveness can be maintained if adequate financial resources are available to upgrade technologies and to train workers.

Improvement of non-reciprocal preferential access and preferential rules of origin

Provision of non-reciprocal preferential access to textiles and clothing from developing countries and LDCs could make an important contribution to the development of those countries in the post-ATC phase. For the current non-reciprocal preferential schemes to work effectively, they must be sensitive to the special needs of developing countries and LDCs, and provided in an impartial and non-discriminatory manner. Inclusion of textiles and clothing in the GSP, inclusion of Asian LDCs in the US preferential scheme, and reducing stringent conditionalities attached to preferences while increasing preference margins would not only cushion the shock of quota lifting but also provide trade solutions to the problems associated with the removal of quotas.

One of the elements for improving the non-reciprocal preferential agreements concerns rules of origin. For example, highly flexible rules of origin for the Canadian preferential scheme for LDCs, as well as the “third-country” fabric rule applied under AGOA (although ideally the rule should be made permanent), are crucial for promoting regional development and South–South cooperation.

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[56] For example, Bhattacharya Debapriya, “The Post-MFA Challenges to the Bangladesh Textile and Clothing Sector”, in *UNCTAD: Trade, Sustainable Development and Gender*, United Nations, 1999, and Veena Jha, edited, *Trade, Globalization and Gender: Evidence from South Asia*, UNIFEM and United Nations, 2003.

[57] “Stitched Up: How Rich-Country Protectionism in Textiles and Clothing Trade Prevents Poverty Alleviation”, Oxfam Briefing Paper 60, April 2004, p. 12.

[58] The IMF evaluates requests for TIM in the light of a country's overall debt and balance-of-payments position as the TIM increases lending from the IMF and raises external debt levels.

Market access negotiations under the Doha Work Programme

In the context of new tariff negotiations taking place in the Negotiating Group on Market Access for Non-Agricultural Products, Governments meeting in Doha in 2001 decided "by modalities to be agreed, to reduce or as appropriate eliminate tariffs, including the reduction or elimination of tariff peaks, high tariffs, and tariff escalation, as well as non-tariff barriers, in particular on products of export interest to developing countries. Product coverage shall be comprehensive and without *a-priori* exclusions" (para. 16 of the Doha Declaration). Full account is to be taken of the special needs and interests of developing and least developed countries, "including through less than full reciprocity in commitments, in accordance with the relevant provisions of Article XXXVIII bis of GATT 1994".

Developing countries have demanded that the tariff peaks be eliminated, but countering this demand, the industrialized countries have insisted that developing countries carry out reciprocal liberalization and that the textiles and clothing sector be included in the sectoral negotiations. Such negotiations aim at rapid and full liberalization of the sectors concerned, and countries participating in the negotiations would have to agree to eliminate all tariffs and non-tariff barriers in the sector on a negotiated specific timetable. While modalities are yet to be fully determined, one of the key proposals in the General Council Decision of 1 August 2004, Annex B, that is to serve as the basis for further work in this area, confirms the intention to use the Chair's Draft Elements of Modalities[59], which proposed that textiles and clothing be included in the sectoral negotiations, as a reference for the ongoing work for the NAMA negotiations.

Developing countries are insisting that their participation in the sectoral negotiations be voluntary. Although textiles and clothing exports from developing countries have grown significantly, the industries remain largely low-value-added in many developing countries, and they would not be ready for sweeping liberalization. Moreover, the sector is a significant source of employment for many developing countries and contributes very substantially to household production.[60] Sweeping liberalization of the sector in these countries would be counterproductive for poverty alleviation, particularly when they also have to go through adjustments because of the quota elimination.

The right of developing-country WTO members to pursue progressive liberalization is ensured by the WTO rules, and this right must be respected for the textiles and clothing sector. On the other hand, developing countries that are gaining competitiveness in the sector should progressively liberalize the sector. Further analysis is required in order to identify effective ways of liberalization, including on a South–South basis through the Global System of Trade Preferences among Developing Countries negotiations. Also, the NAMA negotiations must be sensitive to erosion of

[59] WTO document "Draft Elements of Modalities for Negotiations on Non-Agricultural Products: Revision", TN/MA/W/35/Rev.1, 19 August 2003.

[60] For example, in India the sector provides employment to about 38 million people and is the largest employer after agriculture.

preferences for LDCs and small-economy countries to avoid causing additional difficulties in respect of the problem caused by quota-lifting.

Using regional trade agreements to sustain developing countries' textile and clothing exports

Regional trade agreements (RTAs), including those involving the major importing countries, will continue to expand in the post-ATC period. Examples of ongoing or recently concluded negotiations for such agreements are the US–Central American Free Trade Agreement, the Free Trade Area of the Americas, the United States Middle East Free Trade Area Initiative, the Euro-Mediterranean Association Agreements and the EU–Mercosur agreement. Textiles and clothing will be important components of these agreements. For the major importing countries, promotion of use of their inputs is an important objective of the rules of origin, while for preferred countries it can diminish the competitiveness of their garment exports and hinder their movement up the value chain. Also, it hinders South–South trade and investments. As noted in the earlier section entitled "Costs for non-preferred developing countries", RTAs could significantly increase exports of textile products from preferred countries and contribute to their economies. At the same time, such agreements should also contribute to the promotion of South–South cooperation to mitigate the discriminatory effects of North–North and North–South RTAs. For this to happen, rules of origin are an essential ingredient. Moreover, rules of origin should have minimum criteria ensuring that the exporting LDCs or developing countries themselves contribute to a transformation process, while making allowance for these countries' limitations and their need to benefit from investment in modern technology.

Conclusions

The managed trading system which restricted exports of textiles and clothing from developing countries finally came to an end. The ATC termination is part of the Uruguay Round Agreement which established the WTO. The end of the ATC contributes to the "upholding and safeguarding of an open, non-discriminatory, predictable, rule-based, and equitable multilateral trading system", an objective of the international community recently affirmed in the São Paulo Consensus adopted at UNCTAD XI in June 2004. It will also contribute to the realization of the United Nations Millennium Development Goals, correcting the distortion created by the MFA and allowing developed and developing countries to achieve substantial income gains.

Both developed and developing countries stand to gain substantially from the removal of the quota restrictions and the full integration of textiles and clothing into normal WTO rules. Developing countries with a comparative advantage in the sector should see their production and exports increase in a post-ATC world, and in developed countries, lower prices for clothing will mean that consumers should be big winners. Such predictions are, of course, based on the premise that major developed countries will avoid filling the ATC void with a barrage of new barriers. Should they refrain from such trade distortions, developing-country firms that respond to market demands, move up the value chain, and capture niche markets are poised to reap substantial gains in a post-ATC world.

Certain countries and certain segments of the industry are likely to experience some dislocation and therefore to require assistance with post-ATC adjustment. However, the post-ATC picture needs to be seen in its proper perspective, as there are several factors and assumptions that come into play in determining the extent, type and scope of the post-ATC impact. LDCs and small economies might feel the impact of ATC expiry most, and providing support measures to them would be a priority. There are outstanding issues that could affect development gains to be reaped from ATC expiry, and these must be addressed properly. Giving in to protectionist demands to replace the quota protection by a plethora of protectionist non-tariff barriers, including contingency measures, would amount to taking away with one hand what ATC expiration gives with the other.

The dynamics of textiles and clothing trade will be influenced by the factors discussed above, while the international market for textile and clothing products continues to grow as the world's population, incomes and standards of living increase. Also, the economies of some populous developing countries are growing fast, and markets in the South will thus become increasingly important for textiles and clothing exporters. The sector further provides tremendous opportunities and prospects for developing countries given their leverage with respect to labour costs, as well as the possibility for positive spillover effects into other sectors, particularly upstream commodities sectors and downstream industries.

Current attempts in the WTO to carve out textiles and clothing with the objective of keeping market share should be resisted, as this would negate the integration of the products into the normal trading system. For the issue of the post-ATC adjustment in the vulnerable economies the important question is whether displaced workers could be absorbed by alternative economic activities. In this light the issue needs to be dealt with in the context of overall trade liberalization adjustment and economic reform.

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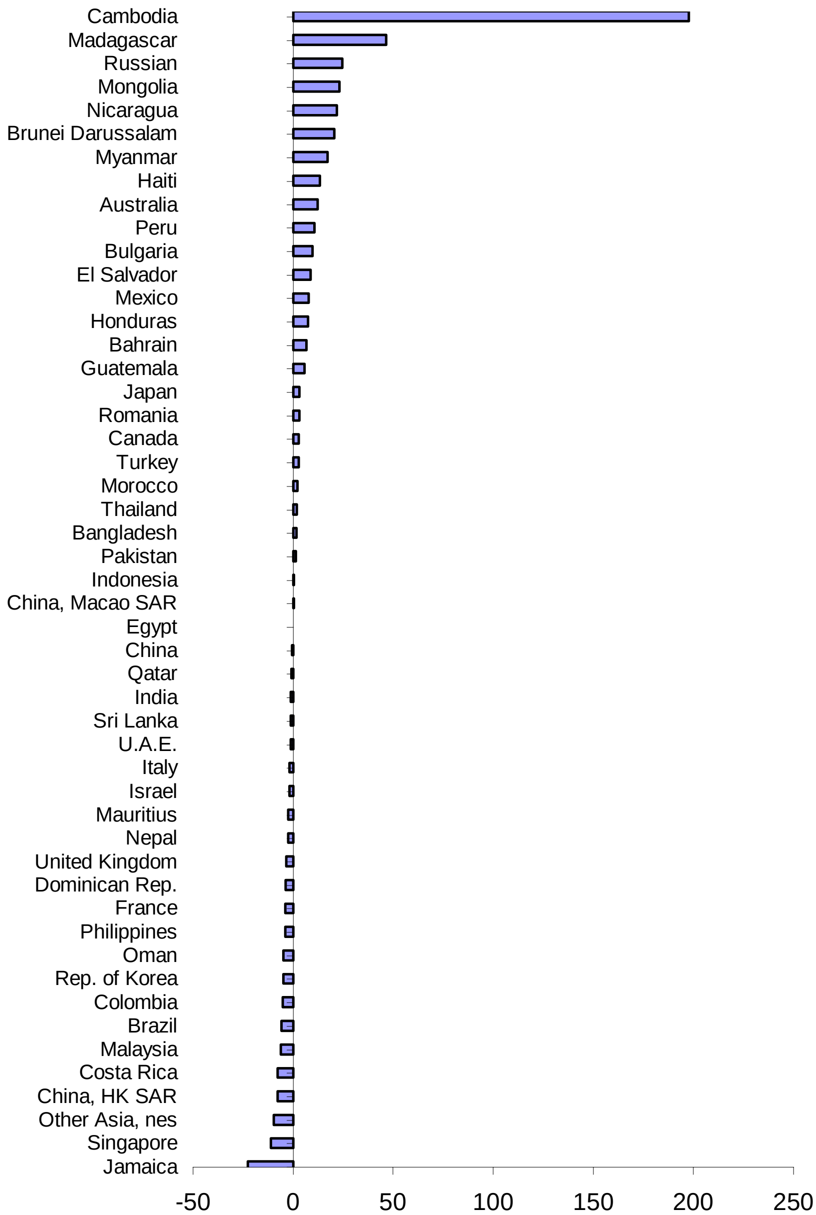
Annex

Table 1. History of international trade in textiles and clothing

Date	Action taken
1957: January	Five-year agreement reached with **Japan** on limiting overall textile exports to **USA**.
1958: November	**United Kingdom** signs "voluntary" limitation on cotton T&C products with **Hong Kong**, by threatening otherwise imposition at lower than prevailing volume levels.
1959: September	**United Kingdom** signs similar restraint agreements with **India** and **Pakistan**.
1960: November	GATT Contracting Parties recognize the problem of "market disruption", even if it is just threatened; serves as "excuse" for establishing future NTBs.
1961: July	The Short Term Arrangement (STA) is agreed upon.
1962: February	The Long Term Arrangement (LTA) is agreed upon to commence on 1 October 1962, and last for five years.
1966: June	The **United Kingdom** implements a global quota scheme in violation of the LTA – the LTA providing only for product-specific restraints.
1967: April	Agreement is reached to extend the LTA for three years.
1969–71	**United States** negotiates VERs with **Asian suppliers** on wool and man-made fibres.
1970: October	Agreement is reached to extend the LTA for three years. It was later extended three months more, to fill the gap until the MFA came into effect.
1973: December	The MFA is agreed to commence on 1 January 1974, and to last for four years.
1977: July–December	The **European Economic Community** and the **United States** negotiate bilateral agreements with developing countries prior to agreeing to extension of the MFA.
1977: December	The MFA is extended for four years.
1981: December	The MFA is renewed for five years. The **USA** is under pressure from increased imports.
1986: July	The MFA is extended for 5 years, to conclude with Uruguay Round.
1991: July	The MFA is extended pending the outcome of the Uruguay Round negotiations.
1993: December	The Uruguay Round (UR) draft final act provides for a 10-year phase-out of all MFA and other quotas on textiles in ATC. MFA extended until UR comes into force.
1995: January 1	1st ATC tranche liberalized by importing countries – 16% of 1990 import volume.
1998: January 1	2nd ATC tranche liberalized by importing countries – 17% of 1990 import volume.
2002: January 1	3rd ATC tranche liberalized by importing countries – 18% of 1990 import volume.
2005: January 1	4th ATC tranche liberalized by importing countries – 49% of 1990 import volume.

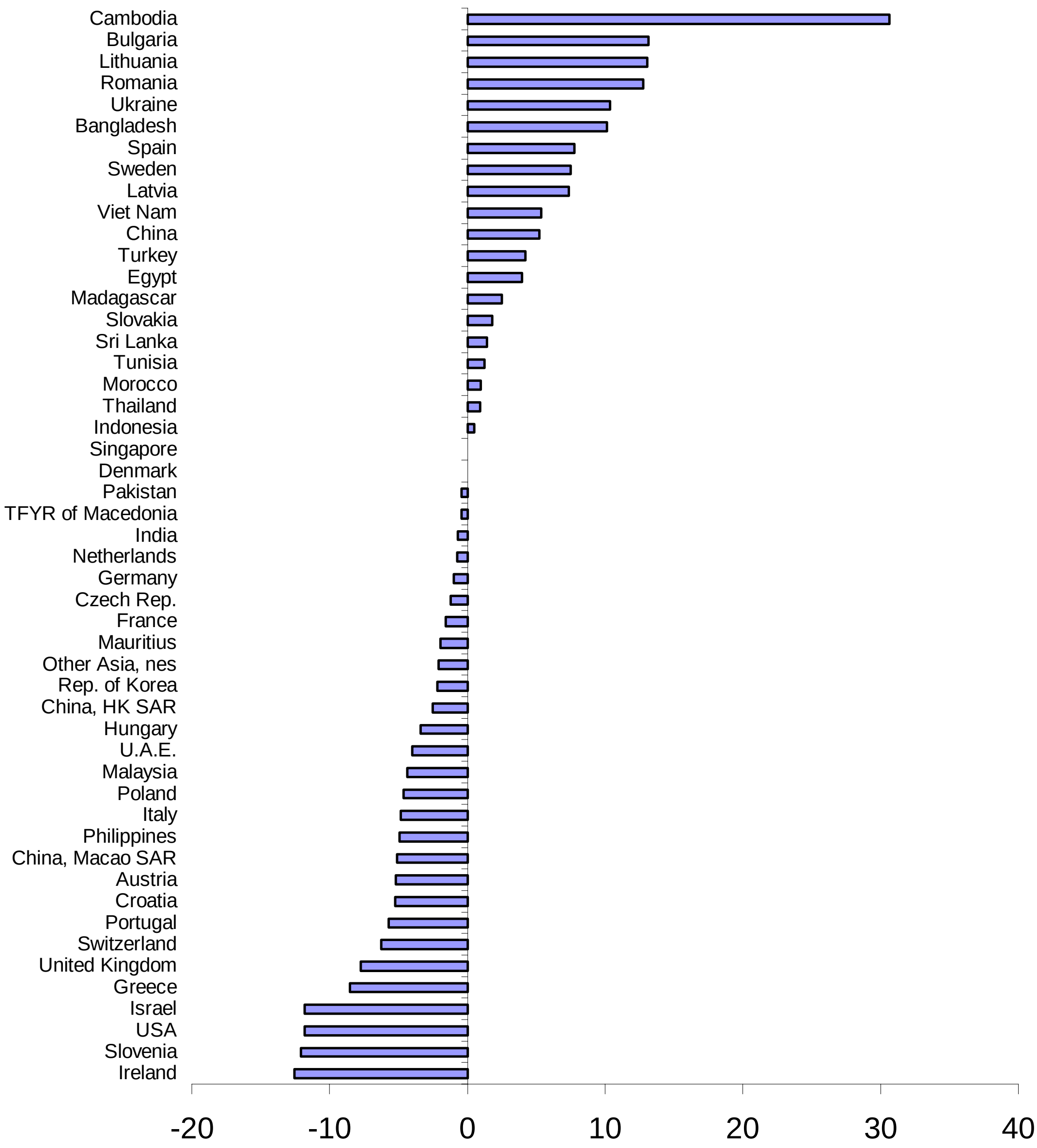
Source: Based on D. Spinanger, "Faking Liberalization and Finagling Protectionism: The ATC at Its Best", Table 1, Background Paper for the WTO 2000 Negotiations: Mediterranean Interests and Perspectives, Cairo, pp. 14–15.

Diagram 1. US imports of clothing by main partner economies: % change in share from 1994 to 2003 (Base year 2000)



Source: UNCTAD.

Diagram 2: EU15 imports of clothing by main partner economies:
% change in share from 1994 to 2003
(Base year 2000)



Source: UNCTAD.

Table 2

Top 20 textile exporters in 2003
(Million dollars and percentage)

	US dollar	Percentage
World	185 596	100.0
EU 15*	59 906	32.3
China	27 176	14.6
China, Hong Kong SAR	13 093	7.1
USA	10 884	5.9
Republic of Korea	10 777	5.8
Taiwan Province of China	9 392	5.1
India	6 856	3.7
Japan	6 426	3.5
Pakistan	6 030	3.2
Turkey	5 263	2.8
Indonesia	2 940	1.6
Canada	2 264	1.2
Thailand	2 195	1.2
Mexico	2 097	1.1
Czech Republic	1 727	0.9
Switzerland	1 499	0.8
Poland	1 144	0.6
Brazil	1 120	0.6
Malaysia	1 022	0.6
Iran (Islamic Rep. of)	793	0.5

Source: UNCTAD.
* Includes intra-EU trade.

Table 3

Top 20 clothing exporters in 2003
(Million dollars and percentage)

	US dollar	Percentage
World	235 825	100.0
EU 15 *	60 721	25.7
China	52 162	22.1
China Hong Kong SAR	23 246	9.9
Turkey	9 963	4.2
Mexico	7 343	3.1
India	6 641	2.8
USA	5 549	2.4
Indonesia	4 151	1.8
Romania	4 069	1.7
Thailand	3 663	1.6
Republic of Korea	3 647	1.5
Bangladesh	3 635	1.5
Pakistan	2 901	1.2
Morocco	2 847	1.2
Tunisia	2 722	1.2
Sri Lanka	2 516	1.1
Viet Nam **	2 490	1.1
Philippines	2 287	1.0
Taiwan Province of China	2 114	0.9
Poland	2 074	0.9

Source: UNCTAD.
* Includes intra-EU trade.
** Includes estimates by the UNCTAD secretariat.

Table 4

Economies where textiles and clothing account for a significant part of exports of goods earnings in 2003

Country	Percentage
Cambodia	85
Haiti	84
Bangladesh	83
China, Macao SAR	83
Northern Mariana Islands	78
Pakistan	70
Lesotho	70
Mauritius	57
Sri Lanka	55
Tokelau	53
Nepal	51
Cape Verde	50
Dominican Republic	43
Lao PDR	42
Tunisia	41

Source: UNCTAD.

Table 5

Ratio of US imports to exports in textiles and clothing with selected trading partners in 2003 (Thousands of US dollars)

	US imports	US exports	Imports/exports
Canada	3 704 240	3 190 797	1.16
Mexico	8 840 939	4 802 979	1.84
ATPA	1 161 397	194 639	5.97
CBI	10 086 994	4 554 809	2.21
China	15 729 281	272 036	57.82
India	3 845 118	30 637	125.51
Pakistan	2 462 431	7 598	324.11
Indonesia	2 602 088	36 676	70.95

Source: UNCTAD.

Table 6

Ratio of EU imports to exports in textiles and clothing with selected trading partners in 2003 (Thousands of US dollars)

	EU imports	EU exports	Imports/exports
EU acceding countries*	26 613 435	14 172 624	1.88
Euro-Med countries	19 678 299	6 917 202	2.84
China	15 526 347	550 602	28.20
India	5 357 854	165 718	32.33
Pakistan	2 664 246	27 284	97.65
Indonesia	2 272 822	132 928	17.10

Source: UNCTAD.

* Cyprus, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, Slovenia, Bulgaria, Romania and Turkey

Table 7. Bound tariff treatment of textiles and clothing imports and average tariffs of industrial products in the three major industrial country markets
(Percentage)

	Distribution of imports													
	Average tariff		Duty-free		0.1per cent-% 5.0per cent %		5.1per cent-% 10.0per cent %		10.1per cent-% 15.0per cent %		15.1per cent-% 35.0per cent %		Over 35per cent %	
United States														
All industrial products	5.4	3.5	10.4	39.5	59.6	42.9	20.4	10.2	2.4	1.3	7.0	6.0	0.2	0.1
Textiles and clothing	16.7	14.6	0.7	4.9	9.2	27.9	27.9	25.9	6.6	8.0	57.7	52.0	0.5	0.0
European Union														
All industrial products	5.7	3.6	23.6	37.7	26.3	34.2	35.5	19.0	13.2	8.2	1.4	0.9	0.0	0.0
Textiles and clothing	11.0	9.1	1.3	5.3	5.3	19.1	29.7	25.5	64.3	54.1	0.1	0.0	0.0	0.0
Japan														
All industrial products	3.9	1.7	34.8	71.0	40.5	16.6	16.7	9.7	5.5	2.0	2.5	0.7	0.0	0.0
Textiles and clothing	11.3	7.6	3.0	4.5	3.3	19.1	33.7	54.7	44.4	21.5	15.6	0.2	0.0	0.0

Source: World Bank, *"The Uruguay Round and Market Access: Opportunities and Challenges for Developing Countries"*, 1995.

Summary of discussions at the UNCTAD Expert Meeting on the New and Dynamic Sectors of World Trade Session on Textiles and Clothing Geneva, 9 February 2005

The textiles and clothing industry is a mature sector, but it will continue to be a dynamic sector driven by demand, change in demography, increasing living standard, and emerging opportunities for innovation, diversification and niche-product development. This is the area where developing countries have comparative advantage, and it contributes significantly to poverty reduction, employment creation, and skill and economic developments in these countries.

During the last two decades textiles and clothing was the second most dynamic product in world trade. Global trade in textiles and clothing totalled $390 billion in 2003. The sector is highly important for developing countries, which supply about 50 per cent of the world market for textiles and over 60 per cent of the world market for clothing. Since 1980, clothing exports from developing countries have increased by a factor of 7 and textile exports by a factor of 5, while the corresponding factors for developed countries were 3 and 2 respectively.

The major importers of textiles and clothing are the United States and the EU, accounting for 22 per cent and 36 per cent (including EU intra-trade) of world imports, respectively, in 2003. China, India, Pakistan, Indonesia and Thailand were the developing countries among the top 20 world textile exporters, whereas for clothing exports, China, India, Bangladesh, Thailand and Pakistan were among the top 20 countries. Also, contrary to the belief that textile trade is dominated by developing countries, the United States and a number of EU countries led by Italy, Germany, France, Belgium and others continue to play leading roles in both the textiles and the clothing trade.

In the post-ATC environment, competition will intensify, and exporters of textiles and clothing will meet heavy pressure for price-cutting. However, at the same time, the post-ATC environment provides opportunities for exporters to get out of the quota captive markets, where competition is severe and profit margins are often low, and to diversify into “dynamic” (as defined below) products with higher valued-added and profit margins. Thus, in the post-ATC competition environment, it is crucial to identify dynamic products, and diversifying into these products becomes all the more important for developing countries exporting textiles and clothing.

Dynamic products in the context of trade in textiles and clothing

There was a general consensus that dynamic products in the textiles and clothing sector would vary from country to country and from market to market, and that the parameters for defining dynamic products would be demand, market access and profit margins. Lifting of quota restrictions has made almost all cotton and man-made fibres (MMF) product lines potentially dynamic. Identifying a dynamic product would be a matter of national and enterprise strategic engineering of niche products through diversification and specialization in the production value chain. MMF products have particularly significant prospects as the demand for the products exceeds supply by about 250,000 tons per year.

Textiles and clothing products for which quota-fill rates were high during the period of the Agreement on Textiles and Clothing, for example cotton and man-made fibre garments, will be dynamic products for the highly restricted countries. Moreover, in the area of traditional product lines small and medium-sized enterprises (SMEs) are investing to follow the trend of “forum shopping”, whereby manufacturers buy inputs such as yarn, fabric and accessories from the most cost-effective suppliers instead of manufacturing them in-house. SMEs are increasingly diversifying to specialized products such as textile accessories, linings, ethnic textiles and special fabrics to capture market niches that emerged under the "forum shopping" system.

Technical textiles that are used for a wide range of areas such as medicine, environment, agriculture, construction, transportation and sport are growing in demand and profitability. Most of the major textile manufacturers in the developing countries are already engaged in rapidly acquiring expertise in technical textiles. The industry forecasts that the world market for technical textiles will increase by 3.5 per cent a year in volume terms, reaching a value of $126 billion by 2010. Also, demand for products with anti-microbial finishes are growing. Examples of such products are anti-microbial-treated cotton T-shirts and trousers. Demand for ethnic textiles is growing in the markets of both the North and the South, where the principal suppliers are India, China, Cambodia and Turkey. China is potentially one of the most dynamic markets for niche products, and an increasing demand is expected for cotton yarns, technical textiles and industrial and tire cord yarn.

In the post-ATC competition environment where there is no quota-secured market, dynamic products offer great potential for developing countries to diversify into higher-value-added products, to differentiate products from competitors and to generate higher profit margins. For LDCs and small countries that might be affected by post-ATC competition, dynamic products could provide new possibilities for export as they do not necessarily require large investments, while providing opportunities for increasing value-added and developing niche markets.

Competitiveness factors for dynamic products

Success factors are productivity, quality, creativity, innovation, speed, reliability, ability to meet social, environmental and security conditions, market access and an enabling domestic environment. Also, attaining competitiveness will require an increase in efficiency in the entire supply chain management. Moreover, to identify niche products and to increase value-added, firms need to understand the value chain of textiles and clothing production. Tariffs and non-tariff barriers are highly relevant to market access, but subsidies and the exchange rate also affect market access.

Proximity to the market, which can result in faster turnaround times, is an important success factor, especially for seasonal, fashion-oriented and quick-turnover products. For example, suppliers in Mexico, which usually take approximately two days to ship to the United States, have a significant advantage compared with suppliers in Asia, whose average shipping time is about 28 days.

Preferential market access in the major importing countries in the context of regional trade agreements may, under certain conditions, provide significant advantage to exporters in preference-receiving countries, given the relatively high tariffs imposed on textiles and clothing.

Challenges and constraints: What firms have to do

Textiles and clothing firms are required to make intelligent decisions on business strategies in diversification and specialization to counter the foreseeable price wars in the ordinary cotton and MMF product lines. This is particularly relevant to firms, which would be heavily impacted by post-ATC competition environment. The main advantage for firms to tap the market for dynamic products is that neither diversification into, nor specialization in, these products necessarily requires huge investments.

Other challenges that textiles and clothing firms need to meet in order to maintain competitiveness are the following: meeting technical, social and environmental standards, having flexible and efficient production lines, and training workers and middle- and upper- managers. Technology upgrading at the stages of ginning, monitoring production, spinning, weaving, dyeing and garmenting is a key aspect of meeting these challenges. Availability of financial resource is crucial for firms if they are to maintain competitiveness.

Exporters of textiles and clothing need to seek collaboration from buyers in setting international standards and to make them locally indigenous standards. Such collaboration could be achieved through joint product development by sharing the management of production and logistics. Also, textile manufacturers in industrialized countries are endeavouring to innovate their products, and they are looking for partners, who could come from developing countries, to fill in the gaps they have in increasing competitiveness.

Firms are required to meet performance requirements relating to social and environmental conditions. Even what is supposed to be a voluntary practice such as eco-labelling is becoming a defacto requirement. Initiatives to tighten performance requirements such as the Worldwide Responsible Apparel Production, the Apparel Industry Initiative and the Clean Clothes Campaign are increasing trends. The optimal approach to deal with such requirements would be to incorporate them into localized indigenous compliance programmes rather than treating them as imported buyer requirements. The market preference for eco-labelled products is also expected to force manufacturers to redesign their products, their packages and their processes to make them more environmentally acceptable.

Companies are working to integrate accountability at the board level, leading to changes in who serves on the board, how directors handle social and environmental issues, and how the board manages itself and fulfils its responsibilities to investors and other stakeholders. However, firms often have difficulties in meeting performance requirements as conditions are imposed unilaterally without consideration of local and regional specificities. As far as environmental aspects are concerned, UNCTAD has been working in the context of environmental measures affecting textiles and clothing, and for social conditions the ILO has started a pilot project in some developing countries.

After the events of 11 September 2001 security compliance under the Trade Partnership Against Terrorism Law has become another challenge for textiles and clothing exporters in developing countries, as it involves lengthy and complicated procedures, as well as substantial costs.

Strategies at the national level

Given the special structure of textiles and clothing created by the quota system, some adjustments in the textiles and clothing sector are inevitable. However, optimism was expressed that, even for small countries which could be impacted by the quota lifting, basic requirements for competitiveness exist and that if adequate financial resources are available to upgrade technologies and train workers through, for example, preferential rate loans, firms could maintain competitiveness.

To support firms' endeavours to maintain competitiveness, reform of domestic labour laws might be necessary in order to increase flexibility in employment while enforcing international labour standards.

Regulations affecting the competitiveness of dynamic products need to be reformed. In this respect, those on energy, telecommunications, transportation, electricity and preferential treatment for specific products at the expense of potential dynamic products are particularly relevant.

Enforcement of laws on intellectual property rights is necessary for the protection of traditional artistic expressions and promotion of niche markets. It is also important for attracting foreign investment and buyer interests.

Other national measures required are investments in infrastructure to support efficient trade logistics, building dry ports, creating export processing zones, providing financial incentives (grants, loans or tax relief) to improve competitiveness, removing bottlenecks that result in delays in shipping and customs clearance, and the removal of export duties and other taxes. Active business advocacy to sensitize Governments about the needs of enterprises is essential.

Being certified by the Governments of major importing countries for labour standards, – for example, Sri Lanka's case vis-à-vis the EU GSP labour standards – increases the bargaining power of textiles and clothing exporters against importers that impose private codes of conduct. Also, developing countries could learn lessons from Japan's experience in the adjustment of its textile sector industry.

Strategies at the international level

On the international trade policy front, several issues were raised. Trade in textiles and clothing still faces considerably higher tariffs than other industrial goods, such tariffs being serious barriers to textiles and clothing exports. Preferential rules of origin for textiles and clothing are highly discriminatory in respect of exporters of those products in countries that do not participate in regional trade agreements. Countries, that have regional trade agreements with the EU and the United States have to use inputs from the two partners to benefit from the preferential market access unless they can use input from the region concerned. The restrictive rules of origin are also a serious constraint for "forum shopping".

Countries which would be seriously impacted by the quota-lifting need substantial technical and financial assistance from bilateral and multilateral donors for enhancing supply capacity and developing forward and backward linkages in their textiles and clothing industries. Special problems faced by LDCs, including those of landlocked countries, need to be taken into account in helping them to adjust to the post-ATC environment. Lack of alternative sectors to absorb displaced workers is a particular problem for these countries. The international community and bilateral donors need to provide adequate assistance through existing mechanisms such as the IMF's Trade Integration Mechanism and new initiatives such as the Trade Adjustment Fund recently proposed by the EU. Also, extending duty-free access to textiles and clothing from all LDCs is crucial in assisting these countries in the post-ATC context.

Developing countries that are entitled to preferential access to the markets in the major importing countries often have low rates of preference utility because of the restrictive preferential rules of origin. Flexible rules of origin are necessary if these countries are to benefit from preferential market access, and for promoting South–South cooperation. In this light, application of the "single transformation" rule, interpretation of transformation, cumulation at the subregional, regional and interregional levels are of particular importance. Developing countries expressed the hope that the new EU GSP scheme would adopt user-friendly rules of origin.

To let competitive textiles and clothing firms grow in the post-ATC phase, introduction of new protectionist measures must be avoided. Obtaining adequate provisions for technical and financial assistance in the ongoing WTO negotiations on trade facilitation is also necessary in order to enhance trade logistics in developing countries.

As regards social and environmental requirements, Governments, the international community and NGOs need to endeavour to ensure that such requirements are not imposed for protectionist motives, and to establish balanced requirements which take into account cultural diversity and local specificities in developing countries.

Concentration of the textiles and clothing market in the major importing countries is making retailers very powerful. Exporters of textiles and clothing in developing countries often face demands by these retailers that prices be cut to an unreasonably low level. It is necessary to examine the problems which exporters face in this respect and to identify ways to counter them.

South–South cooperation could play an important role in increasing trade of dynamic products, as well as technology upgrading, as shown in the case of the joint venture agreement between China and India. There is a need for a service at the international level which could advise textiles and clothing manufacturers in developing countries about the latest technology developments.

UNCTAD could play an important role in helping developing-country Governments to pursue policy measures to strengthen their countries' participation in dynamic textiles and clothing products and in creating a conducive international environment for developing countries to achieve this goal. Specific areas suggested for UNCTAD assistance include:

(i) Identifying dynamic products, and helping developing countries to participate in the trade of dynamic products;
(ii) Monitoring the post-ATC situation in terms of trade patterns, market trends and impact on employment;
(iii) Continuing to analyse the effectiveness of non-reciprocal preferential agreements, particularly in relation to preference utilization and rules of origin;
(iv) Monitoring the developments in regional trade agreements and analysing their implications, particularly those of the rules of origin, for trade in textiles and clothing;
(v) Promoting South–South cooperation, such as the GSTP, in increasing developing countries' participation in the trade of dynamic products;
(vi) Monitoring developments relating to labour conditions, and analysing the implications for the textiles and clothing in developing countries;
(vii) Identifying competitive textile products in developing countries and helping them in countering perceived "country risk";
(viii) Monitoring signs of protectionism in the sector;
(ix) Examining the issue of market concentration in the major markets and analysing the implications for exporters from developing countries;
(x) Calling for coherent trade adjustment support programmes and for donor support in enhancing supply capacity; and
(xi) Examining success stories about attracting foreign direct investment (FDI) in the textiles and clothing sector in LDCs, including African cotton-producing countries, and increasing value added, and advising countries that wish to establish policy measures to attract FDI which could benefit from preferential agreements such as AGOA and EBA.