The North American Free Trade Agreement and its Implications for Sri Lanka: With Special Reference to the Garment Industry

Saman Kelegama

and

Indira Unamboowe

Research Studies
International Economic Series No. 2

THE LIBRARY
SL
339.5
IPS

THE LIBRARY
SL
339.54
KEL
IPS

INSTITUTE OF POLICY STUDIES
99, St. Michael's Road, Colombo 3, Sri Lanka
May, 1994

0722

INSTITUTE OF POLICY STUDIES



The North American Free Trade Agreement and its Implications for Sri Lanka: With Special Reference to the Garment Industry

SL
339.54
KEL
Sri Lanka - Industries - NAFTA - IPS - Trade policies

Saman Kelegama and Indira Unamboowe

0650

© Institute of Policy Studies
ISBN 955-9122-30-4

SL
339.54

MPW 550

Abstract

On 1 January, 1994 the North American Free Trade Agreement (NAFTA) came into operation. Under its terms, existing trade restrictions will be removed against the intra-trade of the United States, Canada and Mexico, but will continue to be in operation for imports from third parties. Countries such as Sri Lanka are naturally concerned about their trade being displaced by the NAFTA, which like all other free trade agreements, discriminate in favour of member countries.

At present, 36 per cent of Sri Lankan exports are concentrated in the US market and out of this amount nearly 84 per cent are garments. Thus the apparel exports remain the major concern for Sri Lanka in the context of NAFTA. Some argue that NAFTA poses a serious threat to Sri Lanka's economy because Sri Lankan apparel exports to US will be substantially displaced by more competitive Mexican apparel while some others argue that the formation of NAFTA is a non-event from the Sri Lankan perspective.

The only available literature that gives at least some indication of NAFTA's implications for Sri Lanka is a study done for the World Bank by Safadi and Yeats (1993) on NAFTA and South Asia. According to this study, the losses for Sri Lanka due to NAFTA, in terms of 1989 statistics, will be about 1 per cent of her exports to the US market. But the study claims that the potential losses from the decline in exports would be more than offset by the successful completion of the Uruguay Round of trade negotiations. The study however is more focussed on South Asia and the conclusions are based on aggregate statistics. An aggregate analysis for the South Asian region is always biased by the inclusion of Indian statistics. Moreover, the analysis of Sri Lanka's case is based on the regional model which may not necessarily be valid for a small country like Sri Lanka.

In this study we have re-examined in detail NAFTA's implications for Sri Lanka. In particular, we have investigated Sri Lanka's competitiveness *vis-a-vis* Mexico in the US market. While supporting the basic conclusion of Safadi and Yeats, we go on to show that NAFTA, and the gradual abolition of the MFA, give new opportunities to further expand the apparel industry of Sri Lanka. However, we argue that this will not happen merely by the market mechanism. Substantial work needs to be done both on the marketing side as well as on the supply side, the latter being weak needing more attention. In regard to the Uruguay Round, our analysis shows that there are gains for Sri Lanka, but the gains are not very significant as argued by Safadi and Yeats (1993).

CONTENTS

1. Introduction 1

2. North American Free Trade Agreement 1

3. Sri Lanka and NAFTA 5

4. NAFTA and the Sri Lankan Garments Sector 10

    4.1 Preamble 10

    4.2 Framework for Examining the Price Competitiveness 15

    4.3 Factors that are not Advantageous to Mexico 18

    4.4 Proximity: Will Quick Turnaround Time Favour Mexico ? 22

5. Conclusion 25

Appendix I 31

Appendix II 34

Reference 37

The North American Free Trade Agreement and its Implications for Sri Lanka: With Special Reference to the Garment Industry*

Saman Kelegama
and
Indira Unamboowe

1. Introduction

There is much discussion at present on the North American Free Trade Agreement (NAFTA) and its implication for the Sri Lankan economy. However, in the absence of more detailed information on it, little is yet known regarding its implications for the Sri Lankan economy. A study of NAFTA in relation to South Asia has been done by Safadi and Yeats (1993) with only a brief reference to Sri Lanka. It does not give a comprehensive analysis of the Sri Lankan case, nor take into account the importance of international market links and the costs of production. This paper attempts to fill in this gap.

The plan of the paper is as follows. Section 2 of this paper gives a general introduction to the NAFTA. Section 3 analyzes Sri Lanka's trading and investment patterns with the NAFTA countries. Section 4 deals with the impact of NAFTA on Sri Lanka's garment exports. Concluding remarks and recommendations are given in Section 5.

2. North American Free Trade Agreement

A Free Trade Agreement among USA, Canada, and Mexico called the North American Free Trade Agreement was first broached in June 1991. Such a regional agreement was thought necessary in view of the increase regional trade among countries, such as those of the European Community (EC) and the Association of South East Asian Nations (ASEAN) in Asia. As Table 1 shows the three countries were major trading partners and thus had much to gain from a free trade agreement.

* An earlier version of this paper was presented to a Seminar on NAFTA organized by the American Chamber of Commerce of Sri Lanka on 23 Feb. 1994. The authors have benefitted from the comments made by Premachandra Athukorala, David Dunham, Howard White, Ravi Rannan-Eliya, and Shelton Wanasinghe. The usual disclaimer in regard to errors and omissions applies.

Table 1: Intra-Regional Trade of NAFTA Countries: 1991 (as a percentage of World Trade of the Country)

	USA	Canada	Mexico
USA	-	20.17	7.9
Canada	75	-	0.3
Mexico	65.2	2.1	-

Note: The table should be read from the left upwards.
Source: World Bank (1993).

Mexico took the initiative in promoting the free trade agreement partly to increase US and other foreign investment in Mexico and partly to improve Mexico's access to the US market. US and Canadian business favoured it in order to expand trade and investment opportunities, to take advantage of relatively low Mexican wages, and to have access to Mexico's oil resources. Mexico was the third most important trading partner of the USA after Canada and Japan, in 1991, while the USA was Mexico's most important trading partner accounting for around two-thirds of her exports and imports (see Table 1).[1]

For the United States which, in the past, stressed the importance of liberalization under GATT, the focus on regional agreements is a recent policy trend. Among other factors, this could perhaps be attributed to the dissatisfaction with multilateral trade negotiations as a means of achieving trade liberalization. The USA had already negotiated free trade arrangements with Israel and the Caribbean, while a free trade agreement between the USA and Canada was in operation since early 1989. The inclusion of Mexico is a significant new feature.

The NAFTA came into full operation on 1 January 1994.[2] As Table 2 shows, NAFTA controls nearly 16 per cent of world trade. Although this share is much smaller than that of the EC, the NAFTA countries would become the largest market in the world with a combined Gross Domestic Product value at US$ 6,550,000 million, and a combined population of about 365 million (based on 1991 data). Mexico's GDP in 1991 accounted for less than 5 per cent of the total. However, Mexico's population of around 81 million accounted for about one-fourth of North America's population (see Table 3).

---

1 The share of US exports purchased by Mexico rose from 5.9 per cent in 1987 to 9.1 per cent in 1992. Moreover, Mexico is USA's fastest growing export market. At present, nearly US $ 1 out of every US $ 10 of US exports goes to Mexico. In 1992, Mexico surpassed Japan to become the second most common export destination for US manufactured goods exceeded only by Canada (Business America, October, 1993).

2 For the history of NAFTA see Business America, 18 October 1993, p. 2.

Table 2: Percent Share of the Value of World Exports During 1990 by Trading Regions

Region	Percent
EC	41
Developing Nations	26
NAFTA	16
Japan	9
CIS + East Europe	7
Other	1

Source: IMF (1992).

Table 3: NAFTA: General Indicators (1991)

	Population (Mn.)	Area (Sq.Km.)	GDP per Capita (US$)
USA	253	9,373	22,535
Canada	27	9,976	14,975
Mexico	81	1,973	3,484

Source: OECD (1992).

The entire agreement of the NAFTA would be enforced through gradual and comprehensive elimination of tariff and non-tariff barriers over a 15-year period, protection of intellectual property rights, and fair and expeditious dispute settlement procedures.

It is said that US $ 2.35 billion in tariffs would be eliminated over five years. It is noteworthy that NAFTA has various safeguards in its supplementals. For example, the agreement for imports and services contains supplementals to safeguard and protect the local industries when they are threatened from imports from the neighbouring countries. In fact, the so-called Import Surge Agreement will complement the NAFTA by improving the effectiveness of safeguard provisions that allow for action against imports that might cause or threaten serious harm to a domestic industry, including the workers of that industry.

NAFTA will ensure a high level of protection under Mexican law for US owners of patents, copyrights, trademarks, trade secrets, and integrated circuits, including strong safeguards for computer programmes, pharmaceutical inventions and sound recordings. NAFTA obligates both Mexico and Canada to enforce intellectual property rights against infringement, both internally and at the border. By protecting intellectual

property rights, NAFTA will increase trade and diminish losses from counterfeiting and piracy.

How soon will the existing tariffs be phased out by NAFTA ?[3] Under NAFTA, the phasing out of tariffs range from immediate duty elimination with effect from 1 January 1994, to 15 years for some agricultural products. Half of all US exports to Mexico are eligible for zero Mexican tariffs from 1 January 1994. Within the first five years, two thirds of US industrial exports will enter Mexico duty-free.[4] As stated, NAFTA provides adjustment periods for import-sensitive industries. Accordingly, half of the textile imports from Mexico will get a phase-out period of six years. For certain other import-sensitive industries, NAFTA provides a 15-year tariff phase-out period.

NAFTA eliminates tariffs only on goods produced in North America. Goods which are wholly produced in the United States, Mexico, or Canada and made entirely of North American components will qualify for NAFTA concessions. Goods made of non-regional components will qualify for reduced tariffs if they are sufficiently transformed in the NAFTA region so as to undergo a specific change in tariff classification. NAFTA exporters of products which contain non-regional components need to know the Harmonized System (HS) numbers of the components to determine whether the product qualifies for duty-free treatment under NAFTA Rules of Origin. Rules of Origin are used to define those goods entitled to NAFTA duty-free treatment.

Rules of Origin are generally established in free trade areas to prevent "trade deflection", whereby goods originating in non-member countries are transshipped from a member country with lowest external protection.[5] In short, Rules of Origin prevent "free riders" from benefitting through minor processing or transshipment of non-NAFTA goods. Mexico and Canada cannot be used as export platforms into the US market (Driscoll, 1993).

---

3 Mexican tariffs (10 per cent) were two and a half times higher than US tariffs (4 per cent) before NAFTA.

4 73-88 per cent of the textile and apparel trade from Mexico would be duty free at the start of the agreement and 99 per cent duty free by January 1999. It is also worth noting that Mexico's maquiladora export-based factories, the largest user of Mexican Custom duty-drawback, will essentially be phased out and merged into the domestic Mexican economy.

5 It is important to note here that NAFTA is not a Customs Union. Unlike a Custom Union, a free trade area does not commit members to a common external trade policy thus enabling them to minimize trade diversion effects. By lowering tariffs unilaterally, a member of a free trade area can switch imports back to more efficient suppliers; this action would, however, simultaneously diminish the value of its trade concessions (and thus available rent) to other members. To avoid this, Rules of Origin are required in a Free Trade Area.

NAFTA does not take away the authority that the USA already has, under Section 301 of the international trade laws, to unilaterally stop trading with a nation that, according to the USA has abrogated her basic rights. NAFTA is a symbol of America's leadership in the global economy, and of America's willingness to face the challenges and changes of the future. Most studies have indicated that NAFTA will result in a "win-win-win" situation for the three countries (see, for instance, Jacobs, 1993). This estimation is based on the assumption that wage differences among the three countries will lead to a mutually beneficial division of labour. The NAFTA will contain an accession clause that would facilitate the subsequent entry of other Latin American countries into the Free Trade Agreement. In that sense NAFTA can be seen as the first step towards a wider trading region encompassing all Americans (Szymczak, 1993).

3. Sri Lanka and NAFTA

Sri Lanka's exports to the NAFTA in 1992 were about US$ 895 million or about 36 per cent of her total exports or around 6.6 per cent of her GDP. Sri Lanka commands a massive trade surplus with the NAFTA region and, in 1991, it was around 30 per cent of Sri Lanka's total exports. North America is Sri Lanka's largest market; the European community accounting for 27 per cent of her exports ranks second (Table 4). Within NAFTA, the USA is the largest annual export earner for Sri Lanka, and in 1992 Sri Lankan exports to US was around US$ 840 million. The bulk of Sri Lanka's exports to North America consists of textiles and garments. In 1992, for instance, nearly 60 per cent of Sri Lanka's total garment exports were concentrated in the US market (Table 5, also see Kelegama, 1993a). Thus, in the context of NAFTA, garments and textiles are undoubtedly products of major importance for Sri Lanka.

Table 4:Percent Share of the Value of Exports from Sri Lanka to Various Trade Blocs (regions) of the World (1991 and 1992)

Region	Percentage of the total annual exports	
	1991	1992
NAFTA	30	36
EC	27	32
Middle East	14	9
ASEAN	5	2
Others	24	21

Source: Export Development Board, Data Base.

Table 5: US Share of Sri Lankan Garment Exports, 1987-92

	1987	1988	1989	1990	1991	1992
US Share	67.3	66.2	68.9	68.2	60.1	59.8

Source: Estimated using Sri Lanka Customs Statistics.

Table 6 shows Sri Lankan exports at a disaggregate level to the NAFTA region. As indicated, garments accounted for nearly 82 per cent of Sri Lanka's total exports to USA, 64 per cent of Sri Lanka's total exports to Canada, and 2.5 per cent of Sri Lanka's exports to Mexico, in 1992. Among the other exports to the NAFTA region, manufactured products accounted for nearly 11 per cent of Sri Lankan exports to the USA and 20 per cent of Sri Lankan exports to Canada. Tea accounted for 11 per cent of Sri Lankan exports to Canada, and the exports to Mexico was dominated by spices.

Since the Canadian and Mexican markets for Sri Lanka's total exports account for about 1.6 per cent and less than 1 per cent, respectively, NAFTA would only marginally affect Sri Lanka's exports to these two markets. In the Mexican market, for example, there appears to be little potential for diversion as a result of NAFTA, because the USA and Canada are not significant exporters of spices, tea and natural rubber to Mexico. However, it is in the US market (which absorbed 34 per cent of Sri Lanka's exports in 1992), that Sri Lankan exports will be affected -- adversely or more favourably -- in the period ahead. In order to assess the impact of NAFTA on the Sri Lankan economy, a detailed analysis of garment exports need to be made, since they account for 82-84 per cent of Sri Lanka's exports to the USA This is done in Section 4.

It is essential to emphasize that Sri Lankan exports will be affected to the extent that (a) Sri Lanka competes on an unequal footing in the US market with exports from Mexico -- a country that has low wages as some developing countries, and (b) the USA favours Mexico vis-a-vis Sri Lanka where protection is concerned in respect of commodity exports. In regard to the latter it is noteworthy that, for certain commodities the USA grants GSP (Generalized System of Preferences) status to Sri Lanka. For instance, for spices (categorised under export crops for the USA, in Table 6), Mexico and Sri Lanka compete in the US market under GSP status, and in such a case, Mexico is likely to gain only a commensurately small competitive edge after NAFTA. This may be due to: (1) the lower transport cost to the USA that Mexico enjoys, and (2) Mexico having guaranteed access to the US market without export limits, while Sri

Lanka is subject to the restrictions and vagaries of the GSP. Such cases account only for relatively few of Sri Lankan exports to the USA. (However, GSP would be effective only till mid-1995 under new GATT rules). Thus in view of the above considerations, a major part of Sri Lanka's exports to the US market will be affected to the extent as stated in (a) above.

Table 6: Sri Lanka's Exports to USA, Canada and Mexico (1991 and 1992)

Market	% Share of Exports to the Market		Product Description	% Share of Export by Product to the market		Value of Exports (SDR Mn.)	
	1991	1992		1991	1992	1991	1992
USA	27.34	34.03	Garments	83.93	81.77	342.16	486.06
			Manufactures	9.06	10.95	36.94	65.11
			Export Crops	1.57	0.76	4.24	4.49
			Gems, Jewellery & Diamonds	0.87	0.75	3.55	4.46
			Natural Rubber	0.003	0.65	1.27	3.86
			Bulk Tea	1.21	0.63	4.12	3.77
			Fisheries Products	0.004	0.35	1.82	2.06
			Others	3.36	4.14	13.58	24.63
			Total	100	100	407.68	594.44
Canada	1.57	1.58	Textiles & Garments	63.59	63.59	14.87	17.5
			Manufactures	17.15	19.58	4.01	5.39
			Tea	11.25	10.86	2.63	2.99
			Export Crops	2.57	2.29	0.60	0.63
			Others	5.44	3.68	1.27	1.01
			Total	100	100	23.38	27.52
Mexico	0.99	0.81	Spices	92.42	87.67	13.69	12.31
			Tea	3.83	4.03	0.60	0.57
			Natural Rubber	1.57	1.23	0.23	0.20
			Textiles and Apparel	1.66	2.51	0.25	0.35
			Desiccated Coconut	0.04	0.23	0.01	0.03
			Misc. Manufactured Articles	0.17	0.53	0.02	0.07
			Others	0.31	3.80	0.05	0.53
			Total	100	100	14.81	14.06

Source: Export Development Board, Data Base.

With NAFTA coming into operation will North American investment in Sri Lanka get adversely affected? Here again, the country that matters most for Sri Lanka is the USA. The major concern for Sri Lankan policy-makers is that US investment flows to Sri Lanka may be diverted in future to Mexico, to take advantage of growing opportunities south of the border.

Currently there are about 48 US companies operating either in full form or joint venture form in Sri Lanka employing approximately 10,000 people. Nineteen of these companies are under BOI (Board of Investment) status and they are export-oriented companies. As shown in Table 7, nine of the BOI companies are in the form of full US investment while 10 are in the form of joint ventures. The remaining 29 are mostly US-Sri Lanka joint ventures located outside the Export Processing Zone. These ventures are in various sectors such as garments, pharmaceuticals, advertising, etc. Major US investment in Sri Lanka includes two banks and several multinational companies. American Express and Citibank have branch offices in Colombo. The other US multinationals, many of them long standing, include IBM, Singer, Muller and Phipps, Pfizer, Union Carbide, and NCR corporation. Some of them are oriented more towards the Sri Lankan domestic market. The more recent US investment has been in the Export Processing Zones and some outside them.

The total US investment in Sri Lanka is 13.2 per cent of Sri Lanka's total Foreign Direct Investment (FDI) and FDI in turn amounted to 1.6 per cent of GDP in 1993. The total US investment in Sri Lanka is roughly in the range US $ 30-35 million. Clearly, Sri Lanka has not been a major centre of the USA for export-oriented investment.

Table 7: US Investment in Sri Lanka (1993)

US Investment	No. of Ventures
USA	9
USA-Sri Lanka	6
USA-Hong Kong-Sri Lanka	1
USA-Germany	1
USA-Hong Kong	1
USA-India	1

Source: Board of Investment, Data Base.

There are three major US joint ventures in the garment industry and they are significant in terms of export earnings and employment generation (see Table 8). Their location in Sri Lanka seems to have been dominated by two factors, *viz:* (1) cheap and efficient labour, and (2) easy access to high quality raw material from the East Asian NICs. In regard to these two factors, Sri Lanka is ranked highly by the US garment buyers. Irrespective of NAFTA, these factors will remain favourable to Sri Lanka in the years to

come. Many US garment-purchasing groups operate in Sri Lanka. The market links with them seem to be an important factor.

Table 8: Export Earnings & Employment of the Three Major US Ventures in Garments

US Investment	Export (Rs Mn) (1990)	Employment (1991)
Smart Shirts Ltd	431.54	3164
Hirdaramani Garments Ltd	258.97	945
Star Garments	563.61	2666
Total	1254.13	6775
As a % of total	5.0	5.6

Source: Board of Investment, Data Base.

The already existing US investment will not be affected by the NAFTA. Most US investment in Mexico would be in areas such as, oil, copper, textiles, and gold and in these fields Sri Lanka will not compete with Mexico. Thus, whatever US investment diversion to Mexico that may occur in the long run is expected to be marginal *vis-a-vis* overall US investment in Sri Lanka. Even the possibility of diversion of East Asian investment from Sri Lanka to Mexico in response to the NAFTA is remote. This is because the type of East Asian investment in Mexico will not be in areas where Sri Lanka was an attractive site for East Asian investors before the NAFTA.

In the context of the NAFTA it needs to be emphasized that US investment is not guided by cheap labour alone. Of the total US direct investment abroad for manufacturing, amounting to US $ 187.3 billion in 1992, over 70 per cent was in Japan, Canada, and the EC, and less than 5 per cent was in Mexico. This shows that US manufacturers do not invest overseas to exploit lower manufacturing wages. Many factors that guide and direct US FDI, such as (a) political stability, (b) consistent economic policy making, (c) infrastructure and skills, etc., may not be available in Sri Lanka in the framework of US FDI decision making. Perhaps this may be the reason why the OPIC (Overseas Private Investment Corporation) delegation that visited Sri Lanka in early January 1992 did not show much enthusiasm in investing in Sri Lanka.

In order to promote stronger business ties and encourage more US investment, Sri Lanka has already finalized a bilateral investment treaty and an intellectual property agreement with the USA. Moreover, a double taxation treaty is to be signed shortly.

4. NAFTA and the Sri Lankan Garments Sector

4.1 Preamble

As is well known, today, garments constitute the largest export of Sri Lanka and also the largest foreign exchange earner. The growth and expansion of the Sri Lankan garment industry were due to two main factors, *viz*: (1) liberal trade regime since 1977, and (2) the Multi-Fibre Agreement (MFA) that assures market access by an allocated quota.[6] At present, Sri Lanka receives a quota for 50 categories of garments.[7] While the MFA provides an assured market, it has the feature of restricting or limiting the export of particular categories of garments that may be popular among exporters.

Table 9 shows both quota and non-quota imports to the US market from Sri Lanka. Of the total Sri Lankan garment exports to the USA, more than 93 per cent come under quota and less than 7 per cent is under non-quota. Sri Lanka cannot afford to be complacent with such a small share of the US non-quota market. This is because the MFA is going to be phased out during the 10 year period, 1995-2005.[8] When this is totally accomplished Sri Lanka will have to compete in the non-quota market where there is severe competition. This is going to be an uphill task with the current loose foothold in the non-quota market. She has much work to do to get a better foothold in the same market -- it is only now that efforts are being made to shift from budget type buyers to upmarket buyers in the non-quota market. However, as we point out in Section 5, Sri Lanka has much work to do at the low-end of the market as well, while gradually switching to garments of the high-end of the market that are popular in the non-quota market.

Sri Lanka does not qualify for any concessions as a small supplier, as its market share of US imports of textiles and garments exceeds the cut-off point of 1.2 per cent. Sri

---

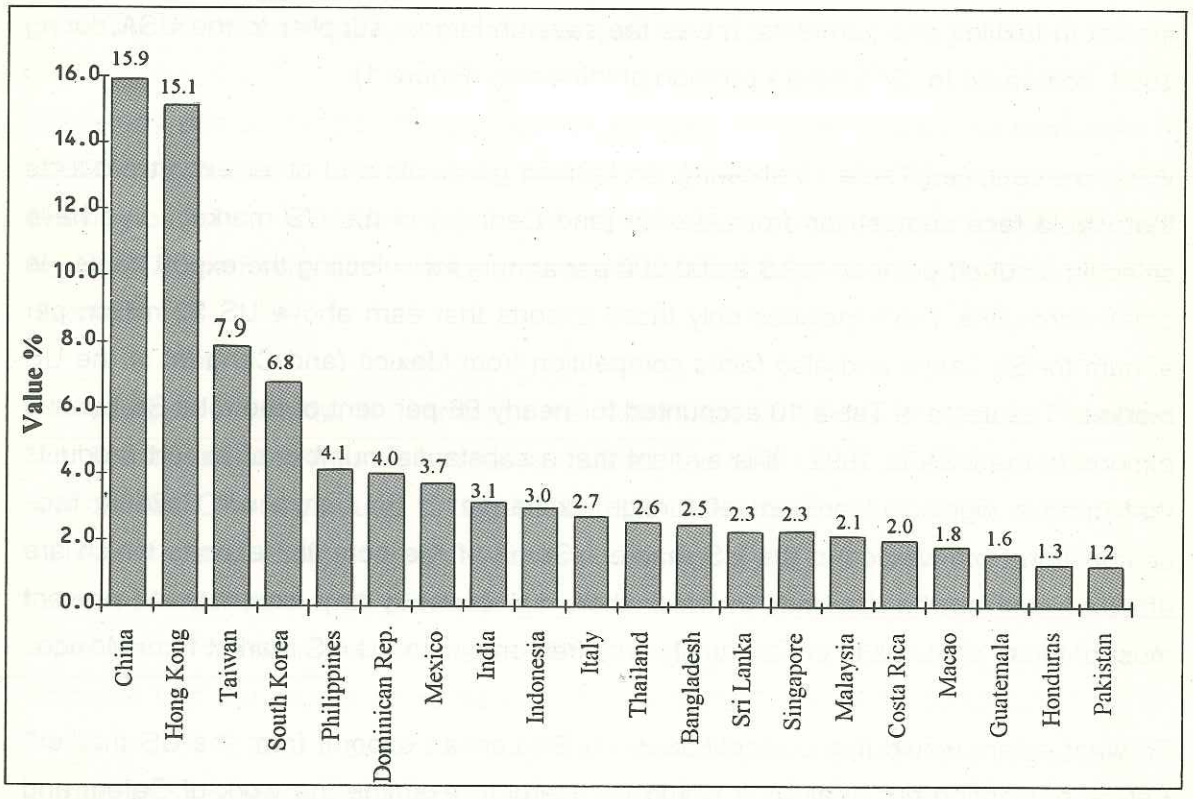
6 It should be emphasized that the MFA has not only protected the markets of the USA and Europe, but has also protected less advanced exporting countries such as Sri Lanka through the allocated quota which protects them from competition from countries such as India and China. In other words, the market assurance is granted by the imposition of quotas on other more advanced and competitive supply sources.

7 In contrast, countries such as Hong Kong have over 90 categories of garments under quota. This is because, compared to Sri Lanka, countries such as Hong Kong export a vast variety of garments.

8 On 1 January 2005, the textiles and clothing sector shall stand integrated into GATT, with all restrictions under this agreement having been eliminated. The 10-year period is divided into three stages of 3:4:3. At the commencement of the first stage, effectively 16 per cent of the total volume of imports for 1990 shall be integrated into GATT. The percentages of integration at the commencement of the second and third stages would be 17 and 18 per cent, respectively. Thus, 51 per cent of the total imports shall be integrated into GATT on 1 January 2002, leaving the remaining 49 per cent to be integrated 1 January 2005.

Lanka's share of US apparel imports in 1991 and 1992 was on average around 2.65 per cent and Sri Lanka was the 13th largest supplier to the US market in 1992 (see Figure 1). Although the USA is Sri Lanka's largest importer of garments, Sri Lanka had a significant number of categories of ready-made garments from South Asia -- 29 -- under restraint in 1993/94 compared to 20 for Bangladesh, 24 for Pakistan, and 21 for India. Moreover, a countervailing duty of 3.06 per cent was imposed on Sri Lankan garment exports in October 1993 (this duty was first imposed in 1985, revoked in 1990 and was reimposed in October 1993) due to the "bounties and grants" that they were enjoying in the process of production.[9]

Figure 1: Percentage Share of US Apparel Imports for 1992



Source: Plotted using data from the EDB Data Base

9 For our calculations in Section 4.2 we have taken into account the impact of countervailing duties on the competitiveness of Sri Lankan garment exports. These duties may be revoked in due course. However, given the marginal nature of the countervailing duty, it will become clear from Section 4.2, that the final results with regard to the competitiveness of the Sri Lankan garments in the US market would not change significantly to alter the basic line of argument in the paper.

Table 9: Apparel Imports into USA from Sri Lanka (Million Square Metres)

Source	1990	1991	1992
World	6007.084	6149.178	7094.275
Sri Lanka			
Quota	140.060	154.062	181.461
(percentage)	2.33	2.51	2.56
Non-Quota	3.005	6.604	12.223
(percentage)	0.05	0.11	0.17
Sri Lanka Total	143.065	160.666	193.684
(percentage)	2.38	2.61	2.73
Rank	12	11	12

Source: Sri Lanka Customs, 1993.

Both Sri Lanka and Mexico could be considered as secondary suppliers of garments to the US and Canadian markets. However, Mexico commands a larger share of the US market in textiles and garments: it was the seventh largest supplier to the USA during 1992, compared to Sri Lanka's position of thirteenth (Figure 1).

We have compiled Table 10 showing Sri Lankan garments and other export products that would face competition from Mexico (and Canada) in the US market. We have selected a cut-off point of US $ 2,000,000 per annum for selecting the export items. In other words, the Table includes only those exports that earn above US $2 million per annum for Sri Lanka and also faces competition from Mexico (and Canada) in the US market. The items in Table 10 accounted for nearly 86 per cent of the total Sri Lankan exports to the USA in 1992. It is evident that a substantial number of export products that bring a significant amount of foreign exchange to Sri Lanka will have to face competition from Mexico in the US market. (Some of the potential exports which are affected may not be the ones in which there are currently any exports). At present most of these products enjoy a virtually duty-free entry into the US market from Mexico.

To what extent would this competition divert Sri Lankan exports from the US market? Before presenting our analysis it would be useful to examine the work of Safadi and Yeats (1993). Their analysis is focussed more on the South Asian region than on Sri Lanka, and their trade diversion estimates are based on a partial equilibrium trade projection model developed by the UNCTAD and the World Bank.

According to this study, approximately 54 per cent of all South Asian exports to the United States face neither tariff nor non-tariff barriers (NTBs) nor any significant

competition from Canada or Mexico. Of the remaining 46 per cent, South Asian exports are highly concentrated in textiles and clothing. For them, the crucial market is the USA which accounts for over 90 per cent of all South Asia's exports to North America. Thus the study states: "Of approximately US $ 2.5 billion of South Asian exports facing trade barriers and competition from Canada and Mexico, over 93 per cent are textile and clothing products (SITC 65 and 84) with the largest single four-digit core group of products (clothing of textile fabrics - SITC 8411) alone accounting for 60 per cent of the total. The competitive position of South Asian exporters will be eroded by the NAFTA's preferential removal of the relatively high United States tariffs on clothing -- these average about 22 per cent on knitted clothing (SITC 8414) and about 18 per cent on the single key product, namely, clothing of textile fabric (SITC 8411) -- as well as by the removal of MFA restrictions. The importance of the latter is likely to be greater than that of tariffs as the .... *ad valorem* incidence of the MFA restrictions generally falls in the 40-80 per cent range" (pp. 10-11).

The study postulates that the abolition of the MFA for Mexico with the formation of NAFTA will favour Mexico vis-a-vis South Asia. However, the authors argue that the phasing-out of the MFA quota by the year 2005 would erode the preferences enjoyed by NAFTA members and reduce the value of third country exports that might be diverted.

According to the study, the impact of the NAFTA on Sri Lanka is marginal. It states: "For the eight South Asian countries combined, the NAFTA-induced losses on the 12 four digit SITC core products (5127, 5310, 6512, 6569, 6576, 6541, 8310, 8411, 8412, 8413, 8414, and 8510) average about one per cent of the 1989 value of exports, with the combined losses of all goods ranging from one-half a percent (India) to eight-tenth a per cent (Pakistan and Sri Lanka) of total exports to the USA" (p. 18). The study indicates that the losses would be incurred for SITC 6569, 6576, 8310, 8411, 8412, 8414, and 8510 and the losses would be 1 per cent of the total core products that amount to 81.8 per cent of total Sri Lankan exports to the USA in 1989.

It is not our intention to re-examine these findings. However, we believe that an analysis of the competitiveness of Sri Lanka's garment exports *vis-a-vis* Mexico, in the US market, could give a better picture of the real threat to Sri Lanka's garment exports that the NAFTA may pose. Such an analysis is attempted below.

Table 10: Sri Lankan Exports to USA that Face Competition from Mexico and Canada

SITC	HSNO	Sri Lanka's value in $US ('000) 1992	Tariffs (pre-GATT)	GSP	MFA	Sri Lanka's value in $US ('000) 1991	Internal competition in $US ('000) 1991	
							Canada	Mexico
841.5	620520	64847	15.1	N	Y	34337	4314	9055
	620590	9603	5.3	N	N	3044	4314	9055
	620530	4240	13.0	N	Y	2534	4314	9055
842.7	620630	53671	9.9	N	Y	15006	5273	27285
	620640	50264	16.2	N	Y	42644	5273	27285
	620690	12093	7.1	N	Y	6009	5273	27285
	620610	2274	7.5	N	Y	1157	5273	27285
842.6	620462	30306	9.8	N	N	18379	13538	131797
	620463	11202	13.8	N	Y	5975	13538	131797
	620469	8790	15.0	N	Y	5440	13538	131797
843.7	610510	27777	21.0	N	N	146	660	2169
	610590	2993	11.5	N	Y	6336	660	2169
841.4	620342	26086	11.1	N	N	25006	23878	216225
	620349	16310	15.7	N	N	13347	23878	216225
	620343	7410	13.2	N	Y	3336	23878	216225
842.3	620439	23329	17.8	N	Y	13171	7905	7668
	620432	7069	6.5	N	N	2227	7905	7668
	620433	19431	13.2	N	Y	13437	7905	7668
842.5	620453	20047	15.3	N	Y	8446	4138	10668
	620452	9979	8.6	N	N	5077	4138	10668
	620459	3101	13.3	N	Y	2690	4138	10668
848.4	650590	18514	7.8	N	N	5046	19971	27963
841.3	620339	16824	19.3	N	Y	6306	9629	11011
	620333	10398	25.5	N	N	11235	9629	11011
	620332	10745	6.5	N	Y	4936	9629	11011
844.7	610690	15654	9.3	N	Y	24204	3460	12362
	610610	11430	21.0	N	N	10701	3460	12362
848.2	401511	15180	3.7	Y	N	2718	13586	27100
842.8	620892	12366	17.0	N	Y	7706	2282	10615
	620822	8260	17.0	N	Y	4376	2282	10615
	620821	4311	9.5	N	Y	3617	2282	10615
842.4	620443	11865	13.4	N	Y	4437	4996	9208
	620442	8012	10.3	N	Y	4611	4996	9208
	620449	3865	7.5	N	Y	3235	4996	9208
845.3	611020	10422	12.8	N	Y	6745	22173	10530
	611030	3937	15.9	N	Y	1478	22173	10530
899.7	960330	10120	4.1	Y	N	1201	8355	28732
845.6	621111	8984	18.8	N	N	7083	12549	1011
666.2	691310	8284	6.2	Y	N	8122	589	11856
845.1	611120	8128	16.7	N	N	1836	2030	6565
845.4	610910	7770	21.0	N	Y	10109	4789	3809
	610990	5767	19.0	N	Y	4685	4789	3809
894.2	950341	6234	6.8	Y	N	846	25653	159616
845.8	621143	6184	17.0	N	Y	4318	4346	27654
658.4	630260	5898	10.3	N	Y	5673	6375	6036
598.6	380210	5820	4.8	Y	N	4806	6550	3810
845.5	621210	5753	25.0	N	N	3275	5030	71833
846.9	611692	5693	10.1	Y	Y	4047	6191	343
625.9	401290	5350	3.2	Y	N	3235	21468	11222
74.1	90240	5311	0.0	N	N	5624	1047	0
666.1	691110	4987	18.2	Y	N	2902	670	5353
831.2	420212	4606	13.4	N	Y	661	3087	20767
667.3	710399	4222	11.5	Y	N	4049	1976	161
695.3	820420	3937	9.0	Y	N	3555	3168	720
75.2	90610	3515	0.0	N	N	2755	669	3793
844.2	610439	3364	18.0	N	Y	2879	18765	18017
	610469	2043	17.7	N	N	1228	18765	18017
893.9	392640	2990	5.3	Y	N	1674	149625	118548
844.8	610821	2966	8.1	N	N	2920	2365	41575
	400129	2657	0.0	N	N	2703	2365	41575
	610831	2722	9.0	N	N	2461	2365	41575
894.7	420321	2895	3.8	Y	N	2288	120622	91062
893.1	392321	2835	3.0	Y	N	2058	170991	31474
841.1	620192	2690	7.1	N	N	274	9039	2236
845.1	620920	2545	14.2	N	N	902	2030	6565
844.7	610620	2435	25.8	N	N	3847	3460	12362
894.4	950590	2390	4.3	Y	N	737	4740	15842
842.2	620413	2320	17.0	N	N	1820	1258	6216
629.9	401699	2164	5.2	Y	N	1848	119803	10178
899.2	670290	2150	10.2	Y	N	1010	158	1913
652.2	521011	2097	10.7	N	N	0	11766	26173

Note: Y = Yes, N = No.
Source: Compiled using the EDB data base and the United Nation Commodity Trade Statistics, 1991.

4.2. Framework for Examining the Price Competitiveness

We stated earlier that it is possible that Sri Lanka's exports to the US market -- mainly those of garments -- could suffer a major setback with Mexico's accession to the NAFTA. Whether it could in fact occur will depend to a great extent on how competitive Mexico has been, or is likely to become, in this regard.

It is believed that although Sri Lankan wages are lower than those of Mexico, this competitive advantage is offset by the low transport cost from Mexico to the USA as well as relatively higher productivity in Mexico. It is imperative in this context to examine how productivity, wages, non-labour costs (fabrics, electricity, telecommunication, machinery, etc.), transport costs, and the price of a garment in Sri Lanka and Mexico are related. In order to bring all these variables under a comparable framework we express the price of a Sri Lankan garment in the US market as a function of, *inter alia*, the above mentioned variables and the price of a Mexican garment in the US market. When this is done the outcome is as follows:

$$P^*_{SL} = \frac{P^*_M (1+\beta+\gamma+\delta)}{\{\alpha(\frac{W_M}{W_{SL}}\frac{PD_M}{PD_{SL}}) + (1-\alpha)(\frac{OC_M}{OC_{SL}} - 1) + 1\}\{1+\Phi\}}$$

Where P^*_{SL}= Price of a Sri Lankan garment in the US market; P^*_M = Price of a Mexican garment in the US market; α = Labour cost as a ratio of total cost or FOB price; Φ = Tariffs for Mexican garments in the USA as a percentage of FOB value; β = Transport cost as a percentage of FOB (both air and sea are considered); γ = Tariffs for Sri Lankan garments in the USA as a percentage of FOB value; δ = Countervailing duties in the USA as a percentage of FOB; W_M = Hourly Wages in Mexico in the garment sector; W_{SL} = Hourly Wages in Sri Lanka in the garment sector; PD_M = Productivity of the garment industry in Mexico, PD_{SL} = Productivity of the garment industry in Sri Lanka; OC_M = Other cost (non-labour cost) of garment production in Mexico; OC_{SL} = Other cost of garment production in Sri Lanka.

The construction of the framework is explained in detail in Appendix I. The framework is used to examine whether Mexico has gained a competitive edge over Sri Lanka for standard garments, after the formation of the NAFTA. More specifically, we examine the price competitiveness of Sri Lanka under four scenarios: (i) pre-NAFTA period (i.e. pre-1994) and pre-GATT (Uruguay Round); (ii) pre-NAFTA (or without NAFTA) and post-GATT (hypothetical case); (iii) post-NAFTA and pre-GATT , and (iv) post-NAFTA

and post-GATT.[10] The competitiveness was determined for garments exported to the USA by air as well as by sea. The estimation of the values for the variables in the equation is shown in Appendix II. The following are the results:

Table11: Sri Lanka's Competitiveness vis-a-vis Mexico For Various Scenarios

Period		Mode of Transport	Comparison -- Sri Lankan & Mexican Prices
Pre GATT (i.e., pre-July 1995)	Pre-NAFTA	Air	$P_{SL}=0.57P_M$
		Sea	$P_{SL}=0.52P_M$
	Post-NAFTA	Air	$P_{SL}=0.65P_M$
		Sea	$P_{SL}=0.59P_M$
Post-GATT (i.e., post-July 1995)	Pre-NAFTA	Air	$P_{SL}=0.55P_M$
		Sea	$P_{SL}=0.49P_M$
	Post-NAFTA	Air	$P_{SL}=0.63P_M$
		Sea	$P_{SL}=0.56P_M$

Clearly, it is evident that irrespective of the NAFTA, Sri Lanka retains her price competitive advantage over Mexico in the US market. The competitive edge is retained by Sri Lanka for garments transported by sea as well as by air.

It is vital to note that the values that have been used in the framework are very favourable for Mexico. For instance, the general Mexican hourly wage in the manufacturing sector is more than 9 times that of Sri Lanka. We have taken a conservative estimate of 6 times. Mexican non-labour costs are twice as high as those of Sri Lanka, but we have taken a conservative estimate of 1.5. We have also assumed the Mexican transport cost to be zero, although this is not the case.

It is expected that, in Mexico, there will be over the years a more rapid increase in wages as well as in non-labour costs than in Sri Lanka (see Section 4.3), which we have not taken into consideration in the framework. We believe that Sri Lanka could take advantage of this to get a better competitive edge over Mexico.

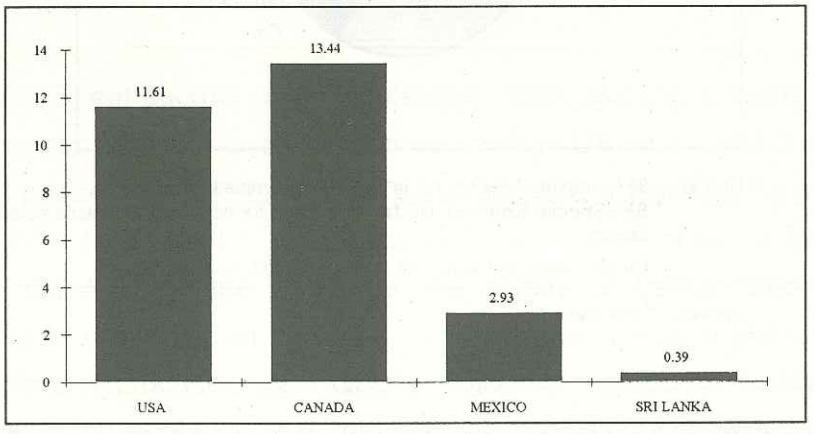
The indications are that, even in the future, despite the absence of cross-border tariffs and countervailing duties for Mexican garments after NAFTA, the average apparel

10 The post-GATT period refers to the post-July 1995 period.

export from Sri Lanka will still have a competitive edge over Mexico in the US market. Clearly, the low cost labour in Sri Lanka has given it a tremendous advantage to still remain competitive in the US market in comparison to Mexico. As Figure 2 shows, Sri Lankan labour is much cheaper than that of Mexico. Moreover, we see that Sri Lanka has benefitted from the Uruguay Round of GATT talks, in the sense that Sri Lanka has managed to get a better competititve edge with post-Uruguay Round tariff reductions.

The study by Safadi and Yeats (1993) states that the potential losses from a decline in exports would be more than offset by the successful completion of the Uruguay Round of Trade Negotiations which would, by lowering the overall level of tariffs, also lower the preferential margins that NAFTA could provide its member countries. Sri Lanka, for instance, is estimated to make a trade gain over the 1991 level of $ 245 million or 49 times the NAFTA-induced losses from a 30 per cent trade liberalization (p. 22). However, our framework shows that the gains from the revised GATT are not very significant. As can be seen in Table11, for garments transported by air the Sri Lankan price improves from $0.65P_M$ to $0.63P_M$, while for garments transported by sea the improvement is from $0.59P_M$ to $0.56P_M$. Thus in regard to Uruguay Round gains we are not so optimistic as Safadi and Yeats (1993).

Figure 2: Hourly Labour Cost Comparison of the USA, Canada, Mexico and Sri Lanka (US $), 1993



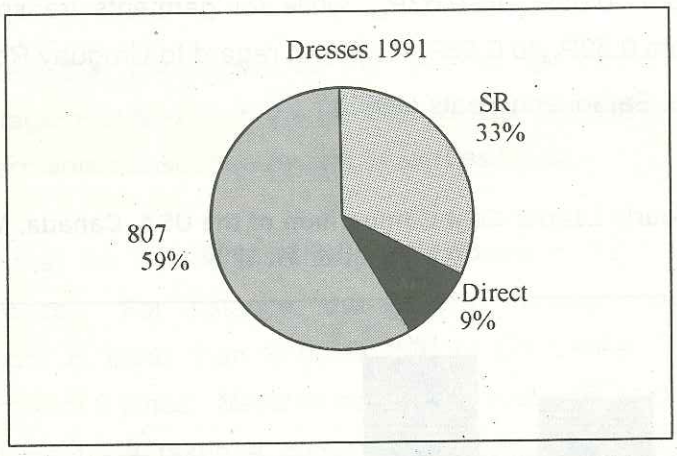
Source: Werner International - Management Consultants, 1993.

In the next Section we explain that there are many advantages that Sri Lanka has over Mexico in the area of garments. However, in order to benefit from the advantages and reap the gains, substantial work needs to be done; this is dealt with in Section 5.

4.3 Factors that are not Advantageous to Mexico

(1) Mexico suffers from domestic supply constraints which have hitherto caused her to consistently underutilize her textile and clothing quotas. In the second half of the 1980s, for instance, her MFA quota utilization rate was about 75 per cent as compared to around 83 per cent for Sri Lanka, and this was in spite of preferential access to the US market under Item 807.[11] Figure 3 shows that 59 per cent of Mexican garment exports to the USA in 1991 were under Item 807. Even with such a large quantity, the Mexican quota utilization rate being below that of Sri Lanka, confirms our observation. In recent years too the Sri Lankan quota-utilization rate has been better than Mexico. Figure 4 shows the quota allocation and utilization pattern for some garment export items common to both Sri Lanka and Mexico. Clearly, except for one item (Coveralls, Cotton/MMF) the quota utilization rate in Sri Lanka has been superior to that of Mexico.

Figure 3: US Imports from Mexico



Notes: **807** : Imported Fabric, cut in the US, assembled in Mexico
SR (Special Regime): US fabric, cut and formed in the US, assembled in Mexico
Direct : Mexican Fabric, cut and assembled in Mexico

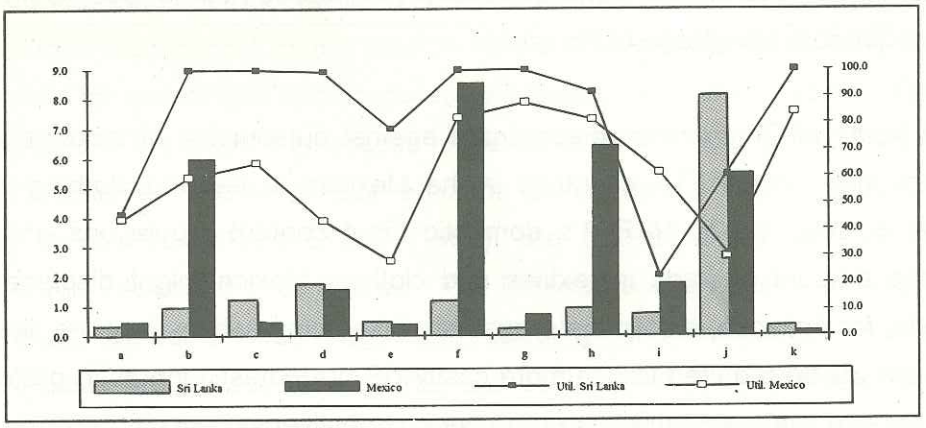
Source: *Trade Resources Inc.*

(2) Labour productivity in Mexico is not very much higher than in Sri Lanka. In Appendix II it is shown that Mexican labour in the manufacturing sector was 1.6 times more productive than Sri Lankan labour in 1989, and twice as much in 1990.

---

11 Under Item 807 Mexico has enjoyed preferential tariffs. Under this clause, garments assembled offshore using US components pay duty only on the value added in the assembly country. This provision helps only those countries that are in close proximity to the USA. The average effective duty rate for Mexico was only 6.5 per cent (pre-NAFTA) because over 60 per cent by value of Mexican garments consisted of US components.

Figure 4: Quota Allocation and Utilization Patterns in Mexico and Sri Lanka during 1992/93



Note:
1. X-axis represents the quota categories that are common to Sri Lanka and Mexico
2. Y-axis (left) represents the total amount of quotas allocated for the given year.
   Y-axis (right) represents the amount utilized
3. The unit of the quotas allocated is in Dozens except for category k which is Nos and category i which is in Kgs.
4.

a	- 336/636/836	-	Dresses cotton/MMF & Other Veg. Fibre
b	- 338/339	-	Shirts and blouses knit, Cotton, MB/WG,
c	- 340/640	-	Shirts woven, cotton/MB, Shirts woven, MMF/MB.
d	- 341/641	-	Blouses Woven, cotton/ Blouses woven MMF.
e	- 342/642/842	-	Skirts, Cotton/ MMF & Other Veg. Fibre.
f	- 347/348/847	-	Trousers, Slacks & Shorts, Cotton & Other Veg. Fibre.
g	- 351/651	-	Nightwear and Pyjamas, Cotton/MMF.
h	- 352/652	-	Underwear, Cotton/MMF.
i	- 359C/659C	-	Coveralls, Cotton/MMF.
j	- 363	-	Terry & other Pile Towels, Cottons.
k	- 635	-	Coats, MMF/WG

Source: International Development Systems, Inc. 1993.

The Asian Wall Street Journal of 30 September 1993, quoting a World Bank study, stated that Mexican labour is one-fifth as productive as US labour and thus US wages are just 2 to 6 per cent higher than Mexico's average after integrating for productivity. It further says that, for some US manufacturers, the cost of labour is less important compared to the skills of the workforce, the quality of transportation, access to technology, etc.[12] And goes on to say, "...in September, 1993, a giant United State electromagnetic coil producer, *viz*: Quality Coils Inc., closed its factory in Mexico because of high absenteeism, low productivity and problems with long distance management".

12 It is well known that high productivity, cost efficient transportation and communication networks, flexible capital markets, access to technology, an educated work force, etc., are factors that the USA enjoys in abundance and which offset lower nominal wages found elsewhere.

The point made here is that the emphasis on higher productivity in Mexico is somewhat misplaced. And above all, the higher productivity in Mexico has not been able to offset the low labour cost advantage of Sri Lanka.

(3) Strict Rules of Origin which discriminate against outsourcing of inputs may impair investment from non-NAFTA countries in the Mexican textile and clothing industries (Bannister & Low, 1992). NAFTA's domestic input content regulations are likely to contain the amount of trade in textiles and clothing Mexico might displace. If such regulations, for instance, discriminate against outsourcing (which they are likely to do) then Mexico will be required to use more costly US or domestic inputs in preference to cheaper outside inputs and thereby erode her competitiveness.

Fernando (1993) has noted that: "Some Taiwanese have already made arrangements to invest in Mexico. A very large Chinese-US joint venture is being formed for the sole purpose of producing apparel in Mexico. Over 200 companies including Levis Strauss, Liz Claireborne and Warnaco Inc. were in the process of setting up manufacturing and sourcing operations in Mexico. Over a third of US apparel firms have confirmed that they plan to invest in Mexico as a result of NAFTA". However, according to Freund et.al (1993), "Although the Mexican textile industry is open to US and other foreign investments, such investments face significant impediments. Textile production requires large capital investment. Mexico's underdeveloped infrastructure, particularly inadequate water supplies for dyeing and finishing yarns and fabrics, will likely discourage significant US and other foreign investment to upgrade Mexico's textile industry". (p 88).

Whatever the case may be, the Rules of Origin will be applicable for all production processes in Mexico and thus the cost of garment raw material would not be cheaper than in East Asian NICs, China, India, etc. Out of the 1100 Rules of Origin, the ones that are relevant to the garment industry are: (a) the "yarn forward" rule or the triple transformation rule where the productive process from yarn forward be implemented within the Free Trade Agreement, (b) the "fibre forward" rule or the quadruple transformation rule where the productive process from fibre forward be implemented within the Agreement. These are the most stringent among the Rules of Origin. There are also: (c) the simple transformation rule where the product needs to be cut and sewn in a member country to qualify as local, and (d) the double transformation rule where the input fabric be manufactured in a NAFTA country.

There is evidence to suggest that the non-labour cost of production in Mexico would be high due to the Rules of Origin as well as to other factors. Bannister and Low (1992) state: "Another hidden cost of the NAFTA is the limited access to third party non-NAFTA inputs for consumers and producers of Mexico. While this cost may seem small now, compared to the gains from access to the US market, it may grow higher if NAFTA production becomes relatively less efficient compared to world markets" (p.32). According to Haufbauer and Schott (1992), the United States has a competitive advantage over Mexico in most textiles. The Mexican textile industry suffers from low quality inputs, outdated technology and capacity under-utilization. As a result, production costs are 25 per cent to 150 per cent higher than in the United States despite much lower Mexican wages. Fabric finishing and dyeing, the weakest links in the Mexican textile value added chain, limit the production of quality fabrics that could be exported or incorporated into apparel exports (op.cit., pp. 267-268).

(4) Mexico needs new investment to expand her export capacity of textiles and clothing, but whether this will be forthcoming or not remains unclear. There is, for instance, no evidence yet whether new US investments in Mexico will be in sectors like automotive parts and computer assembly than in textiles and clothing. Even if there is new foreign investment from the NAFTA countries and others, and Mexico is able to double her exports to the US, she would still remain a small supplier as her share of the US market would expand from about 3.7 per cent to 5.6 per cent during the 1990s causing only an insignificant displacement of third country exports (Safadi and Yeats, 1993).

(5) The cost of production in Mexico will rise much faster than in Sri Lanka during the post-NAFTA period. This is because there is going to be a large influx of US and other investment in Mexico and thus an enormous strain on the country's resources. In fact, as argued earlier, the main benefactor of the NAFTA is Mexico and, according to the OECD (1992), the Mexican growth rate in the next five years would be around 8 per cent.

According to Fortune Magazine: "In 1994 alone US auto-makers expect to ship 60,000 extra vehicles to Mexico. That should add US$ 1 billion to exports and provide employment to an additional 15,000 Americans. Down the road, Boeing estimates that the NAFTA will lift Mexican aircraft purchases by 25 per cent over what they should be without the pact -- which translate into roughly US $ 2 billion in extra sales it hopes to fill. On a smaller scale, Zenith, America's last home-grown TV maker, is already

expanding its Melrose, Illinois, plant to ship more picture tubes to Mexico". (p.53, Fortune, November 29, 1993). Hufbauer and Schott (1992) suggest that by the year 2023 Mexican living standards would surpass the level that the United States reached in 1988 (op.cit.,p. 62). All this clearly indicates that there will be an overheating of the Mexican economy in the near future.

4.4 Proximity: Will Quick Turnaround Time Favour Mexico ?

In recent years, a major change in the garment market has taken place in the form of more buying seasons per year -- they have changed from 2 -4 seasons per year to 6-8. This has happened due, *inter alia*, to the reluctance of firms to carry large stocks because of the recession, and new demand patterns generated by changing trends, i.e., retailers make lower forward commitments in order to have their options open to exploit specific demands during the prevailing season. In other words, production runs are becoming shorter with an increase in style and variety (Fernando, 1993). Thus speed of delivery is extremely important in determining the competitiveness.

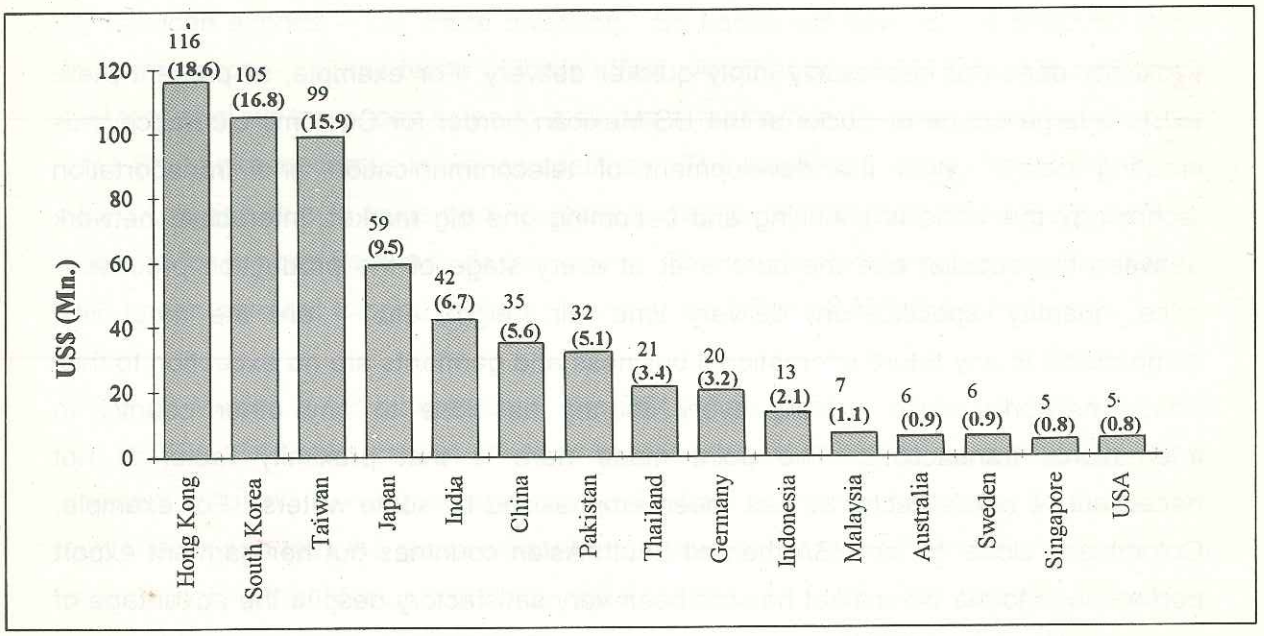
The Sri Lankan garment export industry depends on imports for nearly 95 per cent of fabric requirements and around 50 per cent on imports for other non-fabric ancillaries (Kelegama, 1993b). Due to the high dependence on imported inputs the turn around time of the Sri Lankan garment export industry tend to be nearly 90-150 days, i.e., to import the raw material, manufacture, and export from the date of order. Thus Fernando (1993) has argued that the changing structure of the industry is to the benefit of the exporting countries closer in location to the market and that in this respect Mexico has an advantage over Sri Lanka.

The possible shift of some US apparel industries to Mexico could also be due to faster delivery or quick turnaround time in Mexico. But whether Mexico's proximity to the USA could have a significant adverse effect on Sri Lanka's garment exports has to be examined in more detail. It must be emphasized that the sourcing of garment raw material is very important in any analysis of delivery. We believe that Mexico will be able to respond faster to: (a) CMT/CMP (Cut Make and Trim/Cut Make and Pack) packages based wholly on US raw material, and (b) seasonal garments also based on US raw material. For all other garments, Mexico will not necessarily have an advantage in terms of quick delivery.

In order to justify this, it is necessary to analyze the US garment import structure. Figure 1 shows that the bulk of US imports -- nearly 71 per cent -- originate in Asian countries -- China and the East Asian NICs accounting for 48 per cent; Indonesia, Thailand, Malaysia, Philippines, and Macau accounting for 13.6 per cent; India, Pakistan, Bangladesh, and Sri Lanka accounting for 9.1 per cent. This is because most US garment buyers have their cheaper raw material suppliers in the East Asian NICs. Thus in terms of obtaining the raw material preferred by many US buyers, Sri Lanka is in an advantageous position, because Sri Lanka is closer to East Asian NICs compared to Mexico. Irrespective of the NAFTA this factor will remain favourable to Sri Lanka in the future.

It should also be emphasized that even in regard to CMT/CMP packages, US buyers most often provide the raw material purchased from East Asian NICs. This is evident in an analysis of the fabrics imported by Sri Lanka -- fabrics obviously being the main raw material in garment production (see Figure 5). As shown, the bulk of it -- 87 per cent --

Figure 5: Major Textile Fabric Suppliers to Sri Lanka, 1992, (Value US$ Millions)



Note: Figures in parenthesis represent percentage.
Source: Plotted using data of the Sri Lanka Customs.

comes from Asian countries: 52.1 per cent from East Asian NICs, 11.8 per cent from India and Pakistan, and 22.6 per cent from Japan, Thailand, Indonesia, China, Malaysia, and Australia. The USA accounts only for 0.8 per cent of total fabric imports. The three suppliers -- Hong Kong, South Korea and Taiwan provided mostly medium range fabrics, while India and China supplied cheaper fabrics, and Japan, Germany and the US supplied fabrics to the higher end of the market.

It should be noted that although CMT/CMP packages come under No Foreign Exchange they do get recorded at the Customs. The CMT/CMP packages account only for 30 per cent of garment exports (Kelegama, 1993b). Even for this category it appears that the bulk of the raw material is obtained from Asian countries.

The USA mainly supply fabrics that are at the high-end of the market, and the fabrics to the value of US$ 5 million that were imported by Sri Lanka from the USA in 1992 belonged mainly to this category. It is reasonable to postulate that Mexico will have an edge over Sri Lanka for high fashion garments because the required raw material is available in abundance in the USA. For example, under the former Item 807, raw material supply sources were not East Asian NICs but the USA. Thus, proximity to the USA does place Mexico at an advantage for fabrics and garments of the high-end of the market.

Proximity does not necessarily imply quicker delivery. For example, at present there exists a large queue of trucks at the US-Mexican border for Customs clearance thus creating delays. With the development of telecommunication and transportation technology the world is shrinking and becoming one big market. Interactive network between the supplier and the purchaser at every stage of the production process -- price, quantity, specification, delivery time, air freight, etc. -- are the most vital components in any future international business and garments are no exception to this. These networks make virtually every country as close to any other country in international transactions. The point made here is that proximity factor is not necessarily a crucial factor as has been emphasized by some writers. For example, Colombia is closer to the USA than all South Asian countries but her garment export performance to the US market has not been very satisfactory despite the advantage of proximity (Morwetz, 1981).

All in all, we see that Sri Lanka has a price advantage as well as some non-price advantages over Mexico irrespective of the NAFTA. Whatever non-price advantage that Mexico has in terms of quick turn around time is insignificant in the context of the many standard garment exports of Sri Lanka.

5. Conclusion

In this paper we have argued that the NAFTA is not a great threat to Sri Lanka's external trade. We have used a comparative static framework to analyze Sri Lanka's competitiveness vis-a-vis Mexico in the US market. We showed that Sri Lanka would still retain her competitive advantage over Mexico in standard garment exports irrespective of the NAFTA, and that the advantage that Sri Lanka commands would improve after 1995 with the new GATT tariff reductions coming into operation. However, we have shown that this improvement is not very significant as has been claimed by Safadi and Yeats (1993). Our framework is based on certain assumptions and thus is not rich enough to explore a wide range of alternatives which need to be examined in practice. However, the framework is adequate to obtain a general picture of the standard Sri Lankan garments catered to the low-end of the US market.

We argued that at the high-end of the market Sri Lankan garments would be displaced by Mexican exports -- i.e., trade diversion. Sri Lanka will have to cut prices to match the preference -- i.e., the terms of trade effect. Another possibility is both to reduce the quantity and cut the prices so as to maintain a foothold in the market in the short-run, until Sri Lanka becomes more competitive. The increased economic growth in the NAFTA region due to trade and investment creation in the medium-term will increase demand for imports from outside the region. This would provide some opportunities for Sri Lankan garment exports to the high-end of the US market, in the long run.

Although Mexico is not a big threat to the Sri Lankan garment industry in the context of the NAFTA, Sri Lanka cannot afford to be complacent about the current status of her garment industry. We argued that, unlike Sri Lanka, Mexico has many infrastructural bottlenecks and thus the quota utilization rate was below that of Sri Lanka. However, it is worth noting that Mexico has made rapid progress and very soon she may overcome some of her major supply constraints.

The recent economic reforms have rectified much of the supply bottlenecks in Mexico. For example, in an attempt to improve the telecommunication system, the government-controlled telephone company was sold. Several US telephone companies have now established fibre-optic lines in Mexico. A new highway, which is under construction is intended to link major cities, and the trucking industry is being deregulated for greater efficiency. To counter absenteeism, some plant managers have provided numerous incentives, including free meals, sports activities, showers, bus transport, and a bonus of US$ 5 to those employees who have perfect attendance for a period of one week. Thus in the coming years it is expected that Mexico will overcome some of her present problems.

Using the history of Spain's accession to the European Community as a guide, one need not be surprised if Mexican exports of textiles and apparel increase from US $ 3 billion to US $ 5 billion in ten years -- an export gain of US $ 2 billion. In the five years between 1985 and 1990, after the enlargement of the European Community with the inclusion of Spain and Portugal, Spanish and Portuguese exports of textiles and apparel to the Community soared from $ 1.7 billion to $ 5 billion. According to Haufbauer and Schott (1992), over a ten-year period, Mexicans can achieve even larger gains in the United States and Canadian markets (op.cit., p. 278).

The views of Haufbauer and Scott may be very optimistic, however, Sri Lanka has to be cognizant of the above possibilities and endeavour to remain competitive. Moreover, adapting to the technological changes is essential. For Sri Lanka to remain competitive, more work is necessary on the demand side, and substantial work needs to be done on the supply side. The policy measures that we outline below in (a) and (b) are of a general nature and not specifically in view of NAFTA's impact on Sri Lanka's exports. However, they are also relevant for the future challenges from NAFTA.

(a) Marketing

On the demand side Sri Lanka has progressed well in establishing market links and a good reputation with garment buying offices. However, more work needs to be done. For example, most US entrepreneurs hardly know about Sri Lanka. Besides, there are no big US garment industrialists who would lobby in favour of Sri Lankan exporters in issues such as the removal of the countervailing duties which caused an annual loss in the region of Rs. 1 billion for Sri Lanka. It is because of this lacuna that the Sri Lankan government led by the Prime Minister had to take this issue on a bilateral basis with the

US government in early 1994. Thus there is an urgent need for establishing stronger market links with US buyers.

In the US market, around 20 per cent of the apparel buyers are relatively small shops which are mainly involved in selling apparel to the high end of the market. These shops have established short-term contracts with some garment producers of certain developing countries and place orders with them for fashionable garments according to their market needs. These buyers are, in fact, increasing their market dominance in the US market. Garment exporters in Thailand, for instance, have succeeded in developing strong links with these small buyers and it has helped the Thai garment industry in recent years. It is time now for Sri Lanka's apparel exporters to establish links with these small buyers in the US market. Sri Lanka will find it easier to do this because in many cases the purchasing requirements of large US buyers are too great for many Sri Lankan firms to meet.

Without further delay, Sri Lanka's apparel exporters should make every attempt to compete in the non-quota market and also produce items for the upmarket. Sri Lanka has not made use of the assured market provided by the quota to consolidate her market niche in order to ensure for herself a market in a quota-free world. Sri Lanka's marketing efforts are confined to a few buying offices in Colombo. Thus establishing stronger links with the US Textile and Clothing sector is essential.

There is a belief that the forward integration would take place via the market, i.e., through the buying offices. However, in the context of the rapid changes taking place in the world today, and in view of the marketing barriers facing manufactured items from developing countries (Lall, 1991: 137-150), it is essential that a greater effort be made to establish more rewarding market links.

(b) Improving the Efficiency of the Garment Production Base

Although we have emphasized the importance of the high end of the market, still there is much to be done at the low-end of the market. Here, what is essential is cutting down the cost of production. In cutting down costs, there is a tendency in Sri Lanka to focus mainly on the wage component. Eliminating wastage, imposing penalties for absenteeism, introducing management training, etc., are not seriously considered for the purpose of cutting down the cost of production. Fonseka (1993) states that the "Chief Executive Officers are pre-occupied with day-to-day operational planning to the

neglect of long-term planning" (p.56). It is time for Sri Lankan garment exporters to work on these factors because Sri Lanka's competitors such as Bangladesh, are far ahead of Sri Lanka in this respect.

It is essential for Sri Lanka to increase the productivity of the garment sector because Sri Lanka is no longer considered as a low wage country by international buyers. As stated in Appendix II, Sri Lanka's wages per month in the garment sector is US $ 55 compared to US $ 35 in Bangladesh and US $ 22 in upcoming garment exporters such as Vietnam and Cambodia. It is also vital to note that the garment industry is rapidly undergoing changes in the use of machinery. Automation, computer design, etc., are becoming part and parcel of the garment industry. Sri Lanka has to adjust to these situations in the coming years.

More work has to be done on design development (see for instance, Fonseka, 1993). For this purpose, human resource development in the garment industry has to be enhanced. (See for instance, Fernando, 1994). In India, for instance, designers anticipate fashion trends 5 years ahead. Such schemes should be introduced in Sri Lanka. The initiative that is given by agencies such as SWEDCORP (Swedish International Enterprise Development) should be followed up by local agencies. Design development is essential to reach the high end of the market. For example, Switzerland is a very strong apparel producer for the European market not because of quota benefits or low wages but because of her high quality products and trend-setting designs.

Sri Lanka has so far utilized quotas as an instrument to attract foreign investment and to push industries into rural areas under the 200 Garment Factory Programme. The present distribution strategy of quotas is a serious impediment to product specialization and increasing productivity. Thus the quota distribution strategy requires serious reformulation.

The immediate option for the Sri Lankan garment sector in the context of NAFTA is not backward integration but forward integration -- going up-market while increasing productivity. The State should be extremely selective in its backward integration strategy. Given the multifarious demand for fabrics, buttons, etc., we believe that industries manufacturing these items should not be promoted on a large-scale in Sri Lanka because they will not be able to meet the entire demand of the local garment

export industry. The turn around time could be improved by promoting the garment ancillary industries selectively. But the immediate requirement for improving the turn around time is to reduce the cumbersome procedures and bureaucratic delays that the non-BOI exporters have to go through at the Customs. Liberalization of air freight facilities would also be helpful to improve the cargo space.

(c) Export Diversification should be a Priority in the Context of the NAFTA

The need for diversification of export products in the North American market has to be emphasized. Finding new markets for products that would be displaced by theNAFTA could be done by evaluating future market trends and catering to new market demands. Sri Lanka should diversify markets for her garments and seize opportunities that are emerging in the Middle East, South Africa, CIS, and other countries. Products other than garments that would face a threat from NAFTA are ceramics and porcelain ware, plastic and plastic products, machine tools, leather, footwear and travel goods and other manufactured products. Sri Lanka should intensify new exports to the USA that would not face much competition from Mexico.

Sri Lanka should aim at making maximum use of the opportunities that come from NAFTA. For example, with the growth of the Mexican economy there will be good potential for expanding the export of items such as cinnamon, desiccated coconut, rubber, fibre, brooms, brushes, etc., that have already found a market in Mexico.

(d) Sri Lanka should Exploit the Spin-off Effects of the NAFTA

If the garment firms of East Asian NICs that are catering to the US market find it difficult to compete in the US market with Mexican garments after NAFTA, then these firms are going to relocate themselves in countries where the labour is cheap and the economic environment is liberal. The quota cutting process in the post-1995 period will create its own dynamics in the form of capital flight from garment firms in the NICs towards destinations where the labour is cheap. Thus most of the NICs may relocate their garment industries in low labour cost countries. Sri Lanka is in a very strong position to attract these firms. Once they come, their buying offices will also shift to Sri Lanka ('Flying geese' phenomenon) and further strengthen the international market linkages. Nature of trade regime has been an equally important factor as cheap labour in Sri Lanka's garment export growth during the last decade. Thus the view that most East Asian garment factories would shift to Vietnam, Indonesia, Bangladesh, etc., in the post-NAFTA and during the quota phasing out period is somewhat misplaced. In fact,

Sri Lanka is in a better position to attract some of these firms due to the stronger liberal trade regime and less bureaucratic delays, less cumbersome procedures and red tape at the Customs, than that exist in the abovementioned countries.

In general, the redeeming feature for Sri Lanka is that there is time to adjust. The USA may not strain her trade liberalization with regular trading partners in the short-run as a result of the North American Free Trade Agreement. This gives at least four years for Sri Lankan exporters to adjust to the changing situation and the time is opportune to initiate such action. The NAFTA will possibly become a threat to the Sri Lankan garment exports when at a future date it is expanded to include Central and Latin American countries. At present, NAFTA's negative impact on Sri Lanka is marginal and insignificant.

APPENDIX I

The derivation of the expression in Section 4.2 is as follows. In a competitive framework the price is normally equal to the average cost.

Thus P = AC ---- (1) where P = Price per garment and AC = Average Cost per garment
TC = LC + OC where TC = Total Cost per garment, LC = Labour Cost per garment, and OC = Other Costs (or non-labour costs) per garment

If we use the suffix M for Mexico and SL for Sri Lanka, then
Total Cost for Mexico and Sri Lanka are given by :

$$TC_M = LC_M + OC_M \text{ ----------(2)}$$
$$TC_{SL} = LC_{SL} + OC_{SL} \text{ ----------(3)}$$

$$(2) - (3) = TC_M - TC_{SL} = LC_M - LC_{SL} + OC_M - OC_{SL}$$

$$\frac{TC_M - TC_{SL}}{TC_{SL}} = \frac{LC_M - LC_{SL}}{LC_{SL}} \cdot \frac{LC_{SL}}{TC_{SL}} + \frac{OC_M - OC_{SL}}{OC_{SL}} \cdot \frac{OC_{SL}}{TC_{SL}}$$

$$\frac{TC_M}{TC_{SL}} = \alpha \left(\frac{LC_M - LC_{SL}}{LC_{SL}}\right) + (1 - \alpha)\left(\frac{OC_M}{OC_{SL}} - 1\right) + 1 \text{ .....(4)}$$

Where α = Labour cost as a ratio of total cost.

Now $LC = \frac{LC}{L} \cdot \frac{L}{1}$ where L = Labour needed to produce 1 garment.

$$= \frac{LC}{L} \cdot \frac{1}{(1/L)}$$

$\frac{LC}{L} = W$ and $\frac{1}{L} = PD$; where W = wages and PD = Productivity

$$= \frac{W}{PD}$$

$$LC = \frac{W}{PD} \text{ ---------- (5)}$$

Differentiating equation (5) we get

$$d(LC) = \frac{dW}{PD} - \frac{W}{(PD)^2} d(PD)$$

$$\frac{d(LC)}{LC} = \frac{PD}{W} \cdot \frac{dW}{PD} - \frac{PD}{W} \cdot \frac{W}{(PD)^2} d(PD)$$

$$= \frac{dW}{W} - \frac{d(PD)}{PD}$$

$$\therefore \frac{D(LC)}{LC} = \frac{DW}{W} - \frac{D(PD)}{PD} \text{----------(6)}$$

Equation (6) gives the differential of labour cost between Mexico and Sri Lanka as follows:

$$\frac{LC_M - LC_{SL}}{LC_{SL}} = \frac{W_M - W_{SL}}{W_{SL}} - \frac{PD_M - PD_{SL}}{PD_{SL}}$$

$$= \frac{(W_M - 1)}{W_{SL}} - \frac{(PD_M - 1)}{PD_{SL}}$$

$$= \frac{W_M}{W_{SL}} - \frac{PD_M}{PD_{SL}} \text{----------(7)}$$

(4) & (7) give

$$\frac{TC_M}{TC_{SL}} = \alpha \left(\frac{W_M}{W_{SL}} - \frac{PD_M}{PD_{SL}}\right) + (1-\alpha)\left(\frac{OC_M}{OC_{SL}} - 1\right) + 1 \text{----------(8)}$$

(1) & (8) give

$$\frac{P_M}{P_{SL}} = \frac{AC_M}{AC_{SL}} = \frac{TC_M}{TC_{SL}} = \alpha\left(\frac{W_M}{W_{SL}} - \frac{PD_M}{PD_{SL}}\right) + (1-\alpha)\left(\frac{OC_M}{OC_{SL}} - 1\right) + 1$$

$$\therefore P_M = \left\{\alpha\left(\frac{W_M}{W_{SL}} - \frac{PD_M}{PD_{SL}}\right) + (1-\alpha)\left\{\left(\frac{OC_M}{OC_{SL}} - 1\right) + 1\right\}\right\} P_{SL} \text{----------(9)}$$

P_{SL} refers to the price of a garment before exporting from Sri Lanka. However, what should be analyzed is the price of a garment in the US market. Sri Lankan garments, unlike Mexican ones, have to face transport and insurance cost, tariffs, and countervailing duties in the US market. If we itemize these as a percentage of the FOB value as β, γ and δ respectively, we have

$$P_{SL}(1+\beta+\gamma+\delta) = P^*_{SL} \text{---------- (10)}$$

Where P^*_{SL} is the price of a Sri Lankan garment in the US market. Similarly the Mexican price in the US market needs to be investigated. During the pre-NAFTA period, let the US tariffs for the Mexican garments be Φ. For the post-NAFTA period $\Phi = 0$ or for some garments tariffs would be reduced in stages (in the latter case also we assume $\Phi = 0$).

$$P_M (1+\Phi)=P^*_M \text{----------(10)}$$

(10)+(11) give,

$$P^*_{SL} = \frac{P^*_M (1+\beta+\gamma+\delta)}{\{\alpha(\underline{W_M}-\underline{PD_M}) + (1 - \alpha)\ (\underline{OC_M} - 1) +1\}\{1 + \Phi\}} \quad \text{---------- (11)}$$
$$W_{SL} \quad PD_{SL} \quad OC_{SL}$$

Appendix II provides the values for $\beta, \gamma, \delta, \Phi$ and α.

As shown,
$\delta = 0.03$
$\gamma = 0.20$ for the pre-GATT period and, $\gamma = 0.14$ for the post-GATT period
$\Phi = O$ for post-NAFTA period and, $\Phi = 0.14$ for the pre-NAFTA period.
$\beta = 0.07$ for sea transport, and $\beta = 0.21$ for air transport.

Appendix II also shows $\underline{W_M} = 9$ but for our estimation we use $\underline{W_M} = 6$ in order to give
W_{SL} W_{SL}
Mexico the benefit of doubt.

We use $\underline{PD_M} = 2$ as estimated in the Appendix. However $\underline{OC_M}$ is equated to 1.5
PD_{SL} OC_{SL}
instead of 2 in order to give the benefit of doubt to Mexico (see Appendix II).

APPENDIX II

The Estimation of Variables in the Model

(a) Sea & Air Transport Cost to the USA as a percentage of FOB

Sea

According to MIST (1992, p.52) transport cost per cubic meter (cbm) to the USA = US$ 107.15

Normally 500 shirts occupy an area of 1.34 cbm.

∴ Transport cost per shirt = US$ $(107.15 \times \frac{1.34}{500})$

= US$ 0.30

Air

Assume that the shirts consignment weighs more than 500 kg

According to MIST (1992, p.51) transport cost per kg. for such a consignment to the USA = US$ 3.02

For one shirt(cotton) which normally weighs around $(\frac{325}{1000})$kgs. the transport cost = US$ $(3.20 \times \frac{325}{1000})$

= US$ 1

FOB value of a shirt (cotton) is in the range of US$ 3.50 - US$4.50 at the low-end of the market and in the range of US$ 5 - US$ 8 in the uppermarket. If we take the average FOB value of a shirt to be around US$ 5, then the sea and air transport costs per shirt are around 0.06 of FOB value, and 0.20 of FOB value respectively. Insurance cost is normally about 0.01 of FOB value. Thus transport and insurance costs per shirt by sea and air will be 0.07 and 0.21 of FOB value, respectively.

(b) Average Tariffs to the USA as a percentage of FOB = 20% of FOB

(c) Countervailing Duties as a percentage of FOB = 0.03% of FOB

(d) Wages in Mexico and Sri Lanka

Mexican wages do not rank among the lowest in developing countries. Mexico ranks 29th in the annual costs comparison produced by Werner International with a labour cost (including non-wage payments) of $2.81 (to 2.93) per hour. Although this puts wages in Mexico below a quarter of those in the USA and lower than those in Taiwan ($5.00), South Korea ($3.60), Hong Kong ($3.39), Singapore ($3.36) and Turkey ($3.12), they are nevertheless higher than in all the other major countries in Latin America, South East Asia, South Asia and Africa (excluding Tunisia). Examples are: Argentina ($2.41), Brazil ($1.53), Peru ($1.25), Thailand ($0.87), Philippines ($0.67), India ($0.55), Pakistan ($0.38) and China ($0.34). In particular, Mexican wage rates exceed those among competitive apparel assemblers in Latin America (see Mandelbaum, 1992).

In Sri Lanka, although the minimum wage is Rs. 2000, in the garment sector, actually, it is above this figure due to overtime payments and bonuses. Reliable sources in the garment sector claim that the average wage in the garment sector amounts to nearly Rs. 2,700 or US $ 55. Thus the daily wage in the garment sector would be around US $ 2.3 (assuming 24 days of work in a month) and the hourly wage around US$ 0.30 (assuming eight hours of work a day). The maximum hourly wage would be around US$ 0.39. Clearly, Mexican wages are nearly nine times those of Sri Lanka. This figure is in fact a conservative estimate because, according to the World Bank, the hourly wage in Mexico in most urban areas is around US$ 3.35 (quoted in Asian Wall Street Journal, 30 September 1993) which is eleven times that of Sri Lanka.

(e) Productivity in Mexico and Sri Lanka

If we take 1980 as the base year for measuring productivity (1980 = 100) then Sri Lanka's productivity in the manufacturing sector (defined as (Y/L) 1/P, where Y = nominal output, P = GDP deflator and L = Labour force in the manufacturing sector) in 1989 was 74 and in 1990 productivity was 63 (estimated using statistics given in Department of Census and Statistics, 1992). The corresponding figures for Mexico (with the same base year) are 118.7 in 1989 and 126.2 in 1990 (National Institute of Statistics, Geography, and Information, 1993). Clearly, the productivity in the manufacturing sector is 1.6 times and 2 times higher in 1989 and 1990, respectively, in Mexico compared to that of Sri Lanka. For our purpose we shall take the latest value of $PD_M/PD_{SL} = 2$.

(f) Estimation of labour cost as a percentage of the FOB value of exports

Whether a labourer works or not the cost per machine (which performs cutting, stitching, packing, etc.) per day is close to US $ 8. On average there are about 45 workers per line and approximately 700 shirts are manufactured a day. Clearly, a person produces on average 15 shirts per day. Thus the labour cost amounts to US $ 0.53. With additional payments this increases to US $ 0.68 which is about 17 per cent of the FOB value of a shirt (assuming the price of the shirt to be US $ 4). With overheads the total labour cost works out to be about 20 per cent of the FOB value.

(g) Other Costs in Mexico

Since the Mexican per capita income is about six times higher than that of Sri Lanka, non-labour costs have to be higher in Mexico. As stated in the text, production costs in Mexico are 25 per cent to 150 per cent higher than in the United States. In 1984, the USA supplied 93 per cent of synthetic fabrics and 73 per cent of artificial fibre products, while the remainder was supplied by Asian countries (Mandelbaum, 1992). Given the fact that the US fabrics are much higher in price than the fabrics supplied by East Asian NICs, the non-labour costs in Mexico would be twice as much as those existing in Sri Lanka. For more details on non-labour costs, see for instance, Claudio and Klater, 1992, Madelbaum, 1992, Silva, 1993, & others.

(h) Duty Rates in the USA for Sri Lanka and Mexico

For Sri Lanka, the average duty rates for all imported garments were around 20 per cent in the USA before the GATT (Safadi and Yeats, 1993, p.11), whereas for Mexico it was around 14 per cent (op.cit., p.17). It has been estimated that the overall tariff reduction in the USA for Sri Lanka's exports consequent to the Uruguay Round would be around 7 per cent (Ministry of Foreign Affairs, 1993) and we have used this figure to estimate the post-GATT price values. The post-NAFTA tariffs for Mexico have been equated to zero.

References

Bannister, G. and P. Low (1992), Textiles and Apparel in NAFTA: A Case of Constrained Liberalization, World Bank, Working Paper, WPS 994, Washington, DC.

Claudio, L. and E. Klater (1992), Mexico: The Strategy to Achieve Sustained Economic Growth, IMF Occasional Paper 99, Washington, D.C.

Department of Census and Statistics (1992), Industrial Survey: 1990, Colombo.

National Institute of Statistics, Geography, and Information (1993), Mexico: Economic and Social Information, January-April 1993.

Driscoll, A.M. (1993), "Embracing Change, Enhancing Competitiveness: NAFTA's Key Provisions", Business America, 18 October, 1993.

Fernando, Lakdasa (1994), "Development of Human Resource for the Sri Lankan Textile and Apparel Industries", paper presented to the Annual Conference of the Textile Institute, Ratmalana.

Fernando, Lyn (1993), "NAFTA and its Effect on Sri Lanka's Garment Exports to USA and Canada", Ceylon Daily News, 17-18 December 1993.

Fonseka, T. (1993), "Strategy Making and Marketing Sophistication in Sri Lanka Exporting Firms" in Nanayakkara, G (ed.) The Emerging Economic Order in Sri Lanka : Managerial Leadership, Postgraduate Institute of Management and Goethe Institute publication, Colombo.

Freund, K., A. Harney, O. Holoyda, J. Jones and L. Shelton (1993), "NAFTA and Textiles", in Textile Asia, April 1993.

Hufbauer, G. and J. Schott (1992), North American Free Trade: Issues and Recommendations, Institute for International Economics, Washington D.C.

IMF (1992), Regional Trade Arrangements, Occasional Paper 93, Washington, D.C.

Jacobs, S.P. (1993), "The NAFTA: Exports, Jobs, Wages and Investment", Business America, 18 October, 1993.

Kelegama, S. (1993a), "European Community and Its Impact on Trade with Developing Countries: With Special Reference to Sri Lanka", Economic Review (People's Bank), January.

Kelegama, S. (1993b), "The Development of Backward Linkages from the Garment Industry in Sri Lanka", study for the Ceylon National Chamber of Industries.

Lall, S. (1991), "Marketing Barriers facing Developing Country Manufactured Exporters", Journal of Development Studies, July, London.

Mandelbaum, J (1992), "Competitiveness of the Mexican Textile Chain", Textile Outlook International, November.

Ministry of Industries Science, and Technology (1992), Industrial Factor Costs, Government Press, Colombo (referred to in the text as MIST, 1992).

Ministry of Foreign Affairs (1993), "GATT Negotiation Outcome at the Uruguay Round", Sri Lankan Mission in Geneva, (mimeo).

Morawetz, D. (1981), Why the Emperor's New Clothes are not Made in Colombia: A Case Study in Latin American and East Asian Manufactured Exports, New York, OUP for the World Bank.

National Trade Data Bank (various issues), "The Export Connection", Commercial Division, United States Embassy in Sri Lanka.

OECD (1992), OECD Economic Surveys: Mexico, 1991/1992, OECD, Paris.

Safadi, R. and A. Yeats (1993), The North American Free Trade Agreement: Its Effects on South Asia, World Bank, Working Paper, WPS 1119, Washington, D.C.

Silva, Fernando, B. (1993), "Mexico: The Making of a New Market", Bobbin, August.

Szymczak, P. (1992), "International Trade and Investment Liberalization: Mexico's Experience and Prospects", in Loser, C. and Klater, E. (ed.) Mexico: The Strategy to Achieve Sustained Economic Growth, IMF Occasional Paper 99, Washington, DC.

Tore, A. de la and M. Kelly (1992), Regional Trade Agreements, IMF Occasional Paper 93, Washington, DC.

United States Information Service (various issues), "Trends Backgrounder", Colombo office.

World Bank (1993), International Trade Statistics, Year Book, 1993, Washington, DC.

Stock Verification

Year	Verified
2015	
2020	
2025	