The Uruguay Round and MFA Quotas: The Textiles and Garment Industries in Sri Lanka - The Next 10 Years

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CONTENTS

1. Summary i

1. Introduction 1

2. What is there to gain or lose? The state of the Sri Lankan textiles and garment industry 2

   2.1 The present state of the industries - output, value added and employment 2
   2.2 The development of the industries and major producers 5
   2.3 The future development of the textile and garment industries in Sri Lanka 12

3. MFA quotas - What are they ? And how do they work in Sri Lanka? 13

   3.1 The MFAs - What are they? How do they operate? 13
   3.2 Quotas and Sri Lankan production and exports 16
   3.3 The pressure on quotas for the US market in the 1990s 23
   3.4 Quotas in the garment industry and profits, pressure-groups and prices 26

4. Costs, technology and competitiveness - generally and in Sri Lanka 32

   4.1 Introduction 32
   4.2 The general picture 33
   4.3 Costs and competitiveness in Sri Lanka - fibre production 36
   4.4 Costs and competitiveness in Sri Lanka - yarn production 36
   4.5 Costs and competitiveness in Sri Lanka - fabric production 38
   4.6 Costs and competitiveness in Sri Lanka - accessory production 43
   4.7 Costs and competitiveness in Sri Lanka - garment production 45
   4.8 Devaluation and competitiveness 47

5. The 'phasing-out' of MFA quotas, global demand for textiles and garments and prospects for Sri Lankan production 48

   5.1 The liberalisation - what does it mean? 48
   5.2 The medium-term (to 2005) and the growth of quotas 50
   5.3 The tariff arrangements in the USA and the EU 51
   5.4 The long-term and the phasing-out of quotas 54
   5.5 The long-term, the phasing-out of MFA quotas and the competition; a summary 56

Appendix 1 Abbreviations 59

Appendix 2 Conversion Factors - square metres per unit 60

Appendix 3 Garment Exporters - Sri Lanka 1993 61

Appendix 4 Quotas - Their Effects and Who Gains and Loses? 65

Appendix 5 The Uruguay Round Agreement on Textiles and Clothing 69

Appendix 6 Exports of garments from Sri Lanka to USA (1989-95) 71

References 72

The Uruguay Round and MFA Quotas: The Textiles and Garment Industries in Sri Lanka - The Next 10 Years

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SUMMARY

1. What is there to gain? The Sri Lankan textiles and garment industry past and present

Contrasting views have been expressed regarding the prospects of the textiles and garment (T&G) sector; *an optimistic example comes from the Japanese Textile Garment Newsgroup (JTN) 1995;*

> *"All in all, the Sri Lankan garment industry will grow rapidly for the next 20 years and there are no signs of Sri Lanka losing its comparative advantage in garments exports to newcomers such as Vietnam and Cambodia" (JTN 1995).*

A pessimistic example from the Daily News of March 1st, 1995:

> *"Current trends indicate a reversal and slowing down of the initial momentum of Sri Lanka's garment industry, which could lead to a serious decline and loss of its competitive edge unless remedial measures are implemented soon, two memoranda addressed to the government said yesterday" (Daily News March 1, 1995)*

In discussions following one of the seminars, an industrial adviser to the Sri Lankan government questioned whether Sri Lanka should continue to promote the textile and garments sector. He argued that it was a low-skill, low-technology, low value-added, slow growth and increasingly competitive sector. ***In promoting this sector, he argued, the government would be picking a loser, not a winner. By contrast, we argue that the government should continue to promote this sector.*** *It is a fact that, at present, the sector is a low value-added sector and that at the world level, consumption is growing slowly -- at about 2 per cent to 3 per cent pa. It is also true that in Sri Lanka, it is a low-technology sector, dominated as it is by the garments industry. It is also a sector which, in spite of the panoply of protectionism encompassing it across the world, is subject to intense and increasing competition.*

However the sector has made, and continues to make, a considerable contribution to economic growth in Sri Lanka, as the statistics in Chapter 2 of the Main Report testify. A number of general observations have emerged.

1.1 ***There are many weaknesses and gaps in the statistics on the manufacturing sector in Sri Lanka.*** *Statistics on the T&G sector in Sri Lanka are no exception, although the broad parameters are clear.*

1.2 ***Net output*** *(value-added) in the Textile and Garment industries is about 30 per cent of the total for the manufacturing sector while employment and gross output are about 40 per cent of the manufacturing total. The T&G sector employs nearly 350,000 workers of whom about 60 per cent are in the garments industry. Relative to the manufacturing sector as a whole, the T&G sector seems to have a similar level of value added per employee.*

1.3 *As Table 2.4 in the Main Report shows, the garments industry is highly export-oriented, whereas the fabrics industry is highly geared to production for the domestic market, with direct exports (as opposed to fabrics going through the garments industry) accounting for only about 10 per cent of total domestic production.*

1.4 *There is no significant fibre production in Sri Lanka and little scope for any increase.*

1.5 ***The spinning*** *industry in Sri Lanka is almost 50 per cent self- sufficient. It is widely variable in productivity with about half the spindles in capacity producing at low productivity levels. The industry is highly concentrated with Kabool accounting for over half of all production.*

1.6 *In contrast, no single producer in the* ***fabrics*** *industry produces more than 13 per cent of total output which is mainly geared to production for the domestic market. Direct exports amount to only about 10-15 per cent of the value of gross output (about 215 mn metres); and in 1993, the sector only provided about 5 per cent to 10 per cent of the 450 million metres of fabric used by the garment exporters (TTSC 1994 4, 25). The industry was highly protected before 1977 but, in recent years, the listed import duties have been reduced considerably (see Chapter 4). Nevertheless between 1986 and 1993, the output of fabrics grew at an annual rate of approx. 6 per cent (see Table 2.11 in the Main Report).*

1.7 ***The garment*** *industry is mainly export-oriented and has grown very rapidly. In 1980 exports of garments were only about 10 per cent of Sri Lanka's total exports. By 1993 they were about half. Over this period exports grew by an average of 30 per cent per annum. Between 1986 and 1993 the annual growth rate in output was 12 per cent In spite of this growth, Sri Lanka's exports of garments account for less than 2 per cent of the world total.*

There are between 750 and 800 ***garment factories*** *in Sri Lanka with the largest (in terms of employment) located in the Free Trade Zones. These FTZ garment producers employ about 20 per cent of the total, while as much as a third of the total are employed in factories set up under the '200 Garment Factory' programme (200 GFP). Between 20 per cent and 25 per*

cent of garment workers are employed in factories employing more than 1,000 workers. Some reports estimate that about half of all output comes from foreign-owned firms.

1.8 *The growth of the garments industry was particularly rapid in 1992 and 1993 with the implementation of the* ***200 GFP.*** *This was an attempt to decentralise the industry away from the Western Province. One of the major incentives for establishing a factory under the 200 GFP was the allocation of quotas. The latter, however, soon led to an over- shooting of quotas in the garments industry, particularly for the 'hottest' quotas to the US market.*

1.9 *Even though a large part of the gross input of the garments industry is imported (as much as 65 per cent to 70 per cent),* ***the value added and employment generated by the T&G sector is considerable and since a large part of the production is exported,*** *this development is not wholly at the expense of local consumers. In other words, the domestic resource cost of the foreign exchange earned is small.* ***Thus the T&G sector has been, and continues to be a winner in Sri Lanka.***

There are good historical reasons why this should be so. *Almost every Developed Country in the world has had a major T&G sector at some time in its history. The uneven development of the T&G sector has been a mirror-image of the uneven development of the world economy since the beginning of industrial capitalism in the eighteenth century, when the high-quality, handicraft-based, Indian textile industry was destroyed by the output of the mills of Lancashire in Britain. In its turn, Lancashire gave way to the United States, Germany and Japan; while more recently Korea, Taiwan, Hong Kong and, now, China and the poorer countries of the South, challenge the older locations.*

Thus there tends to be a significant, inverse relationship between the value added in T&G as a percentage of the manufacturing sector in a country and its per capita income or GNP -- the lower the income, the more important the T&G sector. For example in 1992, the (median) percentage (of T&G value added as a proportion of value added in the manufacturing sector) for countries with a per capita income of less than $2000 was 16 per cent; for countries with a per capita income of between $2000 and $10,000 the median percentage was 11 per cent; while for the richer countries with a per capita income of more than $10,000 the median percentage was 6 per cent (see the World Bank's World Development Report, 1994, pgs. 162,163,172 and 173)

1.10 *Thus there is continuing* ***tendency for T&G production to be relocated to the LDCs,*** *and they have become increasingly important in world exports. In the early 1980s, the LDCs' share of world exports of textiles was only 10 per cent, but by the 1990s, their share had risen to well over 25 per cent, while in garments their share was over 40 per cent (see Elson 1995, 191). Garments are by far the most important industry within the T&G sector. By*

1995 the LDC contribution to net imports of garments to developed countries in volume form was two-thirds (EIU 1995, 25).

1.11 The relocation of the textile industry to the LDCs has meant that the technology is more, not less advanced, at least in parts of the South. For example in 1990, in the Asian NICs, shuttleless looms accounted for about 81 per cent of weaving capacity, a greater share than in Western Europe where the proportion was about 75 per cent. (In Sri Lanka, the share of shuttleless capacity in the total was less than 30 per cent)

*1.12 Needless to say, **the established T&G sector in the Developed world is not going to give up without a fight.** For example, in the USA, the production of textiles in 1993 was, in real terms, about the same as in 1987 and net import penetration in textiles (that is, net imports to apparent consumption) was only about 2 per cent. By contrast, and not surprisingly given its labour-intensive character (US gross output per employee in garments in 1993 was $73,000 compared to $116,000 for textiles), the real production of garments declined by about 8 per cent over the same period and, in 1993, net import penetration in garments was about 34 per cent (see US 1994 and US 1994b). The net import penetration in garments rose from about 27 per cent in 1989. The experience is similar in other developed countries in spite of the heavy protection given to the industry by tariff and non-tariff protection.*

2 MFA quotas -- what are they and how do they work in Sri Lanka?

*2.1 **Textile and garment production in the developed countries** is heavily protected both by tariff and non-tariff barriers, with the latter being the most restrictive in the form of quotas. Quotas in the global textile and garments industry date back to the 1930s. There followed a series of bilateral ('Short-Term and Long-Term') Arrangements and then, in the 1970s the LTA was replaced by the Multi Fibre Agreement is both inside and outside the GATT;*

- *inside in the sense that the GATT regularised the bilateral agreements,*
- *outside in the sense that the MFA is a major departure from the GATT principles.*

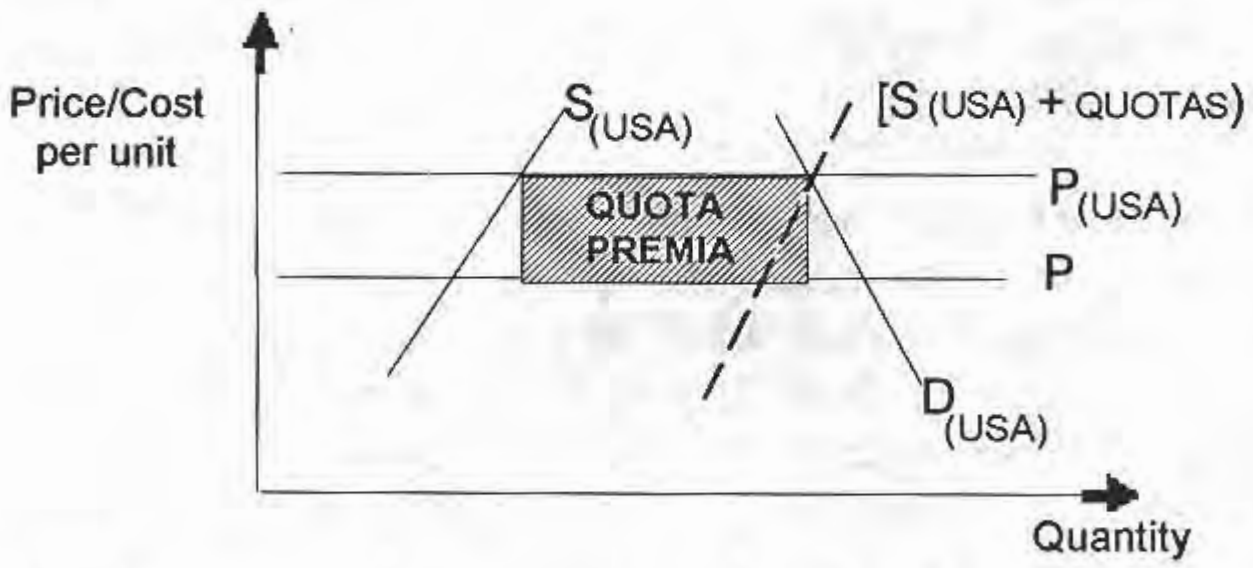
In recent years probably about three quarters of world trade in textiles and clothing has taken place within quotas.

*2.2 **The MFAs are an interesting form of protectionism.** Like import duties, they protect the producers in the importing countries (e.g. in the USA and the EU) at the expense of the consumers in those countries. But unlike import duties, there is no revenue accruing to the governments of the importing countries. Instead, the producers in the exporting countries obtain substantial super-profits or quota premia from the allocation of quotas shared with importers. The situation is as shown in Figure 1 below*

which assumes the US as the importing country. The quota drives the price to US consumers above the world price and the quota premium is obtained by the exporters who are lucky enough to be allocated the quotas (though, depending on the bargaining situation, this may be shared with the importers in the US).

2.3 ***Thus the MFA can be said to be an alliance of producer interests*** *(although the MFAs have prevented the most efficient T&G producers from expanding production beyond the quotas on the restricted categories). Channelling exports through non-quota channels (circumvention) is specifically prohibited under the BTAs (Bilateral Trade Agreements) although 10 per cent of the USA's total imports of T&G products is estimated to enter through circumvention. Of course, the main form of getting round the quotas is by investment in countries which are either not subject to quotas or are not utilising their quotas in full. Thus 'quota-hopping' investment takes place.*

Figure 1 : The Effects of a VER



2.4 *Sri Lanka is one of the countries that has benefitted from this quota-hopping investment and, by 1994,* ***over 90 per cent of all exports of textiles and garments from Sri Lanka consisted of garments. Some details of garment exports are given below:***

* ***of all garment exports, almost two-thirds went to the USA*** *and about 30 per cent to the EU;*

* *most garment exports are under quotas; in 1993, 90 per cent of the value of garment exports to the USA was under quotas; for the EU, less than 20 per cent by volume (pieces) was under quota.* ***Thus it is probable that about two-thirds of the value of garment exports is under quota;***

* *between 1989 and 1993 there was a rapid growth in non-quota exports of garments from Sri Lanka.*

2.5 ***Quotas are allocated in Sri Lanka on the basis of past performance (they are not auctioned).*** *They are allocated by the Textiles Quota Board. As stated earlier, there has been a big expansion in the garments industry (about a third in terms of employment) in the period since 1992, through the 200 GFP. The allocation of quotas to these factories meant that, in 1993 and 1994, there developed a crisis in the allocation of quotas.*

2.6 *As far as the **EU market is concerned, there was an over- shooting of the quotas for blouses (Category 7) and shirts (Category 8).** The average utilisation (in terms of pieces for all four quota categories) rose from 80 per cent in 1989 to 90 per cent in 1994, but for the two hottest categories (blouses and shirts), the average utilisation rose from 84 per cent in 1989 to over 100 per cent in 1994 (see Table 3.5 in the Main Report).*

2.7 ***The picture is similar for quota exports to the USA.** Whereas the average utilisation of all quotas in 1990/91 was 80 per cent, by 1994 it was about 100 per cent and for the 'hottest' categories (gloves and mittens, Men and Boys coats, Women and Girls coats, dresses, underwear), there was considerable overshooting in 1994*

2.8 *Thus by 1993/94, there were difficulties in the quota allocation (particularly for the US market) and in November 1993, the Board of Investment (BOI) was reported as not being able to allocate quotas as an inducement to new garment investors.*

2.9 ***In February 1995, there were negotiations between the US and the Sri Lankan government to cover the quota period after 1995, and in connection with the Uruguay move, to phase out the MFA (see Chapter 5).** The major result of those negotiations was to allow the Sri Lankan exporters (through a 'special carry-forward' arrangement) to spread the over-shooting of the quotas over a number of years through 1997 (see Table 3.9).*

2.10 *The effect of all the complex arrangements for quotas (including shifts, swings, carry-forwards and special carry-forwards) is difficult to see very clearly. It seems that the average growth of quotas to the US market from 1994 through 1997 will be less than 5 per cent p.a. and could be as little as 3 per cent p.a. (see Table 3.10). This compares with a 'natural' growth rate as specified under the first phase of the post-Uruguay arrangements of about 7 per cent (see Chapter 5).*

2.11 *Above we have pointed out that there are premia (or super-profits) associated with the quotas.* ***How much are these quotas worth to the companies in Sri Lanka?*** *We do not know for certain. If we go back to the theory of voluntary export restraint (VER) protectionism (Figure 1) and combine this with a reading of letters to the Sri Lankan press, it would seem that the 'hottest' quotas are highly valuable. But quotas are not officially traded in Sri Lanka and the 'prices' of quotas are not readily available.*

2.12 *Some guidance may be obtained from Hong Kong.* ***In Hong Kong there is some trading (but not auctioning) of quotas*** *and therefore there are some prices quoted for quotas. The worth of the quotas appears to be between 10 per cent and 20 per cent of the FOB export value. The hottest quotas are probably worth (in terms of super-profits) at least 20 per cent of the FOB value. If this is applied to the Sri Lankan situation and using 1994 data, the Sri Lankan quotas to the USA would be worth as much as 20 per cent of the FOB value of Rs 35 bn or over Rs 7 bn. A reasonable estimate is probably about 15 per cent which would give a figure for all quota exports (not just those to the USA) in 1994 of about the same amount, namely, Rs 7 billion.*

2.13 *Given the likely value of quota premia and the increasing tightness of the quota situation, it is hardly surprising that the number of associations in the garments industry increased in 1993 as the producers fought to protect their interests.*

2.14 ***Some backing for our estimates of the worth of the quotas is provided by estimates of the rate of profit in the garments industry.*** *The average rate of profit for all companies (mostly, but not only, garment producers) in the KEPZ over the period between 1990 and 1994 was about 50 per cent on capital employed. Over the period between 1978 and 1994 the average was 68 per cent p.a. It seems from this and supporting information that the rate of profit for producers with access to the 'hottest' quotas has been between 50 per cent and 70 per cent p.a. The profit margin on sales would seem to be 15 per cent - 25 per cent, with the ratio of annual sales to capital employed being between 2 and 4.*

2.15 ***However, there must be some doubt as to whether the super-profits of garment producers are being eroded, or are likely to be eroded over the next five to ten years.*** *However, our picture of price trends in the garments industry is hazy. We looked at the price trends for garment exports from Sri Lanka. For all exports there was a rise in the average rupee price between 1992 and 1994 of about 10 per cent. Over the same period, the rupee depreciated by about 16 per cent so that the unit purchasing power of exports would seem to have declined. For imports from Sri Lanka into the USA (in terms of the dollar), we get a somewhat similar picture, of a decline in the real price.*

2.16 ***Certainly, there is some evidence of a drop in the real price of garments in recent years in Sri Lanka's main market, namely, the USA.*** *However, we need more information on price trends in order to differentiate between;*

* *export price changes due to a decline in the real price of garments in the importing countries;*
* *export price rises due to the upgrading of exports within a particular category; and*
* *export price changes due to changes in the ratio of export prices from Sri Lanka to the final retail prices in the consuming country.*

2.17 *From interviews and trade magazines, it would seem that the export price from Hong Kong for garments is generally between one-quarter and one-third of the final retail price in the US market. In contrast, it seems that the export price from Sri Lanka is between one-sixth and one-quarter, but the reason for this difference is not entirely clear.*

3. *Costs, technology and competitiveness - generally and in Sri Lanka*

3.1 ***In general, the technologies of textiles (fabric) and garments are very different in terms of capital-intensities*** *and technological development and there is no such thing as a fully-automated and integrated textile and garment process. Garment production can be said to be 'awkward' in terms of automating production*

3.2 *About half (by value) of* ***yarn*** *consumption in Sri Lanka is imported. The effective rate of protection on cotton yarn sold to the domestic market is about 20 per cent, based on the February 1995 tariff structure. However, this may be misleading since -- although some direct price comparisons for yarn give a protection on the output similar to the listed tariff -- yarn producers have to buy their fibre at prices that are said to be well above the prices paid by producers in India and Pakistan. In spite of this, investment in spinning in Sri Lanka is a reasonably attractive proposition.*

3.3 *At present the* ***fabric industry*** *is highly variable in terms of international competitiveness. Domestic cost/international price comparisons suggest that some production is highly competitive with imports (only about 5-10 per cent above international prices) while other production is highly uncompetitive (about 50 per cent above international prices).*

The tariff protection on fabrics *sold for domestic consumption is high (with an ERP of about 60 per cent based on February 1995 tariffs) but this is misleading, partly because of the considerable leakages and smuggling of fabric (as much as 80 mn metres or 40 per cent of local production) into the local market and partly because the major source of expansion is not in the domestic consumption market but through sales to the garment exporters.*

However, it seems that the price that garment producers are prepared to pay for cloth of the same quality and width as is available from the world market is about 10 per cent or more above the world price. *Given this, there is a considerable incentive for import-substituting investment in fabric production. In addition to this, the government provides non-tariff incentives for investments in fabric production (see Section 4.5).*

The market in Sri Lanka is large enough to allow for economies of scale and product specialisation. The volume of fabric production in Sri Lanka grew by about 6 per cent between 1986 and 1993. Between 1994 and 2000, there is realistic scope for a growth in fabric production of 11 per cent p.a. even if garment production expands by only about 5 per cent p.a., and even

if the local producers supply only 40 per cent of the garment producers' requirements. The additional production of about 200 mn metres of fabric would require an investment of about Rs 10 bn. (at 1996 prices). This is equivalent to about 10 per cent of the one year's fixed investment in Sri Lanka (at 1993 prices), a target which is by no means impossible. But new investment is essential to produce the fabric capacity of suitable quality and width for the (indirect) export market.

Costs in Sri Lanka are generally internationally competitive with, perhaps, the exception of electricity. *The possible barriers to garment producers using local fabric (assuming it matches the quality and width specifications) stem from the following:*

* *the sub-contracting arrangements where it is common for garment buyers to supply the fabric or specify the source under NFE contracts. However it appears that buyers are happy to use local sources of supply; and*

* *the growing use of outward processing arrangements to get privileged access to the USA and EU markets (we come back to this in the next section).*

3.4 *There is also some scope for backward integration from garments into* ***accessories,*** *particularly for packing materials (polybags, cartons etc), labels and padding.*

3.5 *The technical economies of scale in* ***garment*** *production are small, and well over half of the establishments in Sri Lanka are above the recommended 'minimum economic size' of about 175 employees. However there are also, it seems, considerable financial economies of scale in as much as large companies are more likely to get discounts on 'large' fabric orders and, in addition, more likely to sell their garments for a higher proportion of the final retail price.*

Labour costs are more important for garment than for fabric production but there seem to be considerable differences in productivity between establishments in Sri Lanka. ***It is common for the importance of wage rates in competitiveness to be overrated.***

Since the major part of the market for garments is through exports, tariff protection is largely irrelevant although some garment producers are allowed to sell some of their production in the protected local market on a concessional basis.

3.6 *There is a misconception that exchange rates are unimportant for the textile and garments sector.* ***However, exchange rates do matter even for a low value-added industry like garments.*** *As shown in Table 4.7, a real devaluation is likely to raise the rate of profit for a low value-added producer by more than it is likely to raise the rate of profit for a high value-*

added producer. The exchange rate will affect the rate of profit for quota garments but it is particularly important to those textile and garment products (such as yarns, fabrics and non-quota garments) sold under highly competitive conditions.

It needs to be noted that the Sri Lankan rupee has appreciated against the currencies of LDCs which are close competitors of Sri Lanka (such as Bangladesh, India, Indonesia, Malaysia, Pakistan and Thailand).

4. *The 'phasing-out' of MFA quotas, global demand for textiles and garments and prospects for Sri Lanka's garment production*

4.1 ***Under the post-Uruguay Agreement on Textile and Clothing (ATC), the MFAs are due to be phased out over a 10-year period between 1995 and the end of 2004.*** *The volume of quotas is to be phased out in 4 stages; 16 per cent in 1995; 17 per cent in 1998; 18 per cent in 2002; and the remaining 49 per cent at the end of 2004. There is a general consensus that the present restricted categories are unlikely to be significantly liberalised until the last stage, that is, end-2004.*

4.2 ***Thus there are likely to be two phases of phasing out;***

(i) The medium term (over the period to 2005), when there will still be quotas in existence but their base will grow at a rapid rate;

* *for the US market, the picture is complicated by shifts, swings, sub-limits and carry-overs and carry-forwards, but under the ATC the base quota grows at the faster annual rate of 7 per cent between 1995 and end-1997, at 8.7 per cent between 1998 and end-2001, and at 11 per cent between 2002 and end-2004. Sri Lanka's quotas will grow at a slightly slower rate than for small suppliers and Least Developed Countries. A small supplier is defined as one whose restricted exports represent no more than 1.2 per cent of the total volume of restrictions applied by the importing country. Sri Lanka's exports to the USA were about double this at 2.5 per cent so that it does not qualify for the faster growth rate applicable to small suppliers. After shifts, swings and adjustments for notional over-shipments, Sri Lanka's 1995 quota to the USA is about 5 per cent up in value (and about 3 per cent up in sq. metre volume) on 1994; in 1996 and 1997 there is likely to be a further carry-forward so that the growth in each of those years will probably be much less than 7 per cent. Thus the USA quota situation is likely to be severely constrained for the next two years at least.*

* *in the EU market, Sri Lanka's quotas will grow faster, firstly because of the smaller over-shipments and secondly because the base growth rate is faster. For this market, Sri Lanka does count as*

a small supplier, and the growth in the quota volume for 1995 is 7 per cent plus 25 per cent of 7 per cent = 8.75 per cent. Sri Lanka's quota growth is faster than that of most of the dominant suppliers to the EU although slower than that of Bangladesh, which is classified as a Least Developed and small country. As Table 5.1 shows, Sri Lanka's quotas are likely to grow at about three times the rate of all quota suppliers.

(ii) ***But even in the longer term (that is, beyond the phasing out of quotas in 2005), the textile and garment markets in the Developed Countries are unlikely to be very open.*** *Most sources estimate that the restrictions imposed by the tariffs are almost as great as the restrictions imposed by the quotas. Thus, the abolition of the quotas halve the restrictions but no more. Although, as a result of the Uruguay Round there will be some reduction in textile and garment tariffs, the textile and garment sector will remain one of the most heavily-protected sectors. Furthermore it should be noted that the ATC contains a specific safeguard mechanism which could be applied to products not integrated at the three stages*

4.3 *In addition to tariffs there are various special provisions applicable to textiles and garments;*

* *first, there is the Generalised System of Preferences (GSP). As from Ist January 1995, Sri Lanka has lost its preference to the EU market since it is no longer treated as a Least Developed Country;*

* *second, there are special value-added tariff arrangements for both Sri Lanka's main markets, the USA and the EU. Under these Outward Processing schemes, garment producers can get preferential access (in terms of a relaxation of quotas and slower value-added tariffs) to the US and EU markets if they use cloth from the USA and the EU in making the garments. The possibility of using these arrangements is clearly worthy of further study, although extensive use of such arrangements will militate against backward integration in Sri Lanka into fabric production;*

* ***third, the expansion of the EU and the formation of NAFTA in North America might generate strong competition to Sri Lanka.*** *NAFTA is likely to be less of a threat in this respect since Mexico's advantages were to a great extent in existence before the formation of NAFTA. The greater threat is posed by the expansion of the EU and, in particular, by the incorporation of Turkey into a Customs Union with the EU, although Sri Lanka's exports of garments to the EU are much smaller than to the USA.*

4.4 ***Although the growth in the USA and the EU in the consumption of textiles and garments is between 2 per cent and 3 per cent p.a. their markets are large enough to absorb growth rates of imports of 9 per cent***

p.a. (Sri Lanka's average quota growth through to 2005) for the next 20 years without the import penetration percentage rising much above two-thirds.

4.5 ***However it is likely that competition will become increasingly fierce.*** *If we consider Figure 1 above and imagine that the demand curve is shifting slowly outwards, while quotas grow at a much faster rate, then it is likely that the price in the US market will fall. The rate of decline will depend on how similar the cost structure is of US garment producers. The more similar they are, the slower will be the decline in price since, if they are similar in cost structure, a slight decline in the price will displace a large percentage of US production. We know too little about the cost structure of the US garment industry, the pace of expansion of quotas from existing suppliers and the likelihood of relatively new suppliers (such as Vietnam, Myanmar and Cambodia) coming into the market, to conjecture about the likely future movement in real garment prices in the major markets.*

5. *Policy Issues and Research Questions*

5.1 *How can Sri Lanka move ahead in the textile and garment sector? What policy conclusions follow from this study? The questions raised in this section are very tentative and are put forward to stimulate further discussion and further research.*

5.2 *From the viewpoint of the garment industry, there are three ways of looking at the textile and garment sector -- three ways of seeing that the value added retained from the textile and garment sector in Sri Lanka can be maximised:*

* *forward integration;*
* *backward integration;*
* *productivity and competitiveness.*

5.3 *In terms of* ***forward integration,*** *there are a number of policy issues and research questions;*

* ***How can markets be upgraded? Are the larger companies in Sri Lanka more likely to upgrade?*** *Do the larger companies get a better price for their exports? Do the larger companies get bigger discounts on cloth supplies? If so, should larger companies be encouraged? If so, how? How effective are the moves to help Sri Lankan suppliers to establish their own brand names and to venture into garment design? What lessons, if any, can be learned from Hong Kong?*

* *How can a larger share of the profits from garment production be retained or reinvested in Sri Lanka?* ***Should quotas be auctioned in Sri Lanka?*** *We understand that a Review Committee appointed by the Minister of Industrial Development has unanimously recommended that export quotas should not be auctioned. We have not had access to the*

report of that Committee. However, it does seem that the profits of garment producers have been very large indeed in the late-1980s and early-1990s and that this is likely to be due to the premia or super-profits available from quotas. It is likely that a large proportion of these profits accrue to foreign-owned companies and that they are presumably sent out of the country. Thus the retained value added is less than it would be if more of these exceptional profits could be retained in Sri Lanka. The auctioning of quotas would be one way in which the government could increase the retained value added. ***Possible objections to the auctioning of quotas and counter-objections might be as follows:***

* *"auctions constitute undesirable interference in the market" - but the large profits of garment producers arise from an existing interference with the market, namely the MFA;*

* *"the auctions would be captured by the largest, foreign-owned companies and particularly by those in the least cost sites such as the Western Province" -- this may be a good thing if the biggest companies are the most efficient. But, if not, perhaps only the additions to quotas should be auctioned;*

* *"the 200 GFP would collapse". If this is considered undesirable, should the auctions be sold off in blocks under the various categories of establishment (BOI Zone, 200 GFP, etc)? Would this be feasible?*

* *"the super-profits from the hottest quotas are used to subsidise losses in non-quota markets". Is this the case? If so, why? Or, by contrast, do the high potential profits from the present system generate spare capacity?*

* *"the auctioning of quotas would discourage long-term investment". Possibly, but if so, quotas could be auctioned five years ahead and on a rolling basis to ensure long-term continuity;*

* *"the revenue to the government would be small". Perhaps, if only the additions to quotas were auctioned, but if the base quotas were auctioned, our very tentative guess is that the income to the government could be as much as Rs 20 bn from the auctioning of the 'hottest' quotas over the next five years;*

* *"an auctioning system is inferior to the quota tax system (introduced in the 1995 budget on a Rs.1 per piece basis)". No, on the contrary, an auctioning scheme could be much superior to a taxation per piece scheme since the quota premia vary enormously between categories. This point was argued by the*

200 Garment Factories Association when the tax was introduced (see Daily News, 13 February 1995);

* *"it is impossible to auction the quotas because some companies have been given legal guarantees on quotas in return for making their investments". Is this so? What are the details?*

* *the days of high profits in the garments industry are gone because of increasing competition". Perhaps, but we simply do not know enough about trends in profits and in prices.*

Would the efficient utilisation of quotas be encouraged by the publication of quotas (page 26) as is done in the Philippines? *At present the details of quotas are provided to the various Garment Associations. If the government will not publish a list, why do these Associations not summarise them on a data base and publish them?*

How can new markets be developed?. *How can non-quota markets be best developed? What can the Ministry of Handlooms and Textiles and the EDB do to develop new markets in conjunction with the Trade Associations? How can markets in South Asia be developed? Would further regional integration through SAARC be a help or a hindrance to the textile and garment sector in Sri Lanka? How much is known about the value-added tariff schemes of the USA and the EU? Would their widespread use militate against backward integration into fabric production, or would value-added tariff schemes generate new, additional, non-quota markets for garments? How far has the Sri Lankan government explored this possibility in the US market by discussing it with the Department of Commerce and the Inter-Agency Committee on Textile Arrangements?*

5.4 Backward Integration

How can ***investment in fabric and accessory production*** *be encouraged? What premium would garment producers be prepared to pay to local suppliers? If outward processing trade with the USA and the EU grows rapidly, to what extent would this be an obstacle to backward integration in Sri Lanka?*

What are the incentives to investment in fabric and accessory production? *The Ceylon Textile Manufacturing Association (CTMA) has complained that the incentive structure (both in terms of tariff and non-tariff incentives) has been unstable. What is the actual effective rate of protection allowing for leakages and smuggling? What are the advantages and disadvantages of a pre-shipment verification scheme?*

Do NFE contracts discourage backward integration? *It appears not, but if they do, what steps can be taken to counter this?*

5.5 *Productivity*

How does productivity vary between establishments *in spinning, weaving, knitting and garment production? In this context it is worth noting that the average employee/machine ratio in Sri Lanka is about 1.8 to 1 and yet the most efficient factories have a ratio of 1.25 to 1.*

How can productivity be improved? *How important are product specialisation, capacity utilisation, type of machinery, organisation and layout?*

How is skill development in the industry promoted? *We know that vocational training has been heavily criticised in Sri Lanka (see Kelly, 1992 and Kelly, 1993). Most training centres are criticised as being too small to achieve economies of scale and for having inadequate links with industry. Interestingly the Clothing Industry Training Institute (CITI) and the National Textile Training Centre seem to be exceptions to the general pattern of training institutes in that they do have close links with industry. If there is a case for a levy-grant system in Sri Lanka, should this apply to the textile and garment sector?*

How important are exchange rate changes to competitiveness? *Should the exchange rate be devalued since Sri Lanka appears to be suffering from a revaluation relative to major LDC competitors?*

Would the support by Sri Lanka of the ILO's disapproval of child and prison labour *help to shut out unfair competition, or is this just another way by which Developed Countries protect their textile and garment sector?*

The Uruguay Round and MFA Quotas: The Textiles and Garment Industries in Sri Lanka - The Next 10 Years

1. Introduction

This report sets out to examine the prospects of the Sri Lankan textiles and garment sector over the next decade (1996-2005). Over this period, the Multi-Fibre Arrangement (a set of bilateral trade restriction agreements which governs a large majority of world textiles and garments trade) are due to be phased out. The paper's main objective is to look at the prospects of the Sri Lankan industry in the light of the phasing-out of the MFA quotas.

An article in the Japanese Textile/Garment Newsgroup (JTN) Quarterly in 1995 states that;

> "All in all, the Sri Lankan garment industry will grow rapidly for the next 20 years and there are no signs of Sri Lanka losing its comparative advantage in garments exports to new-comers such as Vietnam and Cambodia".

This optimistic statement is in contrast to a less optimistic report in the *Daily News* of March 1st 1995 which reported that;

> "Current trends indicate a reversal and slowing down of the initial momentum of Sri Lanka's garment industry, which could lead to a serious decline and loss of its competitive edge unless remedial measures are implemented soon, two memoranda addressed to the government said yesterday" (*Daily News* March 1 1995, 1).

This study attempts to choose between these two statements by analysing the competitiveness of the textile and garment industry in Sri Lanka, and by assessing the effects of the phasing-out of MFA quotas. More specifically, the study looks at the policy issues affecting the textile and garments sector in Sri Lanka. What policy changes should the Sri Lankan government adopt to develop the industry in the light of the phasing-out of MFA quotas and other major challenges facing the sector? Thus the report asks the following:

* is the sector under- or over-protected?
* how, if at all, can and should backward linkages in the textile and clothing industry be encouraged?
* since MFA quotas are to be phased-out over an extended period, should they be taxed or auctioned until phased-out?
* how does devaluation of the rupee affect the competitiveness of the sector?

2. What is there to gain or lose? The state of the Sri Lankan textile and garment industries?

2.1 The present state of the industries - output, value added and employment

Both the textile and garment industries (together with leather goods) come under the industrial classification 32. Textiles is 321 and wearing apparel (which in this report is referred to as the **garment industry**) comes under 322.

How big are the textile and garment industries in Sri Lanka? This question is not easy to answer with any precision since the statistical base of the manufacturing sector in Sri Lanka is extremely shaky and the information base on the textile and garment industries is no exception. This is true even if attention is restricted to what the Central Bank calls the 'factory industry' sector. From the figures published in the Central Bank's Annual Report for 1993 (see CBoSL AR 1993, Table 2.2) the factory industry sub-sector accounted for 81 per cent of value added in the manufacturing sector in 1993 (these 1993 figures are listed in the report as 'provisional' figures).

However, even if attention is restricted to this 'factory industry' sector, there are major differences between the statistics of the Central Bank (as revealed by the Annual Report) and those of the Department of Census and Statistics (as revealed by the Annual Survey of Industries -- hitherto ASI). This is shown in Table 2.1.

Table 2.1
Gross output and value added in the manufacturing sector of Sri Lanka for 1990 -- a comparison of data from the Central Bank and the ASI

1990 (Rs. bn.)	Gross output		Value added	
	CBoSL	ASI	CBoSL	ASI
31 Food beverages and tobacco	22.0	34.1	12.1	17.8
32 Textile, wearing apparel and leather products	27.9	23.4	7.2	11.0
33 Wood and Wood Products	0.7	0.5	0.5	0.3
34 Paper and paper products	1.9	2.5	1.0	1.3
35 Chemicals, etc	21.2	22.6	2.4	7.8
36 NMMP (exc. petroleum and coal)	7.6	4.6	4.7	1.6
37 Basic metal products	1.0	1.3	0.2	0.4
38 Metal products, machinery and transport equipment	4.2	5.2	2.7	2.1
39 Other mfed products (nes)	0.3	3.3	0.1	0.4
Total	**66.6**	**97.5**	**30.9**	**42.5**
(*) Does not sum due to rounding	(*)			(*)

Sources: ASI = Annual Survey of Industries 1991 (note that the 1991 Survey year relates to 1990 data); CBoSL; data obtained directly from the Central Bank; see Edwards, 1993(a), Table 4.3, 26.

It is clear from Table 2.1 that the ASI figures (for both gross output and value added) are very much **higher** for the food, beverages and tobacco sub-sector and very much **lower**

(for gross output) for the textiles and clothing sub-sector than the Central Bank's figures. It seems that the Central Bank's coverage for the textiles and clothing industry is more complete than that of the DCS. This is one reason for using the Central Bank's figures. Two further reasons are because more recent figures are available from the Central Bank and because the Central Bank's figures 'tie in' with the national accounts. Thus in this report, the Central Bank figures are used.

The above comparison was for 1990, but table 2.2 brings us more up-to-date by looking at the figures for the textiles, garments and leather goods industries relative to the whole manufacturing sector for **1993**.

Table 2.2
Textiles and garment industries in the context of the manufacturing sector - Sri Lanka; 1993

	Textiles, clothing and leather industries (ISIC 32)	Total manufac-turing sector	Total economy (ISIC 3)
Gross output (Rs.bn.)	70	167	na
Value added (Rs.bn.)	19	61 60 (i)	453
Employment (000)	350	850	6,000

(i) excludes processing of tea, rubber and coconut products
Sources: CBoSL 1993, 54, 56 and Table 2 of the Statistical Appendix; JTN 1995, 127: data in Edwards, 1993(a), 210; MHTI,1992, Table 10; TTSC,1994, Part B, 2.

In terms of **gross output**, the leather goods industry in 1990 was only about 6 per cent of ISIC 32 (see Edwards, 1993(a), 27). Assuming a slightly lower proportion for 1993, then the gross output of the textile and garment industries would have been about Rs. 67 bn. in Sri Lanka. This was about **40 per cent** of the Rs.167 bn. total for the manufacturing sector.

However, the **value-added** share of textiles and garments is a lot smaller. Taking out the value added of the leather goods industry leaves a value added figure for textiles and garments of about Rs. 18 bn. or about **30 per cent** of the manufacturing sector total or a little over **4 per cent** of total GDP.

When we come to **employment**, the figures are even shakier than those for gross output and valued added. Most estimates of the number employed in the textile and garment industries for 1993 range from 250,000 to 350,000, but a paper produced for the Textile Institute Seminar in 1994 estimated employment in the garment industry alone at 350,000 (Textile Institute 1994, 7). However this seems to be on the high side and if 350,000 is taken to be the total textile and garments figure, then this is about **41 per cent** of total employment in the manufacturing sector and about 6 per cent of the total (6 mn.s) working population in Sri Lanka.

To summarise, on the basis of official statistics and relative to the manufacturing sector, in 1993, the textile and garment industries made up about 40 per cent of gross output and employment in the manufacturing sector, and about 30 per cent of net output or value added.

Clearly, the textile and garment industries are an extremely important part of the manufacturing sector. In 1993, and at the 2-digit level, the textile and garment sector was only slightly smaller (in terms of value added) than the food, beverages and tobacco sector (see CBoSL 1993, Table 19). By now (1996), it is almost certainly the largest two-digit sector.

However, it cannot be emphasised too strongly how shaky the figures are. This is particularly apparent when we attempt to derive estimates for apparent domestic consumption in Sri Lanka of fibre, yarn, fabrics and garments. The figures for 1993 are shown in Table 2.3. They are shown in ranges of Rs. bn.

In Table 2.3 the gross output of the garment industry is derived as a residual from the other figures but is clearly too low since the apparent consumption of garments is negative.

Table 2.3
Gross output, exports, imports and apparent domestic consumption - textiles and garments - Sri Lanka 1993

(Rs. bn.)	Gross output	Imports	Exports	Apparent domestic consumption
1. Fibre,	0	2-3	0	2-3
2. Yarns	4-5	4-5	1-2	7-8
3. Fabrics	16-17	35-36	1-2	50-51
4. Garments	46-47	1-2	62	-
Total	66-69	42-46	64-66	44-49

Sources: JTN 1995, 127; CBoSL 1993: 97, MHTI 1993

How do we make sense of the garment figures? The domestic consumption of garments in Sri Lanka is likely to be between Rs. 500 and Rs. 750 per capita per annum or between Rs. 9 bn. and Rs. 13 bn. a year for the whole country. If we (optimistically) assume that the import and export figures are more or less correct (and we ignore smuggling), then the gross output of the garments industry should be between Rs. 70 bn. and Rs. 73 bn. This would give a total gross output for the textile and garment industries as a whole of at least Rs. 90 bn. suggesting that the Central Bank figure of Rs. 70 bn. given in Table 17 of the 1993 Annual Report is gross output for exports and final consumption only. Our estimates for the gross output, imports, exports and apparent domestic use of fibre, yarn, fabric and garments for 1994 are shown in Table 2.4.

As Table 2.4 shows, the garment industry is highly export-oriented with nearly 90 per cent of gross output being exported, whereas the fabric industry is highly geared to production for the domestic market and highly protected, though there is considerable smuggling into Sri Lanka and leakages of fabric from the garment industry.

Table 2.4
Gross output, imports, exports and apparent domestic use
(1994; estimated)

(Rs. bn.)	Gross output	Imports domestic	Exports usage	Apparent dom. usage
Fibre	0	2-3	0	2-3
Yarn	4-5	4-5	1-2	7-8
Fabric	16-18	35-37	2	49-53
Garments	71-77	1-2	63-66	9-13
Total (mid-est)	44	69	71	96

What was the **net output** in 1993? As can be seen from Table 2.1, the ratio of the net to gross output given by the Central Bank was 26 per cent, whereas the ASI ratio was 47 per cent. The Central Bank's estimate is almost certainly more reliable. In terms of output, the biggest industry is the garments industry and the value added to gross output ratio of that industry is almost certainly no more than about 25 per cent-35 per cent (see Chapter 4 for more details). Here we assume a figure of 30 per cent so that the value added in the textile and garment sector in 1994 is as shown in Table 2.5.

Table 2.5
Net output and employment in the textile and garment industries, Sri Lanka (estimated for 1994)

	Net output (Rs. bn.)	Employment (000)	Net output /employee (Rs.000)
Yarn, fabric and finishing	6	100	60
Garments	24	250	96
Total	30	350	86
Manufacturing sector	70	850	82
Total economy	500	6000	83

2.2 The development of the industries and major producers

The textile industry was promoted as an import substitution industry (ISI) in the 1956-77 period. Imports were tightly controlled. Prior to 1977, imports of fabrics were banned and raw materials for textiles were imported and distributed only by the government. With the change of government in 1977, the ban on textile imports was eliminated and price controls were removed. This led to a sharp reduction in the handloom industry. In 1977 there were 115,000 handlooms registered, but by 1989 this was down to 30,000 (*Textile Asia*, August 1989, 134). However, high tariff rates were maintained on textiles until recently, when some restructuring has taken place, and in the period since 1990, a number of fabric producers have been privatised.

As shown in Table 2.5, of the 350,000 estimated to be employed in the textile and garment industries in 1993, about 100,000 are in the yarn and fabric manufacturing

sector (comprising 60,000 in powerlooms and 40,000 in handlooms) and 250,000 are in the export garment sector (TTSC,1994, Part B, 2).

The textile industry in Sri Lanka can be divided into three major sub-industries, as follows:

* spinning (production of yarn);
* weaving or knitting (production of grey fabric);
* finishing, dyeing or printing (production of finished fabric).

Spinning: This industry is widely thought to be the least internationally competitive sector (see Pehlivan 1993). Sri Lanka's spinning industry is (as of 1993) equipped with 285,000 spindles with an annual production capacity of around 28,000 metric tons. This capacity is in 12 mills. About half the spindles are either modern or modified spindles with electronic yarn clearing and yarn splicing capabilities that enable them to produce export quality yarn. These plants are mostly relocations from industrialised countries and they operate to international standards. The labour productivity in these mills is much higher than in the older mills.

Table 2.6
Major producers of yarn in Sri Lanka in 1992

	mn. kgs	%
Kabool Lanka (Pvt) Ltd	12.4	56
Pugoda Textile Mills Ltd	2.6	12
Veyangoda Textile Mills Ltd	2.0	9
Mattegama Textile Mills	1.7	8
Asian Cotton Mills Ltd	1.4	6
United Spinning and Kandy Textile Mills	0.7	3
Others	1.2	6
Total	22.0	100

Source: Pehlivan 1993, 5; and TTSC, 1994, Part B, 24, 65.

The other 145,000 spindles are in factories using mostly outdated machinery and producing poor quality yarn for internal consumption (Pehlivan 1993, 14 and TTSC,1994, Part B, 21, 24). All the fibre is imported.

In 1991 and 1992, imports of yarn were about 15,000-16,000 tons as domestic production is inadequate to meet the demands of the fabric industry (TTSC,1994, part B, 22).

In 1992, the actual production of yarn totalled 22,000 metric tons (22.0 mn. kgs) using just under 80 per cent of installed capacity with five firms producing more than 1 mn. kgs each as shown in Table 2.6.

The major spinners (Kabool Lanka, Pugoda, Veyangoda, United Spinning & Weaving Mills, and Asian Cotton Mills) are large integrated privately-owned mills. As shown in the above Table, Kabool is by far the biggest spinner in Sri Lanka. 30 per cent of the yarn that Kabool produces goes into its own fabric, while 60 per cent is exported (mainly to the European Union) and 10 per cent is sold to the domestic market. (For some details of the other spinners, see the Appendix to Pehlivan 1993, 18-32). Mattegama Textile Mills

produces cotton yarn for the handloom sector only. The other major mills (Asian Cotton, United Spinning and Kandy Textile Mills) are suppliers of yarn to the powerloom sector (Pehlivan 1993, 6). In 1992 and 1993 investment in the yarn industry averaged Rs. 270 mn. a year, about double the investment in the previous two years (see MHTI 1993, 14).

Weaving and knitting: In general this is estimated by Pehlivan (1993, 14) to be an internationally competitive industry. (We look at the competitiveness factors in more detail in Chapter 4). Production in 1992 was 169 mn. metres of woven fabric and 18 mn. metres of knitted fabric. The major producers are listed in Table 2.7.

As can be seen from Table 2.7, no single fabric producer produces more than 13 per cent of fabric in Sri Lanka. The Sri Lankan weaving mills are estimated to supply no more than about 5 per cent to 10 per cent of the fabric used by the garment exporters. The majority of looms are only 36 inches wide and therefore are unable to supply the 45 inch and 60 inch width fabric required by the clothing export industry (for more discussion see Chapter 4). However, in 1992 and 1993 the average investment in weaving was over Rs. 600 mn.. compared to an average of only about Rs. 230 mn. in 1990 and 1991 (see MHTI 1993, 14). There has been substantial investment by some producers (Sigiri Weaving, Pugoda, Cyntex and Swastic Textile Mills Ltd) in recent years, who have increased their capacity to 45-inch-width fabric. Others (Veyangoda, Duro and Velona) were reported by Pehlivan (1993, 6) to be in the process of investing in new equipment The total number of power looms is around 13,000. Until 1990, only about 100 of these were shuttleless looms, but with new investments this number has gone up to over 500. The majority of shuttleless looms are rapier while relatively few are air-jet and water-jet looms. Most of the shuttleless looms can produce fabrics of over 60 inch width. As suitable yarn is not freely available locally, these mills use mostly imported yarn. However, some of the fabric mills possess their own spinning units which can produce quality yarn for export quality fabric (see TTSC 1994, Part B, 16)

There are about 350 circular weft **knitting** machines in Sri Lanka. About 200 of these machines are over 15 years old and most of the remaining 150 less than 10 years old. The older machines cater to the local market, while about 30-50 of the newer machines, using mostly imported yarn, produce fabrics acceptable to the export industry. About 10 to 12 of these newer machines work on recent "contrary technology" in making single jersey fabrics which have the advantage of a marginal increase in the width of the fabric. Sri Lanka now has competent mechanics and operators who can work with new generation single jersey and double jersey machines in producing basic knitted fabrics. However the know-how to handle specialised machines in the production of fleecy and plush fabrics is reportedly limited (TTSC,1994, Part B, 17)

There are about 6,000 hand flat knitting machines and about 150 power flat machines in Sri Lanka. Hand flat knitting machines are used to produce sweaters, cardigans and pullovers for export (TTSC, 1994, Part B, 18)

Finishing, Dyeing and Printing: This is reported by Pehlivan (1993, 14) to be an internationally competitive industry, although the TTSC (1994, Part B, 19) stated that "good dyeing and finishing facilities are limited to the large mills only and cater mainly to woven fabrics". The older machines are only able to process fabrics of up to 45" width.

Table 2.7
Major producers of fabric in Sri Lanka, 1992

	mn.linear metres
*** Knitted Fabric (knitting)**	
Sigiri Weaving Mills Ltd	1.3
Lanka Tricotting Inds.	1.0
Duro Synthetic Textile Mills Ltd	1.0
Janahita Knitting Co. Ltd.	0.8
13 firms listed by Pehlivan	2.7
Other producers	12.0
Total knitted fabric	18.0
*** Woven fabric (weaving)**	
Pugoda Textile Mills Ltd	20.7
Kabool Lanka (Pvt) Ltd.	20.5
Veyangoda Ltd (privatised in 1990)	13.5
Hydro Textile Inds. Ltd	11.4
Kuruwita Textile Mills Ltd	5.0
Ceylon Synthetic Textiles (Cyntex)	4.8
Castle Textile Inds.Ltd	3.6
Welwoven, Kandy	3.2
45 firms listed by Pehlivan	33.8
Other producers	52.5
Total woven fabric	169.0

Source: Pehlivan 1993, 7, 8 (see also TTSC 1994, Part B, annexure 1).

In 1992, 31.2 mn. metres of fabrics were processed (finished, dyed or printed). The main producers involved in finishing are listed in Table 2.8.

The majority of small and medium textile mills utilise the services of the integrated textile mills that undertake commission-finishing of grey fabric. But because of the delays involved in this process, some of the smaller mills (e.g. Niniko Industries (Pvt) Ltd.) have invested in finishing units. The plants in Sri Lanka do not have high finishing quality machinery. Two new plants which can produce for export, have been commissioned to process knitted fabric.

Table 2.8
Production of finished fabric (processing) in Sri Lanka, 1992

	Mn. metres
Pugoda	12.8
Veyangoda	7.7
Kabool	3.5
MKC Industries	3.2
Sigiri Weaving Mills	2.0
Others	2.0
Total	31.2

Source: Pehlivan 1993, 9.

Garments: There seems to be no comprehensive data base on the garment industry in Sri Lanka in terms of producers and employment. The JTN Quarterly 1995, 126 reported

that there are about 1000 firms producing garments in Sri Lanka, whereas Mandelbaum (1993) reported 761 for 1991. The Sri Lanka, Apparel Exporters' Association SLAEA (1995) gave the number of **exporters** as 762 (see SLAEA 1995, 5). Of the 762, 373 were reported to be in the BOI sector and there were therefore 389 non-BOI or "ministry" factories (see SLAEA 1995, 5). The Task Force on Textile and Textile Related Industry's Report of 1994 gave the number of garment manufacturing companies as 700, with 214 under BOI (TTSC 1994, Part B, 5).

Board of Investment (BOI) factories are defined as those in the Export Processing Zones, as well as the 200 Garment Factory establishments and other factories within 'BOI areas'. The non-BOI factories are divided into Provincial and other factories serviced by the Ministry of Industrial Development. Some details of the garment factories are given in Table 2.9.

Note that the total employment of 236,000 is close to the earlier estimate of 250,000. It is clear that the largest garment producers are those in the Zones while the smallest are the non-BOI producers.

Table 2.9
Garment establishments in Sri Lanka, 1994

Type	Number of establishments	Employees		Average no. of emp. per estab.
		000	%	
BOI				
- Zone	47	40	17	851
- '200 GFP'	174	77	33	442
- other	152	66	28	434
Total BOI	373	183	78	491
Non-BOI	389	53	22	136
Total	762	236	100	310

Source: SLAEA 1995, 5.

In 1993, most garment producers were registered for exporting to the USA. A size distribution of these 691 US-exporting establishments is given in Table 2.10

Table 2.10
Size distribution of garment establishments registered in Sri Lanka for exporting to the USA - November 1993

Employment range (no.)	Number of establishments	Employees in. each group	
		Number	%
0	57	0	0
1-99	112	4	2
100-499	337	81	35
500-999	156	95	41
1000 and above	29	50	22
Total	691	230	100

Source: Data base of the MHTI.

The share of gross output of each type of establishment is not available. The number of machines in each firm is given in the data base, but because of variations in the utilisation of machines, the output is likely to be more closely related to the number of employees, and even though the data on the number of employees are not particularly reliable (because of the rapid labour turnover), it is perhaps reasonable to take the number of employees as an indication of gross output.

A list (with some details) of the 185 garment establishments registered as employing more than 500 employees is shown in Appendix 3 to this report.

No analysis seems to be available of the efficiency or productivity of garment producers nor is there any analysis of the share of garments output by ownership. It appears that most of the factories (about 85 per cent by number) are owned by Sri Lankans, but these seem to be the smaller ones. Foreign investment covers only about 6 per cent of the number (JTN 1995, 127) but probably a much greater proportion of the gross and net output. Mandelbaum (1993, 72) suggests that about half of exports come from foreign-owned firms.

In the past 15 years, the garment industry has expanded rapidly in Sri Lanka. In 1980, exports of garments were about 10 per cent of all Sri Lanka's exports, but in 1993 they were about half of the total (see Kelegama 1994, 15). Garment exports from Sri Lanka grew rapidly from the early 1980s, and from 1980 to 1993 the average annual growth rate of garment exports from Sri Lanka was over 30 per cent (derived from SLAEA 1995, 6). In spite of this, Sri Lanka's share of world exports of garments is small at only about 1 or 2 per cent (Kelegama 1994, 15 - see also Section 5 below).

In addition (as already noted), although the garment industry has expanded rapidly over the past decade or more, its net exports are a much smaller proportion than that of gross exports. The net export value (after the deduction of direct imports) is only about 30 per cent of the gross export value. As a result, Sri Lanka is often depicted as a 'glorified tailor' (JTN 1995, 128).

In 1992, the growth rate in garment exports was particularly rapid -- about 55 per cent in rupee terms and 47 per cent in foreign currency terms (SLAEA 1995, 6). In 1993, the growth rate was again very rapid this time about 7 per cent in rupee terms. The rapid growth in these two years was particularly due to a rapid, rise in production capacity under the '200 Garment Factory' (200 GFP) programme. The form that this has taken has had particularly interesting effects on the industry and we look at this in more detail in the next few paragraphs.

The 200 Garment Factories Programme GFP: In 1990, a Cabinet sub-Committee recommended that garment factories should be opened in provincial areas other than the Western Province to meet the high unemployment levels and terrorist problems in those areas. Limited fiscal incentives were offered, and a **20,000 dozen** quota was given to attract investors under this scheme to open provincial factories, with a minimum employment of 112 people and 62 machines (consequently, the quota was increased to 40,000 dozen and minimum employment and machine capacity increased to 225 and 125, respectively). Initially, 83 provincial factories were opened, but the number of factories under this scheme decreased to 57 factories (Kelegama 1994, 20).

In late-1991, the attempted decentralisation of the garment industry went further. In early-1992, the '200 GFP' was launched. It was planned to set up one garment factory in each of 200 Pradeshiya Sabhas (AGA Divisions). A major incentive for setting up a '200 GFP' factory was the allocation of quotas, with the allocation being greater (and more valuable) the more isolated the site. Three types of site were identified, namely non-difficult, difficult and most difficult. About 40 per cent of the sites were classified as difficult, just over 40 per cent as most difficult and just under 20 per cent as non-difficult.

By May 1993 (when President Premadasa was assassinated), a little under 100 factories had been opened (*Sunday Island,* September 25 1995, 13). By November 1993, 130 factories had been initiated, but in 1994 only about 60 were reported to have come into operation (Kelegama 1994, 22 and *Counterpoint* March 1993, 5). By 1994, 174 factories had been initiated within the 200 GFP. *Clothing* (January 1995, 23) reported that 167 plants were operating. Thus there is some doubt about how many are now operating (considerably less than 200) but for convenience we refer to this programme as the 200 GFP.

Each factory was intended to employ 500 people at a minimum wage of Rs.2000 a month, but the actual numbers employed have reputedly been well below this (see *Counterpoint* March 1993, 5). The CCC 1994 report pointed out that at the end of 1993, over a third of the 97 factories for which information was available had 400 or less employees (see CCC 1994, 28). It also reported that over a third of the factories were in default on their EPF and ETF payments, and yet payment of these was intended to be a condition for the renewal of quotas (see CCC 1994, 28).

The 200 GFP was launched, as was the provincial programme that preceded it, in the context of very high unemployment in the south of the country. The Presidential Youth Commission of 1990 had highlighted youth unemployment as a serious problem, and the 200 GFP was an attempt to decentralise a major industry away from the Western Province.

The 200 GFP came under the BOI and various incentives were offered (in addition to quota allocation) including tax holidays and credits, duty-free provisions (on a number of vehicles), loans from FCBUs, loans from the DFCC and the NDB (Kelegama 1994, 24, 25 and CCC 1994, 17-18). The generous incentives provided under the 200 GFP were considered to constitute excessive subsidies on exports by the US government which, in October 1993, imposed a countervailing duty on the imports of garments from Sri Lanka. We discuss this in more detail in Section 5.

The 200 GFP has not been appraised in detail (Kelegama 1994, 28) and (as far as we know) no detailed official evaluation has been done of it. According to the CCC (199, 27), the monitoring of the programme has also been weak. The major **problems** alleged to be associated with the 200 GFP were as follows:

* disruption to existing plants because of the reallocation of quotas. The '200 GFP' was expected to add at least 40 per cent to garment exporting capacity in Sri Lanka (Kelegama 1994, 2) at a time when quotas were already close to full utilisation and only expanding at a little over 6 per cent a year. In the event, the addition to capacity was no more than about 30 per cent but the problem of quota allocation has still been a major one. We discuss this in more detail in Section 3;

* distance from good infrastructure. Many of the factories were not supplied with good infrastructure and yet garment factories were being expected to have a shorter and shorter lead time on contracts;

* lack of experienced and trained labour. The rapid expansion meant that skilled labour was simply not available, particularly at middle management (supervisory) level. 40 per cent of the factories were opened by exporters with no previous experience of the garment industry and, as a result the quality of production was in many cases poor (Kelegama 1994, 26). A significant weakness of the 200 GFP was that, while the government took steps to decentralise the industry, the major training institutions were centralised at Ratmalana -- see Textile Institute, 1994;

* the 200 GFP diverted a considerable volume of low-cost finance -- especially from the DFCC and NDB -- into the garment industry. This would have been acceptably if the investments had been sound but the CCC (1994, 18-21) argued that, in the case of the '200 GFP', this was doubtful. It was unlikely that the banks would have made the same loans in the absence of political pressure.

However, in many of the interviews carried out for this research, the 200 GFP was said to have made a number of positive contributions. They were said to have achieved the following:

* to have increased competition in the industry and, in particular, re-distributed the quota premia across a larger production capacity;

* to have provided a significant redistribution of income into the rural areas (500 employees at Rs. 2000 per month would directly inject Rs. 1 mn. a month into the area around the garment plant); and, in doing so,

* to have set up establishments in areas where the pace of labour turnover is considerably less than in the 'Zone' establishments.

2.3 The future development of the textile and garment industries in Sri Lanka

Details of the past development of the textile and garment industries in Sri Lanka can be found in MHTI 1993 (see also statistics produced by the CTMA and SLAEA). The growth in production volume in each of the three main areas of yarn, fabric and garments is shown in Table 2.11.

Table 2.11
Production volume and growth in the Sri Lankan textile and garment industries, 1986-93

	Production volume		Growth rate (1986-1993) (% per annum)
	1986	1993	
Yarn (mn. kgs)	12.3	24.4	11
Fabric (mn. metres)	141	211	6
Garments (mn. pcs)(i)	171	363	12

(i) exports only
Source: MHTI 1993, 2.

As can be seen, the most rapid growth has been in garments with the growth in fabric production being relatively slow. This pattern is likely to be reversed over the next 10 to 15 years with the potential probably being greater in fabric production. Certainly, the Report of the Textile Task Force in 1994 identified a number of large (over $10 mn.) investments in yarn and fabric production suitable for promotion. These were the following:

* manufacture of polyester fibres;
* manufacture of spun yarn;
* weaving of filament yarn;
* weaving of spun yarn fabrics;
* knitting of spun yarn fabrics;
* dyeing and finishing of woven and knitted cotton and synthetic fabrics (see TTSC 1994, Part A, 19).

We discuss the potential markets and competitiveness for the different parts of the textile and garments industries in more detail in Chapter 4

3. MFA quotas - what are they? And how do they work in Sri Lanka?

3.1 The MFAs - what are they? How do they operate?

World trade in textiles and garments takes place in a very 'managed' market. 75 per cent of world trade has occurred in recent years within the framework of quotas organised within a series of bilateral agreements which, in turn, operate within the framework of what is called the Multi-Fibre Arrangement (MFA). It is worth noting that these arrangements:

* were intended to be temporary when first set up and have in fact lasted for over thirty years;
* are a major departure from the principles of free trade espoused by the GATT; and
* are scheduled to be phased-out between 1995 and 2005. Thus trade in textiles and clothing is restricted not only by tariffs but also by quotas under the MFA.

The origins of the MFA go back a long way. Restrictions on textile exports from the LDCs date back to at least the 1930s, when the UK and the USA used measures to limit the

then growing textile exports of Japan (Kelegama 1994, 6). Thereafter, in the 1950s, a combination of excess capacity in the textile sectors of many of the developed countries coincided with an increase in production in some of the LDCs. This led the UK and other countries to negotiate Voluntary Export Restraints (VERs) with the new suppliers (Japan, Hong Kong and India).

In the early-1960s, these bilateral agreements were arranged within a multilateral agreement negotiated under the auspices of the GATT. The multilateral agreement was called the Short Term Arrangement on Cotton Textiles (STA) which, as the name implies, was designed to deal with these 'short-run' problems. The stated purpose of the STA was to 'maintain orderly access' to developed country markets and to avoid ' market disruptions' in the world market for cotton textiles. The STA **was** short-lived -- it lasted one year. That was the good news for the protected producers in the developed countries. The bad news for the existing and potential producers in the LDCs was that the STA was replaced by the LTA -- the Long Term Arrangement Regarding International Trade in Cotton Textiles. This was referred to as an 'exceptional and transitional measure' originally covering the five years from 1962 to 1967 but it was renewed in 1967 and again in 1970.

Table 3.1
A chronology of textile and garment 'VER' frameworks

Agreements	Period	Products included	Quota growth	Important regulations
STA	I96I-62	Cotton	na	Quantity restrictions on specific suppliers case of market disruption
LTA	I974-77	Cotton products with 50 per cent cotton	>5%	As above
MFA-I	I974-77	Cotton, wool and syn. fibre	>6%	Flexibility provisions provided
MFA-II	I978-82	Same as MFA-I	0.5-I0%	Basket extraction Reasonable departure Flex. prov.
MFA-III	I982-86	Extended to linen ramie and blended silk for the United States	0.00I-6%	Basket extraction Anti-surge Reasonable departure suspended Flex. prov. suspended Reasonable departure restored
MFA-IV	I986-9I		0.00I-7%	Reintroduction of flex. prov. Anti-surge Basket extraction

Source: Suphachalasai 1994, 41.

In 1974, the LTA was replaced by the Multi-Fibre Arrangement (MFA). Like the STA and the LTA, the MFA provided a framework for the international textile and garment trade or, rather, a succession of frameworks since there have been four MFA frameworks as shown in Table 3.1, which summarises the main characteristics of the STA, LTA and MFA1 to MFAIV.

Thus the MFAs have comprised a series of frameworks within the GATT under which the major developed countries (with the European Union counting as one member) have been allowed to put 'VER' restrictions on imports from developing countries. (For a list of member-countries, see Appendix B in Suphachalasai 1994). Within the framework of the MFAs, there are bilateral agreements between the member countries. The MFAs were intended to provide operating principles such as non-discrimination among exporting countries, minimum export growth rate of 6 per cent in terms of volume, and flexibility provisions. The latter included the following:

(i) **swings**, which permit the transferability of quotas among product categories;
(ii) **carry-forward**, which enables advance use of the following year's quotas; and
(iii) **carry-over**, which allows transferability of unused quotas to the following year.

The basic objective of the MFAs is to:

> "...achieve the expansion of trade, the reduction of barriers to such trade and the progressive liberalisation of world trade in textile products... " (GATT 1974, 6 quoted in Suphachalasai 1994, 38).

Thus the MFAs were intended to provide protection and a temporary breathing space to developed countries to adjust their industries over a period of time. The LDC exporters had no choice but to agree to the MFAs for fear of a worse alternative, namely, disorderly and unpredictable unilateral action by developed countries under the GATT safeguard clause. In fact, Suphachalasai claims, the successive MFAs became more complicated and more restrictive especially for the dominant suppliers.

Thus the MFAs can be said to be both **outside** and **inside** the GATT;

* they are 'outside' in the sense that the MFAs are a major departure from the principles of the GATT. They take an entire sector out of the GATT arrangements and thereby avoid the proscriptions of GATT on discrimination and on quantitative restrictions; and

* they are 'inside' in the sense that the MFAs were designed to regularise this departure from the GATT.

Getting round or **circumventing** the restrictions by exporting through non-restricted countries is not permitted although people in the trade estimate the world value of circumventing trade in garments to be as high as 10 per cent of the total garment trade. However, the main way in which the restrictions have been circumvented is through 'quota-hopping' investment. As quotas become fully utilised for particular items of clothing in the established producing countries, investors have expanded in non-quota countries to tap sources of labour which, although initially expensive compared to the established LDC producers, are cheap relative to the Developed Countries. Thus the MFAs have generated a considerable level of trade diversion; that is, the diversion of production into, initially, higher-cost producers as quotas became fully-utilised in country after country.

Thus by 1987, just over half of the textile and garment products exported by LDCs were subject to VERs and the average quota utilisation was more than 90 per cent (Page *et al* 1991, 29). Thus about 45 per cent of all exports of textiles and garments from LDCs were

constrained by quotas. By now (the mid-1990s) the proportion constrained by quotas is almost certainly higher.

There have therefore been **'push'** and **'pull'** factors which have encouraged investment in the production of textiles and garments across Less Developed Countries. Sri Lanka is no exception. The pull factors were the availability of cheap, semi-skilled labour and the tax and other incentives associated with the Free Trade Zone opened in Sri Lanka in the late 1970s. The push factor was the quota system which first encourages production in 'new producers' like Sri Lanka and then holds back specialisation by the lowest-cost producers, including those in Sri Lanka.

With the completion of the Uruguay Round, the MFA is due to be phased-out between 1995 and end-2004. Given the fact that the original arrangements were intended to be temporary and yet have lasted for over 30 years, it is worth asking what is the likelihood of the full phasing-out of the MFA as scheduled by the Uruguay Round. We come back to this issue in Chapter 5, but in the next section of this Chapter we look at the following questions:

* garment products exported from Sri Lanka on which quotas binding;
* how the quotas administered; and
* what the quotas are worth.

3.2 Quotas and Sri Lankan production and exports

Quota and non-quota exports of textiles and garments from Sri Lanka

As can be seen from Table 3.2, the vast majority (over 90 per cent) of exports from the Sri Lankan textile and garment industries consisted of garments in 1994. Thus the focus here is on garments.

Table 3.2
Exports of textiles and garments from Sri Lanka, 1993 and 1994

	1993 (Jan-Dec)		Jan-October		
	(Rs. bn.)	%	1993 (Rs. bn.)	1994 (Rs. bn.)	%
Textiles	4.1	6	3.3	3.6	6
Garments	62.5	92	49.7	54.4	91
Other made-up textile articles	1.5	2	1.2	1.7	3
Total	68.1	100	54.2	59.7	100

Source: SLAEA 1995, table 3, 7.

Most of the exports of garments from Sri Lanka (by value) consist of exports within the quota categories. This is shown in Table 3.3.

It should be noted that some of the figures in Table 3.3 are shaky. Most noticeably the garment exports to the USA are given in SLAEA, 1995, Appendix 8 and SLAEA 1994, 26 as summarised in Table 3.4.

Table 3.3
Exports of garments from Sri Lanka - quota and non-quota, 1989 and 1993

1989	Quota	Non-quota		Total			
	vol.	%	vol.	%	vol.	value	%
	mn.pcs(*)	mn.pcs(*)		mn.pcs(*)		Rs.bn.	
USA	123	97	4	3	106	11.6	69
EU	13	22	47	78	60	4.0	24
Others	na		na		19	1.2	7
Total	na		na		185	16.8	100
1993	**Quota**	**Non-quota**		**Total**			
	vol.	%	vol.	%	vol.	value	%
	mn.pcs(*)	mn.pcs(*)		mn.pcs(*)		Rs.bn.	
USA	251	88	33	12	197	39.3	63
EU	25	17	121	83	146	19.6	31
Others	na		na		20	3.5	6
Total	na		na		363	62.4	100

Sources: EU figures from SLAEA 1994, issue 4, pages 29, 30.
Total figures from SLAEA 1995, page 10 (see also SLAEA 1994, 25).
Notes: Quota and non-quota volume figures for USA for 1993 are in millions of square metres, not pieces. Note that there are major discrepancies for the 1993 US volume figures between those in SLAEA 1994, 26, and those in SLAEA 1995, Appendix 8.
Figures may not add up due to rounding.

Table 3.4
Quota and non-quota exports of garments to the USA from Sri Lanka

	Mn. sq. metres	%	Value ($mn.)	%
SLAEA 1994,26				
Quota	251	88	na	
Non-quota	33	12	na	
Total	284	100	na	
SLAEA 1995, App.8				
Quota	192	81	723	90
Non-quota	45	19	82	10
Total	237	100	805	100

However, some important points can be noted on the basis of Table 3.3:

first, about two-thirds (by value) of total garment exports are to the USA, the percentage being slightly lower in 1993 than in 1989;
second, about 90 per cent of exports (by value) to the USA consist of quota items, while of the exports to the EU, less than 20 per cent (by volume) are quota items;
third, we can estimate that, in 1993, exports of quota items amounted to between 60 per cent and 65 per cent of the total value of garment exports;
fourth, it would seem that the volume of non-quota items grew between 1989 and 1993 for both the US and EU markets. This last point is important because this may be a function of the growing competitiveness of Sri Lankan products or it may be a function of the growth in the **utilisation of quotas**.

Quota utilisation in Sri Lanka - 1989-1994

For garment exports to the EU, Sri Lanka is subject to quotas under four categories, namely, 6, 7 and 8 (which are in the most sensitive category) and 21 (which is in the less sensitive group). These categories, together with the actual and quota volumes are given in Table 3.5.

It shows that the most popular items under quota are blouses (category 7) and shirts (category 8). The average quota utilisation for 1993 and 1994 was 110 per cent for blouses and 103 per cent for shirts. For exporting to the EU these are the 'hot' categories. For all four categories the average utilisation (by unweighted volume) in 1993 and 1994 was 90 per cent.

For garment exports to the USA, there are many more product categories under quota. The Bilateral Trade Agreement covering the period from January 1994 to the middle of 1995 contained 31 quotas covering the trade in 51 categories (SLAEA 1995, 12). The quota utilisation for the US market has been very high in recent years, especially for certain categories. Summary figures are shown in Table 3.6; more details are given in Appendix 6.

Table 3.5
Garment exports from Sri Lanka to the EU (1989-94) Quota utilisation
(all volume figures are in millions of pieces)

	1989			1990			1991		
	Quantities			Quantities			Quantities		
	Quota	Actual	% utili-sation	Quota	Actual	% utili-sation	Quota	Actual	% utili-sation
06 Trousers	3.3	3.0	90	3.6	4.5	126	4.5	4.9	108
07 Blouses	4.6	3.9	84	4.9	4.9	100	7.2	6.2	85
08 Shirts	4.9	3.8	79	5.2	4.2	80	5.8	4.8	82
21 Jackets	3.5	2.4	69	3.8	3.1	82	4.8	3.3	70
Total	16.3	13.1	80	17.4	16.6	95	22.3	19.1	86
	1992			1993			1994		
	Quantities			Quantities			Quantities		
	Quota	Actual	% utili-sation	Quota	Actual	% utili-sation	Quota	Actual	% utili-sation
06 Trousers	4.8	3.8	79	5.4	4.7	88	6.3	5.6	89
07 Blouses	7.8	7.3	94	8.6	9.9	115	10.8	11.4	106
08 Shirts	6.2	4.7	75	6.9	6.7	97	7.5	8.2	109
21 Jackets	5.1	3.1	61	5.8	3.4	59	6.8	2.9	43
Total	23.9	18.9	79	26.6	24.7	93	31.4	28.1	90

Source: Thurairajah, 1993, pages 54 and 55 for 1989 to 1991 inclusive.
Island, Monday 13th March 1995, for 1992.
SLAEA 1994, issue 4, page 31 for 1993 and 1994.

Table 3.6
Exports of Garments from Sri Lanka to USA (1990-95)
Quota Utilisation

Category	1990/91			1991/92			1992/93			1993 (6 month quota)			1994			1995	
	Quota ($mn)	Actual ($mn)	% utiln.	Quota ($mn)	Actual ($mn)	% utiln.	Quota ($mn)	Actual ($mn)	% utiln.	Quota ($mn)	Actual ($mn)	% utiln.	Quota ($mn)	Actual ($mn)	% utiln.	Quota ($mn)	% increase
237 Playsuits	9.7	2.6	26	10.2	6.6	65	9.2	4.6	50	4.6	1.5	33	12.2	10.2	83	15.3	25
331/631 Gloves and mittens	7.2	6.7	93	7.6	6.9	90	8.5	8.3	98	4.5	4.4	98	9.9	10.7	108	9.8	-1
334/634 M and B coats	53.1	35.4	67	61.9	40.4	65	68.2	56.8	83	35.4	35.4	100	74.5	92.2	124	61.9	-17
335/835 W and G coats	25.1	15.3	61	30.6	26.4	86	33.4	32.0	96	13.9	13.9	100	34.8	39.0	112	32.0	-8
336/636/836 Dresses	24.1	12.1	50	26.0	14.9	57	31.6	13.0	41	13.9	9.3	67	39.0	49.2	126	33.4	-14
338/339 Cotton shirts, knitted	65.5	59.9	91	72.4	72.4	100	66.2	63.4	96	40.4	36.2	90	86.4	75.9	88	92.6	7
340/640 M and B shirts, not knitted	49.6	46.6	94	67.1	60.5	90	87.0	87.0	100	25.1	25.1	100	83.4	82.6	99	83.4	0
341/641 W and G shirts/blouses, not knitted	90.9	71.1	78	98.1	83.0	85	114.6	113.9	99	55.3	55.3	100	115.2	113.3	98	119.8	4
342/642/842 Skirts	27.3	17.9	66	36.6	23.0	63	38.7	27.3	70	17.2	8.6	50	29.4	24.4	83	38.7	32
347/348/847 Trousers, slacks, shorts	59.2	56.0	95	65.6	65.6	100	75.8	75.8	100	40.7	40.7	100	95.5	89.8	94	98.7	3
351/651 Nightwear	18.4	17.5	95	20.3	19.4	95	23.1	22.1	96	12.0	12.0	100	29.5	24.9	84	31.4	6
352/652 Underwear	23.2	12.2	52	21.7	18.1	84	23.2	19.0	82	13.5	10.8	80	24.7	26.5	107	27.2	10
635 W and G coats, MMF	32.2	32.2	100	29.9	27.6	92	39.1	39.1	100	12.7	12.7	100	39.1	46.0	118	38.0	-3
638/639/838 Shirts/blouses, knitted	26.6	22.0	83	28.3	27.9	99	30.5	20.7	68	12.3	8.5	69	28.3	22.0	78	34.3	21
647/648 Trousers, MMF	46.9	44.6	95	45.1	45.1	100	41.1	39.9	97	20.3	19.1	94	44.0	39.9	91	57.3	30
Sub Totals - Large categories (*)	558.9	452.0	81	621.5	537.8	87	690.0	623.0	90	321.7	293.5	91	746.0	746.6	100	773.8	4
Sub Totals - Small categories	.4	30.0	66	53.8	35.4	66	50.1	23.9	48	20.7	13.1	63	36.1	28.0	78	45.5	26
Grand Total	604.3	481.9	80	675.3	573.2	85	740.1	646.9	87	342.4	306.6	90	782.1	774.7	99	819.3	5
% increase in quota on previous year (**)				12			10			na			6			5	

Sources: SLAEA 1995 Appendices 5A to 5D for quota and actual 1990-1993.
see Thurairajah 1995 Annex B for 1994 quota & actual.
see Thurairajah, 1995, Annex C for the 1995 quota.
Values are derived by applying the average 1994 export prices taken from SLAEA, 1995, Appendix 8, and based on US input statistics and import statistics. See Appendix 6 of this report for details.
* Categories are defined as large, if the actual value in 1994 is greater than $10m.
** Percentage increase for 1994 is compared with 1992/93.

As Table 3.6 indicates, the average utilisation of the quota was obtained by applying the 1994 average export unit prices to the volumes for each category (as shown in detail in Appendix 6). On this weighted basis, the average utilisation has risen from 80 per cent in 1990/91 to 99 per cent in 1994. There might be some controversy about this method of weighting but we come to a similar conclusion if we work on the basis of square metre equivalent. On this basis the utilisation for the large categories (covering the vast majority of the quota exports) was 101.7 per cent compared to 100 per cent by value. The calculations by square metre equivalent are shown in Table 3.7.

Table 3.7
Exports of garments from Sri Lanka to USA (1994)
Quota utilisation Category

	Conv. factor (sqme) (**)	Unit	1994			
			Quantities			
			Quota n.units	Actual mn.units	Quota Mn.sqme	Actual Mn.sqm
237 Playsuits	19.2	doz	0.24	0.20	4.6	3.8
331/631 Gloves and mittens	2.9	doz.pr	2.58	2.79	7.5	8.1
334/634 M and B Coats	34.5	doz	0.59	0.73	20.4	25.2
335/835 W and G coats - veg fibre	34.5	doz	0.25	0.28	8.6	9.7
336/636/836 Dresses	37.9	doz	0.42	0.53	15.9	20.1
338/339 Cotton shirts, knitted (M and B / W and G)	6.0	doz	1.24	1.09	7.4	6.5
340/640 M and B shirts, not knitted	20.1	doz	1.13	1.12	22.7	22.5
341/641 W and G shirts/blouses, not knitted	12.1	doz	1.75	1.72	21.2	20.8
342/642/842 Skirts	14.9	doz	0.41	0.34	6.1	5.1
347/348/847 Trousers, slacks, shorts -veg	14.9	doz	1.50	1.41	22.4	21.0
351/651 Nightwear	43.5	doz	0.32	0.27	13.9	11.7
352/652 Underwear	9.2	doz	1.12	1.20	10.3	11.0
635 W and G coats, MMF	34.5	doz	0.34	0.40	11.7	13.8
638/639/838 Shirts/blouses, knitted	15.0	doz	0.67	0.52	10.1	7.8
647/648 Trousers, slacks, shorts - MMF	14.9	doz	0.76	0.69	11.3	10.3
Sub Totals - Large categories (*)					194.1	197.5
per cent Utilisation of Quota						101.7

Sources: Quota & Actual 1994 - Thurairajah 1995, Annex B.

* Large categories are those for which the value (at 1994 export prices) was above $10 mn. - see Table 3.5 and Appendix 6.

** Conversion factors are from SLAEA 1995 (see also Appendix 2 to this report).

As stated, it is clear from Table 3.6 that the overall utilisation of the quotas has increased from 80 per cent in 1990/91 to 99 per cent in 1994. It is also clear that, for some of the hottest categories, there was an over-fulfillment of quotas in 1994. The hottest categories were as follows:

	% quota utilisation
Gloves and mittens	108
M and B coats	124
W and G coats -veg fibre	112
Dresses	126
Underwear	107
W & G coats - MMF	118

Thus, for the hottest categories, there was an over-fulfillment of quotas in 1994. The figures given in the SLAEA 1995 brief for the US negotiations are shown in Table 3.8. Note that these are notional because the quota period was not scheduled to finish at the end of 1994, but was extended to finish in the middle of 1995.

Table 3.8
Exports of garments from Sri Lanka to USA -- The over-fulfillment of quotas in 1994

Category	Unit	Notional base limits for 1994	Actual ship-ments in 1994	Notional vership-ments units	%
331/631 Gloves and mittens	dozpr	2.34	2.73	0.39	17
334/634 M and B Coats	doz	0.52	0.74	0.22	42
335/835 W and G coats - veg fibre	doz	0.23	0.28	0.05	22
336/636/836 Dresses	doz	0.34	0.53	0.19	56
338/339 Cotton shirts, knitted (M and B / W and G)	doz	1.04	1.09	0.05	5
340/640 M and B shirts, not knitted	doz	1.01	1.12	0.11	11
341/641 W and G shirts/blouses, not knitted	doz	1.63	1.73	0.10	6
347/348/847 Trousers, slacks, shorts -veg	doz	1.12	1.41	0.29	26
351/651 Nightwear	doz	0.26	0.27	0.01	4
352/652 Underwear	doz	1.11	1.21	0.10	9
635 W and G coats, MMF	doz	0.31	0.40	0.09	29

Source: SLAEA 1995, page 17.

These notional over-fulfillments of the quotas caused a minor crisis in the industry. We look at the causes of this crisis in Section 3.3 but before that, it is important to look at how quotas are administered in Sri Lanka.

The administration of quotas in Sri Lanka

In Sri Lanka, quotas have been administered by the Textiles Quota Board since July 1, 1992. The membership of the Textile Quota Board was given in MHTI 1992, as follows:

* Secretary, Ministry of Finance
* Secretary to the Ministry of Handloom and Textile Industries
* Director-General of the Greater Colombo Economic Commission (now the BOI)
* Director of Commerce
* Chairman, Sri Lanka Apparel Exporters' Association
* Nominee of FTZ Manufacturers' Association
(see MHTI 1992, 2)

The detailed rules of the TQB were formulated by the MHTI in September 1992 (see MHTI 1992). The principal function of the TQB is the management and distribution of export quotas to all approved exporters constituting the apparel export industry, within the policy framework authorised by the Minister under the Rules. Assisting the TQB is a TQB sub-Committee which is charged with the responsibilities of allocating from time to time unallocated quotas (e.g. common pool quotas) and quotas in categories likely to be under-performed, and of sanctioning quota transfers and category changes.

TQB minutes are circulated among all its members and particulars of the sub-Committee decisions are posted on the public notice board at the Ministry.

In general, export quotas are allocated on the basis of past performance. In 1994/95, this applied to all factories including those set up under the 200 GFP. In the years up to 1994/95, quotas had been allocated to the 200 GFP according to their location as follows:

* to factories in the 'most difficult' areas the allocation was 50,000 dozen (600,000 pieces) per factory;
* to factories in the 'difficult' areas (Kandy, Ratnapura and Matara) the allocation was 25,000 dozen (300,000 pieces); and,
* to factories in the non-difficult areas, the allocation was 10,000 dozens (120,000 pieces) (MHTI 1994, 2)

From 1994/95 the quota allocation for **all** factories was on the basis of past performance. The allocation to the 200 GFP factories was split into fast-moving and slow-moving categories, with those factories in the difficult and most difficult areas getting a greater percentage of fast-moving category quotas than those in the non-difficult areas.

Surplus quotas remaining in any category or categories after the issue of 'performance' quotas are transferred to a common pool and distributed among all approved exporters by the TQB. Exporters are permitted to surrender their quotas to the TQB for reallocation and, if done within a prescribed time limit, they will obtain a performance credit for the next quota year. Until March 1994, temporary transfers of quotas were permitted (although they had to be approved by the TQB) but in March 1994, this was no longer permitted and the unused quotas had to be surrendered to the TQB. However, if the surrender is made early enough in the period, the quota-holder would qualify for performance quotas.

The MHTI 1994, 3 stated that exporters who are in arrears on their EPF/ETF monthly contributions are liable to have their quotas cancelled.

Constructing a clear picture of the quota situation in Sri Lanka is difficult. The situation is complicated because of the following:

* changes in the quota periods. Until the end of June 1993, the bilateral agreements between Sri Lanka and the USA have run from the middle of one year to the middle of the next. But the second half of 1993 was a quota period and then the next quota period was from January 1st 1994 to June 30th 1995; and

* a number of adjustment provisions, including:
  - swing (up to 7 per cent of the quota can be switched between products for all categories except wool);
  - carry over (this allows unused quotas to be carried forward to the next quota period);
  - carry forward (this allows some part of the following year's quotas to be used in the current year);
  - special shift (these are shifts between categories in excess of the swings) (see SLAEA 1995, 20).

In addition, periodically, categories have been merged and sub-limits within categories have been removed (for sub-limits see SLAEA 1995, 23). The complexity of the quota situation is not eased by the fact that a summary of the quotas is not published by the TQB. We understand that such a summary is published for quotas in The Philippines, and garment exporters and brokers stated that such a published summary in Sri Lanka would facilitate the fuller utilisation by Sri Lanka of quotas for the 'non-hot' categories. A print-out of the quotas is provided to the Sri Lanka Apparel Exporters' Association, but for the 1994/95 quota period, there were 577 factories to which quotas were allocated, under the following categories:

* 1-161 200 GFP factories
* 162-292 BOI parent factories
* 293-330 FTZ factories
* 331-530 Ministry normal factories
* 531-577 Provincial factories

For this research, we summarised the quotas allocated to FTZ factories but it was beyond the scope of this research to summarise the quotas from 577 pages of print-out.

However it is clear that the pressure on quotas for the US market had built up from the early 1990s, and by 1993 and 1994 pressure was very heavy. It is this that we look at next.

3.3 The pressure on quotas for the US market in the 1990s

The 200 GFP and the increasing pressure on quotas for the US market

As stated in the previous section, there was over-fulfillment of the notional base quotas in 1994. The allocation of quotas had become progressively tighter with the rapid expansion of the garments industry under the 200 GFP. A major incentive for setting up a factory under the 200 GFP was the allocation of quotas and, as we have seen, the more difficult the location, the bigger the allocation of quotas. The garment quotas allocated to the 200 GFP amounted to about 5.5 mn. dozens (see *Sunday Island* 21 November 1993). Most of this was targeted at the US market but this is hardly surprising since the large majority of the quotas were for the US market. Thus it was reported that, of the total quota of 15 mn. dozens, about 12.5 mn. dozens was the US. In addition to the 5.5 mn. dozens. allocated to the 200 GFP, about 45 per cent of the total US quota, amounting to 5.6 mn. dozens was reserved for factories (mostly foreign) in the EPZs. This left only 1.4 mn. dozens (12.5 minus 5.5 and 5.6) for the factories outside the GFP and the EPZs. A press report in the *Island* of 6th September 1993 claimed that the quotas of 'traditional' garments producers had been cut by 25 per cent to facilitate the growth of the 200 garment factories and in November 1993, the BOI was reported as not being able to allocate quotas to new garment factories (*Daily News,* 5 November 1993).

Thus, not surprisingly, by late-1992, there were growing complaints from small and medium garment exporters who had small permanent quotas plus an allocation in 1991/92 of some free pool and additional quotas for the US market. A letter published in one of the national newspapers on 23rd October 1992 complained that small and medium exporters in the districts of the Western Province were feeling the pinch because of their small quotas. They claimed that credit could not be obtained from banks because

of the re-allocation of quotas to the 200 GFP. In a reply (on 26th October 1992), the Secretary to the Ministry of Handloom and Textile Industries Ministry claimed that the allocation of the additional quotas was on the basis of 1991/92 only and was subject to the explicit condition that they would not be entitled to quotas in 1992/93 on the basis of their 1991/92 performance.

Allegations have also been made of 'investors' obtaining quotas under the 200 GFP and not producing the goods, but subcontracting the orders to traditional producers who then supply the 200 GFP 'investor'. A press report in the *Island* of 2and February 1994 claimed that the super-profit creamed off by the sub-contractor was equivalent to Rs.40 a piece.[1]

Thus, by 1993 and 1994, there was a bit of a crisis in the allocation of quotas, and in a paper to the Textiles Quota Board, Thurairajah sounded a warning about the notional over-fulfillment in 1994;

> "It is advisable to caution the apparel export industry in advance that the Textile Quota Board may have no alternative but to impose all round quota-cuts in order to resolve the problem of deficits. Such advance caution will give exporters adequate opportunities of restructuring and diversifying their production programs" (Thurairajah 1994, 3)

The February 1995 negotiations

As of January 1st 1995, the bilateral agreements under the MFA were superseded by the 'transition period' of the Uruguay Round Agreement on Textiles and Clothing (ATC). The transition period of the ATC was to be based on calendar years.

This transition, plus the notional over-fulfillment of quotas and the possibilities offered by the various 'flexibility' provisions (swings, carry-over, carry forward, etc), provided the background to negotiations between the US and Sri Lanka governments held in February 1995. The Sri Lankan delegation was headed by the Minister of Industrial Development.

In a paper produced after the negotiations it was claimed that:

> "In the process of negotiations, it was possible to persuade the US government to grant Sri Lanka concessions in the form of an all round uplift of the notional base levels for 1994, increased growth rates in a few categories, additional special shifts, special carry forwards, removal of one sub-limit which had been impeding growth and the continuation of handloom quotas in three categories which will be available throughout the transition period" (Thurairajah, 1995, 1,2).

What specific changes were made?

Most importantly, there was a carry forward of quotas into future years. The Memorandum of Understanding of February 7 1995 (MOU 1995) between the USA and

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1 This super-profit of Rs 40 compares with an average unit price in 1993 to the US market of about Rs 200 (derived from Table 3.3). Thus the super-profit is equivalent to about 20 per cent of the export value.

Sri Lanka set out the base levels of the quotas for 1994 and in doing so, it made special carry-forward provisions between the years 1994 and 1995 through to 1997 for some categories as shown in Table 3.9.

Table 3.9
Special carry-forward provisions in the MOU 1995

Category	1994 %	Percentage of special carry-forward		
	utilisation	1995	1996	1997
331/631 Gloves and mittens	108	25	15	5
334/634 M and B Coats	124	40	20	5
335/835 W and G coats - veg fibre	112	30	20	5
336/636/836 Dresses	126	50	35	5
338/339 Cotton shirts, knitted (MB/WG)	88	10	5	5
340/640 M and B shirts, not knitted	99	15	10	5
341/641 W and G shirts/blouses, not knitted	98	10	5	5
347/348/847 Trousers, slacks, shorts -veg	94	40	20	5
351/651 Nightwear	84	25	15	5
352/652 Underwear	107	10	5	5
635 W and G coats, MMF	118	30	15	5

Source: Table 3.6 and MOU 1995 paragraph 5.

In addition to the carry-forward provisions, special shifts were included in the Memorandum and the sub-limit on 340-640 was removed (see Thurairajah 1995, 7).

The future for US quotas

It seems that the rates of special carry forward are more than sufficient to resolve the 1994 notional overshipments in the relevant categories which (by virtue of such overshipments) are characterised as sensitive. **However, the carry-forward provisions do of course erode the quotas for later years.** In 1995, the expansion in the US quota can be seen from Table 3.6 to be only about 5 per cent compared to annual rates of growth of 10 per cent or more between 1991 and 1993.

This estimate of a growth of 5 per cent is derived from a paper by Thurairajah produced soon after the negotiations. Estimates from a trade source are very different as can be seen in Table 3.10.

It is not immediately clear how the differences can be explained. The trade source gives a much slower rate of growth for 1995. The annual rate of growth over the period 1995 to 1997 as a whole averages per cent. Thus it does seem clear that the rate of growth for the quotas to the USA over the period to 1997 is likely to be per cent per annum or even less.

3.4 Quotas in the garment industry and profits, pressure-groups and prices

Quota-profits - what are the quotas worth?

Appendix 4 discusses how Voluntary Export Restraints (VERs) operate and who can be expected to gain and lose from quotas. It seems likely that the super-profits from quotas held by Sri Lankan exporters of garments are worth between 10 per cent and 20 per cent of the export value. The quota premia on the 'hottest quotas' (see earlier pages in this Chapter) would be at the top of this range. Given that quota exports in 1994 were about Rs 50 bn., the super-profits from quotas would have been worth between Rs. 5 bn. and Rs. 10 bn.

How does this relate to rates of profit in the garment industry? This question is difficult to answer since no comprehensive figures seem to be available. However the best source of data is an analysis of the profit rate for companies in the Katunayake Export Processing Zone (or KEPZ) carried out with the cooperation of the BOI. Not all companies in the KEPZ are garment exporters but a substantial proportion of the output is from garment companies. In 1994 the value of gross output from KEPZ companies was Rs. 25 bn. (see Edwards and Chandradasa 1996, Table 1). It is clear from an analysis of the quotas that at least 4mn. dozen of the quotas for the largest categories (for the largest categories, see Table 3.7) to the USA are allocated to companies in the FTZs and of this 4 mn., about 3.2 mn. were allocated to companies in the KEPZ. Total quota exports to USA in 1994, were about Rs. 36 bn. for about 13 mn. dozen pieces. On this basis the gross output of the KEPZ garment companies would have been about Rs. 9 bn. If we add on an allowance for non-quota output and quota output to the EU and other areas, it is likely that the gross output of the KEPZ garment companies was about Rs. 15 bn. in 1994, accounting for 60 per cent or more of the total gross output from KEPZ. (In 1990, it was reported in the *Daily News* of November 18 1992 that about two-thirds of the gross output from the KEPZ consisted of garments). Thus it is likely that the profits of garment companies were close to the average for all KEPZ companies.

What is or was the average rate of profit for all KEPZ companies? The average figures for the 1990 to 1994 period are as follows:

1990-94	Annual Rs. bn.	average %
Sales	18.2	100
Imported raw materials	12.7	70
Other imported costs	1.5	8
Local labour costs	1.2	7
Local materials	0.3	2
Gross profit	2.5	14

The above figures exclude capital expenditures. Over this period, these totalled about Rs. 4.5 bn. Thus the net profit after depreciation of about Rs. 0.4 bn., but before any corporate taxes and interest charges, was about Rs. 2.1 bn. giving a rate of profit of just under 50 per cent on capital employed. This rate of profit can be derived from the net profit margin on sales multiplied by the rate of capital turnover. The net profit margin (after depreciation) is about 12 per cent and the capital turnover is about 4 times giving a rate of profit on capital of close to 50 per cent p.a. On a discounted cash flow basis, the rate of profit over the period between 1978 and 1994 was over 68 per cent p.a.

Table 3.10
Quotas from Sri Lanka to the USA for the hottest quota categories Estimates for 1995 to 1997

Category	Units	Average export price	1995 (a)		1995 (b)		1996		1997	
		1994 ($/unit)	Quantities (mn)	Value ($mn)	Quantities (mn)	Value ($mn)	Quantities (mn)	Value ($mn)	Quantities (mn)	Value ($mn)
LARGE CATEGORIES										
237 Playsuits	doz	51.0	0.30	15	0.27	14	0.28	14	0.30	15
331/631 Gloves and mittens	doz pr	3.8	2.55	10	2.20	8	2.76	11	2.95	11
334/634 M and B coats	doz	126.3	0.49	62	0.42	53	0.61	77	0.65	82
335/835 W and G coats -veg fibre	doz	139.2	0.23	32	0.22	31	0.27	38	0.29	40
336/636/836 Dresses	doz	92.9	0.36	33	0.26	24	0.40	37	0.43	40
338/339 Cotton shirts, knitted	doz	69.6	1.33	93	1.14	79	1.22	85	1.30	90
340/640 M and B shirts, not knitted	doz	73.8	1.13	83	1.03	76	1.12	83	1.19	88
341/641 W and G shirts/blouses, not knitted	doz	65.9	1.82	120	1.65	109	1.85	122	1.96	129
342/642/842 Skirts	doz	71.7	0.54	39	0.66	47	0.63	45	0.68	49
347/348/847 Trousers, slacks, shorts - not veg	doz	63.7	1.55	99	1.09	69	1.19	76	1.24	79
351/651 Nightwear	doz	92.2	0.34	31	0.28	26	0.31	29	0.34	31
352/652 Underwear	doz	22.1	1.23	27	1.11	25	1.30	29	1.39	31
635 W and G coats, MMF	doz	115.1	0.33	38	0.28	32	0.36	41	0.38	44
638/639/838 Shirts/blouses, knitted	0	42.3	0.81	34	0.90	38	0.37	16	0.33	14
647/648 Trousers, slacks, shorts - MMF	doz	57.9	0.99	57	1.05	61	1.04	60	1.12	65
Sub Totals - Large categories		1088	14	774	13	692	14	762	15	809
% increase on the previous year				4		-7		10		6
(1994 quota value for the largest categories = $746 mn; see table 3.5)										

Sources: 1995 (a) from Thurairajah 1995, Annex C.
1995(b), 1996 and 1997 from trade source (AO).

In addition to generalised data for the KEPZ, we obtained profit figures for 6 garment-producing companies chosen randomly from the KEPZ by the BOI for the period between 1989 and 1994. Over these five years, the average return on capital employed was 69 per cent. The profit margin on sales averaged 26 per cent and the average ratio of sales to capital turnover was 2.7. Thus it seems that the rate of profit in the garment exporting industry, particularly for companies that are allocated hot quotas, is exceptionally high. It seems likely that the premium for the hottest quotas is at least 20 per cent of the gross output value.

Pressure-groups in the garment industry

In the context of quota premia and the expansion of the industry's capacity with the 200 GFP, it is not surprising that various pressure groups have developed. These are shown in Table 3.11.

Table 3.11
Representative Associations in the Garment Industry

Association	Founding year	No of members
Sri Lanka Apparel Exporters' Association (SLAEA)	?	198
Free Trade Zone Manufacturers' Association	?	56
Small and Medium Apparel Exporters' Association	1993	112
National Apparel Exporters' Association	1993	130
Sri Lanka Buying Offices' Association	1993	70

Source: Kelegama 1994, 21.

The garment industry in Sri Lanka now has five associations. The **Free Trade Zone Manufacturers' Association** and the **SLAEA** are the oldest, with the SLAEA being the most influential of the them all. However, in 1993 and in the wake of the 200 GFP, the Small and Medium exporters broke away from the SLAEA to form their own association - it was later re-named the **Sri Lanka Chamber of Garment Exporters.** Another new association which came into existence in 1993 was the **National Apparel Exporters' Association (NAEA)**, which represents the exporters under the 200 GFP. One of the main factors leading to the formation of this association was the political change that took place after the assassination of President Premadasa in May 1993. It is alleged by officials of the association that most of the incentives promised on the launch of the 200 GFP through the BOI have not been granted (see Kelegama 1994, 21). Finally there is the **Sri Lanka Buying Offices Association** which also started in 1993.

Quotas, upgrading and prices

One alleged effect of the MFAs has been to encourage the upgrading of exports from those countries constrained by quotas. With the quotas being specified in quantity terms, it is argued that there is an incentive to supply higher value quota products so as to maximise super-profits or rents (see Willamson and Milner 1991, 144).

Regrettably, reliable information on this is not easy to obtain. In looking at unit prices for exports from Sri Lanka, there are three factors which can easily be confused with general changes in the price of clothing:

* **first**, the prices of other goods are rising and therefore the prices need to be expressed in real terms;
* **secondly**, if Sri Lanka upgrades the quality of its exports, then the average price might rise in real terms and yet this may be consistent with a falling real price of garments in general; and
* **thirdly,** Sri Lankan exporters may be able, over time, as a result of experience in marketing or reliability of delivery times, to get a higher share of the final retail price.

Thus if the price of a particular category of garment remains constant in real terms, it could be because of:

* **a rise in the average price** either because of a switch to higher-quality exports or because the exporter has been able to negotiate a higher ratio of the export price to the final retail price; or

* **counteraction by a fall due to a general decline in the price of garments compared to other goods.**

It does seem as though the real price of clothing has fallen in real terms over the past decade. The *Economist Global Economic Survey* of October 1 1994, 15 reported that the real price of shoes and clothing had fallen in the USA by 20 per cent over the past ten years. Note that this refers to the average real price of shoes and clothing consumed. As far as the EU market is concerned, Majmudar reports that the average unit price of **imports** of garments from outside the EU had fallen by 2 per cent between 1982 and 1994 (Majmudar 1995, Table 11). Since the average rise in prices in the EU over the same period was at least 20 per cent, this suggests a real fall of at least the same magnitude as in the USA.

Table 3.12
Percentage changes in average unit import prices of selected product categories - USA and EU - 1982-92

	Percentage changes imports into the EU	Percentage changes into the USA	
Shirts	+37	Cotton non-knit shirts	+84
T-shirts	+19	Cotton knit shirts	+50
Pullovers	+53		
Trousers	+22	Cotton trousers	+16
Blouses	0	W&G cotton knit shirts	+76
		W&G cotton non-knit shirts	
		shirts	+39
W and G overcoats	+10	Cotton coats	+14
W and G dresses	-20	Cotton dresses	+49
W and G skirts	+15	Cotton skirts	+32
W and G suits	+ 5	Women's cotton trousers	+26

Sources: Majmudar 1995, Tables 5 and 12.

However, other figures in Majmudar suggest that there was a price rise (at least in nominal terms) for most product categories into the EU (as there was in the USA). Table 3.12 shows the considerable variation in the price trends for different products both in the USA and the EU between 1982 and 1992.

Clearly we have too little evidence on prices to make a clear distinction between the real price of a given unit of clothing of a given quality and the extent to which imports into the USA and EU are being upgraded as a result of the MFA.

Similarly we do not know what the trends are in the ratio of the export price received by Sri Lankan exporters to the final retail price of the product. From interviews and trade magazines, it would seem that the export (FOB) price from Hong Kong for garments is generally between one-quarter and one-third of the final retail price in the US market. By contrast, it seems that the export price from Sri Lanka is more likely to be between one-sixth and a quarter, although it is worth emphasising that the ratio varies considerably between products and even exporters. It seems that Sri Lankan producers get a higher proportion of the final retail price for exports to the USA than for exports to the EU. It is not clear why this is so, but it seems to be due to more direct contact with the final retailer in the US market as compared to the EU market.

Table 3.13
Average unit prices into the USA and EU from the top five suppliers (1992)

Imports into the USA	**Average price per piece**	
	$ per unit	**Index (Hong Kong = 100)**
* Cotton coats from...		
- Hong Kong	21.0	100
- China	18.5	88
- Taiwan	17.3	82
- Sri Lanka	11.2	53
- India	7.0	33
Women's Cotton non-knit shirts from...		
- Hong Kong	12.7	100
- China	9.7	76
- Sri Lanka	8.0	69
- India	6.9	60
- Bangladesh	5.2	41
Imports into the EU	**Average price per piece**	
	ECU per unit	**Index (Hong Kong = 100)**
Blouses from...		
- Hong Kong	5.4	100
- Hungary	6.1	113
- Sri Lanka	4.7	87
- India	4.2	78
- Bangladesh	2.9	54

Source: Majmudar 1995, Tables 6 and 13.

In interviews, it was frequently mentioned that Hong Kong exporters receive a higher ratio of export price to final retail price because of their greater familiarity with fabric and more direct contacts with the buyers. Certainly the evidence is that for particular product

categories, Hong Kong exporters generally receive a higher export price (in dollar terms) than exporters from other countries. This can be seen from Table 3.13 below.

However, it is difficult to say with any confidence whether the higher average unit prices received by Hong Kong producers are due to a higher ratio of export to final retail price or to a higher quality product within the particular category (an 'upgrading').

Thus the highly tentative conclusions of this section are:

* that there seems to be a downward trend in the real price of clothing in the principal markets; and

* that there does seem to be evidence of the upgrading of exports within product categories as suppliers within particular countries obtain experience. Thus for the US market, the large and well-established suppliers (such as Hong Kong, China and Taiwan) seem to get higher prices for particular product categories than the newer suppliers (Bangladesh, India, Sri Lanka). In the case of the EU market, the higher prices seem to be received by the suppliers who are geographically closer to the market (such as Turkey, Tunisia, Morocco, Hungary and Poland) as well as those which are well-established (such as Hong Kong).

What do the price trends for Sri Lankan garment exports look like? For 1992-1994 the prices are as set out in Tables 3.14 (major imports into the USA) and Table 3.15 (for exports from Sri Lanka).

Table 3.14
Exports of garments from Sri Lanka to USA (1992-94)
(for the largest quota categories only)

Category	unit	Average export prices ($/unit) (from US import statistics)		year ending 31.10.94	price index (1992=100)
		1992	1993		
334/634 M and B coats	doz	113.8	113.8	126.3	111
335/835 W and G coats	doz	122.3	131.2	139.2	114
336/636/836 Dresses	doz	102.5	108.4	92.9	91
338/339 Cotton shirts (kn)	doz	66.6	65.7	69.6	105
340/640 M and B shirts (not kn)	doz	63.4	71.2	73.8	116
341/641 W and G Shirts (not kn)	doz	64.1	66.2	65.9	103
342/642/842 Skirts	doz	69.8	74.6	71.7	103
347/348/847 Trousers	doz	64.4	65.6	63.7	99
351/651 Nightwear	doz	83.9	83.9	92.2	110
352/652 Underwear	doz	14.3	19.8	22.1	154
635 WG Coats, MMF	doz	109.2	109.4	115.1	105
638/639/838 Shirts/blouses	doz	41.5	43.9	42.3	102
647/648 Trousers - MMF	doz	49.8	55.8	57.9	116
Simple average					**110**

Source: SLAEA, 1995, Appendix 8.

Table 3.14 shows the average prices of the major export categories into the USA from 1992 to end-October 1994. The simple average price in 1994 is about 10 per cent above the 1992 average. This is probably just below the average inflation rate for goods imported from the USA over the same period. Thus the average price has remained more or less static in real terms.Table 3.15 shows the average prices of garments from Sri Lanka for the major categories (covering just under 30 per cent of all garment exports) from 1992 through 1994. The simple average price in 1994 is about 10 per cent above the 1992 average. This is below the depreciation of the rupee against the dollar and thus in foreign currency terms the average price would seem to have fallen.

Table 3.15
Exports and export prices of garments from Sri Lanka 1992-1994
(only for 6-digit trade categories each with export values of more than Rs. 2000 mn. in 1994)

HS code Description	Price indices (1992=100)	
	1993	1994
Knitted garments		
610510 M and B cotton shirts	1`11	105
Non-knitted garments		
620342 M and B cotton suits	115	92
620462 W and G cotton suits	108	105
620520 M and B cotton shirts	109	120
620630 W and G cotton blouses	117	116
620640 W and G syn. blouses	113	109
Sub-totals		
Average price (*)	112	110
Index of Rupee/$ exchange rate	108	116
Size of sample (the above as a percentage of all exports under 61 and 62)	29	28

Sources: External Trade Statistics Sri Lanka 1992, 1993 and 1994 Central Bank of Sri Lanka, Annual Report, 1993 (Table 56).
Note: * denotes average price weighted by base year (1992) export volumes.

4. Costs, technology and competitiveness - generally and in Sri Lanka

4.1 Introduction

In this Chapter we look at factors determining competitiveness in the textile and garment industry and then at the relevant policy issues in Sri Lanka. Section 4.2 highlights those characteristics of the textile and garment industry that are of most relevance to the analysis of policy in Sri Lanka and is not intended to be exhaustive (for more details refer to Jenkins, 1993; Pack, 1987; and UNIDO, 1989).

4.2 The general picture

In general, the textile-garment industry is a chain which goes from the raw materials (both natural and synthetic) to the final goods. The main stages are set out in Figure 4.1 (see also Jenkins, 1993, 35).

In the first intermediate stage of the chain, natural and synthetic fibres are prepared and spun into yarn of different types (cotton, polyester, etc.,) and count (thickness) or into thread for sewing.

At the next stage, yarn is converted into fabric either by weaving or by knitting. These are two distinct processes, usually found in separate firms. In weaving, flat lengths of cloth of different widths are produced through interlacing sets of yarn at right angles on a loom. In knitting, yarn is interlaced by latched or spring needles arranged in a linear or circular array to produce either flat or tubular goods.

Finishing involves cleaning and preparing fabrics, dyeing or printing, and enhancing functional properties of the fabric through chemical treatment. Woven and knitted fabrics are often finished in separate plants because of differences in fabric structure and processing requirements.

The production of final goods can be divided into three parts -- garments, home furnishings (including carpets, rugs, sheets, curtains and towels) and industrial goods. Garments are by far the most important and are, of course, the main focus of this report.

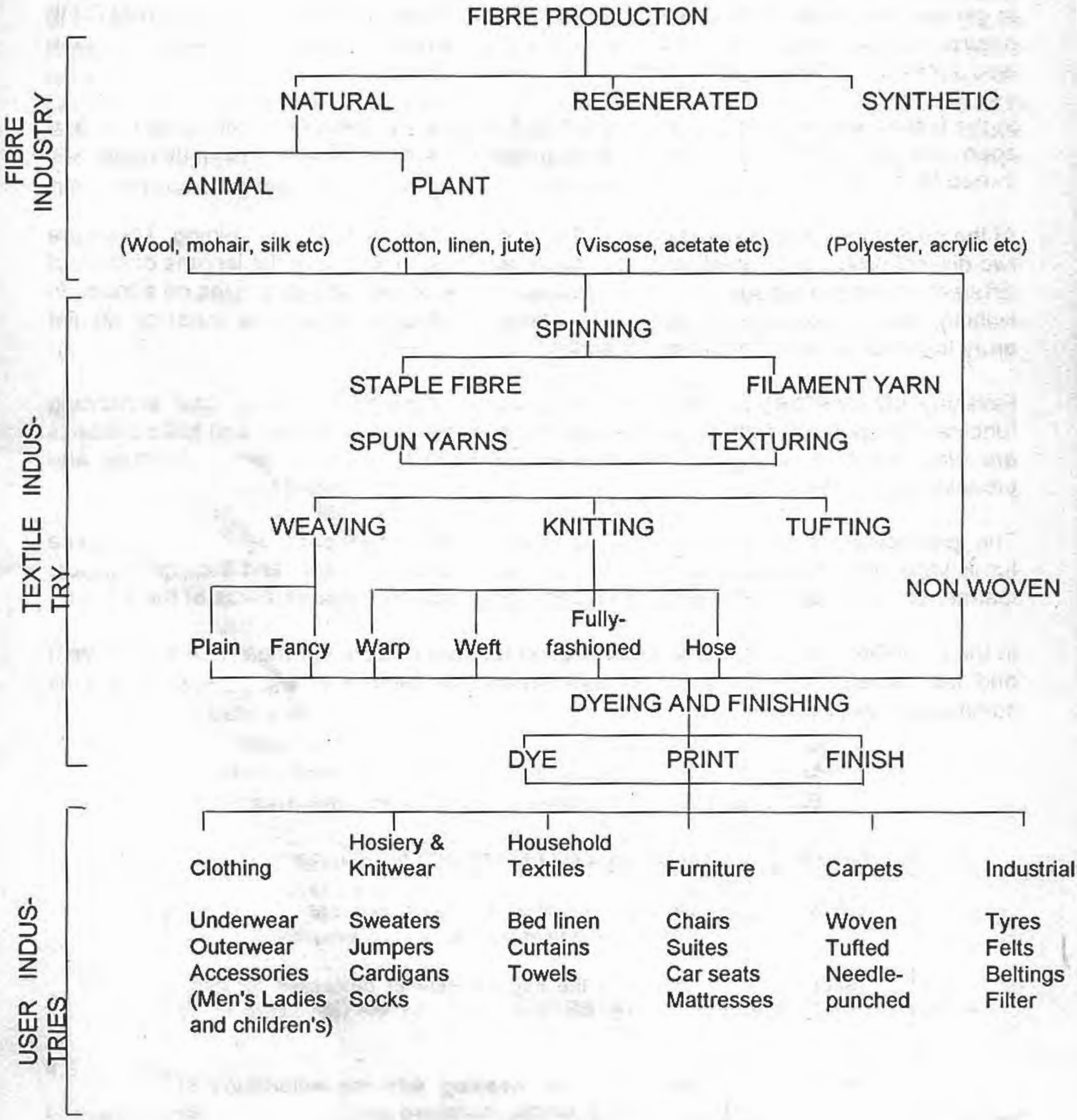
In the post-war period, the pace of innovation has been fastest in the production of yarn and fabrics, although the focus of **innovation** has tended to move downstream as summarised in Table 4.1.

Table 4.1
Major technological changes in textiles and garments

Decade	Technological changes with developments in...
1950s	* **yarn** with the development of man-made fibres (e.g. nylon and later polyester);
1960s	* **yarn** with the improvement of processes for high-speed filament yarn and the development of multi-feed circular knitting;
1970s	* **spinning and weaving** with the automation of opening rooms, increased carding speeds, the introduction of open-end spinning and the development and diffusion of shuttleless looms;
1980s	* **garments** with Computer-Aided Design (CAD) and Computer-Aided Manufacturing (CAM), the introduction of computerised transfer systems such as the Unit Production System (UPS) and programmable sewing machines.

Sources: from Jenkins 1993 (especially page 2 and Annex 3).

Figure 4.1: The Textile and Garment Industry



Source: Kelegama S., 1993, and from CIMA, 1987

It is important to note that developments in technology at one stage have stimulated developments at other stages. Thus, developments in knitting machinery, for example, required fibre developments to serve them in the 1960s and developments in weaving in the 1970s demanded stronger, more uniform fibres in order to run looms at higher speeds. However, although there have been increases in automation across the textile and garment industry, there is no such thing as a fully automated textile and garment process and there is considerable unevenness in technological development. Some technological developments in the industry have led to increased speeds and productivity at the expense of flexibility, as in the case of open-end spinning. In other cases, for example in weaving, some of the new technologies have increased productivity without a significant loss in flexibility (Jenkins, 1993, 3), while in other areas, such as knitting and finishing, both speed and flexibility have been increased.

Accompanying these changes in technology have been changes in organisation. This is particularly the case in **garments** where, with the increased emphasis on quality and changes in design (fashion), there has been a major change in buyer-supplier relationships with the emergence of a 'Quick-Response System' (QRS) (Jenkins, 1993, 3). The emergence of the QRS combined with absenteeism and fast labour turnover in the poorly-paid garment industry has led to organisational changes with some producers moving to a modular manufacturing structure (where operators are multi-skilled) away from the Progressive Bundle Unit (PBU) system. Modular manufacturing (with multi-skilled operators working in separate units to 'assemble' the entire garment) has a number of advantages compared to the PBU system, including faster response times, increased worker motivation reflected in lower labour turnover and absenteeism, better quality, less indirect labour, lower inventories and greater opportunities for change and improvement (see Hunter 1990, 157-158 and US Government 1994b, 32-6). In 1991, it was reported that over one-third of garment producers in the USA had gone over to modular manufacturing (Bobbin 1991). However, in Sri Lanka, it seems that modular manufacturing is not as widespread, probably because a relatively small proportion (probably 20-30 per cent) of output consists of high-fashion garments requiring a particularly quick response.

In **textile production,** the diffusion of new technology is easier to identify and measure than in garment production. For example, in textiles, there is a sharp contrast between shuttle looms and shuttleless looms. Rapier looms in the late-1980s operated at between two and three times the speed of the traditional shuttle looms, while air-jet and water-jet looms were between three and five times as fast as shuttle looms (Jenkins, 1993, 38). In the late-1970s about a quarter of world weaving capacity was on shuttleless looms, but by 1990, more than half of capacity was shuttleless (see Jenkins, 1993, 45). Shuttleless looms represent both a fast and flexible technology (see Pack, 1987, Table 2-4) and are associated with an increased width of fabric. Thus by the 1990s, shuttleless looms were producing cloth which was double the width of that produced by the typical shuttle looms of the mid-1970s (Jenkins, 1993, 38).

By contrast, **in garment production, there is no simple indicator of the diffusion of new technologies.** It is clear that in the developed countries, CAD and computer-controlled cutters have diffused rapidly in the past decade, but automation of sewing is likely to proceed much more slowly. Even the simpler innovations in sewing such as the needle positioner and thread trimmer spread only slowly (Jenkins, 1993, 6). This 'awkwardness' of garment production and the importance of wage rates in the determination of unit labour costs is, of course, the main reason for the rapid

encroachment of LDC garment producers in the Developed Country markets. In 1980, Frobel, Heinrichs and Kreye used the example of garments to emphasise the spread into the South of offshore assembly where fabrics are sent to the countries of the 'South' for cutting and assembling. As a result, the level of firm concentration in the garments industry is very limited and most garment producers are small firms, and even most textile firms are not large (see Elson, 1995, 195).

In **textile production**, labour productivity has increased significantly in the OECD countries over the past 30 years, slightly faster than in manufacturing as a whole, belying its image as a traditional, low-technology industry (see Cline 1987, Tables 4.1 and 5.7). Whereas in weaving, in 1980, about 10 operative hours were required to produce 100 metres of cloth, today less than 30 minutes is all that is required (TTSC 1994, Part B, 54). By contrast, the 'awkwardness' of garments has inhibited the growth of labour productivity, so that inter-firm variations in labour productivity are somewhat less in textiles compared with garments.

These are general points about technology in the textile and garment industries. In the remaining sections of this Chapter we look at the factors determining the competitiveness of fibre, yarn, fabric, ancillary and garment production in Sri Lanka, with the emphasis being on fabrics and garments.

4.3 Costs and competitiveness in Sri Lanka - fibre production

In the production of **synthetic fibre**, economies of scale are important determinants of competitiveness as are access to cheap raw materials, since raw materials account for over half of the manufacturing costs of synthetic fibre in Europe (see UNIDO 1992, Table V.59). A difference of $1 a barrel in the cost of crude oil reduces the prices of fibre by almost a US cent a pound (Jenkins, 1993, 8).

Thus there seems little realistic hope of synthetic fibre production in Sri Lanka being internationally competitive. As far as vegetable fibre production is concerned, a report on backward linkages in the Sri Lankan garment export industry produced in 1988 recommended that a scheme to grow 5000 acres of irrigated cotton in Sri Lanka should receive 'serious consideration', although the recommendation was not backed up by any cost-benefit study (see Hague *et al,* 1988, 31).

4.4 Costs and competitiveness in Sri Lanka - yarn production

In Chapter 2, we saw that the value of yarn production in Sri Lanka was about equal to gross imports. Yarn production in 1992 and 1993 was about 22 mn. kgs. By far the biggest single producer, in 1992, accounting for more than half of all yarn production, was the Korean-owned Kabool Lanka which took over the previously government-owned Thulhiriya Mills. Kabool reportedly incorporates about 30 per cent of the yarn produced into its own fabric, about 10 per cent is sold into the Sri Lankan market as yarn and the remaining 60 per cent is exported (mostly to the EU).

There is some considerable controversy in Sri Lanka about the protection received by yarn producers in Sri Lanka. Spinning and weaving are in the same 4-digit ISIC category,

namely, 3211, so that the effective protection figures produced at this level of aggregation are not very useful. The import duty rates on fibre and yarn imported into Sri Lanka have fluctuated as follows;

	Import duty (per cent) Cotton fibre	(inc. surcharge) on; Cotton yarn
1984 (Nov)	0	5
1987 (Dec)	5	25 (or Rs.25/kg)
1989 (March)	10	25 (or Rs.25/kg)
1991 (Nov)	0	20
1993 (April)	10	25
1993 (Nov)	3	25
1995 (February)	0	10

Sources: CTMA, 14/3/95 interview; MoF 1993, 5 and PTC 1994, 33.

The effective protection can be crudely calculated for the 1995 duty levels by assuming that fibre represents about 50 per cent of the cost of yarn.[2] On this basis the effective rate of protection in 1995 can be estimated to be 20 per cent (based on value added) down from almost 50 per cent in late-1993. Thus the ERP would seem to have been reduced substantially between 1993 and 1995, but the rate based on published tariffs may be misleading. **First,** the actual rate of import duty levied on imported yarn would seem to have been substantially less than the listed rate. Figures produced by Roberston for 1992 estimated that the actual rate of duty collected on yarn was less than 10 per cent compared to the listed rate of 20 per cent. Much of the yarn was being imported into Sri Lanka on a concessionary basis. It appears that BOI producers can sell a proportion (10 per cent) of their yarn in the Sri Lankan market, on which duty is paid only on the material (fibre) component (see PTC 1994, 31). **Secondly,** the yarn producers in Sri Lanka have claimed that the producers in India and Pakistan have had access to cotton fibre which is as much as 35 per cent cheaper than the price which the Sri Lankan producer pays (see MoF 1993, 1 and PTC 1994, 30).

It has been beyond the scope of this study to carry out a direct price comparison of domestic and equivalent imported yarn, but an estimate in 1993 showed that the domestic price of cotton yarn was at least 25 per cent (the listed tariff at the time) above the imported price (see Pehlivan 1993, 13). On this basis the effective protection would have been about 40 per cent, about equal to the maximum ERP guideline recommended in Edwards 1993(b), viii and 38-40. But, as we have seen, the tariff protection on yarn production has since been reduced.

How competitive is Sri Lankan production? This is difficult to say since we have no access to reliable profit figures for yarn production at the present notional effective protection level of about 20 per cent. According to information from Kabool, labour productivity in spinning in Sri Lanka is much lower than in South Korea. In South Korea, each supervisor looks after 8 sets of spinning machines whereas at Kabool in Sri Lanka the figure is 5 and, it was claimed, only 2 at Pugoda and Veyangoda. On the other hand,

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2. The assumption of 50 per cent is probably on the low side and to that extent the effective rate of protection would be understated. Data in Jenkins (1993, 49) give fibre costs ranging from 50 per cent to 64 per cent of yarn output for producers in Brazil, Germany, India, Japan, Korea and USA. The lowest percentage (50 per cent) was for India because (Jenkins argued) India had access to cheap cotton.

wage rates in Sri Lankan spinning are, it seems, considerably less than those in South Korea so that wage costs are probably about the same. In 1991 in Brazil, India and South Korea, wage costs were about 3 to 4 per cent of total yarn costs whereas in Germany and the USA they were 10 per cent and 14 per cent, respectively (Jenkins, 1993, 49).

4.5 Costs and competitiveness in Sri Lanka - fabric production

As stated in Chapter 2, the production of textile fabric in 1993 was about 215 mn. metres and in 1994 about 227 mn. metres (see TTSC 1994, Part A, 25). Of the 1993 production, about 85 per cent was woven fabric produced on powerlooms and the rest was split equally between woven fabric produced on handlooms and knitted fabric (TTSC 1994, Part B, 6).

The 1993 production figure of 215 mn. metres compared with about 140 mn. metres in 1983, representing a growth rate between 1983 and 1993 of about 4.5 per cent p.a. However the production figure in 1986 was about the same as in 1983 (see Hague *et al* 1988, 6) so that the growth rate between 1986 and 1993 was about 6.5 per cent p.a.

Investment in the textile fabric sector has recently (in the 1990s) seen a rapid rise in Sri Lanka with investments by the Hayleys group, Techstream and South Textiles (TTSC 1994, Part B, 6). The further growth potential is considerable. Some production and consumption figures given in the report of the Task Force Textile and Textile - Related Industry (TTSC 1994) are shown in Table 4.2.

Table 4.2
Production, consumption, exports and imports of fabric - Sri Lanka (1994-2000)

(mn. metres of fabric)	1994	2000	1994-2000 growth (per cent p.a.)
Domestic final consumption	220	256	2.5
Indirect exports (in garments)	520	1203	13.5
Direct exports (in fabric form; on projected expansions)	30	100	22.2
Projected requirements	770	1559	12.5
Domestic production (on existing capacities and marginal increases)	227	260	2.4
Projected imports	543	1299	15.6

Source: TTSC 1994, Part A, 25.

Domestic production is therefore roughly equal to the domestic final consumption and that the existing capacity is sufficient to meet the anticipated domestic consumption.

Clearly, there is **considerable scope for expansion** even if only a proportion of the indirect exports are to be met from domestic production. However, it is likely that the growth in garment exports assumed in the above Table is too optimistic. Nevertheless,

even if this rate of growth is as 'little' as, say, 5 per cent p.a. rather than the 13.5 per cent assumed in the Table, the capacity for further expansion in the textile industry is considerable. A growth rate of 5 per cent p.a. would mean that indirect exports in the year 2000 would be 700 mn. metres. Together with the above domestic final consumption and projected direct fabric exports, this would mean a projected fabric requirement of about 1050 mn. metres. To meet even just 40 per cent of this would mean an output of about 420 mn. metres, or an additional capacity of about 200 mn. metres even without any scrapping of existing capacity. This would represent a growth rate in fabric production of almost 11 per cent p.a.

A considerable investment is required to produce an additional output of 200 mn. metres. It would be similar to the investment target set out in the TTSC report (TTSC 1994). For fabrics, this investment target over the 1995-2000 period was $200 mn.[3] or about Rs. 10 bn. at the end-1993 rupee-dollar exchange rate. This was expected to meet 20 per cent of the projected requirement of 1300 mn. metres or an additional 260 mn. metres (see TTSC 1994, Part A, 15). Thus, if we assume (conservatively) a projected fabric requirement (from all sources, namely, domestic final consumption, fabric exports and indirect exports through garments) of 1050 mn. metres, and if we further assume that capacity is established to meet 40 per cent of this,[4] then this probably requires an investment of about Rs. 10 bn. (at 1996 prices) equivalent to about 10 per cent of the gross domestic capital formation in Sri Lanka in 1993 - not an impossible target.

Sri Lanka should be able to meet such a target. The domestic and indirect export market is large enough to achieve economies of scale alongside plant specialisation. The minimum efficient output for a cotton weaving manufacturing plant (according to Jenkins 1993,26) is 2,500 tons, equivalent to about 19 mn. metres, assuming 135 grams per metre for cotton or cotton-like fibre (see Hague *et al*, 1988, 6). Thus the minimum efficient scale is equivalent to just under 10 per cent of existing domestic production in Sri Lanka. However, in addition, it is desirable for each domestic plant to achieve a high level of product specialisation, since the detailed work on textile productivity carried out by Howard Pack suggests that the most important factor in explaining differences in total factor (not just labour) productivity between fabric manufacturing plants was product specialisation or the lack of it (see Pack 1987, 52,53 and 171).

In Sri Lanka the demand for particular types of fabric are likely to permit the achievement of both economies of scale and product specialisation. In 1992 well over 50 mn. square metres of cotton sheeting were imported as well as a little less than 50 mn. square metres of polyester/cotton shirting or poplin and over 40 mn. square metres of single jersey knitted fabric (see TTSC 1994, Part B, 8 - see also pages 9 and 11, SLAEA 1995, 28-30 and Hague *et al* 1988, 9,10).

What is certain is that, if there is to be sufficient domestic capacity to meet a significant part of the 'indirect export demand', then there has to be new investment to produce fabric of sufficient width. At present only a little over a quarter of the 13,000 powerlooms in Sri Lanka can produce fabric of a sufficient width (45 inches or more) to meet the demands of the garment exporting industry (see TTSC 1994, Part B, 16).

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3. This represents an investment of about $0.8 per metre of production at 1993 prices. This compares with the $0.6 per metre given for 1986/87 prices by Hague et al 1988, 13,15, implying an inflation of about a third over 7 years or about 5 per cent p.a. which seems likely.

4. The Hague et al study argued that Sri Lanka could and should produce over half of the 200 mn metres of fabric imported in 1986.

What incentives can or should be given for investment in Sri Lanka for fabric production? We consider these under two headings, namely, tariff protection and other (non-protection) incentives:

(i) **tariff protection**:
It is as difficult to estimate the level of effective protection for fabric production as it was for yarn production. First we assume that the major raw material input (namely yarn) represents about 50 per cent of the total cost of the fabric. Estimates that we received ranged from 60 per cent from Kabool for grey fabric, to 50-55 per cent from other interviews. The percentage given in Jenkins was much lower, ranging from 30 per cent for India to 44 per cent for South Korea (see Jenkins 1993, 50). The percentage of yarn to output given for the years 1985 and 1988 by the PTC reports for industry 3211 (spinning, weaving and finishing) was 40 per cent.

The history of tariff protection for fabric and the major raw material input (yarn) is as follows:

	Import duty (%) Cotton yarn	(inc. surcharge) on Cotton fabric
1984 (Nov)	5	45
1987 (Dec)	25 (or Rs.25/kg)	60 (or Rs. 15/sq.m)
1991 (Nov)	20	35 (or Rs. 20/sq.m)
1993 (April)	25	100
1993 (Nov)	25	50 (+ Rs. 10/sq.m)
1995 (February)	10	35

Sources: CTMA, 14/3/95 interview.

Working on the basis of the 1995 tariff figures and a yarn to fabric percentage of 50 per cent, the **effective protection on fabric produced for sale in the domestic market would be 60 per cent.** This is an extremely attractive rate of protection to potential producers but it is unlikely to be an accurate figure. It is acknowledged that conisderable leakage and smuggling of fabric take places into the domestic market. In *Textile* Today of October 1993, the CTMA claimed that almost a third of the fabric domestically consumed was illegally imported or leaked from duty-free sources. The volume involved was alleged to be 70 mn. metres (see MoF 1993, 2). There is leakage of garments which are sold in the domestic market and on which less than the listed duty is paid, as well as leakage of fabrics. In terms of fabrics, Kabool has a special concession in that they can sell 10 per cent of their fabric production in the domestic market on a duty-free basis (CTMA interview 14 March 1995). This was 20 per cent in their first year of operation (see *Clothing,* March 1992, 11, *Daily News,* November 1992 -- see also MoF 1993, 4). Given this considerable leakage, it is hardly surprising to find that the actual import duty paid on the fabric imported on a non-bonded basis into the country averaged less than 10 per cent in 1992 (see Bertrand and Robertson, 1992).[5]

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5. Given the problems of smuggling and under-valuation of fabric imports, it is hardly surprising that there have been calls for a pre-shipment verification scheme (PSVS) to be introduced on Sri Lankan imports. Under such a scheme (recently introduced in Indonesia) the imports into Sri Lanka would be verified

The **few direct price comparisons** that are available however give conflicting signals as to the level of protection. The figures given by Pehlivan for 1993 are shown in Table 4.5.

Table 4.5
Comparisons of fabric prices (March 1993)
(average prices; US cents per sq. metre)

	Domestic	International	% difference
Grey Fabric	53	50	6
Suiting	288	260	11
Twill	155	145	7
Poly-cotton shirting	115	90	28
Dress fabric	92	69	33
Nylon fabric	139	135	3
Simple average			13

Source: Pehlivan, 1993, 11.

If we take the nominal tariff on the fabric to be the same as the average price differential of 13 per cent, then the effective protection on fabric production would be about 16 per cent.

This still provides an attractive rate of protection since this 16 per cent is on value added and would be very much higher relative to gross profits. However, even this corrected rate may be misleading since, as we have seen, the major potential for the expansion of fabric production is for the indirect export market, that is, for providing the garment exporters with supplies of fabric. In interviews we have been assured that garment exporters would be prepared to pay a premium of 10 per cent or even 15 per cent for local fabric equal in quality to imported fabric. If this is the case, then the effective protection would be between 10 per cent and 20 per cent (calculated on value added).

Thus there is some production incentive, partly from the protection on any preferential sales of fabric into the domestic market (see MoF 1993, 8) and partly from the price premium that garment exporters are prepared to pay for local supplies. In addition, there are other incentives which the government provides for investment in fabric production.

(ii) **other, non-tariff, protection:**
In December 1990, the government announced a scheme of (non-tariff) support for the textile industry in the form of duty-free and turnover-tax-free import of machinery and spare parts and cheap loans although the CTMA claimed, it was not implemented until February 1994. In 1993, a Committee under the Ministry of Finance had recommended that export-oriented fabric producers be given tax concessions as well as various other concessions (see MoF, 1993, 6 and 7). For

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and sealed at the point of export for a commission of 0.5 per cent payable to the company carrying out the PSVS (see CTMA interview, March 14 1995 and MoF 1993, 3,4).

these concessions to be effective, it is important that they be maintained for some time at the same level and that potential investors have some assurance that the incentive structure will be stable. Investment in fabric production is, relative to investment in garment production, capital-intensive and to that extent more risky (see Pack, 1987, 172).

Thus it would seem that the potential for the expansion of fabric production in Sri Lanka to supply the garment exporters is considerable. To what extent can Sri Lanka be competitive?

We have seen that the major input (accounting for about 50 per cent of the total cost of fabric) is yarn, and, as discussed in the previous section, there is no reason why Sri Lanka should not be reasonably competitive in yarn supplies.

The other cost components of fabric are as follows, as a percentage of total costs:

Dyes,chemicals and other materials	5-9
Wages	4-7
Fuel/water	5-6
Capital depreciation and interest and overheads	20-46
Total (average)	50

The cost structure varies enormously between different countries. The above ranges are for Kabool in Sri Lanka. Other LDC data (Brazil, India and Korea) used below are taken from Jenkins (1993, 50).

The size of the **capital depreciation, interest and overheads** item indicates the importance of working to a high capacity utilisation. It should be noted that in Germany, Japan and USA capital depreciation and interest make up a much smaller share (average of 31 per cent) of the total costs than they do in Brazil, India and South Korea (average of 42 per cent). Conversely, wages make up a higher proportion (21 per cent) in Germany, Japan and the USA than they do (5 per cent) in Brazil, India and Korea. In terms of competition between the LDC producers and those in the DCs, these are clearly the countervailing factors.

As far as **wage costs** are concerned, it is clear that hourly wage rates in the developed countries (Germany, Japan, UK and USA) were over 4 times as high as those in some middle-income LDCs (South Korea, Hong Kong, Turkey, and Mexico) in 1991, and more than 20 times as high as those in lower-income LDCs such as China, the Philippines and Sri Lanka (Jenkins, 1993, 27, 28). In 1995, the wage rates in fabric production in the USA, UK and Germany were averaging about $16 per hour compared to an average of only about $2 in Brazil, Hungary, Mexico and Poland (*Financial Times*, 21 September 1995), These ratios of 8 to 1 in wage rates more than offset the ratios of 1 to 2 or 1 to 3 in labour productivity, thus making the wage costs in the middle income LDCs about a quarter of those in the developed world. As the TTSC pointed out, Sri Lanka is well placed in terms of labour skills and wage rates (TTSC 1994, Part A, 2 and Part B, 36).

Sri Lanka is not as well-placed when it comes to **electricity** costs. While comparable to Bangladesh and Hong Kong, Sri Lanka's electricity is almost twice as expensive as that in South Korea (TTSC 1994, Part A, 4 and Part B, 35, 37).

With regard to **finance** charges, Sri Lankan investors are badly situated with real interest rates very high relative to those in the developed countries (Pehlivan 1993, 15).

On balance, Sri Lanka is an attractive location for investment in fabric production. **One possible barrier** is inherent in the sub-contracting structure of the garment industry. Garments are usually made to buyers' specifications and fabric requirements. When fabric and/or accessories are supplied by the buyer, the manufacturer will quote the price based on;

(i) a CMP (Cut, Make and Pac) contract -- here the buyer provides materials on a No Foreign Exchange (NFE) basis, or directs (under a conditional FOB contract) the sources of the fabric and accessories;
(ii) a CMT (Cut, Mark and Trim) basis where the buyer provides the fabric and the accessories.

CMP is more common, and Kelegama estimates that about 20-40 per cent of garment exports are on a NFE basis where the buyer provides the inputs (see Kelegama, 1993, 30 and Kelegama and Unamboowe, 1994, 24). Such contracts are reported to be on the increase (they reduce the foreign exchange commitment for the garment producers) as are conditional FOB contracts (about 10 per cent of the total -- see Kelegama, 1993, 32). This means that the garment producers are not free to choose their source of supply for fabrics and accessories. In fact, it seems that the buyers are very willing to use a local supplier (see Kelegama, 1993, 31) though this may not be as big a barrier to backward integration as it appears at first sight.

It is not likely to be as large as the barriers posed by:

(i) increasing competition in the world textile industry as a result of excess capacity in many of the established supplying countries and by the growth of capacity in new producing countries; and
(ii) the growth of outward processing arrangements in both the USA and the EU under which garment producers get preferential access to the US and EU markets but only on the condition that fabrics from the USA and the EU are used. We look at this in more detail in the next Chapter.

4.6 Costs and competitiveness in Sri Lanka - accessory production

A detailed report on backward linkages from the garment industry was prepared out in 1993 by Kelegama (Kelegama, 1993). Although that report did not cover dyes and chemicals nor textile machinery, it did cover the production of accessories in some detail. The accessories account for about 7-10 per cent of the total production costs of a garment.
The accessories that are made in Sri Lanka are limited in variety and only suffice to meet the demand of a few firms. Even these, in most cases, are assembled with imported components. About half of the different types of accessories are imported (Kelegama

1993, 5) but these represent between 70 per cent and 90 per cent by value (Kelegama 1993, 9 and 40). In 1993 the situation was as follows (see Kelegama 1993, 19-23; for details of imports in 1991, see page 62 of Kelegama 1993):

* Labels - mostly imported but there is a lot of potential for development;
* Buttons - mostly (95 per cent) imported; there is a shortage of plants for dyeing buttons;
* Zip fasteners - there are 3 local manufacturers but their products are low in quality compared to YKK;
* Padding - moulded padding is all imported, whereas 15 per cent of other padding is produced locally. Freight charges on padding are high so this should be an attractive local investment;
* Lining - more than 50 per cent imported;
* Cartons and other packaging material- between 60 and 95 per cent produced locally (see Kelegama 1993, 22 and 36);
* Polybags - about half imported (again there is considerable potential);
* Hangers - about 50 per cent imported;
* Elastic bands - about half imported.

Barriers to investment in the production of accessories were discussed by Kelegama (1993), were the following;

* the slow receipt of payments for orders, though this seems to have been resolved by the introduction of the Temporary Importation for Export Promotion Scheme (TIEPs) which was introduced in September 1992 (see Kelegama, 1993, 26 and 42). Kelegama reports that this has been a most influential package for indirect exporters in reducing the duty paid up-front and in reducing the financing required (see Kelegama, 1993, 41);
* uncertainty and risk in investment (Kelegama, 1993, 27,28). Kelegama argues that there has been little institutional coordination to reduce the risk of investment, and he points out that the sub-contracting exchange (SCX) set up in 1980 has not been effective.

Other policies which can be used to encourage the use of local inputs are discussed in Kelegama, 1993 on pages 56 and 57. Briefly they are the following:

* quota rewards for higher local resource utilisation. But this requires an overhauling of quotas since, with the expansion of the garment industry under the '200 GFP', the quota utilisation is full;
* more local sales allowed for garment producers, the more local resources are used; and
* preference be given to local resource utilisation when deciding on annual export awards for garment exporters.

4.7 Costs and competitiveness in Sri Lanka - garment production

As we saw in Chapter 2, this is the largest part of the Sri Lankan textile and garment industries. It has expanded rapidly over the past 10 years selling overwhelmingly to the export market.

The industry is one of small production units (see Chapter 2) with considerable sub-contracting. In garment production, the economies of scale are much less than in fabric production although it is safe to say that, in Sri Lanka, many of the factories are below what is considered in Jenkins (1993) to be the minimum efficient size. For shirt production this is given as 175 employees and a gross output of 550,000 pieces or about 46,000 dozen (see Jenkins 1993, 26). In addition to technical economies of scale, there are almost certainly financial economies of scale in marketing (both in obtaining discounts on large fabric orders and in obtaining a better price for sales). Once the minimum efficient size is reached, the organisation and layout of production is important in determining labour productivity.

In the garment industry, computer applications have been slow to spread. In the early-1980s it was estimated that only about a fifth of the **largest** clothing firms in the USA and EU were using computer aided design (CAD). By the 1990s, the use of CAD and of computer-aided cutting had spread to the majority of the largest firms and to many of the medium-sized firms. In Sri Lanka, computer applications seem to be limited in the garment industry and even in Hong Kong, only a little over a fifth of the firms were using computer applications to any degree (Redding, 1994, 77).

It is difficult to derive reliable, general figures for the cost structure in garment production. If we assume a profit margin on sales of about 20 per cent, then the total costs are 80 per cent of gross output. Our picture of the cost structure is set out in Table 4.6.

Table 4.6
Cost structures in garment production - USA and Sri Lanka

	USA % of costs	Sri Lanka % of gross output	
Fabric	40-50	65-75	55-63
Accessories	6-12	7-10	5-8
Elec./water	1-2	4-5	3-4
Labour	34-50	14-18	11-14
Depreciation and other	4-5	1-3	1-3
Total costs	100	100	80
Profit margin			20
Gross output			100

Sources: Jenkins 1993, 51 for USA; for Sri Lanka, PTC data for apparel industry (ISIC 3220) and interviews.

As can be seen from Table 4.6, garment production is an industry in which labour costs are highly significant. In addition, because it is an 'awkward' industry for improving labour productivity, wage rate differentials matter even more than they do in fabric production, which of course explains why there is so much sub-contracting of garment assembly to LDCs.

The wage rates in the garment industry in Sri Lanka in 1991 were similar to those in the poorest of the Less Developed Countries (in the range of US 20-50 cents per hour) compared to a range of $7-$15 per hour in the most developed countries, and about $2-$4 per hour in the middle-income countries (see Jenkins, 1993, 53,54). We have not been able to derive any useful figures on labour productivity either in Sri Lanka or elsewhere, but one thing is clear from our interviews, namely, that labour productivity does vary enormously between factories within Sri Lanka (by a factor of 2 or more), so that **it is possible to overstate the significance of wage rates in competitiveness.**

It can be seen from Table 4.6, that electricity costs are much less important in the garment industry than they are in fabric production, so that Sri Lanka's high costs (compared to some competitors) of electricity are not as significant a factor.

As argued in Chapter 3, the rate of profit in the garment industry can be very high indeed if a company has access to 'hot' quotas and if the company is producing at full capacity. If this is the case then the profit margin on sales will be as much as 25 per cent. And if the company is also making full use of its production capacity, the turnover of capital by sales will be over 4 times, thus giving an annual rate of profit on capital of between 50 per cent and 100 per cent p.a. Of course, we need to emphasise that this is not the rate of profit on capital that all companies in the industry are earning. The average sales per employee in the garment industry is probably about Rs. 220,000 (sales of about Rs. 60 bn. divided by 250,000 employees).[6] The average investment per employee is probably between Rs. 100,000 and Rs. 150,000 so that the average sales/capital turnover ratio is around two. Thus the median rate of profit is probably around 30 per cent p.a. with the weighted average being much higher. Clearly, for some companies with access to substantial 'hot' quotas, garment production can be said to have been a licence to print money.

Even less than in fabric production, tariff protection is unimportant in the Sri Lankan garment industry. Non-BOI garment producers are legally allowed to sell 2 per cent of their fabric production in the local market, while BOI garment producers are allowed to sell 10 per cent of their fabric imports on the local market, only paying 10 per cent duty on the fabric plus turnover tax and defence levy on the output value (see SLAEA 1995, 25 and Appendix 9). However, these are small 'perks' compared to access to quotas and particularly, hot quotas.

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6 This compares with sales per employee in the US garment industry in 1993 of over Rs 3 million at the end-1993 official exchange rate. Gross output in 1993 was $68 bn or Rs 3,400 bn at an exchange rate of Rs 50 to the $. The total number of employees in the US garment industry in 1993 was 939,000 (US Government 1994b, 32-1). Thus the average sales per employee at 1993 prices and exchange rates were Rs 3.6 million.

4.8 Devaluation and competitiveness

One factor which would seem to be important in determining the competitiveness of the textile and garment sector is the exchange rate of the Sri Lankan rupee to other currencies.

In this respect, it is important to clear away a **misunderstanding**. In doing the research for this study, it was often stated that a real devaluation of the Sri Lankan rupee would not be of much assistance to Sri Lankan textile producers and even less to garment exporters. The argument was frequently put forward that a devaluation would push up garment costs to almost as much as the value of sales because of the high ratio of imported costs to gross output. In fact, of course, the rise in value added is proportionally the same in both cases but, as Table 4.7 shows, if the capital costs are assumed to be 'sunk' (treated on a 'historic cost' basis), the real devaluation will raise the rate of profit of the low value-added producer to a greater extent than it will for the high value-added producer.

In Table 4.7, a real devaluation of 10 per cent increases the rate of profit for the low value-added exporter by more (from 20 per cent to 28 per cent) than it increases the rate of profit (from 20 per cent to 25 per cent) of the high value-added exporter. So it could be said it is **because of**, rather than **in spite of,** the high imported cost ratio that the exchange rate matters for garment exporters.

Table 4.7
A real devaluation and its effects on low value-added and high value-added industries

	Before devaluation		After a real devaluation of 10%	
	Low value-added activity	High value-added activity	Low value-added activity	High value-added activity
Gross output	100	100	110	110
Material inputs				
- imported	60	30	66	33
- local non-traded (inc. electricity)	10	10	10	10
Value added	30	60	34	67
Labour	15	15	15	15
Depreciation	5	15	5	15
Profit and interest	10	30	14	37
Capital	50	150	50	150
Rate of profit (%)	20	20	28	25

The evidence on whether the Sri Lankan rupee is overvalued or undervalued is conflicting and the issue is highly controversial. In 1978 there was a sharp real devaluation of the rupee against its trading partners (the index went from 100 in 1977 to 184 in 1978, the rise signifying a sharp **devaluation**) and there has been some devaluation since then, with the index rising from 178 in 1978 to 203 in 1993 (see

Edwards 1995, 7). **However, relative to its major competitors (Bangladesh, Indonesia, Malaysia, Pakistan and Thailand), the Sri Lankan rupee has appreciated in real terms since 1978 with the real exchange rate index (1977 =100) against these five countries falling from 169 in 1978 to 112 in 1993.**

These are the trends. These figures tell us how the exchange rate is moving, but they tell us little about which base figure is 'correct'. So we need to ask whether the exchange rate is in equilibrium or not. Is the Sri Lankan rupee overvalued? Some economists argue 'no'. Examples are Walton (1984) and Cuthbertson *et al,* (1992). Their argument is that Sri Lanka has no overall Balance of Payments deficit and yet exchange controls have been substantially liberalised and there are no obviously temporary inflows of foreign capital. Since 1992, these conditions still hold. Exchange controls have been completely liberalised, for current account transactions and there have been no large, unusual and obviously temporary inflows of foreign capital. There is no black-market for the Sri Lankan rupee and official reserves at the end of 1993 were equivalent to 6.5 months of imports compared to 3.7 at the end of 1990 (CBoSL, 1993, 15).

Along these lines then the argument is that the rupee is not overvalued. A contrary argument is that it is overvalued and substantially so for two reasons:

(i) first because Sri Lanka aims to become independent of foreign aid inflows and yet it has been running a deficit on the current account -- of over 6 per cent of GDP between 1991 and 1993;[7] and
(ii) secondly because the exchange rate needs to be set at a level which makes exports (particularly high value-added exports) competitive.

Of course, in so far as the exports of garments from Sri Lanka have a somewhat captive market and earn a very high rate of profit, then a devaluation will simply add to these profits and may do little to change things. On the other hand, devaluation is likely to make exports of non-quota garments more competitive and the production of yarn and fabric, whether for direct or indirect export, more competitive.

5. The 'phasing-out' of MFA quotas, global demand for textiles and garments and prospects for Sri Lankan production

5.1 The liberalisation - what does it mean?

The Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations is 550 pages long and contains 40 separate Agreements, Understandings and Texts as well as several Decisions and Declarations. These spell out the results of

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7. There is conflicting evidence on the level of prices (for all commodities not just textiles and garments) in Sri Lanka ralative to other countries. Perkins has argued that, in 1975, prices in Sri Lanka were very much higher than international prices (see Perkins in Perkins and Roemer (ed) 1991,22) and yet on the basis of data for 1976-85 in an article by Dollar (1992, 541), Sri Lanka seems to be the most competitive nation in the world in that her price level is well below that of other countries once an allowance is made for differences in per capita incomes (this adjustment has to be made because non-traded goods tend to be relatively cheaper in lower income countries). Even allowing for the subsntial devaluation in Sri Lanka in 1977/78, it is not easy to reconcile these figures.

the negotiations since the Round was launched in Punta del Este in Uruguay in September 1986. The Final Act was signed on 15th April 1994 by 125 countries that participated in the Ministerial Trade Negotiations Committee meeting in Marrakesh, Morocco. 121 countries signed the agreement on the same day. The remaining four (including the USA and Japan) were expected to sign before the coming into force of the Agreement on 1st July 1995 (PTC 1994, 89).

The Agrèement on Textiles and Clothing (ATC) was summarised in a press release of December 14 1993 from the GATT which is reproduced in Appendix 5.

What does the liberalisation amount to?

First, it is clear that the quotas will be progressively relaxed over the period up to 2005 but only very gradually. Under the Uruguay Round, textiles and garments are to be taken out of the quota arrangements in four phases as follows:

(i) on 1st January 1995, 16 per cent of the volume of imported textiles and garments are to be integrated -- that is, taken out of the scope of the quota arrangements;
(ii) on 1st January 1998, a further 17 per cent of the volume of imported textiles and garments are to be integrated;
(iii) on 1st January 2002, a further 18 per cent of the volume of imported textiles and garments are to be integrated; and finally
(iv) at the end of the transitional period (31st December 2004), the remaining 49 per cent of products are to be liberalised (PTC 1994, 95 - see also Majmudar 1995, 5,7, SLAEA 1994, pp. 5-11).

The product groups for integration are fibre and yarn, fabrics, textile products and garments. All MFA restraints will be carried over to the new Agreement and maintained until such time as the restrictions are removed. The textile and clothing products listed in the Annex to the Agreement include many products which are not currently restricted under the MFA by the importing countries (PTC 1994, 99).

An assessment by the International Textile and Clothing Bureau suggests that, with over one-third of US and EU textile and clothing imports now unrestricted, the USA and the EU will be able to delay any real liberalisation until at least the third stage of the phase, that is, until 2002 (see *Textile Asia*, December 1994, 8; see also Majmudar, 1995, 1). This assessment is backed up by the fact that, for the first stage, the EU and the USA have chosen products where the restriction is smallest and where imports into the USA and the EU are least competitive. Furthermore, as far as the US quotas are concerned, Thurairajah 1995 (page 11) stated that the products to be relaxed by 2002 constitute only about 4 per cent of all the restricted products currently exported by Sri Lanka to the USA. The remaining 96 per cent of the restricted products are expected to be under restraint until the end of 2004. Thus it is reasonable to assume that the quota restrictions will remain effectively in force until 2005.

As a result, we consider here the liberalisation in two phases; first, the period up to 2005 with the growth in quotas, and second, the longer run from 2005 with the phasing-out of quotas.

5.2 The medium term (to 2005) and the growth of quotas

It is important to note that under the Uruguay Round arrangements, quotas are to be increased at a faster pace than under the BTAs. The increases are as follows:

(i) in the first stage, up to 1998, the annual rate of quota growth will be increased by 16 per cent;
(ii) in the second stage, from 1998 to 2002, the annual rate of growth will be increased by 25 per cent; and
(iii) in the third stage, from 2002 to 2005, the annual rate of growth will be increased by 27 per cent (see Majmudar 1995, 5,7).

Here we discuss the growth in quotas for the two main markets -- the USA and the EU.

USA

Sri Lanka's garment quotas into the USA grew in 1994 by 6 per cent, so that, in the first phase under the ATC, that is from 1st January 1995, the quota volumes will increase by 6 per cent plus 16 per cent of 6 per cent = 6.96 per cent. In the second stage, that is from January 1998, the quota volumes will increase by 6.96 per cent plus 25 per cent of 6.96 per cent = 8.7 per cent. In the third phase (from January 2002) the percentage increase in the quota volumes (of those categories still left in the quota system) will be 8.7 per cent plus 27 per cent of 8.7 per cent = 11 per cent. Thus the quota growth will be:

from January 1st 1995; 6.96% per annum
from January 1st 1998; 8.7% per annum
from January 1st 2002; 11% per annum.

However, it should be noted that the growth rate of 6.96 per cent p.a. to 1998 makes no allowance for the over-utilisation of quotas in recent years. It is likely, once allowance has been made for these special carried-forward volumes, that the actual maximum rate of growth in quota categories to 1998 will be not more than 5 per cent p.a.

Not all countries' quotas are growing at the same rate as those of Sri Lanka. There are special provisions for certain categories of countries -- for example, those which have not been MFA members since 1986, small suppliers and the Least Developed Countries.

The definition of a **small supplier** is one whose restricted exports represent not more than 1.2 per cent of the total volume of the restrictions applied by an importing member as of December 31, 1991. For the US market, Sri Lanka is not a small supplier. Even in 1983, her share of the US garment market was 1.3 per cent, but by 1993 her share of the US market was 2.5 per cent (Majmudar, 1995, 10a) and, for a large number of garment types, she ranks among the USA's ten biggest suppliers (see SLAEA, 1995, 10). The significance of being a small supplier is that small suppliers can advance one stage on the above growth ladder (Thurairajah, 1994, 5).

EU

By contrast, for the EU garment market, Sri Lanka **is a small supplier** and as such receives a faster than otherwise quota growth. In 1991, Sri Lanka had a share (by volume) of less than 1 per cent of the EU market (Thurairajah, 1993, 74). On the other

hand, Sri Lanka is not defined as a **Least Developed Country** unlike one of her major competitors, viz. Bangladesh. The significance of this is that, under the BTA of the MFA, Bangladesh's quota was increasing even faster than Sri Lanka's. Bangladesh's quota was increasing by 10 per cent rather than the 7 per cent p.a. applicable to Sri Lanka, and in the first stage of the post-MFA arrangements, this quota growth rate will increase by 25 per cent.

But the news is not all bad for Sri Lanka. For the EU market, her quota growth (at least for categories 6, 7, and 8) will be much faster than for most other exporters to the EU (see Majmudar, 1995, Annexes). For the 06, 07 and 08 categories, Sri Lanka's quota growth rate will be considerably faster than the growth rates of some of the largest suppliers to the EU (most notably China, Hong Kong, India and South Korea (see again Majmudar, 1995, Annexes). For the largest ('dominant') suppliers the quota growth rates are only about 1 per cent for most of the restricted products (Majmudar, 1995, 7).

Thus, according to figures in Majmudar's report, Sri Lanka's quotas to the EU (for categories 06, 07 and 08) are scheduled to grow at between two and three times the average growth rate (as shown in Table 5.1).

Table 5.1
Quotas to EU for Sri Lanka and all suppliers (1994- 2005)

	Quotas for Sri Lanka			All quota suppliers	
	1994	2005	1994-2005 ratio	quantity	quantity
06 Trousers	6.3	23.9	3.79	13	5
07 Blouses	10.8	36.7	3.40	12	5
08 Shirts	7.5	30.0	4.41	14	4
21 Jackets	6.8	na	na	na	na

Source: Majmudar, 1995, Table 15.

5.3 The tariff arrangements in the USA and the EU

The discussion in Section 5.2 focussed on the growth rates for quotas up to the year 2005. However, in addition to quotas, there are tariff restrictions on imports of textiles and clothing into the USA and the EU. Some studies of trade liberalisation in textiles and garments suggest that the welfare gains to LDCs from the abolition of both quotas and tariffs would be at least double the gains from the abolition of quotas alone (see Majmudar 1995, 17).[8]

The removal of tariffs on textile and garment is highly unlikely and although, under the Uruguay Round, some relaxation of tariffs is scheduled, despite the quota liberalisation, the textile and garment sector will remain one of the most highly protected sectors as a result of the tariffs. Thus while the average tariff rate for the goods sector will be cut by a third over the period to 1999 to 4 per cent, in comparison to 6 per cent for pre-Uruguay

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8. Note that arising from liberalisation, there are gains to consumers in the Developed Countries, losses to producers in the Developed Countries and gains to exporters in the Less Developed Countries. The latter will gain as a whole through increases in the volume of exports, although some existing exporters will lose as a result of the loss in their quota premia.

(TPMP 1994, 7), for textiles and clothing the post-Uruguay tariff rate is scheduled to be about 12 per cent compared to the pre-Uruguay rate of 16 per cent (see Majmudar, 1995, 7).

There are maximum tariff rates specified for all products, except for textiles and clothing which are exceptions. For these, there is a 12-year phasing-in period for the reductions and the maximum tariff rates at the end of the 12-year period are 45 per cent for garments and 25 per cent for textiles (see TPMP 1994, 7). The pre-Uruguay tariff rate for clothing into the USA given in Safadi and Yeats (1993, 11) averaged about 20 per cent.

Furthermore, it should be noted that the ATC contains a specific transitional safeguard mechanism which could be applied to products not integrated into the GATT at the three stages, although handloom fabrics are exempted from it (PTC 1994, 96). As the PTC stated in 1994:

> "A recent enquiry into dumping by the EC, based on representations by the European Textile Group against China, India, Indonesia, Pakistan, Thailand on imports of textiles into the EC market.....is perhaps a reminder that the developed countries will continue to forestall any large-scale imports of textiles and clothing into their countries from the developing countries" (PTC 1994, 100).

In addition to these points on tariffs, it should be noted that the protectionist position for textiles and clothing is complicated by a number of special arrangements.

First, there are the arrangements under the **Generalised System of Preferences** (GSP). Under the GSP, Sri Lanka and a number of other LDCs were accorded preferential tariff treatment by the European Community in 1971. However, as from January 1st 1995, Sri Lanka has lost her GSP status for textiles. Sri Lanka is no longer to be treated as a Least Developed Country, unlike some of her major competitors and potential competitors such as Bangladesh and Nepal (*Island* Sunday March 26 1995, 20; *Sunday Observer*, March 12 1995, 42) although it seems that Sri Lanka has not been able to make much use of the tariff concessions for textiles (Thurairajah, 1993b, 58).

Second, there are preferential tariff rates into both the USA and the EU on garments where the cloth is provided by suppliers based in the USA and the EU. These **value-added** tariffs apply in the USA to imports under the Harmonised Code 9802 (formerly under 807). The tariffs into the USA are only payable on the value-added (and there are special quotas) provided that the garments are made from fabrics produced in the USA (Mandelbaum, 1992, 20). Under this provision, exports from Mexico and the Caribbean Basin have grown dramatically (Mandelbaum, 1992, 36). In 1991, Caribbean Basin suppliers contributed over 10 per cent of US garment imports compared with less than 6 per cent in 1987 (Mandelbaum, 1992, 37), and more than half of all (not just garment) Mexico's exports to the USA in 1991 entered the USA under the heading 9802. Although the 9802 special provision can apply to any country, Mexico and the Caribbean Basin countries have an obvious transport advantage relative to Sri Lanka. South Korean investors are reported to have invested heavily in Guatemala to take advantage of the quota and tariff concessions (*Island*, 31 August 1992). In 1993, the largest increases of garment imports into the USA were from countries with large 9802 operations, namely, Mexico, the Dominican Republic and The Philippines. 9802 imports of garments accounted in 1993 for 15 per cent of all garment imports into the USA up from 9 per cent

as recently as 1990 (US 1994b, 32-8). In 1991, Sri Lanka imported 0.5 per cent of its total fabrics from the USA and by 1993 this had risen to 2.2 per cent. The possibility of using the 9802 provision is clearly worth more investigation (see SLAEA 1995, 30, 31 and Thurairajah, 1995, 9).

A similar **Outward Processing Trade** (OPT) arrangement operates for garment exports to the EU with special quotas and concessional tariffs applicable. In 1991, OPT imports accounted for about 11 per cent of all garment imports into the EU and have become particularly important into Germany and from North Africa and Eastern Europe (Jenkins, 1993, 19 and SLAEA 1993, 5).

Third, there may be serious implications for Sri Lankan textile and garment exports arising from the expansion of **regional blocs** within the developed countries. The **European Union** now consists of 15 full-member nations, but in addition to the full members, there are those Central and Eastern European countries which are affiliated with the EU under the Europe (Free Trade) Agreements (see Anderson and Neary, 1994, 140,141) and, more importantly, the EU has entered into a customs union with Turkey from the beginning of 1995. This arrangement with Turkey is reported to have been agreed to by Greece (one of the EU 15) on condition that:

(i) negotiations begin on the EU membership of Cyprus
and that,
(ii) Greek textile manufacturers receive aid from the EU (*International Herald Tribune*, 4th/5th March, 1995).

Textile and garment supplies from Turkey have the advantage of shorter lead times into the European market (Thurairajah, 1993b, 82) and Turkey must be considered a major competitor to Sri Lanka. Even before the customs union move, Turkey's exports of textiles and garments to the EU were substantial. In 1994, Turkey's textile exports to the EU were $400 mn. and garment exports to the EU were about $1.4 bn. (see *Textile Asia* November 1994).

With Mexico and Canada joining the USA in the **North American Free Trade Agreement (NAFTA)** in January 1994, Sri Lanka's textiles and garments may face strong competition. A study of NAFTA was carried out by Safadi and Yeats (1993) in relation to South Asia but with only brief reference to Sri Lanka. However, one important argument of the Safadi and Yeats study was derived from the low import penetration by Mexico in textiles and garments to the North American (Canada and USA) market in the 1970s and 1980s. Safadi and Yeats pointed out that through the 1970s and 1980s Mexican exports accounted for less than 0.2 per cent of the apparent consumption in North America of textiles and less than 0.5 per cent of garments. The growth in the import penetration ratios for Mexico was much slower and the level lower than for all developing countries combined. Mexico's performance was also weak compared to that of South Asia. Safadi and Yeats concluded from this that special supply constraints exist that would limit Mexico's ability to displace third countries in North America (Safadi and Yeats 1993, 13).

A study by **Kelegama and Unamboowe** in May 1994 looked at the likely effect of NAFTA on Sri Lanka in more detail, and with special reference to the garment industry. As we have seen, in the 1990s, over 60 per cent of Sri Lanka's exports of garments have been to the North American market. Kelegama and Unamboowe looked at the possibility of Sri Lanka losing investments to Mexico as well as Sri Lanka losing trade shares to

Mexico. The conclusion on **investment diversion** was that the existing US investment in Sri Lanka would not be diverted by NAFTA nor would there be a significant diversion of East Asian investment from Sri Lanka to Mexico (1994, 9). They argued that strict rules of origin within NAFTA were likely to be a major obstacle to investment from non-NAFTA countries into the Mexican textile and garment industries. In the early 1990s, textile manufacture in Mexico was generally uncompetitive compared to the USA (Kelegama and Unamboowe, 1994, 21).

On **trade diversion**, Kelegama and Unamboowe were more circumspect but still optimistic that the threat to Sri Lanka was not as great as some had feared. Safadi and Yeats had argued that the Uruguay Round reductions in trade barriers would reduce the advantages that Mexico would gain through membership of the NAFTA, and Kelegama and Unamboowe pointed out that the Uruguay reductions would make little difference to the Sri Lankan/Mexican price differential (1994, 17). Kelegama and Unamboowe supported Safadi and Yeats by arguing that Mexico's inability to fully utilise the garment quotas (in spite of the value added tariffs under 807 -- HS 9802) was indicative of domestic supply constraints although Fernando has been less optimistic (See *Daily News*, December 17, 18, 1993). Kelegama and Unamboowe concluded that Mexico's advantage over Sri Lanka in sea transport costs (about 7 per cent of the landed cost of a garment), in labour productivity (Mexico's being about twice as high as that of Sri Lanka) and in the tariff differential (14 per cent post-Uruguay and post-NAFTA) was likely to be more than offset by the nine-fold difference in wage rates between Mexico and Sri Lanka and by the higher fabric costs in Mexico compared to Sri Lanka (see Kelegama and Unamboowe, 1994, 16, 18, 33-36). Mexico was likely to have an advantage in terms of lead times for garments with a high fashion component but not otherwise (Kelegama and Unamboowe, 1994, 22).

Kelegama and Unamboowe may have been a little too optimistic in assuming labour costs to be 20 per cent of the FOB value of a garment (1994, 35) and in assuming that fabric costs to Mexico would be 1.5 times those to Sri Lanka (1994, 33). These would seem to be somewhat on the high side, but even if lower figures are taken of, say, 10 per cent and 1.2, Sri Lanka would still seem to have the edge in terms of average costs. **In short, Mexico's advantages were to a great extent in existence before the formation of NAFTA** since Mexican garment manufacturers could use the 807 value-added tariff which reduced the pre-Uruguay 20 per cent tariff by about two-thirds (the proportion imported from the USA) to about 7 per cent. The post-Uruguay, post-NAFTA tariff differential will remain more or less the same because of the rules of origin within NAFTA. Mexican garment exporters will still have to use US materials from the yarn stage to get tariff-free access to the US market, although there are some important exceptions (see Fernando in *Daily News*, December 17 1993). Thus in respect of competition from Mexican garments, there will be some changes as a result of NAFTA but competition will still be muted (or so, Kelegama and Unamboowe claim) by the considerable difference between Mexico and Sri Lanka both in wage rates and fabric costs. Fernando is less optimistic.

5.4 The long-term and the phasing out of quotas

Having looked at the tariff structures and the special conditions arising from the GSP, regional blocs, etc., we now look in more detail at the effects of the phasing-out of quotas.

Table 5.2
Final fibre consumption (mn. tons and growth rates), 1980-2004

	1980	1995	1980-95 growth (mn. tons)	2004 growth (% p.a.)	1995-2004 (mn. tons)	(% p.a.)
Western DCs	13.6	19.5	2.5	24.0	2.3	
Eastern DCs	5.1	3.0	negative	4.5	4.8	
Less DCs	11.1	17.8	3.1	23.0		2.9
Total	29.8	40.3	2.1	51.5		2.7

Source: EIU 1995, 15.

The growth in the apparent world consumption of textiles and clothing averaged a little over 2 per cent p.a. between 1980 and 1995. Final fibre consumption rose from 30 mn. tons in 1980 to about 40 mn. tons in 1995. Consumption is projected by the EIU to rise to 51.5 mn. tons in 2004, a rise of a little under 3 per cent pa. The consumption figures are shown in Table 5.2 below.

With world population growth averaging a little over 1 per cent p.a. the world consumption per capita of textiles and clothing has grown at a little under 1 per cent p.a. Between 1995 and 2004, this is projected to grow at a little over 1 per cent p.a. as shown in table 5.3 below.

Table 5.3
Consumption per capita of textiles and clothing in DCs and LDCs, 1980-2004 (final fibre consumption; kgs per capita)

	1980	1995	1980-95 growth (% p.a.)	2004 growth (kgs)	1995-2004 (% p.a.)
	(kgs per capita)				
Western DCs	16.8	22.6	2.0	26.4	1.7
Eastern DCs	14.1	7.6	negative	11.0	4.1
Less DCs	3.4	4.5	1.8	5.0	1.1
World average	6.8	7.7	0.8	8.6	1.3

Source: EIU 1995 18.

Thus the growth in world consumption has been, and is likely to continue to be slow. However, the growth of demand for LDC exports has been, and is likely to continue to be very much faster because of growing import penetration. The self-sufficiency ratios for all fibre consumption are shown in Table 5.4 below.

Table 5.4
Self-sufficiency percentages, 1980-2004 (final fibres)

	1980	1995	2004
Western DCs	90	65	58
Eastern DCs	98	102	104
LDCs	113	146	148

Source: EIU 1995 22.

In **garments,** the import penetration has been particularly rapid. In the USA, the percentage of apparent consumption met from imports was about 7 per cent in the early-1970s, about 22 per cent in the mid-1980s and about 37 per cent in 1993 (see Anderson (ed) 1992, 11 and US 1994b 32-1). In the EU, the import penetration percentages, (also by value), were 15 per cent up to the mid-1980s and about 25 per cent in 1993 (Majmudar, 1995, 13).[9]

Import penetration figures (by value) are therefore higher in the USA than in the EU although it should be noted that there are huge variations in the import penetration percentages of the member-countries within the EU (varying, in 1991, from 55 per cent in Germany to 17 per cent in Italy - see Thurairajah, 1993b, 72).

Assuming a current average import penetration figure of about 30 per cent and a future annual growth in apparent consumption of (optimistically) about 3 per cent, a growth in imports into the USA and the EU of 9 per cent p.a. (approximately equal to Sri Lanka's average growth in quotas to 2005) would lead to an average (net) import penetration percentage of about 70 per cent in the year 2010 -- that is, 15 years from now. And, if we allow for some specialist garment **exports** from the USA and the EU equivalent to about a quarter of imports, there is considerable scope for a rapid rate of growth (9 per cent p.a.) of garment exports to the US and EU over at least the next 20 years. Thus a continued rapid growth in the value of garment imports into the USA and the EU is likely well into the next century, although the competition from producers within the USA and EU is likely to become increasingly fierce, especially as productivity-enhancing assistance is provided to the textile and clothing industries in the USA and the EU (see Jenkins, 1993, 21; US 1994b, 32-5 and 32-6).

The growth in the volume of imports into the USA and the EU is likely to be very much faster than the growth in value because of a likely decline in the average price of those imports. The decline in price will result from a decline in quota premia as competition increases, with the expansion in capacity and productivity outpacing the growth in the volume of demand. The drop in price is, in turn, likely to generate a greater volume of demand but not by a substantial amount since the price elasticity of demand for garments is thought to be only about minus 1.1. That is, a drop in unit price of 10 per cent is likely to generate a rise in the volume of demand of about 11 per cent. Thus the drop in price is likely to be counteracted (but only just) by an increase in volume.

5.5 The long-term, the phasing-out of MFA quotas and the competition; a summary

All studies of the removal of MFA quotas suggest that the LDCs as a whole will have a net gain. The gain from the volume of exports is expected to outweigh the loss from the fall in the average export price. If the gains to consumers in the developed countries are added to this and the losses to existing producers in the developed countries deducted, the net gain from the abolition of the MFA quotas is estimated to run into billions of dollars. However, the estimates of the total gains and losses to all LDCs vary enormously

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9. Majmudar's figures are very different from those in Anderson (ed) 1992. Anderson's figure for import penetration in garments in the European Community (the EC6) in 1982-85 was 56 per cent. The latter seems to be in value terms and in that sense comparable with Majmudar's figure of only 15 per cent for the mid-1980s. (Majmudar's import penetration figure in volume terms was 32 per cent for the early-1980s rising to about 40 per cent in 1992).

(see Anderson (ed) 1992, 83; Majmudar, 1995, 17; Sodersten and Reed 1994, 451; and Suphachalasai, 1994 77) and when we try to ascertain which of the LDCs are likely to gain and which to lose, the results are highly uncertain. For example, a study by Trela and Whalley suggested a net gain for Sri Lanka of $53 mn. (in 1986 prices) (see Anderson (ed) 1992, 84), whereas a study by Page and Davenport suggested that Sri Lanka would be among the net losers from the phasing-out of quotas (see Majmudar, 1995, 22).

Clearly, from what we have seen, as MFA quotas are phased-out there will be increased competition in the world market. The competition will come from existing producers who are presently constrained by the quotas from increasing their production and exports. This will be the increased competition as a result of the abolition of quotas. In addition, of course, there will be competition arising as a result, not of the phasing-out of quotas, but from relatively new producers of textiles and garments.

It is not possible to say anything very definite about the intensity of competition in the future and its effects, even if we limit our attention to garments. It is clear that import penetration into the main developed country markets is likely to increase substantially even in terms of value and even in the face of attempts taken by the USA and the EU to protect their own producers. These attempts will include anti-dumping measures and safeguard measures under the post-Uruguay arrangements. For some details of anti-dumping measures taken by the EU in recent years see Anderson (ed) (1992, 136-137).

However, our assessment is that protectionism in the USA and the EU will be deeper and longer-lasting for textiles as opposed to garments since it is in the area of textiles that the competitiveness of the USA and the EU is likely to be greatest, since it is in these areas where the economies of scale are greatest.

Finally, it is useful here to discuss three issues which connect with Sri Lanka's competitiveness in the textile and garment sector.

First, direct subsidies. It is worthwhile pointing out that direct subsidies are likely to be counter-productive for there is within the Uruguay Round an Agreement on Subsidies and Countervailing Measures. This allows action (including the imposition of selective tariffs) to be taken in response to subsidies on exports (see PTC 1994, 97). Sri Lanka has had countervailing duties imposed by the USA in 1985, which were then revoked in 1990, and reimposed in 1993 (see Kelegama and Unamboowe, 1994, 11 and Thurairajah, 1993).

Second, one issue that the Sri Lankan government has to confront is whether to support the campaigns of certain countries and organisations for trade agreements to be conditional on the achievement of certain labour standards. For example, in March 1995, France was reported to be urging the EU that trade agreements should require trading partners to respect a set of minimum labour standards (*International Herald Tribune,* March 27 1995). There is a danger that such standards will be used as an excuse for protectionism, but it might be in Sri Lanka's interests to back the call of France and the International Labour Organisation (ILO) for the outlawing of child and forced labour.[10] In this respect Sri Lanka has a good record whereas the same cannot be said for some of

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10. The ILO's conventions 29, 105 and 138 deal with forced and child labour (see OECD July 1994, 139 for details of the ILO's convention on child labour).

her competitors (for example, India and China). (The *Mail on Sunday* in the UK, in November 1994, criticised the use of child labour allegedly being paid only about $0.5 a day for work in a garment factory in Tiripur in Tamil Nadu, India).

The **third** issue which arises in the promotion of trade in textiles and clothing is that of South-South cooperation -- that is, whether Sri Lanka should grant preferences to other LDCs through the Global System of Trade Preferences (GSTP) or, more formally, through a regional agreement such as the South Asian Association for Regional Cooperation (SAARC) Preferential Trading Arrangement (SAPTA). Under the GSTP the only concession which Sri Lanka has offered relating to the textile and clothing industry is a duty concession to Brazil on sewing machines (see PTC 1994, 103, 104). The 1994 PTC report stated that the first round of trade negotiations is under way within the SAPTA, but an agreement on trade concessions was not expected to be complete until the end of 1995 (PTC 1994, 105)

The above are three relatively minor issues in the textile and garment sector. Restricting our attention to garment production, the more important issues are those of marketing links and the levels of costs within the industry. In terms of the cost of production, Sri Lanka seems to be reasonably competitive although in the 1990 study by Trela and Whalley, Sri Lanka's unit costs were ranked alongside China, India and Pakistan, about 10 per cent above South Korea and almost 50 per cent above Bangladesh (Trela and Whalley in Hamilton C B, 1990, Table 2.9). A more recent KSA study (1995) quoted by Majmudar gave the estimated cost (in DM) per standard minute of standard clothing item for a number of countries. The KSA figures placed Hong Kong and Taiwan in the highest cost band (0.32 DM and 0.35 DM), followed by India (0.25 DM in Bombay), Malaysia, the Philippines, Indonesia, Thailand and **Sri Lanka**. The cheapest sources were South Korea (0.15 DM -- somewhat surprisingly) and China (at 0.14 DM). These estimates, which are updated every two or three years, are not surprisingly quite sensitive to exchange rate changes (see the end of Chapter 4).

Appendix 1
Abbreviations

*	ACP	-	African, Caribbean and Pacific
*	ATC	-	Agreement on Textiles and Clothing
*	CBI	-	Caribbean Basin Initiative
*	CIMA	-	Chartered Institute of Management Accountants
*	CITI	-	Clothing Industry Training Institute
*	CTMA	-	Ceylon Textile Manufacturing Association
*	DCs	-	Developed Countries (includes all the OECD countries of Western Europe, Canada, USA, Japan, Australia and New Zealand) - refer to the World Development Report of the World Bank
*	EC	-	European Community
*	EFTA	-	European Free Trade Association
*	EU	-	European Union
*	GATT	-	The General Agreement on Tariffs and Trade
*	GDP	-	Gross Domestic Product
*	GFP (200 GFP)	-	200 Garment Factory Programme
*	GNP	-	Gross National Product
*	IPS	-	Institute of Policy Studies
*	KEPZ	-	Katunayake Export Processing Zone
*	LDCs	-	Least Developed Countries
*	LTA	-	the Long Term Arrangement Regarding International Trade in Cotton Textiles.
*	MFA	-	Multi-Fibre Arrangement
*	MFN	-	Most Favoured Nation
*	MTN	-	Multilateral Trade Negotiations
*	NAFTA	-	North American Free Trade Association
*	NIC	-	Newly Industrialized Country
*	OECD	-	Organisation for Economic Co-operation and Development
*	PTC	-	Presidential Tariff Commission
*	SAARC	-	South Asian Association for Regional Co- operation
*	SITC	-	Standard International Trade Classification
*	STA	-	Short Term Arrangement on Cotton Textiles
*	TSB	-	Textiles Surveillance Body
*	UNCTAD	-	United Nations Conference on Trade and Development
*	VER	-	Voluntary Export Restraint

Appendix 2
Conversion factors - square metres per unit

US quota category and description (most important categories only)	Unit	Conv. factor (sqme)
237 Playsuits	doz	19.2
331/631 Gloves and mittens	doz.pr	2.9
334/634 M and B Coats	doz	34.5
335/835 W and G coats - veg fibre	doz	34.5
336/636/836 Dresses	doz	37.9
338/339 Cotton shirts, knitted (M and B/W and G)	doz	6.0
340/640 M and B shirts, not knitted	doz	20.1
341/641 W and G shirts/blouses, not knitted	doz	12.1
342/642/842 Skirts	doz	14.9
347/348/847 Trousers, slacks, shorts -veg	doz	14.9
351/651 Nightwear	doz	43.5
352/652 Underwear	doz	9.2
635 W and G coats, MMF	doz	34.5
638/639/838 shirts/blouses, knitted	doz	15.0
647/648 trousers, slacks, shorts - MMF	doz	14.9
Source; from MOU 1992, Annex A		
EU quota category and description		
06 Trousers	doz	14.9
07 Blouses	doz	12.1
08 Shirts	doz	20.1
21 Jackets	doz	14.4

Appendix 3
Garment Exporters - Sri Lanka 1993

Name of Firm	Number of Employees	Number of Mechines
Kokila Garments (Pvt) Ltd	500	250
Winter Quilts	500	250
De Livera Industries Ltd	500	250
Dilruk Garments Ind Ltd	500	250
Candy Garments Ltd	500	250
D M Industries Ltd	500	268
Oxford Garment Industries Ltd	500	250
Nipuna Garments (Pvt) Ltd	500	200
North Penn Apparel (Pvt) Ltd	500	250
Koggala Manufacturing (Pvt) Ltd	500	300
South East Asian App Ltd	500	250
P T K Enterprises (Pvt) Ltd	500	300
M Samson Silva & Co Ltd	500	200
Lankapura Apparels (Pvt) Ltd	500	221
Union Apparels (Pvt) Ltd	500	250
Rajarata Garments Ltd	500	200
Asia Tex (Pvt) Ltd	500	325
D S I Associates (Pvt) Ltd	500	211
Jewelarts Garments Ltd	500	225
Kings Inter. Garments (Pvt) Ltd	500	217
Dresswell Apparels (Pvt) Ltd	500	230
Vino Lanka App. Exp (Pvt) Ltd	500	250
Finn-tex Lanka (Pvt) Ltd	500	200
SBLC Super Lanka Apparel Ltd	500	350
Sinotex (Lanka) Ltd	500	350
Hyfashion Garments Ind. Ltd	500	250
Winter Quilts (Pvt) Ltd	500	250
Accent Clothing (Pvt) Ltd	500	230
S P I Exports (Pvt) Ltd	500	225
Agnanea (Pvt) Ltd	500	295
J S N Apparel (Pvt) Ltd	500	250
Timex Garment Ltd	500	250
Ayumi Apparels (Pvt) Ltd	500	225
Candy Garments Ltd	500	200
Catex (Pvt) Ltd	500	265
505 Apparels Ltd	500	250
Actca Garments (Pvt) Ltd	500	191
Vilco Lanka (Pvt) Ltd	500	300
Contex Lanka (Pvt) Ltd	500	280
Hayleys Shangkalpam App.	500	330
Innovative Knitwear (Pvt) Ltd	500	275
International Fashions (Pvt) Ltd	500	220
Slimline (Pvt) Ltd	500	350
Wijeya Lanka Fashion App.	500	210
Koggala Manufacturing (Pvt) Ltd	500	300
Regancy Garments Ltd	501	408
Bernard Boteju Industries Ltd	502	218

Contd...../ Appendix 3

Name of Firm	Number of Employees	Number of Machines
Aitken Spence Garments Ltd	502	250
Champion Apparels Exp. Ltd	504	220
Hidramani Industries Ltd	505	236
Mapbu Industries (Pvt) Ltd	506	282
Everbest Gar. Com. (Pvt) Ltd	508	275
Kenmatex (Pvt) Ltd	508	243
S L Exports (Pvt) Ltd	510	200
Bestform Garments (Pvt) Ltd	510	309
Wasantha Senarath App Ltd	510	213
Bonaventure Tex. Lanka Ltd	510	340
Bontex (Lanka) Ltd	510	340
Maliban Textiles Ltd	513	396
Tri Star Apparels	514	255
Nelum Fashions (Pvt) Ltd	514	294
Unilak Feshions (Pvt) Ltd	514	277
Jaqalanka Int. (Pvt) Ltd	514	236
Lanka Garments Industries Ltd	515	260
Smart Shirts (Lanka) Ltd	515	330
Summit Industries Ltd	516	200
Gabo Apparels (Pvt) Ltd	517	230
Eve's Apparel Ltd	518	297
Tri Star Apparels	519	225
Merigold Garments (Pvt) Ltd	519	200
Subashi Apparels (Pvt) Ltd	520	204
Activewear (Pvt) Ltd	520	235
Ruhunuputha Apparels (Pvt) Ltd	520	225
Tri Star Apparels	523	242
Tri Star Apparels	523	249
Merigold Garments (Pvt) Ltd	525	225
Amrita Apparels (Pvt) Ltd	525	230
Readywear Industries Ltd	526	223
Tri Star Apparels	527	250
Polytex Garment Ltd	528	256
Mandarin Knits Garments	530	350
Sampath Exports (Pvt) Ltd	530	100
Shiran Garments Ltd	531	220
High Level Textiles (Pvt) Ltd	533	261
Taj Garments (Exports) Ltd	533	286
Alexandra Ind. (Ceylon) Ltd	535	356
Cadillac Garments Ltd	538	545
Heenatigala Garments (Pvt) Ltd	539	250
Texvel Jersey Ltd	539	215
Million Apparels Ltd	540	256
Martin Emprex (Ceylon) Ltd	540	329
Shiran Apprels (Pvt) Ltd	544	300
Giorgio Morandi (Pvt) Ltd	546	413
Luk Shirts (Pvt) Ltd	547	222
Kundanmal Garments Ltd	549	250
Nipuna Garments (Pvt) Ltd	550	250
Creations (Pvt) Ltd	550	231
M R C Associates Gar. Ltd	550	349
Everstrong Garment H/Kong	550	280
Modern Apparels (Pvt) Ltd	552	358

Contd...../ Appendix 3

Name of Firm	Number of Employees	Number of Machines
Gavesha Apparel Exports	552	250
Fashion Trends (Pvt) Ltd	555	294
Tri Star Apparels	556	221
Tammanna Garments (Pvt) Ltd	558	209
Tammanna Garments (Pvt) Ltd	558	209
Dinesh Apparels (Pvt) Ltd	562	362
Austin Gloves (Ceylon) Ltd	566	350
Dial Tex. Insudtries Ltd	567	220
Hently Garments Ltd	570	400
Swastik Textiles Industries Ltd	574	270
Orient Garments Ltd	575	298
Shadowline (Pvt) Ltd	575	300
Jewelarts Ltd	585	300
Sylvie Honor Industrial (Pvt) Ltd	600	325
Viking Fashions (Pvt) Ltd	600	340
Broadsword Apparels (Pvt) Ltd	604	223
Texwood Industries Ltd	605	298
Trend Setters (Pvt) Ltd	609	231
S P I Exports (Pvt) Ltd	615	297
Koggala Garments (Pvt) Ltd	616	302
Trend Setters (Pvt) Ltd	619	342
Bernard Boteju Ltd	621	307
Fashionwear Gar. Industries Ltd	625	300
Mono Garments Ltd	631	335
Gil Garments (Pvt) Ltd	641	426
C N A Ltd	650	375
Lanka Garments Manuf. Com. Ltd	660	250
Industial Clothing Ltd	661	233
International Dresses (Pvt) Ltd	664	381
Korea Lanka Garments Ltd	675	300
Canada Lanka App. (Pvt) Ltd	678	368
Candy Garments	680	300
Tri Star Apparels	698	228
Oxford Garment Industries Ltd	700	375
Favourite Garments Ltd	715	386
Favourite Garments Ltd	715	385
Colmons Garments	723	336
Upali Garments (Pvt) Ltd	750	500
Poly Gloves Lanka (Pvt) Ltd	750	260
Janatha Garments Ltd	751	399
Mercury Garments (Pvt) Ltd	754	275
Elphis Lanka (Pvt) Ltd	760	499
Phoenix Fashions (Pvt) Ltd	765	403
Jaqalanka Int. (Pvt) Ltd	775	285
Ranliya Garments Ltd	790	589
A J S Apparels (Pvt) Ltd	800	800
Ceylon Knit Trend Ltd	816	425
Shiran Garments (Pvt) Ltd	825	290
Unichela (Pvt) Ltd	835	424
Samson Exports Ltd	870	527
A J Milton (Lanka) Ltd	923	397
Gartex Ind. Lanka (Pvt) Ltd	950	525
Univogue Garments Ltd	950	500
Cosmos Macky Industries Ltd	951	690
Hidramani Industries Ltd	980	550

Contd...../ Appendix 3

Name of Firm	Number of Employees	Number of Machines
Hidramani Garments Ltd	987	452
Estelle Trading Company	1,000	448
Texlinen (Pvt) Ltd	1,004	122
L M Apparel (Pvt) Ltd	1,005	418
Union Apparels (Pvt) Ltd	1,006	315
Lux Shirts (Pvt) Ltd	1,010	392
Katunayake	1,042	500
Tri Star Apparels	1,057	477
Tri Star Apparels	1,057	477
Translanka Apparel Ltd	1,080	650
Tri Star Apparels	1,090	414
M Samson Silva & Com. Ltd	1,100	480
Orient Garments Ltd	1,154	504
Aitken Spence (Garments) Ltd	1,167	620
Maliban Textiles	1,320	620
Creations (Pvt) Ltd	1,531	518
Bratex (Pvt) Ltd	1,546	1,110
Transworld Garments (H/K) Ltd	1,595	625
Bontex Lanka (Pvt) Ltd	1,600	1,000
Caddilac Garments Ltd	1,912	850
Readywear Industries Ltd	2,050	1,287
Alexandra Ltd	2,105	1,000
Inter Fashion Company Ltd	2,173	968
Ansell Lanka (Pvt) Ltd	2,224	0
Sinotex Lanka Ltd	2,595	1,657
Polytex Garments Ltd	2,643	1,381
Star Garments Ltd	2,900	1,300
Smart Shirts (Lanka) Ltd	2,965	1,706
Laws Gar. & Knitting Fty Ltd	3,107	1,601
Bonaventure Textile Lanka Ltd	3,535	1,984
Sub Totals	139,850	69,877
Total for all firms	230,023	125,127

Source: MHTI, DataBase 1993.
Note: (i) Only exporters registered as employing more than 500 employees are listed.

Appendix 4
Quotas - Their Effects and Who Gains and Loses?

A4.1 The theory on the effects of MFA quotas

To understand the effects of the MFA it is useful first to understand the effects of, first, an **import duty** and, second, a **quota** imposed and administered by an importing country.

The effects of an import duty

If we assume that the country (say, Sri Lanka) imposing the import duty is a 'small country' (that is, that the world import price remains fixed, regardless of the volume of Sri Lanka's imports of the product), then the imposition of a tariff will raise the domestic price of the product and therefore will tend to protect domestic production. The volume of imports will be squeezed and domestic consumers will pay a higher price. Unless the tariff is prohibitive (that is, it shuts out all competing imports), there will be some import duty revenue to the government. In addition, those producers who were already making profits before the tariff, will make bigger profits, while those producers newly attracted into production will have higher unit costs than the without-tariff world price.

Under these assumptions, economists agree that there will be a net short-term loss from protection (for a diagrammatic presentation of the effects of an import duty, see Williamson and Milner 1991, 125). With the import duty, consumers will pay a higher price for the product. A part of this higher cost will accrue to the government in the form of import duty, a part will accrue to domestic producers in the form of higher net income, and a part will be spent on the higher-than-world costs of those producers for whom the higher price is an incentive to produce more. The net short-term 'loss' is the higher cost of production plus the loss stemming from reduced consumption.

It should be noted that **measuring** the protection is not as simple as it might appear, not least because a part of the tariff may not be used and may therefore be redundant. That is, the price to the consumer may be less than the world price plus the listed duty. It is easiest to consider this in terms of a listed tariff which shuts out all competing imports but behind which either the producers compete at a price which is less than the world-price-plus-the-tariff or behind which there is a monopolist who can maximise the rate of profit at a price less than the world-price-plus-the-tariff. These are two reasons for the listed tariff being redundant. However, in addition, there may be a third reason for the tariff being eroded, namely, smuggling. In Sri Lanka, it is estimated that one-third of the apparent domestic consumption of textiles (fabric) is either smuggled in or 'leaked' (the latter through sales in the local market by the garment exporters). This means that the listed duty almost certainly overstates the level of protection in the domestic market. To discover whether such tariff redundancy occurs and to discover the actual level of nominal protection require a comparison of the international prices with domestic prices. Since such comparisons are time-consuming, studies of tariff protection rarely include them.

The effects of an import quota:

However, in spite of these measurement complications, the effects of an import duty are reasonably straightforward. Similarly, the effects of an import **quota** imposed by the government of the importing country are also straightforward. An import quota limits the

imports to a specified quantity in a specified time period, the volume being less than that previously imported. (The effects are shown diagrammatically in Williamson and Milner 1991, 129 and in Sodersten and Reed 1994, 205).

For the purposes of this report, the major difference between an import tariff and a quota is in the allocation of revenue. Whereas with an import duty, the government may collect some revenue through the duty on any remaining imports, with a quota the revenue accrues to the importers who are allocated the quotas. The government can only recapture a part or all of this by selling the import licences. Otherwise, this will accrue as super-profit to the importers.

The effects of Voluntary Export Restraints (VERs):

The MFA quotas described in Chapter 3 are akin to VERs and VERs act like import quotas. The essence of a VER is that the importing country negotiates quantitative restrictions with its foreign suppliers on the amount of exports that they will supply to the domestic market. The negotiations may be between two governments or associations of producers working with the delegated approval of the governments.

In most respects (effects on quantity of imports, domestic production, domestic demand) the VER has effects which are the same as those of the import quota levied by the importing government. Again, any super-profits arising from the quotas will accrue to the agents holding the quotas, but this time the quota rights are held by the exporters, not by the importers. This opportunity for the exporters to obtain super-profits is one reason why foreign suppliers might be more readily persuaded to 'voluntarily' restrict their exports. The exporting country is effectively 'bribed' to accept the arrangement (Williamson and Milner 1991, 145).

For our purposes, there are two major issues associated with the MFA quotas;

(i) who gets the super-profits? how big are they? and should they be taxed or auctioned by the government?
(ii) what is the effect of removing the quotas?

Here we consider only the first issue. The second is discussed in Chapter 5.

However, before we look at these, it is useful to discuss four possible complications which arise from the analysis.

The **first** is that the importing country may impose a tariff as well as a VER. Import tariffs are levied on garments imported into both the USA and the EU. However, this does not pose any great analytical problem for working out the effects of VERs. The tariff raises the domestic price and reduces (all other things remaining the same) the differential attributable to the VERs. Thus the super-profits accruing to the foreign exporters are reduced. We looked at tariff protection in Chapter 5.

The **second** issue is that the importing countries impose VERs on not just one but a number of textile and garment exporting countries. Again this poses no analytical problem. The super-profits are simply split between exporters in a number of countries.

The **third** complication may arise where due, say, to productivity increases in the world textile and garment industry, the world price may fall. If this happens (and assuming that there is no change in productivity in the protected domestic industry), the gap between the world price and the price in the importing country widens and, for a given VER quantity, there is an increase in the super-profits accruing to holders of the quotas.

The **fourth** complication arises where there is an increase in domestic demand in the importing country. If there is no increase in the quota, then the increase in demand is met from higher-cost domestic production and the price paid by the consumers in the domestic market will rise. This will mean that the super-profits of the quota-holding exporters will also rise. Conversely, if the growth in quotas is faster than the domestic demand in the importing country, then the super-profits of the quota-holders are likely to fall. We looked at this issue in Chapter 5.

.... and estimating the size of the quota-premia

The above four complications are not too serious in theoretical terms; they are small problems compared to those of estimating the **super-profits arising as a result of the quotas.**

If we start by looking at the tariff-equivalent of the VERs for garments imported into the USA (since this is the major market for Sri Lanka's garments) we find that for 1982-84, the tariff-equivalent was estimated by Hamilton (for imports from Hong Kong) to average 31 per cent (see Anderson 1992, 135). However it seems that this figure is derived from the quota premia in Hong Kong. Cline (1987) also estimated that the tariff-equivalent of VERs on clothing imports into the USA in 1986 was 32 per cent (see Anderson 1992, 163). Thus the tariff equivalent of the VERs for clothing imports into the USA in the mid-1980s would seem to have been about 30 per cent of the c.i.f. price.

The studies on quota-premia mostly focus on Hong Kong because, although it is entirely wrong to say that the Hong Kong government auctions its quotas, Hong Kong does have a well-developed and legal market in quota licences.[1] Thus, in a study published in 1985, Greenaway focused on Hong Kong because there were (for the year of Greenaway's study, namely, 1982) prices quoted for quota transfers. Greenaway looked at the exports of textiles and clothing to the UK because 45 per cent of Hong Kong's textile and clothing exports were to the UK.

In 1982 the average quota premium per unit was £0.34 compared to an average c.i.f. price into the UK of £2.67 per unit. Thus the quota premium (£0.34) was equal to about 15 per cent of the unrestrained c.i.f. price (£2.33). This figure of 15 per cent is in line with data for Hong Kong exports to the EC given in Anderson (1992, 135). Anderson gives an average premium for 1980 to 1988 of 13 per cent.

Thus, for the 1980s, we have quota-premia of about 30 per cent for Hong Kong exports to the USA and about 15 per cent for Hong Kong exports to the EC. Have things

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1 Quotas are allocated to exporters on the basis of their past shipments to the market in question over a designated reference period. Exporters are constrained by regulations administered by the Department of Trade in Hong Kong, but they can sell or transfer up to 50 per cent of their quota to other firms (for further details of Hong Kong quota allocation, see Erzan et al 1991, 17-91, Suphachalasai 1994, 62-63 and Williamson and Milner 1991, 151).

changed since the 1980s? It is hard to say. From the flimsy data available, it seems not. The average (Hong Kong) market value of the quotas in February 1994 to the f.o.b. price of the (Sri Lankan) exports to the USA varied for each of the major categories of garment exports from zero to 31 per cent. The simple average for 15 categories was just under 15 per cent. By contrast in 1991, Erzan *et al* suggested that the quota premium for garment exports from Hong Kong to the USA was something like 25 per cent (page 46).[2]

What are the quota-premia for Sri Lankan exports to the USA and the EU? With the information available to us, it is not possible to give an answer with any confidence. Sri Lankan exporters have asserted that the quota premia in Sri Lanka are not as large (as a proportion of the f.o.b. value) as in Hong Kong. The exporters claim that the ratio of the export (f.o.b.) price from Sri Lanka to the retail price in the USA is lower than for Hong Kong exports. This might mean that the share of the quota premium accruing to the Sri Lankan exporter is lower. In addition some exporters claim that not all of the quota income premium accrues to them due to the 'transactions costs' associated with the sales of the quotas.

However, it does seem that even if not all the rent accrues to the Sri Lankan exporters, quota premium income is substantial. If we assume that about two-thirds of all Sri Lanka's garment exports consist of quota exports, then the value of quota garment exports in 1994 was about Rs. 50 bn. If we work on a conservative (or minimum) estimate of an average quota premium of 15 per cent on all Sri Lanka's quota exports, the quota premium income would have been about Rs. 7.5 bn.

Such an income makes an enormous difference to profitability in the garment industry as we discussed in detail in Chapter 3.

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2 Interestingly, Erzan et al suggested that the quota-premium was shared between the exporters and importers. That is, the exporter was not able to hold on to all the quota premium with as much as half being retained in the USA (see Erzan *et al* 1991, 46).

Appendix 5
The Uruguay Round Agreement on Textiles and Clothing

The object of this negotiation has been to secure the eventual integration of the textile and clothing sector -- where much of the trade is currently subject to bilateral quotas negotiated under the Multi-fibre Arrangement (MFA) -- into the GATT on the basis of strengthened GATT rules and disciplines.

Integration of the sector into the GATT would take place as follows : first, on 1 January 1995, each party would integrate into the GATT products from the specific list in the Agreement which accounted for not less than 16 per cent of its total volume of imports in 1990. Integration means that trade in these products will be governed by the general rules of GATT.

At the beginning of Stage 2, on 1 January 1998, products which accounted for not less than 17 per cent of 1990 imports would be integrated. On 1 January 2002, products which accounted for not less than 18 per cent of 1990 imports would be integrated. All remaining products would be integrated at the end of the transition period 1 January 2005. At each of the first three stages, products should be chosen from each of the following categories: tops and yarn, fabrics, made-up textile products, and clothing.

All MFA restrictions in place on 31 December 1994 would be carried over into the new Agreement and maintained until such time as the restrictions are removed or the products integrated into GATT. For products remaining under restraint, at whatever stage, the Agreement lays down a formula for increasing the existing growth rates. Thus, during Stage 1, and for each restriction previously under MFA bilateral agreements in force for 1994, annual growth should be not less than 16 per cent higher than the growth rate established for the previous MFA restriction. For Stage 2 (1998 to 2001 inclusive), annual growth rates should be 25 per cent higher than the Stage 1 rates. For Stage 3 (2002 to 2004 inclusive), annual growth rates should be 27 per cent higher than the Stage 2 rates.

While the agreement focuses largely on the phasing-out of MFA restrictions, it also recognizes that some members maintain non-MFA restrictions not justified under a GATT provision. These would also be brought into conformity with GATT within one year of the entry into force of the Agreement or phased-out progressively during a period not exceeding the duration of the Agreement (that is by 2005).

It also contains a specific transitional safeguard mechanism which could be applied to products not yet integrated into the GATT at any stage. Action under the safeguard mechanism could be taken against individual exporting countries if it were demonstrated by the importing country that overall imports of a product were entering the country in such increased quantities as to cause serious damage -- or to threaten it -- to the relevant domestic industry, and that there was a sharp and substantial increase of imports from the individual country concerned. Action under the safeguard mechanism could be taken either by mutual agreement, following consultations, or unilaterally, but subject to review by the Textiles Monitoring Body. If such action is taken, the level of restraints should be fixed at a level not lower than the actual level of exports or imports from the country concerned during the twelve-month period ending two months before the month in which a request for consultation was made. Safeguard restraints could

remain in place for up to three years without extension or until the product is removed from the scope of the Agreement (that is, integrated into the GATT), whichever comes first.

The Agreement includes provisions to cope with possible circumvention of commitments through transshipment, re-routing, false declaration concerning country or place of origin and falsification of official documents.

The Agreement also stipulates that, as part of the integration process, all members shall take such action in the area of textiles and clothing as may be necessary to abide by GATT rules and disciplines so as to improve market access, ensure the application of policies relating to fair and equitable trading conditions, and avoid discrimination against imports when taking measures for general trade policy reasons.

In the context of a major review of the operation of the Agreement to be conducted by the Council for Trade in Goods before the end of each stage of the integration process, the Council for Trade in Goods shall by consensus take such decisions as it deems appropriate to ensure that the balance of rights and obligations in this Agreement is not upset. Moreover, the Dispute Settlement Body may authorise adjustments to the annual growth of quotas for the stage subsequent to the review with respect to Members it has found not to be complying with their obligations under this Agreement.

A Textiles Monitoring Body (TMB) would be established to oversee the implementation of commitments and to prepare reports for the major reviews mentioned above. The Agreement also has provisions for special treatment to certain categories - for example, those which have not been MFA members since 1986, new entrants, small suppliers, and Least-Developed Countries.

Appendix 6
Exports of garments from Sri Lanka to USA (1989-95)

Category	unit	1993 Six Month Quota					1994					1995-		
		Quantities			Value ($ mn)		Quantities			Value ($ mn)		Quantities		
		Quota (mn)	Actual (mn)	average export price 1994 ($/unit)	Quota	Actual	Quota (mn)	Actual (mn)	average export price 1994 ($/unit)	Quota	Actual	Quota (mn)	average export price 1994 ($/unit)	Value ($ mn) Quota
237 Playsuits	doz	0.09	0.03	51.0	4.6	1.5	0.24	0.20	51.0	12.2	10.2	0.30	51.0	15.3
331/631 Cotton gloves	dozpr	1.17	1.15	3.8	4.5	4.4	2.58	2.79	3.8	9.9	10.7	2.55	3.8	9.8
334/834 Other Coats	doz	0.28	0.28	126.3	35.4	35.4	0.59	0.73	126.3	74.5	92.2	0.49	126.3	61.9
335/835 Coats & other fiber	doz	0.10	0.10	139.2	13.9	13.9	0.25	0.28	139.2	34.8	39.0	0.23	139.2	32.0
336/636/836 Dresses cotton	doz	0.15	0.10	92.9	13.9	9.3	0.42	0.53	92.9	39.0	49.2	0.36	92.9	33.4
338/339 Knit shirts cotton	doz	0.58	0.52	69.6	40.4	36.2	1.24	1.09	69.6	86.4	75.9	1.33	69.6	92.6
340/640 Non knit cotton	doz	0.34	0.34	73.8	25.1	25.1	1.13	1.12	73.8	83.4	82.6	1.13	73.8	83.4
341/641 Shirts & blouses	doz	0.84	0.84	65.9	55.3	55.3	1.75	1.72	65.9	115.2	113.3	1.82	65.9	119.8
342/642/842 Shirts & other fibre	doz	0.24	0.12	71.7	17.2	8.6	0.41	0.34	71.7	29.4	24.4	0.54	71.7	38.7
347/348/847 Trousers	doz	0.64	0.64	63.7	40.7	40.7	1.50	1.41	63.7	95.5	89.8	1.55	63.7	98.7
351/651 Nightwear	doz	0.13	0.13	92.2	12.0	12.0	0.32	0.27	92.2	29.5	24.9	0.34	92.2	31.4
352/652 Underwear	doz	0.61	0.49	22.1	13.5	10.8	1.12	1.20	22.1	24.7	26.5	1.23	22.1	27.2
635 Coats	doz	0.11	0.11	115.1	12.7	12.7	0.34	0.40	115.1	39.1	46.0	0.33	115.1	38.0
638/639/838 Shirts Knit & other fibre	doz	0.29	0.20	42.3	12.3	8.5	0.67	0.52	42.3	28.3	22.0	0.81	42.3	34.3
647/648 Trousers	doz	0.35	0.33	57.9	20.3	19.1	0.76	0.69	57.9	44.0	39.9	0.99	57.9	57.3
Sub Totals - Large categories					**321.7**	**293.5**				**746.0**	**746.6**			**773.7**
SMALL CATEGORIES														
314 Cotton Cloth	Sq Mtr	1.48	1.02	0.3	0.5	0.4	3.74	2.95	0.3	1.3	1.0	4.12	0.3	1.4
333/633 Suits	doz	0.00	0.00		0.0	0.0	0.02	0.00	0.0	0.0	0.0	0.00	0.0	0.0
345/845 Sweaters & other fibre	doz	0.04	0.04	103.4	4.1	4.1	0.09	0.09	103.4	9.3	9.3	0.10	103.4	10.3
350/650 Cotton Dressing Gowns	doz	0.06	0.05	102.8	6.2	5.1	0.05	0.05	102.8	5.1	5.1	0.09	102.8	9.2
359C/659-C Overalls	Kgs	0.23	0.05	12.0	2.8	0.6	0.77	0.70	12.0	9.2	8.4	0.76	12.0	9.1
363 Towels Cotton	Nos	2.76	1.70	0.5	1.5	0.9	6.75	3.44	0.5	3.7	1.9	6.29	0.5	3.5
369-D Dish Towels	Kg	0.23	0.05	3.9	0.9	0.2	0.64	0.17	3.9	2.5	0.7	0.91	3.9	3.5
369-S Shopp Towels	doz	0.32	0.25	2.7	0.9	0.7	0.64	0.44	2.7	1.7	1.2	0.76	2.7	2.1
644 Suits	doz	0.13	0.04	9.4	1.2	0.4	0.20	0.05	9.4	1.9	0.5	0.26	9.4	2.5
645/646 Sweaters	doz	0.04	0.01	65.6	2.6	0.7	0.02	0.00	65.6	1.3	0.0	0.06	65.6	3.9
Sub Totals - Small categories					**20.7**	**13.1**				**36.1**	**28.0**			45.5
Grand Total					**342.4**	**306.6**				**782.1**	**774.7**			**819.2**
% Utilisation of Quota					**89.5%**					**99.1%**				

Quota & Actual 1990-1993 - Appendix 5A-5D SLAEA 1995.
Average 1994 Export Price taken from SLAEA, 1995 - Appendix 8 and based on US input statistics.
Quota 1995 - Thurairajah, 1995, Annex C.
Quota & Actual 1994 - Thurairajah 1995, Annex B.
Large- when the actual value in 1994 is greater than $10m.

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