Sri Lanka Apparel Industry

- In The Midst Of A Challenge -

The role played by the garment industry in Sri Lanka is significant in several respects. The contributions made by this industry to foreign exchange earnings and the employment generation are the most important among them.

The garment industry is generally referred to as a 'foot-loose' industry moving from country to country where the cost of production is low. This is evident by the closure of a large number of garment factories in Europe and the United States when developing countries commenced the export of garments produced at a low cost,due to low cost of labour, and the relocation by those manufacturers who have been running the factories in the developing countries. It is well known that there are several such factories with internationally reputed European brands of garments also in Sri Lanka at present.

The manufacture of garments is a labour-intensive production and is not depended on heavy capital investment or long lead times to train and establish a manufacturing facility. Neither is a long gestation period needed to commence production. Fabrics or textiles are the single largest input used in this industry accounting for 60-70 percent of the finished products and are readily available world wide at competitive prices. Therefore, the competition of the product output in the market mainly depends on the cost of labour and the cost of overheads. The comparative advantage of the location of industry is another vital factor to enter the market competitively. However, the quality of the finished goods has to be considered as a very important factor when it is marketed in developed markets like USA, Europe and Japan.

In case of technology, compared to textile manufacture or any other Industry which has scope for enormous application of new technology to reduce the labour, the garment industry is highly labour intensive and needs a lot of manual labour. The possibility of the garment industry to be a high tech capital-intensive industry is remote, although some labour intensive automation is being already adopted.

As long as the cost of labour is low any country may be able to run this industry as a profit-making venture. This is why this industry is vital for Sri Lanka. During the past 50 years after independence various large-scale heavy industries as well as medium scale industries were established in Sri Lanka. But with the increasing competition they face with the gradual opening up of the economy, products of those industries have been marginalized from the market and many industries have been closed down due to non-profitability, and others have become a burden for the country. Inability to acquire modern technology, needed to produce goods that are competitive in the market was the main reason for their failure.

Comparatively, the garment industry has become one of the fastest growing industries during the last decade in Sri Lanka. Growth has been stimulated by a very large installed capacity, a high level of technical and managerial skill. However, still there are excellent investment opportunities in the production of up-market higher quality and better-designed garments to meet the needs of sophisticated and rich markets around the world, which may not be affected by the problems expected after 2005.

The capacity to cater to those markets is not a problem for Sri Lanka with its intelligent, educated and energetic workforce that is familiar with modern production techniques and having acquired a high level of skill. In fact, Sri Lanka has a very high quality workforce at wage level affordable to the industrialists in the region.

Another encouraging factor for the development of this industry is the infrastructure facilities, which, as mentioned earlier is another important requirement for the expansion of this industry. Sri Lanka is among the countries with very good infrastructure facilities in South Asia. The port has facilities to handle large tonnage of containers and trans-shipment of cargo together with the location of Colombo as a major shipping hub. The telecommunication facilities with modern technology and the non-interrupted power generation through hydro and thermal generation and central location of Sri Lanka in the South Asian region are the other major advantageous factors, in this regard.

Table 1 - Utilisation Summary of Garment Quotas - As at 24-07-1999

USA

Category	Adjusted Limit-1999.	Utilization: Visas issued in 1999	Overshipmets in 1998	Miss Match Qty.(as at 31-05-99)	Total Utilization	Percentage
237	411,423	109,127	-	1,500	110,627	27
314	6,141,971	2,332,598	-	308,000	2,640,598	43
331/631	4,117,858	1,124,247	-	3,500	1,127,747	27
333/633	21,475	0	-	-	0	0
334/634	1,018,923	325,840	81,091	3,500	410,431	40
335/835	223,410	56,641	-	200	56,841	25
336/636/836	623,107	380,568	28,722	10,000	419,290	67
338/339	1,807,112	962,669	53,105	32,000	1,047,774	58
340/640	1,606,813	875,791	220,588	18,500	1,114,879	69
341	1,667,068	679,586	-	4,000	683,586	41
341/641	2,143,130	878,580	0	5,000	883,580	41
342/642/842	879,426	464,329	-	3,500	467,829	53
345/845	244,438	47,016	-		47,016	19
347/348/847	1,865,019	1,302,795	61,200	110,000	1,473,995	79
350/650	125,883	55,600	94	950	56,644	45
351/651	508,718	165,230	-	750	165,980	33
352/652	1,783,034	544,478	-	7,000	551,478	31
359/659 C	1,466,930	265,935	-	10,000	275,935	19
360	1,925,873	272,128	-		272,128	14
363	14,940,909	5,401,512	-	46,000	5,447,512	36
369 D	52,668	9,304	-		9,304	18
369 S	1,012,467	686,610	-		686,610	68
434	8,278	1,230	-		1,230	15
435	17,739	888	-		888	5
440	11,826	0	-		0	0
611	7,128,958	831,276	-	15,000	846,276	12
635	530,087	197,965	41,521	5,000	244,486	46
638/639/838	1,145,685	268,521	-	1,000	269,521	24
641	585,727	198,994	-	1,000	199,994	34
644	652,207	158,839	-		158,839	24
645/646	144,821	9,861	-		9,861	7
647/648	1,175,981	420,268	12,676	10,000	442,944	38
840	253,210	101,077	25,466	3,500	130,043	51

CANADA

Category	Proposed Adjusted Limit-1999.	Utilization: Quantity	Percentage
01	1,157,072	160,413	14
01A	157,808	24,564	16
02	348,815	106,704	31
03/04	1,066,187	161,083	15
03/04A	35,067	360	1
05	1,204,681	542,480	45
07/08	1,078,128	79,757	7
07/08A	892,862	454,463	51
09	1,566,792	9,160	1
10	876,699	77,246	9
11	417,391	7,330	2
12	876,699	101,350	12
14	438,350	169,731	39
41A	912,675	38,320	4

EC

Category	Proposed Adjusted Limit-1999.	Utilization: Quantity	Percentage
06	12,179,180	6,092,547	50
07	18,542,200	6,303,703	34
08	11,698,560	2,160,932	18
21.	13,326,340	1,114,635	8

Source : Textile Quota Board

However, all these encouraging factors could be utilized towards the development of the industry only with commitment and genuine effort. Matters like the recently recorded incidence of export of garments using counterfeit or forged documents and the export of garments of low standard the industry would not bring credit.

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In table I under the column "mismatch" gives the amount of recent exports of garment under counterfeit documents. This fraud was discovered when the Textile Quota Board found U.S. import figures of Sri Lankan apparel exports were

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Table 2

Textile and Garments Exports (1994-98)

Rupees Million

Item	1994	1995(a)	1996	1997	1998(b)
Textiles & Garments	76,685	94,948	105,341	134,455	159,303
Woven Fabrics	2,077	2,263	2,863	4,015	4,566
Knitted/Crocheted Fabrics	146	379	402	587	1,112
Yarn	1,694	2,283	2,347	2,447	2,184
Garments	68,945	84,806	93,813	121,083	142,332
Other Madeup Textile Articles	2,208	3,334	3,948	3,989	6,552
Other	1,614	1,880	1,966	2,334	2,457
Total Manufacturing	118,543	147,094	166,545	203,114	229,437

much more than the export figures maintained by the Island's customs department. The Minister of Industrial Development, Mr. C V Guneratne who took immediate action on this, branded the group who involved in this racket as an 'Apparel Mafia'. According to the information available there are some 71 errant exporters who were suspected of making fraudulent exports to USA of among 800 exporters. Fortunately, there is no immediate danger of the US government imposing an embargo, because Sri Lanka is still within her textile quota. If the quota is exhausted before the end of the year and an embargo imposed, it would be a serious problem for the genuine exporters. Government quota allocation for 32 quota categories of garments among some 800 registered exporters is done in a transparent manner by the officers of relevant government authorities like the Quota Board, Ministry of Industrial Development, BOI, EDB and representatives from the Industrialists.

Earnings of Foreign Exchange

Sri Lanka was heavily dependent on the traditional exports of tea, rubber and coconut for foreign exchange earnings until the early eighties when non-traditional exports emerged as a leading foreign exchange earner. The reason for this high growth in the non-traditional sector was the high contribution made by the garment sector to this sector. In 1975 garment exports amounted to only 4.9 per cent of the total value of exports of all manufactured goods. In 1976 and 1977 these exports rose to 9.6 per cent and 10.6 per cent respectively. In 1978 and 1979 it was ranging between 20 and 30 per cent. Accordingly, it has recorded a growth rate between a minimum of 36 per cent and a maximum of 150 per cent in this period. The latest statistics show that this industry is responsible for over 69.4 percent of the total industrial exports. The lavish incentive packages that were given since the liberalization policy was announced, in 1977, helped the export garments manufacturing industry to expand rapidly. The opening of the Free Trade Zone, the implementation of the 200 garment factories in 1988 and the 50-garment factory project in 1997 could be identified as important milestones of the development of this sector. The share of world trade in clothing is valued at about US$ 133 billion and Sri Lanka's share in that however, is just above one percent. Hence, the opportunity and the openings for Sri Lanka in the world garment trade are immense.

Table 3

Value of Industrial Production (Rs Million)

				Percentage Change	
	1996	1997	1998	'97 over '96	'98 over '97
Total	154,937	170,818	183,598	10.2	7.5
Textile wearing apparel & leather products	58,332	69,269	72,391	18.7	4.5
Apparel	49,292	59,280	62,050	20.3	4.7
Textile	6,299	6,926	7,226	10.0	4.3
Leather	2,741	3,063	3,115	11.7	1.7

Source: Central Bank of Sri Lanka Annual Report 1998

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Manufacturers point of View -

Lack of Implementation

The Government has now implemented a 'Duty Free" system for textile imports instead of ensuring that the problem faced by the Domestic Textile Manufacturing Sector are remedied, thus providing a level playing field for these sector to compete and survive in a market oriented economy. Unless immediate remedial action is taken, so this Duty Free System will necessarily wipe out this vital manufacturing sector.

It is strange that some of the measures like Pre-Shipment Cargo Verification Scheme which would have gone a long way to mitigate the problems faced by this sector, have still not been implemented by the Government. Further, it is perplexing to note that even the agreed course of action to bring the BOI imports under custom's control has not been implemented.

Exit of Quota System in 2005

Presently, except for a few units, most of the export Garment Manufacturing Units are surviving because of the "Quota System" adopted by U.S.A. and the European Union, and it is relevant to note that, by year 2005, the "Quota System" will cease to exist in terms of WTO Agreement.

Instead of ensuring the attainment of the concept of backward integration" in the form of more and more textile manufacturing industries in the country which will provide the required raw material for the Export Garment Manufacturing Sector by the time removal of "Quota System" is put in place, the Government's action in the form of "Duty Free" Textiles is paving the way for the closure of existing Domestic Textile Manufacturing sector and eventually, even the closure of major percentage of Export Garment Units after the "Quota" is removed by 2005 onwards.

The removal of the "Quota System" will mean that the prospective buyers of garments will purchase their requirements from countries who can supply their requirements at short notice and at competitive prices. Our Export Garment Manufacturing Sector has to depend for 95% of it's input on foreign countries and in the absence of any other comparative advantages, this sector will automatically be left behind vis-à-vis Export Garment Orders. Countries like India, China, Pakistan and Indonesia, with their backward integration right up to spinning as well as raw material base along with other comparative advantages will benefit at the expense of Sri Lanka Garment Export Units.

Foreign Investments

If on the other hand, the officials think that there will be an influx of Foreign Investment into the Textile Manufacturing Sector of the country when the textile imports are made "Duty Free", it will be a dream only. With all the concessions like Tax Free Status, Duty Free Imports of Spares, Raw Materials etc., apart from international investment promotion campaign by BOI, there has not been any significant foreign investment in the textile sector in Sri Lanka.

The industrial output in 1998 recorded a weaker growth of 7.5 per cent compared with 10.2 per cent in 1997. Similarly, the exports of the apparel industry, which continued to expand in the face of global competition, tended to slow down towards the end of the year. However, this situation has become a global phenomenon mainly due to depressed global trading environment following the East Asian financial crisis and subsequent economic problems in many developing countries and developed countries including Japan, Russia, South and Central America.

When the quota system is fully phased out by 2005, international competition is likely to be intense. In order to face this future challenges successfully, the industry needs to invest in new technology and enhance its skills to improve productivity. Improved information systems would help the industry respond quickly to changing market conditions particularly in preferences and designs.

Among the contributing sectors to the value of industrial production, the major set back in 1988 was recorded in the textiles, apparel and leather producers sector, which consists of three major industries, namely, apparel, textile and leather. The apparel sector (Table 3).

According to Table 3 contribution made by the Apparel Indsutry to the total value of industrial production has recorded a considerable decline

Table 4

Country Classification of Garment Exports

Country	Value (Rs.Mn)		% of Total Value		Percentage Change	
	1997	1998(a)	1997	1998(a)	1997	1998 (a)
European Union	41,094	44,759	33.9	31.4	24.7	8.9
USA	74,355	91,361	61.4	64.2	29.1	22.9
Total	121,083	142,332	100.0	100.0	29.1	17.5

(a) Provisional
Source: Sri Lanka Customs

from 18.7% in 1997 to 4.5% in 1998. If the depreciation of the Sri Lanka rupee against US$ is adjusted, this value would further decline.

The Textile & Garment sector benefitted from the package of incentives introduced in the 1998 Budget, which made all intermediate and capital goods used in the industry non-dutiable. Textile and garment exports continued to be the leading export sub category, contributing 69 per cent to total industrial exports in 1998.

The BOI apparel and garment enterprise registered an output growth of 4.6 per cent during the year 1998. The amount of quotas increased from 73.6 per cent in 1997 to 74.1 per cent in 1998.

Export of Apparel and Use of Quotas

The performance based quota system, introduced in 1995, was continued in 1998. The Shipment of products under quota categories is allowed only on proof of payment of EPF and ETF contributions in allocating new quota. Priority was given to exporters who made new investments or expanded their existing capacities. Immediately after the allocation of performance quota, the remaining quotas were allocated under the main pool quota scheme on a pro rata basis of the number of employees, and preference was given to exporters to no quota countries and exporters of non quota items to quota countries. The under-utilised categories in the previous year were declared as 'cold' categories and allocated on the condition that shipment would be made within seven working days. The various schemes that have evolved under pool quota systems reflect cumbersome procedures that require close supervision and monitoring to achieve maximum utilisation. As mentioned before, quota administration had been in some disarray in 1998 as quotas to the USA for some items such as men's and boy's jackets and shirts were over utilized, and the Textile Quota Board had to take action to avoid the possible imposition of an embargo by the USA government.

The USA was Sri Lanka's biggest market, followed by EU. However EU stands mainly as a non-quota market. Exports of textiles and apparel from Sri Lanka to the USA accounted for 2.1 per cent of the USA requirement Export of apparel to USA increased by 3.4 per cent from 322 million square meter equivalents (SME) in 1997 to 333 SME in 1998. Of these, 77 per cent are under quota. The value of these exports increased by 8.7 per cent, from US dollars 1,204 million in 1997 to US dollars 1,308 million in 1998. There was a price gain of 5.5 per cent. This was a favourable development compared with a decline in the overall import price of apparel to the USA from all countries. Manufacturers were moving to higher value added items and Sri Lanka's apparel attracted higher prices in the USA under a highly competitive market environment. Other textile exports to the USA

Emerging Countries; Cambodia

Today one of the emerging garment manufacturers to be considered as a threat to Sri Lankan garment exports is Cambodia. According to information garment factories are mushrooming along the roads and across the rice fields around Phnom Penh, which is still in infant age. More than 90 per cent of the garments manufactured in Cambodia exported to USA which are product in rang of US brand-names.

The growth of the Cambodian garment sector is surprising. In 1996 the value of their garment export was only $ 79 million. In 1997 it increased to $ 227 million and in1998 to $ 378 million showing a 250.6 percent and 66.5 percent growth respectively 1998. Further the value of Cambodia's garment exports surged 96 per cent to $ 275.5 million in the first half of the year, compared with the same period last year.

There are 100,000 workers employed in about 170 garment factories, many of them owned by manufacturers from South Korea, Hong Kong, Malaysia, Taiwan and Singapore. In 1997 there were only 70 factories (Reuters)

Now the garment has become the leading export sector of Cambodia. In January the first quotas was imposed on Cambodian garment export to the US after seine surge in Carmbodian garment to US.

The average monthly salary of a garment worker in Cambodia is $ 40. However this is 30 to 50 higher than in Indonesia.

increased from 157 SME in 1997 to 195 SME, indicating 24 per cent growth. Exports of non-quota items increased by 25 per cent.

The total availability of quotas in 1998 increased by 4.5 per cent with a 3.2 per cent increase in the US quota, 13.3 per cent increase in the EU quota and 7.8 per cent increase in the Canadian quota. The quotas in respect of shirts and blouses, nightwear, underwear, terry and other pile towels, shop towels and fabrics, such as spun cell, woven and poplin, to the USA increased significantly during the year. In the EU market, the availability of quotas, except for men's and boy's woven shirts, increased in 1998. The reduction of quotas in the men's and boy's woven shirt category did not have significant impact on apparel exports because the utilization rate of this category has been below 50 per cent. There were significant increases in the quotas for coats, jackets and rainwear, sleepwear and bath robes and bed sheets to the Canadian market. However, the quota in respect of high value added items such as coats for women and men, dressing gowns and trousers, did not reflect an adequate growth in 1998.

As in the previous year, the rate of utilization of quotas shifted from low value added items to high value added items. The quotas in the US market were fully utilized in respect of some items of coats, men's and boy's non-knit shirts, trousers and dressing gowns. In the Canadian market, the utilization rates were high in the case of quota items of trousers, overalls and shorts. The largest demand for other quota items in 1998 was in the categories of skirts, nightwear, underwear, shop towels and trousers. The utilization rates in respect of low value added items such as pillowcases, dish towels, non-knit shirts and blouses were low, as manufacturers shifted into high value added items. However, the lower utilization rates in respect of parkas, amoral, wind-cheaters and fine suits have been mainly due to the inadequacy of the necessary technology and skills in Sri Lanka to manufacture these items with the required quality at competitive prices.

Quota availability to the USA, the EU and Canada rose by 3 per cent, 13 per cent and 8 per cent respectively, under the flexibility provisions. Accordingly, overall quota availability increased by 5 per cent in 1998. The overall quota utilisation rate remained at around 74 per cent as in the previous year. The utilisation of quotas varied widely across different categories and countries. The under utilisation was partly due to insufficient demand for particular items and local producers used their capacity to produce high value added garments under other quota categories or to produce non quota garments. This was evident from the increased garment exports by the non-quota garment sector, and over utilisation of some popular categories to the USA and Canadian markets. Quota utilisation increased significantly for certain items such as men's and boy's jackets, men's and boy's shirts, women's and girls' coats and dresses, shirts and blouses, women's and girl's suits, and shirts, nightwear, dressing gowns, coats and trousers. To the same market, allocation and utilisation were higher than in 1997 for other items such as skirts and towels. At the same time, even though the quota availability was raised for certain items, utilisation was much lower for those items. The quota utilisation rates for all items to the EU declined, despite the rise in the available quota. With regard to the Canadian quota, only a few categories indicated satisfactory quota utilisation. In spite of the 9 per cent growth recorded in garment exports to quota countries, the share of garment exports under the quota system declined from 63 per cent in 1996 to 62 per cent in 1997. Exports under quota to the USA declined from 88 per cent in1996 to 8.3 per cent in 1997, while quota shares to the EU and Canada remained at 28 per cent and 87 per cent respectively.

Quotas continued to be an important regulator of trade in textiles and garments. Until quotas are fully phased out in 2005 under the Uruguay Round Agreement on Textiles and Clothing, optimal utilisation of quotas needs to be ensured to reap the full potential benefits under the existing framework. Hence, the quota administration needs to be done efficiently. Although market based quota distribution through auctioning of quotas would have other targets. Certain other objectives, such as the need to promote new investments, regionalise industries and generate more employment, have entered into the quota administration in Sri Lanka. Although a fundamental change in the quota allocation system may not be necessary, it should be the responsibility of quota administrators to ensure the smooth functioning of the system, so that the growth of the textiles and garments industry and trade will not be interrupted. This is all the more important as the global competition among suppliers has intensified in the context of depressed world market conditions and there needs to be smooth transition to face more intense competition in a quota-free trading environment after 2005.