ASEAN-US Technical Assistance and Training Facility

Integration of the ASEAN Textile and Apparel Industries in the Post-quota Era

Executive Summary

Photo: Douglas Lucius

January 2006

Presented By
Nathan Associates Inc.
2101 Wilson Blvd., Arlington VA 22201
www.nathaninc.com

EXECUTIVE SUMMARY

Integration of the ASEAN Textile and Apparel Industries in the Post-quota Era

SUBMITTED BY
Nathan Associates Inc.

AUTHORED BY:
Peter Minor
Principal Associate
Nathan Associates Inc.

Donald Feeney
Senior consultant
Werner International

UNDER CONTRACT NO.
PCE-I-28-98-00016-00, Task Order 28
ASEAN-US Technical Assistance & Training Facility

January 2006

NATHAN
ASSOCIATES INC.
www.nathaninc.com

This report was sponsored by the ASEAN–US Technical Assistance & Training Facility, a joint project of the U.S. State Department and U.S. Agency for International Development being implemented by Nathan Associates under Contract No. PCE-I-28-98-00016-00, Task Order 28. The project is advancing the goals of the US ASEAN Cooperation Plan (ACP) and contributes to ASEAN's effort to become a stronger regional institution. The ASEAN-US Facility endeavors to

- Strengthen the Secretariat by increasing its capacity to fulfill its mandate to provide technical input and to facilitate effective decision-making in ASEAN; and
- Enhance ASEAN integration and cooperation consistent with the Vientiane Action Programme.

ASEAN-US Facility activities consist of demand-driven policy studies, assessments, training programs, and other activities. The project runs from October 2004 through December 2007.

For more information or copies of project publications, please contact

Teri Simpson Lojewski
Nathan Associates Inc.
Chief of Party, ASEAN-US Technical Assistance and Training Facility
tlojewski@nathaninc.com

Executive Summary

ASEAN aspires to become a single market and production base by 2020. In November 2004 in pursuit of that goal, ASEAN Member Countries signed the Vientiane Action Programme (VAP). Among other things, the VAP calls for the accelerated integration by 2010 of eleven ASEAN priority sectors, including the textile and apparel products sector. Thus for the textile and apparel products sector, this VAP directive presents a unique opportunity to advance the twin objectives of ASEAN integration and the strategic restructuring of the ASEAN textile and apparel industries.

ASEAN offers a wide range of products and services along the entire textile and apparel supply chain including fibers, fabrics, garments, machinery, design and logistics. ASEAN can meet the challenges that will face its textile and apparel industries over the next ten years and beyond. It can maintain and advance its manufacturing competencies through, for example, training factory managers and supervisors. It can eliminate trade barriers and take advantage of trade opportunities through tariff elimination, trade facilitation, and carefully devised trade agreements. Finally, it can invest in production machinery and engage in explicit and effective trade promotion.

Since the elimination of quotas in the major export markets of the United States and the European Union, the textile and apparel industries have known only one certainty: the next ten years will bring considerable change and competitive pressures will escalate. Sourcing methods, for example, will be simpler and more efficient. Instead of knocking on many doors to find fabrics, accessories, and garment manufacturers, buyers and their agents are seeking "full-package" solutions that allow them to work with fewer suppliers who can provide the full complement of services and products they require and who maintain compliance with labor standards. Companies that used to handle only a part of the garment making process will have to offer a fuller range of services -- design, sample making, material and accessory sourcing, financing and making up. These changes will favor producers who have ready access to a wide range of needed materials and services of the highest quality and cost effectiveness—producers who operate in an integrated supply chain.

Each ASEAN Member Country has strengths and weaknesses in each area of the textile and apparel supply chain. Some Member Countries have cost competitive making up operations while others excel in yarn production and fabric dying and finishing. Still others specialize in logistics, design and marketing. Producers who employ regional rather than only local—isolated—strengths will be in a far better position to defend and advance their market positions in the post-quota era. National and industry leaders seeking to "do it all", by maintaining protection for local industries, risk loosing what they already have in the new competitive era. ASEAN must integrate its supply chain in this priority sector in order to leverage all of its competitive advantages. That integrated supply chain can pay high dividends over many years, not only by sustaining and growing valuable exports, but by employing many of the most disadvantaged in society.

Manufacturing Competencies. The ASEAN region is home to many world-class companies in the textile and apparel industries that have refined their abilities over many years and have earned solid reputations among apparel buyers and agents. Still, they need to boost their efficiency and innovative capacities by training managers and supervisors, especially in apparel firms. Better industrial processes and controls can boost productivity by 10-15 percent in a relatively short period of time. More efficient sampling processes in textile companies can reduce costs and improve service. Apparel companies need new design, management, and marketing skills, while textile companies need to devise new fabrics for niche markets. Many of these needs are common to all ASEAN Member Countries and cooperation among Member Countries could prove very beneficial.

Trade Barriers and Opportunities. Under the ASEAN Free Trade Area (AFTA), which pre-dated the VAP, ASEAN Member Countries have been reducing and eliminating tariffs; but progress has been uneven. The six original ASEAN Member Countries (Brunei, Indonesia, Malaysia, the Philippines Thailand, and Singapore) have cut their intra-ASEAN tariffs on fibers, yarns, fabrics and apparel, and have met their AFTA obligations. Vietnam, Laos and Myanmar have until 2008 to meet their AFTA obligations, but Vietnam has agreed to do so ahead of schedule, by 2006. Cambodia, one of ASEAN's engines of apparel export growth, has until 2010 to meet its tariff-reducing obligations under the AFTA.

Further, AFTA requires ASEAN Member Countries to reduce tariffs to 5 percent or less. It does not require them to eliminate them. Implementing the additional VAP directive to eliminate all remaining tariffs will provide significant gains for the textile and apparel sector. For example, ASEAN materials will clear customs more quickly because elimination of tariffs will eliminate a major cause of customs delay—clarification of product classifications for revenue collection. While most ASEAN Member Countries have promised to eliminate all but a handful of tariffs on textile and apparel products by 2010, Cambodia, the Philippines, and Vietnam have exempted a significant number of tariff lines from elimination. Exempting these tariffs from elimination allows a troublesome barrier in the supply chains of some of ASEAN's most dynamic apparel exporters to continue. These exemptions thus pose a threat

to the successful integration of ASEAN's textile and apparel sector and to its chances for competing successfully in the global market. Eliminating tariffs will improve ASEAN market and production integration, and the competitiveness of domestic producers n the ASEAN market. Many apparel producers in the region, however, operate under special tax regimes, such as free trade zones and bonded warehouses, so ASEAN must do more than eliminate tariffs to facilitate the rapid flow of goods. Standardizing and implementing regional electronic pre-arrival documentation, for example, could make customs procedures more predictable, facilitate financing and help make intraregional supply chains more rapid and reliable.

Preferential trade arrangements, such as the EU GSP program, and free trade agreements, such as ASEAN's regional trade initiatives with China, India, Japan and Korea, can be the catalyst for rapidly increasing the volume of materials traded between ASEAN Member Countries. Great care must to be taken to ensure that the rules of trade negotiated for such arrangements enable and encourage the integration of the regional textile and apparel industries. Most important, rules of origin and cumulation of origin among Member Countries must be reviewed to ensure that they permit full leveraging of regional strengths and industry integration.

Today, intra-industry trade in ASEAN accounts for only about 10 percent of ASEAN imports of fabrics and yarns. This level of trade is not sufficient to encourage the creation in ASEAN of services that will be essential to a globally competitive, integrated ASEAN textile and apparel products sector – services like dedicated ASEAN sales agents and brokers with comprehensive knowledge of ASEAN producers and their products. Increasing the volume of intraregional trade could thus have a dynamic effect on the sector's competitiveness since higher volumes of intra-ASEAN trade would lead to improved regional trade services, such as dedicated sales agents and brokers.

Investment and Trade Promotion. New investment is needed to maintain and advance the competitiveness of the regional textile supply chain. Machinery older than seven to ten years, for example, will be hard pressed to meet the quality and cost standards of modern textile machinery, especially weaving looms. Investment in new textile machinery in ASEAN has been at historically low levels since the Asian financial crisis of 1997–1998. Some ASEAN Member Countries, such as Thailand and Vietnam, have started increasing their investment in new equipment, but ASEAN still lags significantly behind the major East Asian producers (China, Hong Kong, Taiwan, Korea). In 2004 for example, ASEAN producers augmented or replaced less than 1 percent of their stock of shuttle–less looms while East Asian (China, Hong Kong, Taiwan, Korea) producers augmented or replaced stock at a rate of nearly 10 percent.

Similary, if ASEAN producers are to take advantage of new supply chain relationships, intraregional trade must not only be encouraged through elimination of tariffs, trade facilitation and customs improvements, and carefully crafted trade agreements; it must also be explicitly and aggressively promoted. Textile trade among ASEAN countries is modest but

growing. ASEAN's biggest trade promotion expo, held annually in Hong Kong, brings together ASEAN producers to form partnerships; but more sustained promotion and market linkage-building is needed, perhaps in the form of geographic hubs in Malaysia, Singapore and Thailand.

What then should ASEAN members do to ensure that the region's resources are marshaled to compete with large integrated producers such as those in China, India and Pakistan? Industry and government should coordinate in

- Advancing technical and managerial training to boost and maintain ASEAN's manufacturing competencies;
- Implementing and accelerating programs called for under the VAP such as tariff elimination (which would necessarily include eliminating products on exclusion lists) and advancement of key customs practices (e.g. the green lane and electronic documentation) as soon as possible -- before the January 1, 2010 target;
- Ensuring that regional trade agreements encourage regional strengths rather than only bilateral relationships in new markets;
- Addressing issues discouraging investment in new textile machinery, which has lagged because of the waning confidence of financial institutions and high local interest rates; and
- Creating trade promotion hubs in key locations to promote the use of regional fabrics and materials.

No single action will ensure the strategic success of ASEAN's textile and apparel industries or the VAP. With nearly US$20 billion in regional exports and millions of jobs for some of the most disadvantaged in society at stake, however, the region cannot afford to neglect the integration of ASEAN's textile and apparel markets and their industry supply chains.