Looking beyond Export Gains:
Human development linkages in garment industry of Asian LDCs

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For years, the textile and clothing industry has contributed a great deal to drive the economies of many developing countries in Asia. A nearly 40-year-old quota-based trade helped small developing countries to establish the industry, expand production and obtain access to major markets. The industry provided jobs to millions, most of them women, and generated foreign currency earnings and export revenue, which would not have been possible otherwise.

When the WTO Agreement on Textiles and Clothing (ATC) was fully implemented in January 2005, it was feared that less competitive exporters such as the least developed countries (LDCs) might lose out against global competition. Expected outcomes were factory closures and job losses as well as lower wages and longer working hours that would be required to meet lower prices and shorter lead time. These concerns were not foreign to Asian LDCs, e.g., Bangladesh, Cambodia, Lao PDR and Nepal, where export-oriented garment industry was significant.

Trade gains for some LDCs, but....

Contrary to such pessimistic expectations, export data illustrates the growth of ready-made garment (RMG) exports from Bangladesh, Cambodia and Lao PDR. Nepal's RMG exports, which experienced a dip in 2001-2002, returned to a downward trend after the ATC expiry (Table 1). Temporary quantitative restrictions (safeguards) imposed on Chinese products by the United States and EU in late 2005 provided a few years of breathing space for these countries to stay in the competition but fears remain. The EU removed the safeguards at the end of 2007, and the US action will follow in 2008.

Moreover, more than 90 percent of the RMG products from these four Asian LDCs are shipped to the United States and the EU. A lack of market diversity makes these countries vulnerable to any changes in trade preferences in the two markets. The RMG share of total exports is considerably large for Bangladesh and Cambodia, 75 and 78 percent respectively in 2006. The share of RMG in total exports dropped in Lao PDR due to the good performance of non-RMG export sectors, e.g., minerals and mineral fuels. On the other hand, the RMG share of total exports in Nepal, which was more than 30 percent in 1993-1994 fiscal year (SAWTEE and AAN 2007), declined as RMG exports fell. Any shocks to the RMG industry could potentially affect the development process of these LDCs, especially Bangladesh and Cambodia.

Table 1: RMG Exports, US and EU market and RMG Share of Total Exports.

		Bangladesh	Cambodia	Lao PDR	Nepal
RMG exports in US$ million	2004	6,296[1]	1,981[1]	99	103 (2002)
	2005	7,751[1]	2,193[1]	108	91
	2006	7,901	2,675[1]	126	88
US & EU market share (%)		94.0[2]	90.0	92.6	89.3
RMGs as % of Total Exports		75.1	78.0	14.4	11.7

Source: Raihan et al. (2007), [1]WTO Statistical Database, [2] Razzaque (2005),

Human development linkages

The RMG production process is labour-intensive in nature; the industry has created millions jobs in developing countries, especially for young women with limited education attainment. In Bangladesh, Cambodia and Lao PDR, the number of workers increased as the production and export grew in the post-ATC years (Table 2). Women account for 80-85 percent of the RMG workforce in those countries.

For the majority of workers, this is their first paid job. One should not ignore rough work environment including low pay and long-working hours; but the industry is important as it provides regular income to women, many of whom would otherwise still be excluded from participating in the formal economy. The job in the RMG industry has become a vital component for the family's financial security in developing countries as the majority of the workers remit a significant proportion of their salary to their families in rural areas. Remittances are used to buy necessities, pay education fees for RMG worker's siblings and/or children, invest in agricultural inputs, and construct or renovate the house, among others.

The number of indirect jobs created by the RMG industry is also important. In Cambodia it is estimated that one job in the RMG industry creates another indirect job in the economy as the demand for housing, services, dining, and transportation arise.

Little evidence on human gains in the post-ATC

Has trade liberalization in this industry had positive impacts on human development? Human gains were minimal in the post-ATC experiences of the four LDCs.

Employment

A drastic reduction in employment was confirmed in Nepal (Table 2) as the removal of quota systems affected its RMG exports negatively. Consequently, a number of factories closed down or cut down the operations. Sixty percent of the former RMG workers surveyed in Nepal in 2006 reported that they lost their jobs after the ATC, mainly due to factory closures. About 82 percent of the former workers surveyed did not find an alternative job immediately after leaving the RMG industry; 29 percent remained unemployed for 1-2 years. As Nepal's RMG industry is dominated by male workers, more men than women lost their jobs in terms of the numbers of persons. However, former female RMG workers have been unemployed for longer periods than

Table 2: Employment and Work Conditions in RMG Industry

		Bangladesh	Cambodia	Lao PDR	Nepal
No .of Workers	2004	2,000,000	250,000	26,000	18,134 (2001)
	2005-2006	2,200,000	270,000	28,000	4,450
Female share of RMG workers (%)		80.0	85.0	80.0	45.0
Ave. Monthly Salary (Min. W)		$57 (2007)[1]	$73 ($45)	$41 ($26)	$76
% of Workers with Contract		n/a	40 %	n/a	11 %

Note: Figures above, unless specified, are from the surveys in 2006. Source: EIC (2007), NSC (2007), SAWTEE and AAN (2007). [1]Authors' calculation based on the data from Bangladesh Bureau of Statistics (2007).

male counterparts; 29 percent of men and 47 percent of women surveyed are still unemployed at the time of the survey in 2006. Lower educational attainment by women, lack of skills (in both RMG and other sectors), and economic and social discrimination against women in the society may explain the gender gap. Among RMG workers currently working, the majority did not have a contract at the time of the survey. This makes workers more vulnerable to downturn of the production cycle and creates job insecurity.

Income

Sixty-four percent of the former RMG workers surveyed in Nepal claimed a fall in income after leaving the RMG industry. The level of income is not sufficient for most of the current RMG workers to meet their basic needs even in countries with a rapid growth of RMG exports. The basic salary for RMG workers was fixed at US$45 per month as minimum wage in Cambodia and about US$26 per month in Lao PDR at the time of survey in 2006 (Table 2). With overtime pay and other benefits, the average monthly salary for the Cambodian RMG workers was US$73 and US$41 for Lao workers. About 90 percent of Cambodian and 56 percent of Nepali workers surveyed responded that their basic salary was not sufficient for their daily needs. Moreover, high inflation triggered by price hikes of petroleum and staple food contributed to deterioration in their real wages. Overall, the majority of workers surveyed were satisfied with their current jobs but a significant share of workers complained about their low wage.

Bangladesh's legal minimum wage was probably the lowest in the region, about US$16 per month, as it had not changed since 1994. The wage commission recommended raising the minimum wage to about US$24 in 2007. As for Cambodia, the minimum wage was increased to US$50 per month in 2007 and recently a US$6 allowance raise was instituted to compliment monthly salary (ILO and BFC 2008). Although legal wage hikes is a welcomed trend, the wage hikes barely offset the inflation shocks.

The survey found RMG workers spend average 50-60 percent of their income on the basic necessities; food, housing, and clothing. Remittance accounts for 10-20 percent of their income. In order to cope with real wage loss, the former RMG workers in Nepal cut their savings, expenditures in entertainment and remittances. Some limit their spending on food. Without an appropriate compensation mechanism, lower consumption of food worsens worker's health whereas lower amounts of remittances are likely to bring deterioration in human development, especially among rural populations. Further deterioration in real wages put both workers' and their family members' well-being at risk.

Health

Garment worker's poor health conditions are well documented. With the implementation of codes of conduct and stricter labour standards, T&C industry/firms are making efforts. Yet many workers are still experiencing health problems after being in the industry for several years. The causes behind workers' poor health conditions vary, but one is the long working hours endured in order to meet 'just-in-time' delivery. Despite potential health risks, RMG workers are willing to work overtime, or often they do not have a choice because they are required in order to meet the targets when more orders come in. Too often, their basic salary is too low to meet their daily needs, hence their 'willingness' to take on overtime increases. In addition to the 8 regular working hours, 2-4 hours overtime is common among RMG workers, and they usually work 6 days a week. With these conditions, many workers reported problems of back pain and eye-sight strain.

Access to health care services is a big issue in developing countries because universal health care is rare among developing countries. Many firms have First Aid or small clinics in the factories, but most workers must pay for serious injuries caused during the shifts, with potential huge costs, especially if they do not have medical insurance or other social benefits to cover them. In Lao PDR, all factories surveyed claimed that they covered 100 percent of the medical expenses for initial treatments. However, in case of long-term work-related injuries, the financial burden for treatment fell under the social security scheme. In the case of Lao PDR, the RMG firm's contribution to workers' social security has increased by 16 percent from 2004 to 2005; yet only 73 percent of RMG factories surveyed are participating in social welfare benefit programs for their employees. Cases of the RMG industry mentioned above are relatively organized.

Given the barriers for women to enter the labour force, including their responsibilities at home and in society which is shaped by the gender division of labour, informal wage employment is dominated by women. Since labour protections such as minimum wage legislation often do not apply to informal workers, the negative impacts of the ATC expiry – e.g., the low wages vis-à-vis inflation rates – will more severely affect informal workers in the region.

Implication of the removal of safeguards on China

The socio-economic conditions of Bangladesh, Cambodia and Lao PDR did not deteriorate much as expected, partly due to the safeguards which were imposed on Chinese T&C products in late 2005. Yet, this is a temporary quantitative restriction mechanism. The EU removed it at the end of 2007, and the United States is planning the same at the end of this year.

When the safeguards on China are completely removed, there would be undisputed consequences on the four Asian LDCs as well as other developing countries. Simulation assumes a scenario of no quantitative restriction on T&C export. The results are devastating. Bangladesh is likely to suffer the most in absolute terms. The export of RMG from Bangladesh to the US and EU markets will decline by US$215 million and US$178 million respectively. This will lead to a welfare loss of US$486 million. For Cambodia, the RMG export loss was estimated to US$90 million in the US market and to US$21 million in the EU market, resulting in the welfare loss of US$94 million. Export loss for Lao PDR was estimated to US$30 million in the EU market where 90 percent of the Lao RMG products were sold. Welfare loss was also severe with estimation of US$37 million. With a full removal of the safeguards on Chinese products, Nepal would lose US$14 million and US$6 million in the US and EU market respectively. The country's welfare loss was also high at US$25 million. As a result of these losses, workers in the four countries will face wage cuts and job losses.

Policy options for Asian LDCs

So what can these Asian LDCs do to overcome the challenges in the post-ATC era? There are a number of demand- and supply-side constraints that these LDCs have in common. Overcoming the constraints will be critical to remain in global competition so as to keep employment and the level of labour compensation high.

Demand for duty-free quota-free market access

The US tariffs on T&C products appear to be the most severe constraint for the Asian LDCs. The United States has provided preferential market access opportunities to 34 African LDCs and a large number of non-LDCs, mainly in the Americas, but none to the Asian LDCs. Therefore, RMG exports from Bangladesh, Cambodia, Lao PDR and Nepal are subjected to the full US most favoured nation (MFN) tariff rates. In the case of Bangladesh, more than 40 percent of the US MFN tariff rates on T&C products across the Harmonised Tariff Schedule (HTS) at the 8-digit level are 15 percent or higher whereas the share for the rest of the world is only 18 percent. That is, Bangladesh's products face higher tariff rates than the average tariff rates of other countries. Average tariffs on T&C exports ranging from 15 to 20 percent apply to Cambodia. Similarly, Lao PDR, under Normal Trade Relation in 2005, are also subjected to the average of 12.5 percent for export to the US market. As for Nepal, among selected top apparel items exported to the United States, the highest applied rate is 19.7 percent, with a simple average across all products of 11.3 percent.

At the sixth Ministerial Conference of the WTO in Hong Kong in December 2005, developed Members agreed to provide duty-free quota-free (DFQF) market access to 97 percent of the products originating from the LDCs. However, there are concerns that such provision would not help the LDCs much because their exports to the US market are heavily concentrated in T&C products, which may be excluded from the 'covered list' as the importing countries have the discretion to exclude 3 percent of the import tariff lines from such treatment.

Therefore, DFQF market access for the LDCs in developed countries, especially in the US market, is crucial. Estimated gains for Bangladesh, Cambodia, Lao PDR and Nepal under the scenario of a full DFQF market access in the United States are increased exports by US$559 million, US$626 million, US$6.3 million and US$5.9 million respectively. The export gains for Lao PDR and Nepal are smaller than the others due to their small market shares; however, they are sizeable in terms of percentage share in their total exports.

Export growth will provide additional employment in the RMG industry. For Bangladesh, by assuming that 70 percent of the increased export will be in woven RMG products, an export growth will create 180,000 new jobs. Similarly, an additional 77,000 people will be absorbed by the RMG industry in Cambodia, representing 29 percent of total employment in the industry in 2005. Additionally, around 69,000 indirect jobs will be created in the supporting industries. As for Lao PDR, the number of RMG workers could rise to 35,280, representing a 31 percent increase over the number of workers in 2005.

Demand for the EU Flexible Rules of Origin

When it comes to the EU market, the four LDCs remain strong as the EU has offered preferential treatment to them under the Everything But Arms (EBA) initiative. However, to qualify for the EU treatment, LDCs have to comply with the rules of origin (ROO) by meeting criteria that at least two stages of production process take place in the exporting countries. In all the four countries domestic supply capacity of fabrics and other accessories are still low. Therefore, obtaining preferential treatment from the EU is rather difficult. The situation could get worse since the safeguards on China's T&C products have been lifted and as ROO will continue to act as a binding constraint on the expansion of the LDC exports due to lack of backward linkage.

The simulation estimated that full relaxation of ROO by the EU, even though this might not be realistic scenario, could increase RMG exports of Cambodia and Nepal by US$36 million and US$24.5 million respectively.

A more realistic alternative is to request the EU to simplify its ROO that is similar to Canada ROO, which requires a 25 percent domestic value addition by LDCs to gain zero-tariff access. Another unique feature of Canada ROO is an extremely liberal accumulation mechanism, which allows the LDCs to source raw materials from Canada or any other developing country. Relaxation of ROO criteria would benefit Asian LDCs a great deal and give another stimulus to their RMG sector in the post-ATC years.

Overcoming supply-side constraints

Long lead time is troublesome for the Asian LDCs. Presently, the average lead time for an export consignment in the case of Bangladesh and Cambodia varies between 90 and 120 days whereas the lead time for Lao PDR is 70 days. An envisaged ideal situation is 30 to 45 days. Nepal has the longest lead time among the four Asian LDCs due to its geographical location and far sea port (660 miles away from Nepal). Since the four countries depend on imported raw materials, long lead time proves to be ineffective for production and incurs high costs for exporters.

Part of the problems in long lead time are poor inland transportation, weak physical infrastructure for roads, ports, utilities and telecommunication, and other services, which incur costs for exporters in these countries. For instance, high electricity and water prices are the bottleneck for many T&C producers. Unreliability of the services provided is another setback for the Asian LDCs. Bureaucracy in export processing and inefficient custom services result in unofficial fees and high cost. Increased public investment and private sector participation can help address this constraint.

Easy access to finance is necessary to enable T&C firms to undertake productive investments for initiating or expanding a business. Effective government policies, including the easing of restrictions on the provision of formal credit, need to be in place to facilitate better access to capital and technology.

Shortage of a skilled workforce is perceived to be a major constraint on the production of high value-added RMG products in these countries. This would bring about low productivity for the industry, which is a crucial element of competitiveness. Significant parts of RMGs from these LDCs comprise very low domestic value addition due to lack of backward linkages and skilled workers. Most workers in this sector are illiterate or only with primary or secondary education. Public investment in basic education as well as vocational training is another important tool to boost the high productivity in the industry.

RMG industry is important in all four Asian LDCs for export earnings, economic growth, and employment generation. The countries need to diversify their products to higher value added products as well as markets to reduce vulnerability to changes in export volume of RMG products. Appropriate strategies with maximum support from the governments and private sector participation are important to mitigate the negative impacts of any external shock to the sector and enhance competitiveness of the industry and labour productivities for sustainable human development.

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