IV. THE EFFECTS OF RESTRICTIONS ON LDCs

65. The MFA declares that "a principal aim of this Arrangement shall be to further the economic and social development of developing countries and secure a substantial increase in their export earnings from textile products and to provide scope for a greater share for them in world trade in these products" (Article 1.3). In considering questions of "market disruption" (Annex A) "account shall be taken of the interests of the exporting country, especially in regard to its stage of development, the importance of the textile sector to the economy, the employment situation, overall balance of trade in textiles, trade balance with the importing country concerned and overall balance of payments", and efforts shall be taken to ensure "the avoidance of disruptive effects in individual markets and on individual lines of production in both importing and exporting countries" (Article 1.2).

Benefits of Textile and Clothing Exports to LDCs

66. The benefits to ldcs from being able to increase their export earnings from textiles and clothing should be self- evident, but perhaps need restating since there has grown up in Western countries a critique of development strategies which rely on a substantial labour intensive manufacturing export sector. These criticisms usually represent a somewhat odd fusion of special pleading by Western textile manufacturers and unions and Marxist or 'dependency' development theorists, to the effect that protection in dcs safeguards not only the interests of Western workers (and manufacturers) but also the people of ldcs who would be better served by 'self-reliance', and 'freedom' from 'dependence' on trade, transnational corporations etc. To this there are various replies. First, the majority of ldc members of the MFA are not 'export-orientated' ldcs in the Korean/ Taiwan mould. They include countries with a large variety of size, economic structure and guiding ideology - from Romania to Hong Kong, from Communist China to Uruguay - which nonetheless have a common interest in the expansion of their export earnings (and therefore import capacity) and employment opportunities. Second, it is true that the bulk of textile and clothing exports by value do originate in the small number of 'export orientated' ldcs (Korea, Taiwan, Hong Kong), but the development experience of these countries (especially the two former since they have large agricultural sectors) is both relevant and encouraging for others. Other ldcs - the ASEAN countries, Sri Lanka, and in varying degrees most others - have moved in the same direction with generally favourable results. Third,

Western dominated agencies like the IMF are urging upon their ldc clients (often making it a condition for assistance) that they adopt exchange rate and export promotion policies to facilitate manufactured exports, including textiles - on the grounds that such policies make economic sense.

67. The most tangible benefit derived by ldcs is in terms of employment. This is partly because clothing, especially, is a, relatively, very labour intensive industry but also because a given quantity of output will generate more employment than in dcs where less labour intensive methods are employed (including the use of less ancillary staff). An OECD survey suggests that a spinning or weaving mill in India or Korea will typically have around twice as many workers per unit of output as a comparable establishment in the US or Germany, and rather more in the Indian than the Korean case.[28] Where handloom textiles are considered, the labour intensity is, naturally, greater: perhaps ten times that in the mill sector and three times that in powerlooms (in respect of output - the labour intensity with respect to capital is vastly greater).

Effect of Restrictions

68. The effect of restrictions on exporters clearly varies depending upon (inter alia) the importance of clothing and textiles in the economy, on the stage of overall development, on the severity of restrictions and the capacity of the industry to adjust to changing quota and market conditions. Tables 21 and 22 try to capture the main features of textiles and clothing exports in relation to the various ldc economies. There are countries which are major net exporters of both textiles and clothing (Korea, Taiwan, India and Thailand), others which are predominantly textile exporters (Brazil, Pakistan, Egypt and Turkey), and others which export clothing incorporating imported fabrics (Hong Kong, Philippines, Singapore, most of the newer exporters such as Sri Lanka and Indonesia and others engaged in offshore processing - Tunisia, Malta and Cyprus). It is also possible to classify countries in terms of the importance of the textiles and clothing industries in relation to manufacturing as a whole (it is particularly high in Hong Kong and to a lesser degree in low income ldcs; Pakistan , Egypt and India) and of exports in relation to production and overall exports (both high in Hong Kong, Taiwan and Korea and to a lesser extent in India and Pakistan). These differences are reflected in the classification below.

(1) Major NIC Suppliers

69. Three countries - Hong Kong, Taiwan and Korea - are regularly separated out for special treatment as 'major suppliers'. This is done explicitly for Hong Kong, Taiwan and Korea in the US while the EEC and other importing countries have adopted particularly restrictive measures for these countries. Thus, in the US, partly as a result of measures taken in 1979, exports in that year from these three countries were lower than in any year since 1975 and little higher than in 1972. In exports to the EEC, Hong Kong, despite having perhaps the most adaptable industry of all the exporters, could only register 2.2% real growth p.a. in the 1976-79 period (see Table 23). The concern of these countries (and we are here primarily concerned with Hong Kong) is that since exports of textiles and clothing form such a large component of national economic activity, any sharp slow down in permitted exports could have serious repercussions for the economy as a whole. Exports form 75% of the output of Hong Kong's textile and clothing industries, while the industry accounts for 36% of all exports(1979) and employs 42% (1979) of the colony's labour force. There appears to have been a sharp slow down in growth in 1980 and 1981 after a succession of years in which quite spectacular growth had been recorded (from 17% in 1976 to 7% in 1979). The combination of restrictions on textile and clothing exports and a large influx of Vietnamese and Chinese refugees represent a considerable problem in the near future.

70. However, restrictions are not without some compensating benefits for this group of countries. First, there is a scarcity rent to exporters. Since Hong Kong's products usually face demand in excess of permitted exports under quota, the premium is particularly large. This was measured in 1976 at 15 to 25% of restrained textile export value, or at least 4% of Hong Kong's GDP (though 'rent' will fluctuate with demand and could even be negative in a recession year).[29] While 'rent' can be seen as a national gain for the economy - turning the terms of trade in its favour - it does have disadvantages: engendering amongst businessmen a speculative rather than productive motivation; widening income maldistribution in favour of manufacturers (and quota speculators) and against workers whose real wages are affected by a standstill or decline in export volume. Second, there is a strong incentive to move 'upmarket' into higher quality lines within quota categories and to specialised products for which protection is less of a threat. Such a move is particularly appropriate in Hong Kong which is seeking successfully to establish a reputation for quality fabrics and

fashionable product design. Third, restrictions intensify pressure on these economies to diversify out of clothing (in particular) and textiles into more capital intensive industries (heavy engineering, steel, chemicals and cars in Korea and, to a degree, in Taiwan), more income elastic, and technologically sophisticated industries (electronics, in each of the countries), and traded services. Rising wage costs are, in any event, promoting the relocation of clothing production to lower labour cost economies in Asia. Restrictions on exports, while they may affect the smoothness of this adjustment, should not fundamentally alter the long term economic prospects of these countries - though Hong Kong is likely to have an ability to supply quality textiles and clothing for a long time, quotas permitting, and is currently more specialised, and therefore, vulnerable.

(2) Small Suppliers

71. At the other extreme are suppliers whose exports, usually of clothing, are at present so minor in relation to world trade that one might question why they are affected by controls at all. At first sight, the MFA has some attractions for small suppliers whose position is recognised within it in general terms, and several of which were drawn into exporting in the first place by companies seeking to escape from quota control in major suppliers (eg Hong Kong businessmen setting up in Sri Lanka and Mauritius). This is in addition to several new suppliers which have benefitted from offshore processing (OP) trade - Malta, Tunisia and Cyprus - though in those cases geographical proximity and the special preferential access offered by the EEC to Mediterranean countries are important considerations. But the benefits of being small suppliers - reflected in spectacular growth rates rendered by Sri Lanka and Indonesia in the first two or three years of exporting - have now been curtailed by quota action, long before the countries concerned were exporting substantial quantities. These restrictions threaten severely to limit the development possibilities of potential textile and clothing exporting countries.

72. Of the Commonwealth small suppliers, Sri Lanka has had considerable difficulties as a result of quotas imposed in the EEC, the US, Canada and Sweden. The EEC imposed a quota limit in 1978 on five items of approximately 11mn pieces (in a four year agreement) and the US imposed a one year restriction of 17.5mn pieces covering 7 items. With roughly half of exports going to these countries, the quotas amounted to less than half of the 1978 capacity of the Free Trade Zone (quite apart from the substantial

industry outside it) and a small fraction of that originally planned (over 500 mn pieces capacity, some of it under construction). Hitherto, garment exports played a useful role in lifting Sri Lanka's hitherto unimpressive export growth; garment exports rose in value from $3.3 mn in 1975 to $70.8 mn in 1979 (almost half of the total export increment). Export growth, in turn, contributed much to improved overall economic growth. The Sri Lankan economic revival is now threatened by severe external financing problems, with a current account deficit of $125mn (1978) likely to have risen to $695 mn in 1980 (official estimate; some estimates are closer to $1,013 mn) and expected to rise officially to $815 mn in 1984. Even these future projections are based on fairly optimistic assumptions about export growth. If these are frustrated, as they may now be, the external prospects of Sri Lanka are not bright.

73. <u>Mauritius</u> provides a similar story on a small scale. After a long period of stagnation caused by almost total dependence on sugar, Mauritius emerged, in the 1970s, into a period of impressive economic growth (over 7% in the 1970s). One factor in this success was diversification, particularly into manufactures for export. By 1977/78 an export processing zone accounted for 20% of exports, with textiles well to the fore. Mauritius has, however, now been hit by textile restrictions in the EEC despite the provision within the Lomé convention of free access (subject to safeguards). The French held up shipments of knitwear at port, by administrative means, in 1979 until the seasonal peak was past, and then introduced quotas. Action by the UK led to agreed quotas for 1980, 25% below previous shipment levels. Both countries have quotas or informal understandings on mixed fibre garments also. The effects of a slow down in exports of non-traditional items are serious for an economy otherwise dependent on one product, sugar, which faced a depressed world market and little opportunities for volume expansion. There is a backlog of 30,000 unemployed in a population of under 1 million with 10,000 entrants to the labour market every year. Only the employment opportunities in manufacturing have hitherto kept the problem manageable.

74. A similar situation to that now faced by Mauritius would face any Commonwealth ACP country trying to export to the EEC. The EEC has sought, so far unsuccessfully, to incorporate an ACP global ceiling into its larger global ceilings. Though this has been resisted, it is clear that action will in any event, be taken bilaterally. Similar restrictions would

face other potential suppliers, such as Bangladesh - which has been served notice by the EEC in the form of a bilateral agreement - although for that country, with its immense problems of surplus labour and serious external imbalance, the possibility of manufactured exports is one of the few options available of reducing dependence on foreign aid. (Bangladesh's Plan suggests that by 1985, even with an optimistic 11% growth in non-traditional exports, projected imports will exceed exports by \$3.44 bn. to \$1.07 bn., and the current account deficit will increase to over \$2bn.). Although problems for small suppliers have so far mainly concerned the EEC, the US has been more accommodating towards small suppliers in the Caribbean and Central America (possibly for strategic reasons) but the existence of a consultative agreement with Jamaica, and quotas for Haiti and the Dominican Republic suggest only limited flexibility in this respect.

(3) Major Low Income, Expanding, Producers

75. The third category of countries is perhaps the most seriously affected by the prospect of serious restraint. These are ldcs with relatively low incomes, a clear long term comparative advantage in the most labour intensive forms of production and with substantial experience already in exporting. India is the main Commonwealth country in this category. India has in the past seemingly been fairly tolerant of quotas on its relatively uncompetitive cotton textile goods (in 1980, only 60% of its piece goods quotas were used and, in the US, only 22%). But the effects on India of the MFA system have recently changed for the worse, for several reasons. First, as India has started to realise its comparative advantage in labour intensive garments production, it has been constrained by quotas on women's blouses, skirts and men's shirts. Moreover, as it has diversified, it has been caught - by the EEC - in the 'basket extractor', more times than any ldc except the Philippines. Second India has, uniquely, a well developed handloom sector whose fabrics form an important input to the garment industry, generating hundreds of thousands of jobs. The treatment in practice of handlooms under the MFA has been a serious problem for India. Third, India faces a growing problem of external disequilibrium having weathered the first oil crisis reasonably well; a trade deficit of \$6.6 bn in 1980/81 - which is not sustainable for more than a few years without improbable levels of aid and of other external resource flows - could well widen even further, necessitating a more intense effort to develop exports.

(4) Middle Income LDCs

76. The final group is something of a mixed bag. It includes the Communist bloc countries, the Latin American and some of the Mediterranean countries. In the long term, most are unlikely to be able to compete on price with the really poor ldcs for standard items or with the specialised exporters (like Hong Kong or Italy) on items of fashion. But, in the short run, clothing exports (and less frequently, textiles) are a useful source of foreign exchange and of diversification. Singapore's exports are now beginning to decline, less because of quotas than because of high wages causing a structural shift in the economy. Malaysia has greater cause for concern. Despite its relatively high per capita income Malaysia is heavily dependent on commodities for export. Manufactures have played a growing role, and textiles and clothing firms, based on Export Processing Zones, succeeded in increasing exports from M$52mn in 1971 to M$452mn in 1978 making a useful contribution to overall growth. This growth has now largely been capped by quotas in the main markets.

77. There is a different problem for some of the Mediterranean suppliers, Malta and Cyprus (and also Portugal and Tunisia). These use a high proportion of EEC fabrics in clothing exports, either formally under OP provisions, or independently of them. It should be easier for the importing country to accept such trade without restrictions, though there has been pressure from clothing interests to curb it. Where action has been taken (with Malta for example) this is particularly damaging for exporters since they are largely tied to specific markets.

Conclusions

78. A few general points can be made about the consequences of textile protection for ldcs in general quite apart from the effect on specific countries. First the system introduces extreme rigidity into an international market which should be characterised by flexibility. As a result, emerging trends in both comparative advantage and disadvantage, as between specific products and as between textiles, clothing and the rest of the economy, are stifled. Restrictions inevitably fall mainly on the marginal entrepreneur who is seeking to become established. Tighter restrictions - and the threat of others - are a major disincentive to his taking risk investing over and above those already inherent in the trade. Second, administrative controls introduce, inevitably, possibilities for cartelisation

amongst existing exporters, favouritism in the award of export licences, corruption and speculative hoarding of quotas, all of which are damaging to the development of sensible industrial and trade policies and demoralising for efficient and competitive businesses. Third, the removal of much competition from international markets, as it affects MFA suppliers, removes for most newcomers to textile or clothing exports the vital element of 'learning by doing' - that of being forced to adapt to design and consumer taste and price competition through productivity improvement - which was available to major MFA suppliers as they become established and still is to dcs.