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EXPORT COMPETITIVENESS OF INDIA'S APPAREL SECTOR – A STUDY ON IMPACT OF GSP ON INDIAN APPAREL SECTOR

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ABSTRACT

It is to be noted that according to the Apparel Export Promotion Council (AEPC), India ranks 6th in the Global Apparel export market. As of 2018-19 the export of garments stood at US$ 16.2 billion. This sector is the second largest employer after agriculture in India and it employs around 12.9 million workers. This has been possible because India is the largest producer of cotton in the world and has a strong base for manufacture of raw materials needed for apparel manufacturing.

Focusing on the export competitiveness, various studies indicate that India's apparel exports faces intense competitions from countries like Vietnam, Bangladesh and Turkey. One of the primary reasons for this is the impact of Generalized Scheme of Preferences (GSP) on Indian apparel exports. Vietnam and Bangladesh enjoy preferential tax and duty treatments in major import markets like the US and EU. We will take various matters, agreements and policies into consideration for our research. Based on these factors, we aim at recommending how to design fully comprehensive policies that will enhance the export competitiveness and efficiency of this sector and provide greater market access to Indian apparel exporters for the sector's growth and employment creation.

KEYWORDS - COMPREHENSIVE, COMPETITIVENESS, EFFICIENCY, PREFERENTIAL.

INTRODUCTION

United States and European Union have always been the World's major apparel importers accounting for 60% of the total global imports. Indian Apparel industry can be classified into 2 primary segments: (i) Consumption within the nation and (ii) Exports outside the nation. Data regarding the exports are readily available whereas the data regarding internal consumption is not available. In the domestic market the demand varies substantially, major contribution is from the men's wear segment which contributes 41%, women's wear contributes 38% and 21% from the kids wear section. Also India has been able to maintain trade surplus among other supplier nations and imports are lower than exports. The Multi Fiber Agreement helped India to increase its exports from the beginning of 2005.It's also been noticed that India's apparel and textile exports grew at a CAGR of 5.7% starting from $ 10.7 billion in the year FY10 to $16.7 billion in FY 18. But in the year 2017 – 2018 Indian apparel exports reduced primarily due to the implementation of GST and also due to the competition from countries like China,

Bangladesh and Vietnam. It’s also noticed that this growth is confronted by many challenges such as lower infrastructure in the country, locational barriers and proposed withdrawal of GSP (Generalized System of Preferences) by US who allow various countries to diversify their business with the United States by eliminating duties on a number of products.
India has an advantage over Bangladesh and Vietnam in terms of raw materials and labor. We always compare and try to be competitive with China but due to strict laws and regulations we are not able to be competent enough. Therefore, there is a need to study this industry and understand the intricacies faced by the Indian Textiles and Apparel sector. Raw materials, advanced technology and labor have made it easy for Cotton Production and Fabric.

Major Impact of GSP on Indian Exports:

India mainly exports apparels, machinery, vehicles, articles of iron or steel, plastics, organic chemicals under the GSP regime and mainly all of this fall under the ‘Industrial Supplies’ to the US and withdrawal of this benefit from India can create increase in cost of production by the domestic industries in the US. Intention here by US is that they will be using “Substitution effect” in importing apparels from least developed countries like the Vietnam, Bangladesh etc and due to this India will significantly be losing business in the overseas market.
India is waiting for withdrawal of GSP on Indian apparel exports and is in continuous negotiations with the US. It has been viewed that this setback to India is more of a diplomatic one rather than economic. From the short run perspective it’s time for Indian policy makers and the customs department to manage custom duties on foreign imports and easing regulations on overseas companies which helps them to conduct business in India. From the long term perspective it’s beneficial to India as they can improve their foreign investment and trade policies and it’s a reminder to the Indian Government that short term benefits are always not compatible with the long term goals of the developing countries.

Impact of withdrawal of GSP in Indian exports:

As of 2017, India was a major beneficiary, in the terms of export volume under GSP as it received duty free benefit on nearly $ 5.7 worth of imports. The USTR annually revises the countries and products to be benefited under the scheme.
GSP benefits on 94 products are stopped. India exports nearly 50 products out of these 94 products. Out of global Apparel exports of $324.7 billion, India enjoyed preferential tariffs on nearly $6.35 billion worth of exports out of total exports of $54.1 billion to US in the year 2018- 2019 under the GSP scheme, hence having a reasonable impact on the Indian exports. The share of GSP qualifying products in total exports from India to USA accounted to 12 per cent in the same year. India exports nearly 1937 products under the GSP under US. It can thus be said with certainty that India benefitted much from the program.
The US on June 5th, 2019 declared its decision to withdraw the 43 year old GSP and terminate India’s designation as a beneficiary country. This decision will end preferential tariffs on $6.35 billion worth of exports. This decision was taken after determining that India has not assured US that it will provide "equitable and reasonable access to its markets."

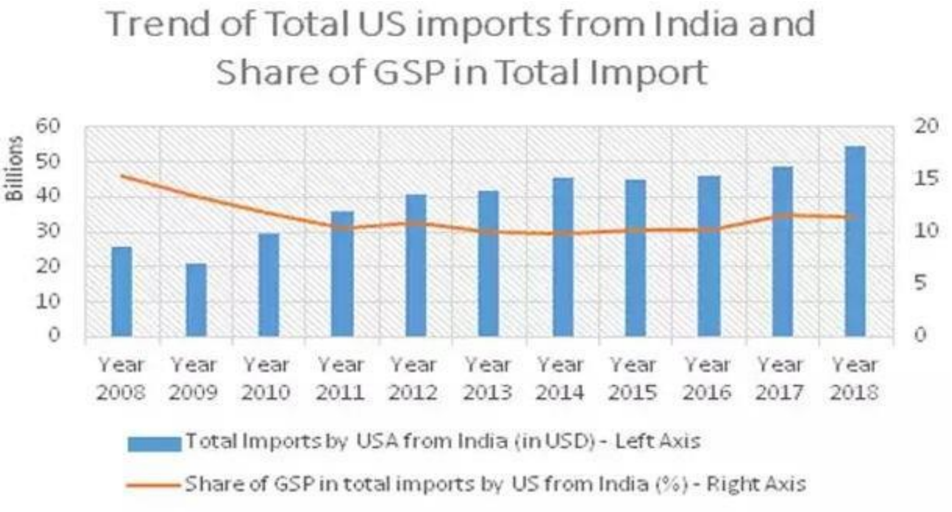
With preferential duties coming to an end, duties on Apparel exports will become higher which means Indian apparel exports will become more expensive and will lose their competitiveness vis-à-vis other developing countries' exports to the US. India is facing strong competition from Vietnam and Bangladesh and the export segment of apparel. This will hamper India's apparel export growth in the US.

The US has been displeased with India when it comes to a number of things which lead to its decision to withdraw the benefits under GSP program:

1. Firstly, the case of Harley Davidson that is manufactured in the US, on which India has increased duties on. President Trump has questioned "Why is it that Indian motor cycles are entering free in the US, when American motorcycles are forced to pay high duties in India?
2. Secondly, the medical device industry has been displeased as well about the hike in duties on the coronary stents and knee implant components. In 2017, the government imposed price caps on US manufactured medical devices in order to make Healthcare more affordable for the residents of India and the US government insists on softening these price caps.
3. Thirdly, the US feels that India has not met "adequate and efficient Intellectual property protection" which is a paramount GSP eligibility criterion. They are displeased about the lack of protection of intellectual property and patent rights in India and they want stricter enforcement of the IPR.
4. The US is peeved by India's lack of assurance of providing an equitable and reasonable access to its markets. They are vouching for an improvement in data localization norms and better e-commerce rules that do not discriminate against foreign players in favor of local Indian e-commerce players. They want access to Indian markets for US manufactured dairy products and hence they are pushing India towards the removal of certain mandatory certifications for dairy product exports and a removal or reduction of import duties on information and communications technology products.
5. The US is also unhappy with India's trade surplus and is insisting India to reduce it. India enjoyed a trade surplus of 21 billion in the year 2017-18 and is the 11th largest trade surplus country for the US.

Lastly, It can be said with certainty that, US has been displeased about the lack of freer access for US imports to Indian markets and offers it as a justification for withdrawing GSP on India's exports to the US.

FIGURES AND TABLES



Source: Economic Times

Policy Recommendations:

1. India's textile exports are falling viz-a- viz its competitor's Bangladesh and Vietnam. What is the plausible solution to tackle this?

Solution: After the withdrawal of benefits under GSP, the exporters of that apparel eligible under GSP are bogged down by higher tariffs than their competitors. These exporters need more government support, incentives and protection to access new markets and to preserve their existing market share.

For this the government needs to enter into bilateral negotiations with major apparel importers like EU and US. One way to address the stagnation of exports in this sector is to enter into a Free trade agreement (FTA) with the US.

a. The signing of several Trade agreements amongst countries has increased apparel trade flows over the decade.
b. Regional and Bilateral trade agreements have led to zero or preferential tariffs among members of the trade agreement and hence has led to an increase in trade between them. India is not a party to such agreements with the US and EU and hence has witnessed an adverse effect on its competitiveness.

The US has high autonomous tariffs on apparel imports whereas it offers zero or preferential tariffs in their trade agreements. As of now, apparel exports of India suffer 9%-32% duty from the US market which is a hindrance to its competitiveness.

India's competitor Vietnam has enforced a FTA with the US which is the US-Vietnam Bilateral Trade Agreement as of December 10, 2001. This has led to Vietnamese apparel exports enjoying zero duty. Bangladesh has also benefited from its status and least developing country and hence enjoys zero tariffs on its exports. These two factors will impact Indian exports to the US massively. Indian exports will take a hit as they will end up being expensive compared to its competitors and hence lose their market share to Vietnam and Bangladesh.

2. In the year 2018, US made a complaint to the WTO stating that a few export related schemes provided by India are in violation of the WTO agreement on subsidies and countervailing measures (SCM). What factors should the policy makers keep in mind while designing schemes that are WTO complaint?

Solution: Amongst the schemes that weren't WTO compliant, the MEIS (Merchandise Exports from India Scheme) were one of the most challenged one. The MEIS scheme which was meant to offset infrastructural inefficient was supposed to expire by June 30, 2018, but the scheme was extended anyway due to declining apparel exports. MEIS is calculated as a percentage of total value of FOB and is then given in the form of tradable scrips which can be sold to other importers or it can be used as currency to pay customs duty.

Due to this India will face the possibility of trade slowdown in this sector, as it is now required to phase out this subsidy. As these trade promotion schemes are now being challenged under the WTO's SCM Agreement, policy makers should ensure that their promotion schemes and policies are WTO compliant. In order for a subsidy to be WTO compliant, it shouldn't be: (i) Sector specific and (ii) It shouldn't be export contingent as the export contingency clause of the incentives is not WTO compliant. (iii)Instead, India should focus on adopting subsidy schemes that is linked to performance indicators such as investment in technology, expansion and growth. These are some of the factors to be kept in mind while designing schemes that cannot be challenged by the WTO. In order to design WTO subsidies, the government can also refer to subsidies adopted by other countries.

3. Some of the special economic zones in India are not helping textile firms to bring in desired investment to the sector and are struggling in tackling foreign policy related concerns.

Solution: Special Economic Zones are meant to help the textile firms to become part of a Global Value Chain (GVC) but this has not been happening in India due to its trade policies. This can be explained with an example: Bangladesh and Vietnam have been able to attract foreign investment from various countries like Korea and when compared to India's labour laws, Bangladeshi's labour laws are flexible. Land acquisition and power supply are provided at subsidized rates whereas Indian government has not been supportive in such avenues. Vietnam has been able to successfully remove export-contingent subsidies given to its textile sector.

Therefore, Indian Government should provide support to this sector by removing stringent laws and provide overall support to this sector through various subsidized schemes.

4. How is India tackling systematic infrastructure problems?

Solution: (i) **By adopting Policies to Shorten Lead Times:**

An alternative strategy to reduce lead time is by implementing clustering- this would reduce lead times as it co-locates the parts of supply chain and hence reduces the time taken for common procedures.

Indian Government created a new scheme for integrated textile parks in 2005 to set up individual manufacturing units in a cluster and provide them with advanced, modern infrastructure to foreign and domestic producers. It was created by merging 2 schemes

- in 2002 (the Apparel Parks for Exports Scheme and the Textile Center Infrastructure Development Scheme). Currently, there are 27 operational parks and 13 have been approved. These units commonly have an export - oriented focus.

(ii) By Provision of quality Infrastructure:

Transport, logistics and customs are components of infrastructure that are of paramount importance. Given that India is large in terms of land area and that concentration of firms is grater in and rather than near the ports, the quality transportation infrastructure is important. The textile apparel industry suffers due to a lack of adequate quality transportation facilities. The conditions of roads, railways and pots are substandard. In addition to this, there are regulatory barriers such as checks posts involved in internal traffic.

India has introduced a risk management system for customs to be more efficient and responsive to security issues, smuggling, and human trafficking, however firms report that implementation is lagging. Although customs procedures are already reformed and automated, there is still room for further improvements.

5. Lack of Research and Development in Indian Textile sector has resulted in closure of many business outlets as when compared to its competitors. (Bangladesh and Vietnam).

Solution: The above scenario exists primarily due to the fragmented nature of Indian textile sector which is concentrated with many small and mid -size textile firms affecting its competitiveness globally and these firms don't invest in R&D. If we compare with Vietnam they have a five stage integration scheme which is initiated by Vietnam National Textile and Garment Group but India has no such scheme to boost Research and Development in the sector.

It is observed that the weaving works are highly unorganized and the output is low and of variable quality and this is due to lack of technological advancement and this will create problems with respect to product traceability and quality standards. India should focus on creating a R&D team in each of the sectors in Indian economy to understand the root cause of the problem and try to attract more investors into these sectors.

India is currently low productivity, product diversity, and lead times. Elasticity estimates shown in studies indicates that that a 10 percent increase in Chinese prices to the EU can increase male employment by 4.3 percent and female employment by 3.26 percent. Given these potential gains and the current situation in India, the above policies could help India boost its apparel exports.

6. Labor policies, especially policies governing wage levels play's a critical role in shaping costs. How effective is Indian labor policies in shaping costs and increasing productivity?

Solution: Bangladesh's rise as an apparel powerhouse is in large part due to its low wages. India's wage rates remain one of the lowest among the major apparel-exporting nations. Factory owners have reported an average of 16-18% annual wage and mandatory benefit increases due to rising living costs in the core apparel manufacturing areas. This might lead to a reduce in the future availability of labour pool.

Against this backdrop, India to find ways to boost productivity to boost or maintain its current level of competitiveness.

A fundamental way to increase productivity is by reforming labour regulations, such as those governing hiring and firing and number of hours worked. A study by Besley and Burgess, 2004 finds that India's stringent labour regulations results in lower output, employment, investment, and productivity in the formal manufacturing sector.
The Apparel Export Promotion Council (AEPC) in India contends that India's strict laws governing `number of overtime hours worked which is 50 hours per quarter are tougher than what the International Labor Organization (ILO) mandates and leads to lower productivity and underuse of capacity. Indian firms also claim that limitations on overtime working hours imposed by the Factories Act (1948) as a key barrier to growth. Termination of jobs is another issue. India's Industrial Dispute Act (1947) requires the involvement of state in firing decisions if the size of the firm exceeds 100 employees. Most exporting firms exceed this threshold and hence are opting to use other means of introducing flexibility in their use of labor like hiring of as contract workers to avoid permanent employment. The downside of this is that, this leads to high employee turnover which is a drag on productivity.

In India:

- In 2010- a government-led skill development program was created.
- In 2014 - Ministry of Skill Development and Entrepreneurship was created.

Human resources and skill development are key components of labor policies. Skill development is another component that affects productivity, given that investment in skills at different stages of the apparel value chain can lead to higher efficiency and lower costs. A network of Apparel and textile specific training institutes is required.

7. Foreign investment has played a major role in the initial setup of the apparel industry in Bangladesh and Sri Lanka but not in India. Why?

Solution: Many of the top Asian apparel exporters, except India and Pakistan, grew due to foreign direct Investment (FDI). One reason is that India was restricted by quotas during the MFA and thus was not a target for quota -avoiding investors. Factories with owners of foreign descent or multinational manufactures usually employ a well-established structure of production and distribution networks that have textile and apparel investment and sourcing ties throughout Asia. These firms started outsourcing and off shoring production during the multi fiber agreement (MFA) to take advantage of quota preferences and lower operating costs. These countries are now are part of existing networks. Today these decisions are driven by market access preferences and favorable investment incentives hence calling for favorable FDI policies. This connection of being part of existing networks is important because buyers evaluate suppliers on their ability to supply products across numerous product categories. Buyers are looking at what the vendor is capable of supplying on a global level and not just what is manufactured at one factory.

India has managed to maintain its position as one of the top exporters without FDI, but it is better for the industry to attract it in order to make deeper inroads into the U.S. and EU markets, particularly given buyers' inclination to reduce the number of firms they want to work with directly. India is well equipped to capitalize on emerging end markets considering the dominance of domestic ownership. But in order to succeed, it must create stronger ties with Argentina, Australia, Brazil, Canada, China, the Russian Federation, Saudi Arabia, and the UAE on forward linkages. This means:

- preferable tariffs for its apparel exports,
- Knowledge on how the retail industry operates, particularly in these countries.
- Relationships retailers that have large market shares in these emerging end markets.

India should also ease its FDI policies and scrap initial restrictions on foreign ownership and simplify its overly complex legal system that will make it difficult for a foreigner to navigate alone.

In India, theoretical speaking a 100 percent FDI is possible, but in practice there are still many challenges due to the number of authorities involved and the specific conditions or permits required. India actually allows 100 percent FDI in the textile sector under the automatic route and the Ministry of Textiles has recently set up FDI Cell to attract FDI. However, the textiles sector is not one of the top sectors receiving FDI in the country. And as of now, no explicit policy exists to attract FDI to apparel.

CONCLUSIONS

We can conclude with certainty by saying that the policy environment of India for the apparel industry is not at par with its competitors and is also not conducive in a competitive international political economy. The government must not only provide export incentives but most also protect and provide the required support to this sector that will favourably impact the economy.

The apparel sector viz-a-viz any other sector offers mass employment generation. This is a pressure issue and hence steps need to be taken urgently to re-focus on low tech mass-employment generation in order to sustain and nurture this unique attribute of the apparel sector. The sector needs more support and salient policy making in order to enhance its exports despite the competition it faces from other countries that have a tariff advantage.

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