

Research paper

**The Competitiveness of Ready Made Garments Industry
of Bangladesh in Post MFA era: How does the industry
behave to face the competitive challenge?**

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31 **ABSTRACT:**

32 The challenges that originate from changes in the global trade regime and the relative competitive environment
 33 in the global markets are reasons for deep concern for Bangladesh. Because of quota system abolition many of
 34 the less efficient suppliers will lose quota rents and market shares as they are forced to compete with more
 35 efficient suppliers among developing countries. Since 1974, Bangladesh was enjoying a quota free access of
 36 garments under the Multi- Fibre Arrangement (MFA). But the phase out of the Multi- Fibre Arrangement (MFA)
 37 has completed in 2005 under the Uruguay round of GATT (General Agreement for Tariffs and Trade) in 1994.
 38 The freeing of trade in textiles and clothing has created a formidable challenge to the Bangladesh Ready Made
 39 Garments (RMG) Industry. The phase-out of the MFA, emergence of competitors such as China, India, Vietnam,
 40 Turkey, Mexico and African nations have negatively impacted on the fortunes of Bangladesh RMG sector.
 41 Dependence on imported raw materials, political instability, turbulent economy, high bank interest rates, lack of
 42 government incentives, poor knowledge of international marketing, port problem, poor infrastructure and labor
 43 union are some of the internal problems of Bangladesh RMG. This sector is being incrementally faced with the
 44 burden of obligations imposed by the developed countries in the guise of compliance issues. There are two
 45 types of views about the future of Bangladesh Ready Made Garments (RMG) Industry after MFA era. The
 46 optimistic view emphasized that Bangladesh had held a strong position in the global market due to its abundant
 47 supply of cheap labor. On the other hand the pessimistic view revealed that there is no opportunity for
 48 Bangladesh to survive in the competition. This paper is prepared in the context of phasing out of the MFA and
 49 its impact on the export performance of Bangladesh Ready Made Garments (RMG) industry.

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51 **Keywords:** Ready Made Garments (RMG), MFA (Multi Fibre Arrangement), Quota System, Competitiveness,
 52 Export potential, International trade.

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60 1. INTRODUCTION:

61 The RMG industry in Bangladesh has developed from outside pressure rather than emerging to meet local
 62 demands (Siddiqi, 2004). The increasing wages in the clothing producing countries paved the way to establish
 63 RMG industry in Bangladesh, as the countries started looking for low-wage situation of factories (Ahmed, 2002).
 64 The industry is the most prominent export oriented industry of the country which has achieved very significant
 65 growth during last two decades (Ahmed, 2002). Now there are about 4,000 RMG industries in the country with
 66 export earnings of \$6.40 billion per year. The industry employs about 2 million workers with 80% participation of
 67 women labor force. RMG industry alone fetches 79% of the total export earnings of the country (BGMEA, 2010).
 68 The export income from the industry is among one of the top three sources of economic development and GDP
 69 growth of the country (Gibson et al. 2004).

70 Two factors such as cheap labor force and captive market under quota system facilitated the development of
 71 RMG industry in Bangladesh. The favorable policies of the governments in the form of duty, preferential tax, tax
 72 holidays, duty free machinery inputs, central warehouse facilities, letter of credit facilities without deposit, loans
 73 at low interest rate etc. have also supported the growth of the industry (The Financial Express, 2008).

74 2. BACKGROUND OF MFA:

75 Since 1974, the world textile and clothing trade has been regulated by the GATT approved Multi-fibre
 76 Arrangement (MFA). It is an exception to the GATT's (General Agreement on Tariffs and Trade) principle of non
 77 discrimination. MFA came into effect to set the rules and regulations for apparels and textiles trading. These
 78 rules provided the framework for bilaterally agreed-upon quantitative restrictions set by major importing
 79 countries which took trade in textiles and apparels products beyond the basic GATT principles through the
 80 imposition of export quota for particular countries (The Centre for Policy Dialogues, 2003). On 1st January 1995,
 81 MFA was substituted by the WTO Agreement on Textiles and Clothing (ATC) which lay out a step by step
 82 process for the final withdrawal of clothing quotas (The World Trade Organization, 2010). Under the provisions
 83 of ATC, the quota under MFA was terminating over a 10-year period and after the integration, regular GATT
 84 safeguards have been applied (Yang and Mlachila, 2004).

85 3. OBJECTIVES:

86 The aim of the research is to identify the export performance and challenges facing by the ready-made
 87 garments industry in Bangladesh in the post quota free globalized market. The objectives of the research are:

- 88 1. To analyze the impact of quota system (Multi Fibre Arrangement) abolition on the readymade garment
 89 industry of Bangladesh.
- 90 2. To critically examine the competitiveness of the industry in major international markets due to global
 91 economic policy changes.
- 92 3. To explore the export potential of the industry in future and their influencing factors

4. LITERATURE REVIEW:

Different authors have provided different opinions on the issue of phasing out of MFA and their possible impacts. Nordas (2004) concluded the four possible consequences of phasing out of MFA: First, there is a political gain where the acceptability of multilateral trading system is experiencing severe difficulties. Second, there are efficiency gains from the elimination of quotas which led to an unjustified global allocation of textiles and clothing. Third, there is a loss to ATC exporters as they are not enjoying the quotas to export certain volumes. Fourth, there is the gain to consumers who can enjoy quality products at competitive price. Chowdhury, Ali and Rahman (2006) depicted that due to the rules and regulations of WTO most adverse affected country will be the LDCs like Bangladesh. According to him, Macroeconomic instability may arise as it will distort the market condition. Moreover, this will create an increase competition which will not only create problems for the female labor force of the garments sector but will also increase the risks regarding their empowerment, dependency syndrome and even they may choose prostitution.

Rahman (2005) implied that apart from China, new entrants like Cambodia, Vietnam and Lesotho are expected to pose a formidable challenge to some of Bangladesh's markets. The author argued that some of the competitors of the Bangladesh RMG industry enjoyed the preferential access to international markets, especially to USA under the initiatives such as NAFTA, CBI (Caribbean Basin Initiative), US-Vietnam trade agreement, European Free Trade Areas and other Bilateral foreign trade agreements. Huda, Karim and Ahmed (2007) suggested that the new era of quota free trade has created a huge opportunity for growth but at the same time scientifically managed foreign competitors should also be taken in account. The practice of strategic human resource development will be an efficient measure to utilize the opportunities and countering threats. On the other hand, according to Ahmed and Hossain (2006), Bangladesh cannot compete long with its only comparative advantage of cheap labor. The country needs to establish its own backward linkage industry by decreasing the number of back to back letter of credit. They also suggested that Bangladesh needs to increase the import of new technologies so that the domestic firms can improve their efficiencies, reduce cost and remain competitive in the global market.

Hiebert (2003) pointed out that Bangladesh produce few of the inputs to manufacture garments. He also added that China can supply textile and garments 40% cheaper than Bangladesh. The competitors like China, India and Pakistan will be the winners because they have a low cost efficient workforce and invested heavily on new equipments and have efficient backward linkages. He recommended that Bangladesh has to invest heavily on its infrastructure to remain competitive. Kumar (2006) also pointed out on similar views of infrastructural problems of Bangladesh RMG industry. According to him garment factories are not being able to use its full capacity of production due to shortage of power. The author argued that due to shortage of power the cost of production is increased to 25 percent. Mohiuddin (2008) argued that Bangladesh RMG sector is growing with old and inefficient technology. Hence, trained manpower, innovative technology, available raw materials, better working environments and effective supervision of workforce will bring out the best from the industry. On the other hand factors like export policy, infrastructure, economic development and regional agreements will reduce

the external barriers of the industry (Chowdhury et al., 2006). Compliance issue is very important for Bangladesh industry. The issue of child labor was solved successfully by Bangladesh but other issues like minimum wages, factory location, suffocating environment, fire exits, separate lunch room, women common room and toilets are some of the major compliance issues that needs to be addressed to maintain the compliance standards referred by foreign buyers (Paul-Majumder, 2001)

5. METHODOLOGY:

This research by its nature relies on descriptive research design because the researcher attempts to explain the crucial features of Bangladesh readymade garments industry in post MFA era. Because the previous knowledge about this research is in advanced level, the researcher avoids the rigorous research feature of exploratory study that requires extensive interviews with many people and designs a comprehensive investigation. Rather the researcher will rely on survey among a small sample to collect primary data. The researcher has collected primary data by carrying out a close ended questionnaire survey among 15 managers working in different garments industry. The primary data was collected initially by sending e-mail questionnaires to some of the managers. The author was able to get only 6 responses through email even though every possible effort was made to get all the responses by online. As there was not enough response, 9 respondents were surveyed personally by the researcher.

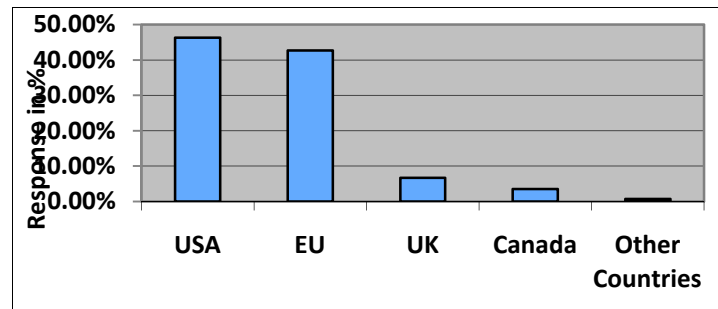
The author has used purposive sampling technique in this research. Reeves and Harper (1981) defines purposive sampling as taking slices through organization, selects people because of the positions they occupy (Reeves and Harpe, 1981 quoted in Jankowicz, 2005). Managers are selected as respondents because they are the key informant of the status of Bangladesh RMG industry- people who have specialized and unique knowledge and experience of the issue the researcher is trying to find out. While selecting the managers, the author has made it sure that the managers occupy the strategic positions of the company and are working before and after the quota system so that they can compare different scenarios. The advantage of such technique is that the researcher feel confident that the data gathered will reflect perspectives pertinent to the inquiry being undertaken (Anderson, 2004).

According to Gay and Diehl (1991), Samples should be as large as possible. On the other hand, Bancroft and O'Sullivan (2000) argued that sample size tend to be matter of judgment rather than a matter of calculation. The researcher has chosen 15 managers from different garments companies located in Dhaka, Gazipur and Narayongonj where most of the garments factories in Bangladesh are located.

6. RESULTS AND DISCUSSION:

6.1 EXPORT DESTINATION:

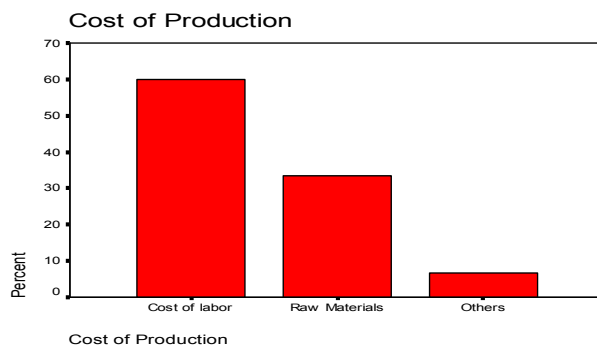
The combined export of garments from Bangladesh to USA and European Union (including UK) is 94.7%. The export of garments to Canada and other countries are 2.6% and 2.6% respectively. This reveals that the garments export from Bangladesh is still very much dependent on USA and EU while the diversification of market is at primitive stage.



Category label	Code	Count	Responses (%)
USA	1	14	36.8
EU	2	14	36.8
UK	3	8	21.1
Canada	4	1	2.6
Others	5	1	2.6
		Total responses = 38	

6.2 COST OF PRODUCTION:

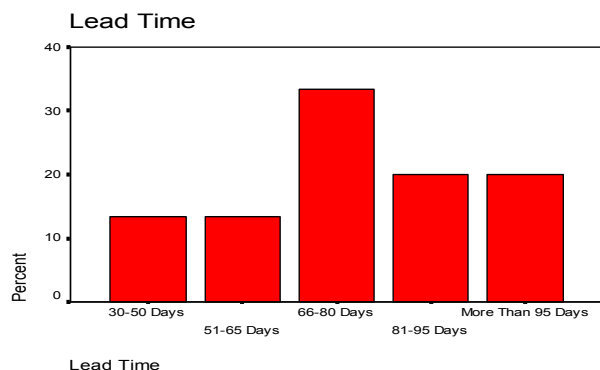
The survey result shows that the cost of labor covers the most substantial portion of total production cost in Bangladesh RMG industry. This reveals that the RMG industry of Bangladesh enjoys cost competitiveness in global market with its lowest wage rate.



	Frequency	Percent	Valid Percent
Cost of labor	9	60.0	60.0
Raw Material	5	33.3	33.3
Others	1	6.7	6.7
Total	15	100.0	100.0

6.3 LEAD TIME:

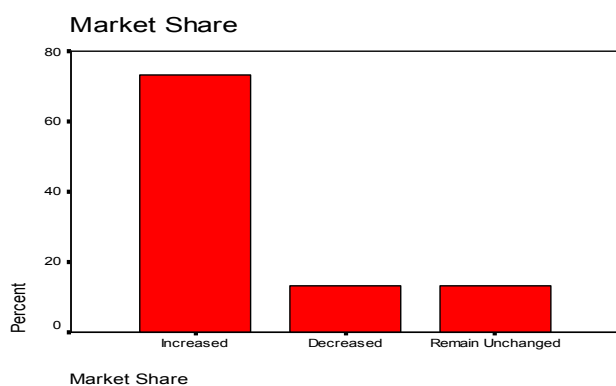
According to the survey, most of the respondents have said that they maintain a lead time of 66 to 95 days to export the garments. Only 26.6% of the exporter's have said that they take 35 to 65 days to export their products which are the global benchmark for exporting garments products.



	Frequency	Percent	Valid Percent
30-50 Days	2	13.3	13.3
51-65 Days	2	13.3	13.3
66-80 Days	5	33.3	33.3
81-95 Days	3	20.0	20.0
Above 95	3	20.0	20.0
Total	15	100.0	100.0

6.4 MARKET SHARE:

The figure shows that 73.3% of the respondents said that the market share of garments export has increased since 2005 which means the RMG industry of Bangladesh maintained its growth even after the abolition of preferential market access to USA and EU.



	Frequency	Percent	Valid Percent
Increased	11	73.3	73.3
Decreased	2	13.3	13.3
Remain Unchanged	2	13.3	13.3
Total	15	100.0	100.0

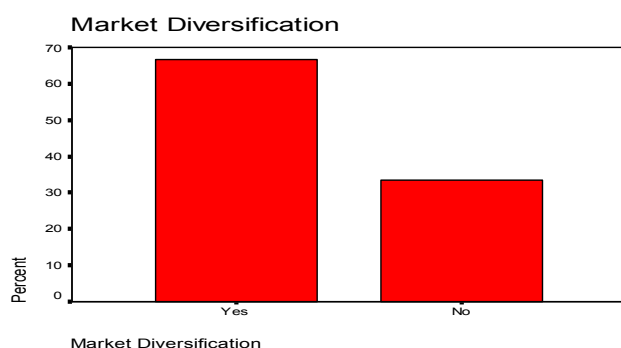
6.5 PROFIT MARGIN:

The empirical data shows that most of the respondents have said that their profit margin have either declined or remained unchanged since 2005. The profitability of RMG industry of Bangladesh is affected by the problems like cut prices by buyers, soaking of profit in the name of compliance and increased costs of raw materials, transport and infrastructure.

		Frequency	Percent	Valid Percent
Valid	Increased	3	20.0	20.0
	Decreased	8	53.3	53.3
	Remain Unchanged	4	26.7	26.7
	Total	15	100.0	100.0

6.6 MARKET DIVERSIFICATION:

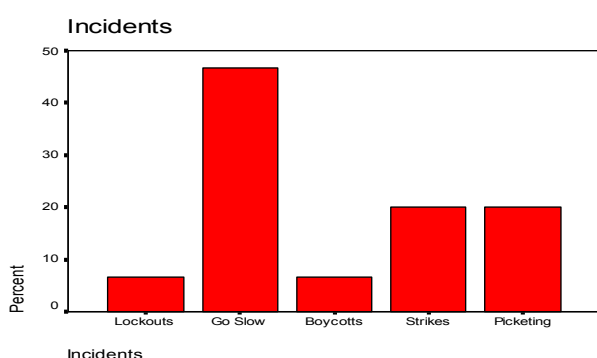
The analysis of empirical data reveals that 66.7% of the respondents are looking for new market to keep export growth while 28.57% of the respondents are not exploring to new markets. The data findings demonstrate that the industry is trying to reduce its dependency on two markets for the long term sustainability and growth. The countries like Russia, Japan, Brazil and China are offering potential market access for RMG industry of Bangladesh.



		Frequency	Percent	Valid Percent
Valid	Yes	10	66.7	66.7
	No	5	33.3	33.3
	Total	15	100.0	100.0

6.7 INCIDENTS:

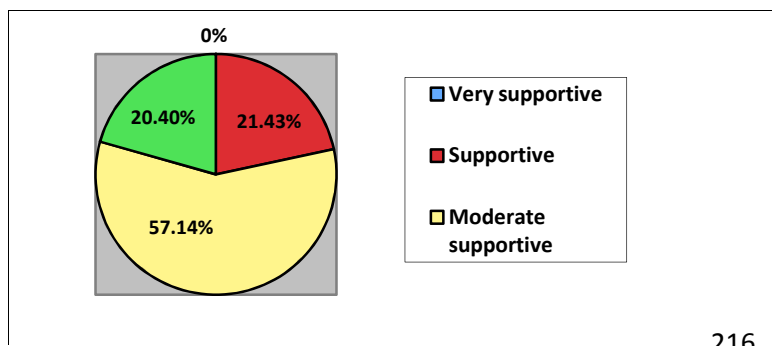
The figure shows that the most common incident happened last four years was the go slow of business which means the industry was affected by the quota system abolition many times. But the previous data of export shows that the industry has absorbed the shocks by maintaining the positive export growth. The industry faced some incidents of lockouts, boycotting, strikes and picketing during last four year.



		Frequency	Percent	Valid Percent
Valid	Lockout	1	6.7	6.7
	Go Slow	7	46.7	46.7
	Boycotts	1	6.7	6.7
	Strikes	3	20.0	20.0
	Picketing	3	20.0	20.0
	Total	15	100.0	100.0

6.8 GOVERNMENT SUPPORT:

The figure shows an interesting picture that none of the respondents have said that the government policy is not very supportive to the industry while only few of the respondents said that the policy is supportive. Most of the respondents said that government policy is either moderate favorable or not favorable. It is very difficult for the RMG industry of Bangladesh to compete in the open market without the proper help of government.



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6.9 POTENTIAL MEASURES IN FUTURE:

The diversification to new markets, government support, development of support industries and reduce lead time are the key issues among the respondents that need to be addressed after the abolition of quota. The respondents also suggested that effective measures should be taken for product diversification, participation of foreign investors in market development, improving labor skills and factory modernization.

Category	Code	Count	Responses (%)
Foreign Investment	1	6	10.2
Diversification to new markets	2	10	16.9
Product Diversification	3	7	11.9
Factory Modernization	4	3	5.1
Improve labor skills	5	6	10.2
Reduce lead time	6	8	13.6
Develop own backward linkage	7	9	15.3
Government support	8	10	16.9
Total responses		59	100%

7. CONCLUSION:

Evidence gathered with regard to performance of RMG industry in post MFA regime show that the phasing out of MFA and emergent of new competitors could not restrict the ongoing growth of Bangladesh RMG industry. The entrepreneurs of Bangladesh have demonstrated a remarkable ability to take the advantages of business opportunities that had emerged in quota free globalised world. Since 2005, the industry has continued its positive growth and the export income from the industry are expected to be double in next five years. A close look at the industry reveals that the industry has maintained its competitive strength in the market by exporting low cost apparels based on the availability of cheap labor. But the industry is also facing some internal problems such as poor infrastructure, lack of backward linkages, high lead time and market and product diversification. Some of the external threats to the industry are arising from regional agreements, competitor's

actions, political instability etc. If the country can mitigate these problems effectively, the industry can grasp the opportunity to export unlimited merchandise by exploiting its comparative advantage of low cost and highly trainable labor force over other exporting nations.

However it is too early to comment on the competitiveness of Bangladesh RMG industry because; the industry has only gone through seven years after the abolition of quota. The long term sustainability of the industry depends on how it can handle all the obstacles and maintain its competitive strength in the global market. So, the issues related to the competitiveness of the RMG industry of Bangladesh in post MFA era needs to be further studied and examined.

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