

**Development Policy Research Unit
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**What are the implications of the
SADC Protocol for the clothing and
textile sector in Southern Africa?**

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Foreword

The Development Policy Research Unit (DPRU), located within the University of Cape Town's School of Economics, was formed in 1990 to undertake economic policy-oriented research.

The aim of the unit's work is the achievement of more effective public policy for industrial development in South and Southern Africa.

The DPRU's mission is to undertake internationally recognised policy research that contributes to the quality and effectiveness of such policy.

The unit is involved in research activities in the following areas:

- labour markets and poverty
- regulatory reform
- regional integration

These policy briefs are intended to catalyse policy debate. They express the views of their respective authors and not necessarily those of the DPRU.

They present the major research findings of the *Industrial Strategy Project (ISP)*. The aim of the ISP is to promote industrial development in the *Southern African Development Community (SADC)* through regional economic integration and cooperation. It is a three-year project that commenced in August 1998 and is funded by the *International Development Research Centre (IDRC)*. Ultimately, this project will identify the policies and programmes that support regional interactions that contribute to the industrialisation of SADC national economies.

This policy brief is a shortened version of the following paper:

Prospects for the Clothing and Textile Industry in Zimbabwe: The Implications of the SADC Trade Protocol

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Introduction

This policy brief seeks to outline the potential benefits for, and threats to the clothing and textile sector in Zimbabwe as a result of a free trade area among the Southern African Development Community (SADC) countries. Previously protected industries, such as the clothing and textile sector, now face the prospect of fierce competition in their respective product lines as trade barriers are reduced across the region. It is therefore significant from a policy point of view to understand the intra-regional business, trade and investment linkages that may be destroyed, or created due to the trade integration process in Southern Africa.

Clothing and Textiles in Zimbabwe: A brief background

The clothing and textile industry in Zimbabwe is a vast sector with significant forward and backward linkages. The industry is largely cotton-based and all activities and processes that constitute the 'textile chain' are present in Zimbabwe, from cotton farming to garment production.

Textile Chain:

Cotton farming ⇒ Lint production ⇒ Yarn spinning ⇒ Weaving/knitting ⇒ Garment production ⇒ Domestic retailers

Shrinking sub-sectors

In 1991 there were 284 registered clothing companies and 50 textile companies. By the end of 1999 a total of 115 firms in the clothing sector, and 6 textile firms had shut down representing a 44% and 12% shrinking of the respective sub-sectors.

Low capacity utilisation levels

Capacity utilisation levels in the industry are low, averaging between 42 and 50 percent across the industry.

Low levels of FDI

Most companies in the clothing and textile sector are locally owned (90%), suggesting very little foreign direct investment (FDI) in this sector.

Declining employment

Employment in the industry has been declining over the past six years. From 28 000 and 25 000 workers in the clothing and textile sectors respectively to 17 600 and 15 900 representing a combined fall in employment of over 36% over ten years.

Increasing role of the informal sector

Although there is no appropriate data, there is a strong possibility that a significant proportion of the employees in the formal sector have joined the ranks of the informal sector.

Labour costs

Labour costs account for approximately 33% and 25% of the total costs in the clothing and textile sectors, respectively. The average wage (1999) in the clothing sector was Z\$ 600 per week, and Z\$ 850 a week in the textile sector. In textiles, Zimbabwe has a labour cost advantage over its neighbours in the region, and over the textile –producing countries in Europe, Asia and the USA.

Clothing and textile exports and imports

Exports and imports occur at every stage of textile and clothing production in Zimbabwe.

- The major destination of **clothing exports** from Zimbabwe is the European Union (EU), which accounted for up to 50% of all garment exports in 1998.
- There are two different kinds of clothing exporters: a handful of committed exporters producing larger volume runs for foreign markets with 70% or more for production for export, and a much larger number of exporters whose production is mainly for the domestic market with typically no more than 25% for the export market.
- Clothing exports to the SADC region have grown from a paltry 5% of total clothing exports to almost 19% between 1991 and 1998. However, in this period, exports to South Africa, the region's largest market, have remained constant. The implication is that some of the smaller countries in the region have increased in importance as a destination for Zimbabwean clothing exports.
- **Textile exports** have performed relatively better, especially within the SADC region. Exports of yarn and fabrics to the region accounts for up to 30% of total textile exports with Botswana (14%) and South Africa (9%) dominating..
- Although all stages of the textile chain are represented in Zimbabwe, the problem has been that various inputs are unavailable from domestic production therefore necessitating **textile imports**.
- **Clothing imports** into Zimbabwe have grown steadily since liberalisation measures were introduced to the Zimbabwe economy in 1991. Asia has grown in importance as a source of imported yarn and fabric and by 1997 accounted for almost a third of total textile imports. SADC accounted for up

to 38% of textile imports in 1997 and therefore creating an important export market for 'SADC' textile exports.

Export and import problems

Second-hand clothing market and illegal imports

Of growing concern in the clothing sector, especially among the smaller companies, is the continuous growth in the second-hand clothing market and, illegal imports from within the SADC region.

Import-dependency

The clothing and textile industry in Zimbabwe is also entirely dependent on imported machinery/technology. It is partly because of this huge import-dependency that the industry has not been able to reinvest in capital equipment over the past 4 years due to the steep depreciation of the Zimbabwe dollar against all major currencies.

Negative effects of trade liberalisation

The liberalisation of trade (1991) led to a loss of value-added output, company liquidations, employee retrenchments and a general loss in welfare for society.

- Exports would have been assisted by currency depreciations but a poor overall economic climate clearly prevented firms taking advantage of a weak currency.
- In 1994 the export incentive scheme were removed and the rate of growth of exports began to decline. To a certain extent this seems to suggest that the growth in exports is over-dependent upon generous state assistance. It would also suggest that the incentives have not made the industry competitive enough in the long term because firms continue to rely on these incentives.
- The top factors cited by firms that have acted as major barriers to expanding exports are:
 - lack of government support,
 - policy/political uncertainty,
 - mismanagement of the economy, and
 - a fixed exchange rate.

Implications of Free Trade

Rules of origin

With respect to the rules of origin, SADC negotiations have led to an agreement on a **two-stage transformation** process that is consistent with the cotton-based nature of textiles and clothing in the SADC region. According to this rule if a country produces clothing, then the cotton and the fabric has to be sourced from within the region.

It is a two-stage process in the sense that the conversion of basic cotton to cotton yarn, and cotton yarn into fabric have to be stages that are present in a SADC member country, using SADC-sourced inputs, if the country is to enjoy free trade status in clothing products.

In light of the status of some of the least developed countries in the region, a significant concession has been made by the proponents of this two-stage transformation process, the Southern African Customs Union (SACU). For the least developed member states (Malawi, Mozambique, Tanzania and Zambia), only one stage of the transformation is required for the next five years.

For the Zimbabwean producers, this requirement could be problematic because

- some raw materials such as silk, synthetics, wool, dye are not readily available in satisfactory quantities and quality in the SADC region.
- furthermore, existing sources of these products in the region are by no means competitive in terms of prices and quality.

Investment

The emergence of a free trade area ought to provide a host of investment opportunities for domestic, regional and global investors. Investment is a critical component of the trade protocol because those countries in an integrating region that have industries that are “injured” by free trade need to be compensated by increases in investment in other sectors of the economy. The level of direct SADC investment into the clothing and textile industry in Zimbabwe has been relatively low, as has been Zimbabwe’s investment in the regional clothing and textile industry.

Firm-level Constraints

Small firms suffer from a greater demand constraint than larger firms. This is largely because they are geared towards small niche markets and have more difficulty of obtaining finance.

The high cost of capital is a constraint plaguing the entire industry, in fact, the entire economy. Small firms also suffer from relatively low skills availability – and this is probably due to the unavailability of adequate financial resources to attract the necessary quality and quantity of skills. This is however not true for the larger firms who are better equipped with financial options, networks and organisational capacities. A Free Trade Area (FTA) in the region at a time when the industry in Zimbabwe is under a lot of stress could result in a repeat of the events of the 1990's.

Critical Success Factors

- The general **labour-intensity** of the industry creates competitive advantages for Zimbabwe, which is well endowed with relatively cheap and literate labour. In addition, the high **quality of hand-picked cotton** available in Zimbabwe, the **established infrastructure** and the **nation's central location** in Southern Africa provide numerous opportunities for firms already in the industry, and potential entrants into the industry.
- Excess capacity, coupled with the small size of the domestic market, suggests that the industry's survival in the long term is dependent upon the successful expansion into, and maintenance of, **export markets**.

Conclusions/Recommendations

Industrial policy

Apart from the other factors militating against the industry, the lack of a detailed and comprehensive industrial policy is probably the most serious.

- The manufacturing sector in Zimbabwe needs an industrial policy under which various sectors can be in a position to quickly **identify opportunities** and utilise them particularly for export production.
- The manufacturing sector should be encouraged to establish and foster **strategic alliances** between large and small firms, and the informal sector. The policy would involve the provision of incentives to the larger firms to link with smaller ones through sub-contracts, particularly in areas where the smaller firms could perform much more efficiently, such as in low volume niche products.
- **Regular tariff reviews** are necessary to ensure that that the sector is always taking advantages of its strengths and opportunities. These tariff schedules need to be stable and credible.
- Firms must be able to **acquire inputs into production** at world prices so as to facilitate competitiveness in international and regional markets.
- A **duty drawback system** that allows exporters of finished products to import technology, machinery and raw materials dutyfree would also provide firms with a competitive environment.

Improvements to Infrastructure

There is an urgent need to improve infrastructure that would help reduce production costs and improve product quality. The following factors can improve business in Zimbabwe:

- **Access to information**, which assists the fashion-oriented sectors obtain information on market trends in various export markets is needed.
- Reliable, fast and cost-effective **transport corridors** to the main harbours. Being a landlocked country, Zimbabwe needs an efficient road and rail transport network, and reasonable freight charges greatly reduce the landlocked-related disadvantages faced by local industries.
- An efficient and reliable **telecommunications system** that enables firms and industries to communicate quickly and at low cost would also help local industries to improve competitiveness.

Second-hand Clothing

Second-hand imports have become a source of affordable clothing for the majority of Zimbabweans, but this injures the domestic industry. The use of ***licenses and quotas*** to restrict the influx of second hand clothing could be considered so as to control and monitor the trade in such clothing.

Product Development and Quality Improvements

- The textile sector has a competitive advantage in modern machinery but is unable to satisfy the demand by local export-oriented clothing firms that require high quality fabric/yarn to maintain their export market share, and expand into new markets.
- Most clothing companies, particularly the smaller less-resourced ones have problems in meeting quality levels required by the global market. This therefore makes the garment producers dependent upon imported fabrics, particularly those firms that are geared toward the export market.
- In terms of fashion and product developments, the larger clothing firms have their own brand names and generally tend to have a better and more advanced strategic direction. On the other hand, the smaller clothing companies mostly carry out pattern making and design to meet their buyers' specification and as such, this limits the fashion content of most of the collections by small companies who have insufficient information on market and consumer trends.
- In addition, small firms are also less able and less willing to engage in R&D activities and rather opt for cut-make-and-trim (CMT) operations that have lower margins but nevertheless have considerable profit potential in a low-income country like Zimbabwe.

Institutional Development

- There is an urgent need to strengthen the capacity of various domestic institutions that can be directly involved in promoting investment and trade in the clothing and textile industry. The Zimbabwe Investment Centre (ZIC), which promotes Zimbabwe as a location for new investment, is also responsible for assisting in the start-up of young enterprises. Other institutions also need to be strengthened and used as vehicles to promote the growth and development of the clothing and textile industry.
- Southern Africa has not been the first choice for European and American investors and this has been attributed to a relatively uncertain economic environment, high transportation costs and long delivery times. This necessitates the need to improve the incentive structure in the region.

Opportunities in the US Market

- The clothing and textile industry in Zimbabwe, and in the rest of the region has been presented with better growth and development prospects by the promulgation in the USA of the trade and development act, known as the African Growth and Opportunities Act (AGOA).
- The Act, which expires in 2008, offers 44 Sub-Saharan African countries duty-free and quota-free status into the USA for those products meeting the eligibility requirements, and for the clothing and textile firms in the region, the potential benefits appear to be up for grabs.
- The basic premise of the Act is the development of bilateral trade between Sub-Saharan Africa and the USA, meaning products, such as clothing garments (apparel), which are eligible for the 'free-entry' status must be manufactured either from locally produced textiles or textiles imported from the USA and then exported as a value-added product to the USA.
- But there is a significant concession for those countries whose per capita income was less than US \$1 500 in 1998. These countries, Zimbabwe included, have a four-year window in which to import fabric/textiles from a third country – expected to be Asia – and then export the finished product to the USA. Zimbabwe, which does import a large quantity of textiles from Asia (32%), is set to benefit substantially from this arrangement, depending on the extent to which firms respond positively to these developments, and the extent to which Zimbabwe meets the eligibility requirements.