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Trade Liberalisation and the Clothing and Textile Industry in Malawi

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Introduction

Malawi is a landlocked country located in the north-eastern part of Southern Africa with a population currently estimated to be around 10.7 million people. At the regional level, Malawi's manufacturing and industrial sector is among the least developed in the *Southern African Development Community* (SADC). This has been attributed to 20 years of protectionist policies, the small domestic market, high distribution costs and fierce competition from other SADC countries (e.g. South Africa and Zimbabwe) and the Far East.

In light of this fragile industrial base, and against a background of trade liberalisation, what are the prospects for the industrial and manufacturing sector in Malawi? This policy brief seeks to provide some direction in answering the above question. In so doing, this brief focuses on the clothing and textile sector in Malawi as a case study.

Overview of the Clothing and Textile Sector in Malawi

The clothing and textile sector in Malawi is characterised by the following features:

- Import substitution has been one of the driving strategic forces behind the development and growth of the clothing and textile sector in most African countries, including Malawi.
- The number of formal-sector companies currently engaged in the clothing and textile sector (both small and large) in Malawi range between 25 and 30 in all.
- In addition to these formal-sector companies, there are many informal clothing/ garments manufacturing enterprises scattered throughout the country. Most of them are cottage enterprises of self-employed people producing dresses, blouses, school uniform, shirts, trousers and many others garments for women and children.
- The informal clothing manufacturing sector provides employment to around 30, 000 people country-wide. The formal clothing and textile sector employs between 10,000 and 11,000 people[1]. The majority are semi-skilled employees.
- The single largest employer is the clothing sub-sector, which at the 75% operation capacity employs about 5,600 people. At full operational capacity, the clothing and textile sector is likely to employ between 14,000 and 15,000 people.

[1] When the sector is operating at 75% capacity!

- In terms of Malawi's non-farm economic sectors' employment distribution (currently at around 78,000 people), the clothing and textile sector is one of the major labour force employers in the country.

- Up to 95% of the products of the clothing and textile sector in Malawi (estimated at about 38.0 million units of households and garments, and 37.2 million of loom-state textiles and woven/knit per year) are exported to South Africa[2].

- Indeed, Malawi has become South Africa's major supplier of household textiles. The value of household textiles exported to South Africa from Malawi has increased by a massive 130% from 1997 to 1998. It is now 90% more than the total value of household textiles South Africa imports from China and Pakistan together.

- It is estimated that in 1999, the clothing and textile sector's total export earnings was around US$77.14 million. With a projected total country's export earnings of US$579 million in 1999, the clothing and textile sector contributed about 13,3% to the country's total export earnings in that year.

Problems Faced by Enterprises in the Clothing and Textile Sector in Malawi

Major problems facing enterprises in the clothing and textile sector include:

- **Low levels of investment.** The current level of investment in the clothing and textile sector in Malawi is estimated to be in the region of ±MK700 million. For the textile sub-sector in particular, the investment levels are so low that it is not possible for this sector to produce all the fabric types demanded by the garment manufacturing sub-sector.

- **Access to finance.** Access to financial credits from commercial banks and other lending institutions is characterised by restrictive collateral lending policies. This is an issue that severely affects the small and medium sized firms.

- **Dependency on imported inputs.** Currently, the garment or clothing manufacturers obtain their key products inputs and accessories from countries within the SADC region (mainly South Africa and Zimbabwe) and from the Far East, such as, Taiwan, Hong Kong, Japan, Singapore, India and South Korea. According to the Ministry of Commerce and Industry, 33,3% of the inputs come from South Africa and Zimbabwe, and 66,7% come from the Far East. Most of the garment/clothing manufacturers rely heavily on the Asian inputs, because of their relatively lower price on world markets, in addition to their good quality and the variety available.

[2] These are 1999 figures.

- **Outdated technologies.** Although there is a high level of awareness of the need for technological change in their production of clothing and textile goods, the majority of firms use old production technology. *Computer Aided Design* and advanced manufacturing systems are not being used in Malawi.

- **Second-hand clothing market.** The massive importation of cheaper second-hand garments/clothes has also adversely affected the performance of the clothing and textile sector in the country. Although these garments provide a means of cheaper clothing for the poorer sections of the population, it also reduces the market share of local producers who could be forced out of business. Indeed, this could lead to a case of de-industrialisation.

Trade Liberalisation and the Clothing and Textile Sector in Malawi

Trade liberalisation will affect the sector through the *World Trade Organisation* (WTO) agreement and the SADC Trade Protocol.

Impact of the WTO agreement (Agreement on clothing and textile (ATC))

- The Agreement provides a timetable for the phased dismantling of the Multi-Fibre Agreement (MFA) and the full integration of the international trade in clothing and textile into the normal WTO disciplines. However, the ATC will not result in significant liberalisation in developing countries (Malawi being one of them) until 2005. The critical analysis reveals that there is very little short-to medium-term negative impact of the WTO Agreement (Uruguay Round of the Marrakesh Declarations) on trade in the clothing and textile sector in Malawi.

- In fact, the WTO Agreement on the clothing and textile trade is protective of the infant firms – the majority of which form the bulk of Malawi's clothing and textile producers. The ATC gives room for the gradual liberalisation of trade in this sector, meaningful increases in access possibilities for small suppliers of the products, and the development of commercially significant opportunities for the new entrants into this sector. The time period for the full implementation of this Agreement and the integration of each Member's clothing and textile products is up to the end of 2004.

- The WTO Agreement on the clothing and textile products is not restrictive on bilateral trade agreements between Members. Malawi has recently signed a Clothing and textile trade agreement with the USA, which gives Malawi a preferential treatment in the export of her clothing and textile goods to the USA.

- The WTO Agreement on the clothing and textile products provides more opportunities than constraints to this sector in Malawi because being one of the least developed countries; Malawi is likely to benefit from these WTO agreements that are biased in favour of LDC's.

Impact of the SADC Trade Protocol

- The SADC Trade Protocol has been formulated within the general global trade liberalisation agreements of the *General Agreement on Trade and Tariffs* (GATT) 1994 as embodied in the WTO Agreement. The full implementation of this Trade Protocol will start after the expiry of 8 years from the date of the signing of the protocol.

- A close scrutiny of all the 39 articles of the SADC Trade Protocol shows that this Protocol does not adversely affect the performance of the clothing and textile sector in Malawi.

- In general trading terms, the proposed SADC *Free Trade Area* (FTA) agreement might have more serious problems with customs revenue. Under the worst-case scenario, Malawi and Mozambique would lose about 90% of their customs revenue because most of their trade is with SADC countries (especially South Africa) and these would not attract any duty.

- Zambia and Zimbabwe would lose 25% and 41% respectively when the SADC FTA is fully implemented. The revenue impact on other SADC countries would be minor.

- The analysis of the clothing and textile sector in Malawi reveals that approximately 95% of this sector's products are exported to South Africa, which is a Member of both SADC and the *Southern African Customs Union* (SACU).

- The latter (SACU) grouping however has developed its own trade proposals, (especially on the clothing and textile products from non-SACU but SADC Member States).

- The SACU proposals and derogations on the Rules of Origin have potential negative effects on the performance and sustainability of the clothing and textile sector in Malawi in particular, and in other least developed country Members of SADC in general.

- The biggest challenge facing the clothing and textile sector in Malawi is the anticipated or potential aggressive regional and international competition on the sector's products. Malawi, as an economy, and the clothing and textile manufacturers, have to prepare themselves for this challenge.

Impact of the COMESA Free Trade Area Agreement

- The full implementation of FTA among the *Common Market for Eastern and Southern Africa* (COMESA) Member States, will take effect from October 2000. This means that goods produced and traded among the COMESA Member States are traded free of duties and *non-tariff barriers* (NTBs).

- The removal of tariffs and NTBs also means that firms, businesses and industries in the Member States will be exposed to intense competition. Those that are located in the more industrially developed member states are likely to capture a larger share of additional income benefits from their products, resulting from the FTA.

- The less competitive firms, businesses and industries in the less industrially developed member states are likely to benefit less in the process. The anticipated fear among COMESA member states is that the FTA is likely not only to worsen existing development imbalances, but might also lead to loss of employment and the creation of potential social problems.

- Most of the COMESA member states are members of other regional groupings. This is likely to create problems in the effective implementation of the COMESA FTA agreement.

- The current trends in the volume of trade in clothing and textile products (imports and exports) between Malawi and other COMESA Member States show that the implementation of the COMESA FTA will have no major adverse effects on the Malawi clothing and textile sector.

- The majority of the clothing and textile product imports for Malawi (finished goods, intermediate goods and inputs) come from the Far East (Hong Kong, Singapore, Taiwan, Japan, India, South Korea etc) and the USA and Europe. Very little come from the COMESA Member States. This importation trend is not likely to shift much after the full commencement of the COMESA Free Trade Area.

- Regarding the export of Malawi clothing and textile goods, the situation is likely also to remain the same – the continuation of exporting the goods to South Africa.

- The demand for the Malawi clothing and textile goods will not shift drastically as a result of the implementation of the COMESA Free Trade Area. South Africa will still be the dominant importer of Malawi's clothing and textile goods in the short-to medium-term.

- Paradoxically, the Free Trade Area within COMESA could lead to expanded market for Malawi's exportable goods, such as clothing and textile.

- The COMESA Treaty (article 49)[3] allows member states to protect strategic, sensitive or infant industries by imposing quantitative or like restrictions or prohibitions on similar goods originating from member states. This restriction is also applicable when injury to such industry is a result of the implementation of the COMESA programme.

- Therefore, if the Malawi clothing and textile sector is negatively affected by the application of the COMESA Free Trade Agreement, then she is in a position to apply the various COMESA Treaty articles to safeguard this sector and its firms.

[3] There are other safeguard clauses such as Articles 51, 52 and 61 which provide safeguards with respect to dumping, subsidies, and general economic disturbances, respectively.

Policy Recommendations

Clothing and Textile Manufacturers

- To get ahead or stay ahead, a firm or industry needs to be **constantly innovating and upgrading** – constantly seeking new markets, better suppliers of inputs, improved ways of doing business, more productive use of human resources – all the things that help maintain a competitive edge. With the current wave of global liberalisation of trade among countries, the clothing and textile manufacturers face a daunting task to maintain their existence, improve the quality of their products and increase the market share of such products.

- **Upgrade the technical and institutional capacities and capabilities** of their firms by enhancing their management and information systems, and their technological expertise in order to improve the quality of their products so that they compete squarely with those of other countries on international markets. Everyone is aware that competitiveness requires quality products and services offered, better prices and efficient delivery.

- **Develop aggressive marketing strategies** for their products and marketing intelligence, in order to have a grip on the world trade trends in similar products. This has to be done in close collaboration with the *Malawi Export Promotion Council* to ensure proper market positioning. Also take advantage of the *USA-AGOA* trade initiative in clothing and textile goods.

- **Increase investment** in all aspects through expansion, consolidation and possible mergers. This will not only lead to the expansion of their export role, the diversification of their activities and the production of a variety of products, but will also contribute significantly to economic growth and to employment creation as their activities are labour-intensive. So far, Malawi trade statistics show that the demand for Malawi clothing and textile products is increasing at the international market.

Malawi Government

It is recommended that the Malawi Government:

- rationalises the country's current complex tariff regime and lowers the overall level of nominal and effective protection to clothing and textile manufacturing firms, and eliminates all non-trade barriers.

- maintains macro-economic stability, develops the private sector–friendly policy environment and puts in place incorruptible efficient exchange rate management system to improve export growth prospects. Research shows that there is a close positive linkage between the exchange rate and the success of trade liberalisation and the improvement of export performance.

- upgrades the institutional capabilities of the *Malawi Export Promotion Council*, the *Malawi Investment Promotion Agency* and the *Small Enterprises Development Organisation* so as to enable them conduct their mandates efficiently and effectively.

- intensifies and upgrades the products quality control mechanisms by upgrading the technical and institutional capacity of the *Malawi Bureau of Standards* (MBS), so that it carries out its responsibilities efficiently and effectively.

- formulates comprehensive and integrative multi-sectoral policies and development-oriented strategies of sectors that are supportive of each other (e.g. agriculture sector-cotton production, and the textiles production).

- improves the economic infrastructure services (e.g. roads, railways, telecommunications, air services, transport facilities, etc) which are of vital importance to the performance and success of trade between Malawi and her trading partners. Being a landlocked country, Malawi needs to seriously cultivate regional co-operation in transport services for her trade and economic survival. Revenue from transport services provides a crucial component of national income.

- strengthens corporate performance through the formulation of fair and transparent laws, regulations, competitive trade policies and forward–looking incentive–based tax policies.

- Implements strict policies aimed at controlling and curbing the current high level of illegal importation and smuggling of clothing and textile goods into the country.