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IMPLICATIONS OF THE TERMINATION OF THE AGREEMENT ON TEXTILES AND CLOTHING (ATC) FOR LATIN AMERICA AND THE CARIBBEAN

The impacts of quota elimination under the Agreement on Textiles and Clothing (ATC) applicable since 1 January 2005 are already becoming apparent on Latin American and Caribbean countries' exports to the United States ; despite vastly different performances from country to country, the region as a whole experienced a reduction in market share, in contrast to a marked increase by China . In theory, if this rhythm of growth were to be sustained, the market share of United States imports from China in this sector could increase or even surpass the 50% mark in the next three years.

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I. INTRODUCTION

The impacts of quota elimination under the Agreement on Textiles and Clothing (ATC) applicable since 1 January 2005 on the countries of the region are already becoming evident. Since that date, the rate of growth of China 's share in United States textile and clothing imports has continued to increase steadily: market share in the first nine months of the year, compared to the same period

the previous year, increased by over 61% in value and about 46% by volume. Consequently, China's share in the imports in the sector over the same period increased in value from 17% to 26%, and in volume from 25% to 33%.^[1] In the light of this massive increase, the United States Government began to apply special safeguard mechanisms to the main categories of textile and clothing products from China from about mid-May 2005. Despite the application of these mechanisms, the upward trend has persisted. If this rhythm of growth were to be sustained, China's share in the United States market could surpass 50% of total imports of this sector in about three years, at the expense of countries in Africa and Latin America relying on preferential access.

Nevertheless, the overall behaviour of exports to the United States since 1 January 2005 has been extremely heterogeneous between countries and regions (see table 1); the somewhat disappointing overall performance of Latin America and the Caribbean during the first nine months compared to the same period in 2004 has been wrought mainly by the performance of Mexico whose exports have dropped by about 6% both in volume and value. Great disparity has also become evident between the performances of signatory countries to the United States-Dominican Republic-Central America Free Trade Agreement (US-DR-CAFTA): in terms of value, Costa Rica, Dominican Republic and El Salvador have not been able to maintain exports to the United States at the previous period's levels. In contrast, Nicaragua has been able to increase textile and clothing exports considerably. The same upward tendency can be observed in the remaining countries of the US-Caribbean Trade Partnership Act (CBTPA) although with great disparity between countries. Of the four Andean Trade Promotion and Drug Eradication Act (ATPDEA) countries, Ecuador and Bolivia have experienced a decline especially in volume, in contrast with the case of Peru. Despite the relatively small quantity of their exports, countries like Chile and Paraguay have been able to increase their exports significantly. Argentina has demonstrated very erratic behaviour in terms of both value and volume. It is interesting to note that Asia (excluding China and India) has also experienced negative growth during the same period with great variations between countries (not included in table 1).

Table 1

UNITED STATES: RATE OF GROWTH OF TEXTILE AND CLOTHING SECTOR IMPORTS 2003-2004

BY VALUE & VOLUME, COUNTRY OR REGION OF ORIGIN,

JANUARY 2005-SEPTEMBER 2005 AND OCTOBER 2004-SEPTEMBER 2005

(%)

Country /Region of origin	Value			Volume		
	2003/	January 2005/	October 2004/	2003/	January 2005/	October 2004/
	2004	September 2005	September 2005	2004	September 2005	September 2005
World	7.6	8.5	9.7	11.2	8.5	9.0
China	25.5	61.3	54.1	40.7	46.0	42.1
India	13.1	25.6	26.3	14.9	20.3	20.3
Mexico	-1.9	-6.3	-4.6	4.4	-5.7	-4.1
DR-CAFTA	3.6	-1.5	1.3	3.4	2.0	2.8
Dominican Republic	-2.9	-6.7	-4.3	1.9	-1.7	-0.5

Guatemala	10.5	-1.5	3.8	12.9	-0.5	3.4
Honduras	6.8	0.1	2.8	3.8	5.9	6.8
El Salvador	0.0-	-3.7	-2.5	0.0	2.7	0.3
Nicaragua	22.9	21.0	25.5	17.9	16.5	20.7
Costa Rica	-11.8	-7.5	-6.4	-5.6	-8.4	-6.9
ATPDEA	25.3	10.1	13.8	18.8	-3.9	1.0
Colombia	18.1	0.8	5.2	11.5	-4.6	-0.3
Peru	34.0	20.4	23.5	33.1	8.6	13.2
Ecuador	10.3	-6.0	-5.1	19.6	-29.2	-16.7
Bolivia	15.3	-10.2	-3.9	28.6	-56.3	-48.4
Brazil	0.6	6.0	1.1	14.8	-13.8	-11.9
B. Rep. of Venezuela	-23.6	-33.9	-26.9	119.0	1.4	49.0
Chile	125.7	15.9	45.2	149.6	58.2	83.4
Argentina	40.9	15.0	27.2	5.1	-60.2	-55.2
Uruguay	18.5	1.9	13.5	17.9	10.9	11.9
Paraguay	-67.2	3.3	-40.4	-67.6	307.3	112.7
TOTAL						
Latin America & Caribbean	2.6	-2.1	0.1	4.9	-2.6	-1.1
Total Asia *	3.9	-4.1	-0.5	4.3	-3.9	-1.8

Source: Author's compilation based on data from the Office of Textiles and Apparel (OTEXA), United States Department of Commerce.

* Excluding China and India

II. BACKGROUND TO THE AGREEMENT ON TEXTILES AND CLOTHING (ATC)

The bilateral agreements between importing and exporting countries to impose quantitative restrictions on the imports of these products – outside the norms and disciplines of the General Agreement on Tariffs and Trade, GATT) – originated in the second half of the twentieth century. In 1960 GATT, recognising the problems occasioned by these bilateral agreements and in an attempt to avoid market disruption, authorized Members to negotiate or impose bilateral import quotas outside the rules and regime of GATT itself. This policy led to the signing of other agreements on the application of quantitative restrictions and eventually to the Multifibre Arrangement (MFA) in 1973, whose objective was to protect the domestic industries of textile and clothing importing countries for four years by means of import quotas, after which the restricted products would be integrated into the norms and disciplines of GATT. However, the Arrangement was extended on four occasions until 1994 due to protectionist positions of Members.

The MFA was the target of criticisms from detractors who indicated that it violated the principles of multilateralism and free trade represented by GATT: the MFA departed from the principle of most-favoured nation (MFN); it applied quantitative restrictions instead of tariffs; it was discriminatory towards developing countries and had no clear rules. In view of this, the Uruguay Round of GATT began to incorporate the sector into GATT rules. In December 1993, the ATC was signed whose goal was to integrate textiles and clothing products into the norms and disciplines of the World Trade Organization (WTO) over a period of 10 years between 1995 and 2005.

A. The ATC “integration process”

The first stage of the ATC began on 1 January 1995 when each signatory to the Agreement had to select and integrate products from the list in the Annex of the ATC which had represented not less than 16% of the total volume of that Member's 1990 imports in that sector. In January 1998 the second stage began, during which products had to be integrated that had had represented no less than a further 17% of the Member's imports during 1990. In January 2002 the third stage began, in which products had to stand integrated that had represented no less than a further 18% and finally on 1 January 2005, the remaining 49% of all products had to stand integrated.

The only WTO Members to apply the quota growth rate commitments (the United States , the European Union, Canada and Norway) left the products that were most sensitive to their domestic producers for the final stage of the integration process.^[2] In other words, the products integrated during the first three stages turned out to represent a smaller percentage in value than in volume (on which the “integration process” had been based).

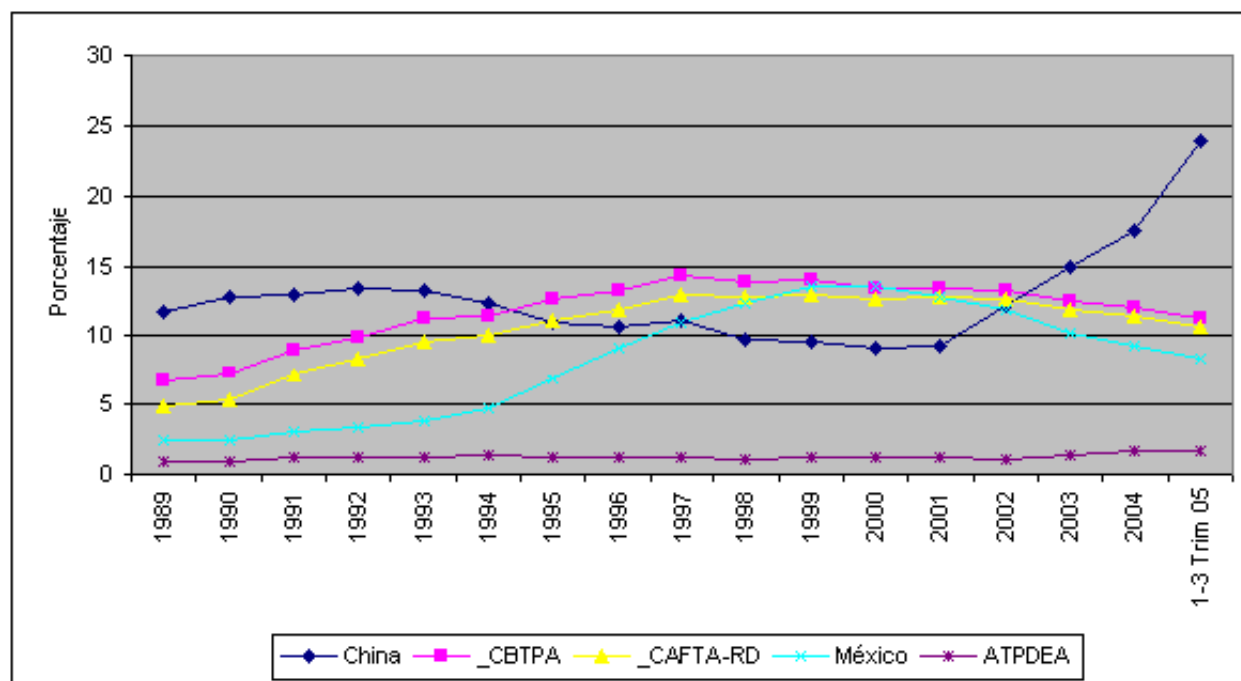
This also implied that the liberalization of products with higher trade potential had not occurred. Neither had the three stages of the integration process guaranteed a smooth transition for importing and exporting countries towards the termination of the ATC.

Chart 1

UNITED STATES: SHARE IN CLOTHING IMPORTS BY COUNTRY/REGION

1989-THIRD QUARTER 2005

(%)



1st_
3rd
Quarter
2005

Percentage

Source:
Author's
elaboration
based
on
data
from
the
Office
of
Textiles
and
Apparel
(OTEXA),
United
States
Department
of
Commerce.

Estimates of the impact, expressed in Export Tax Equivalents (ETEs) taking 1997 as base year, show that in general, quotas associated with clothing have been much higher than those corresponding to textiles, in both the United States and the European Union. The United States and Canada have had the most restrictive quotas, reason why the impact of reductions on their imports in that sector has tended to be more dramatic. The manifestly high ETEs of China and India would imply a greater openness of the market to products from these countries during stage 4, and intensified competition with other Asian countries and with Latin America on the eve of the termination of the ATC. Indeed, the ETEs for some Members are much higher than the average tariffs for manufactured products imported by the United States and the European Union.

B. The level of quota utilization

From an economic standpoint, there are clear benefits to be had from quota elimination: in theory quotas, like tariffs, raise the domestic price of that product in the importing country and diminish domestic demand for that product. However, as this concerns quotas and not tariffs, increases in price benefit domestic both producers and exporters. Quota elimination would damage not only local producers in import markets but importers as well. Many domestic producers protected from external competition by the quota system would have to compete through cost effectiveness. Consumers in importing countries would be the ones to benefit.

Various studies confirm that quota fill-rates during the first two stages were relatively low. In the United States market during the nineties, only about 40% of United States imports in the textile and clothing industry entered that market under "binding" quotas and this percentage remained relatively stable throughout the decade. Later, during 2001-2002, the quota fill-rates by China in the 90 categories of quotas applied by the United States reached 76% on average. However, in the category of sensitive products, by implication having higher quantitative restrictions, the quota fill-rate for the United States was almost 100%.

Under the quota regime, the majority of clothing exports from China have been arranged through middlemen located in Hong Kong (China), the Separate Customs Territory of Taiwan, and Macao , and accredited as exports from those economies and not from China . The significant reduction in the unit cost of exports from China registered in recent years probably reflects the elimination of previously incurred intermediary charges.

In practice, quotas probably have not been that “binding”. The constraints to trade contributed to the fragmentation of the international supply chain through internationally integrated production systems. The dismantling of the production chain in this sector began when the production of one Member like China filled its quota to the maximum. The process of clothing assembly was sub-contracted to low-wage developing countries like Bangladesh . Thus when a country had filled its quota, the companies that had been in production there redirected their operations to other countries that had not yet filled the export quotas set by the importing country. At the same time, developed countries guaranteed preferential market access to a number of low-wage countries for the assembling of pieces of clothing that would later be re-imported under preferential conditions.

III. APPLICATION OF SAFEGUARD MECHANISMS BY THE UNITED STATES AND THE EUROPEAN UNION TO CHECK IMPORTS FROM CHINA

A. UNITED STATES

As a result of the surge in imports, manufacturers of textile products and clothing apparel pressed the United States Government to re-apply import quotas to goods from China based on the argument that since the elimination of global quotas on 1 January 2005, products from China had flooded the United States market. From the moment this petition was received on 27 May 2005, China has had to restrict its exports in seven groups of products to a level 7.5% higher than the previous year, in compliance with the stipulations of the Agreement for the Accession of China to the WTO. As no mutually satisfying solution was agreed within the 90-day consultation process, the United States added two further products to the restricted categories of imports from China . Strictly speaking, the new import quotas applied by the United States do not violate WTO rules since China accepted the application of safeguards until 2008 as part of its conditions of accession to WTO in 2001. Subsequently, on 7 November 2005, the United States and China agreed that exports from China could increase by 10% in 2006, by 12.5 % in 2007, and between 15% and 16% in 2008, integrating over 30 items of clothing.

B. EUROPEAN UNION

European authorities also considered the application of some trade restricting instruments to stem the tide of imports of textiles and clothing from China . On the basis of import statistics corresponding to the first quarter of 2005, the Commission initiated an investigation into 10 categories of textile exports to the European Union and verified that, in every case, the volume of goods imported had exceeded the defined “alert levels”.

Following arduous consultations and in an attempt to avoid a trade war, both parties agreed on 10 June that, from 11 June 2005 until the end of 2007, the increase in textile exports from China to the European Union would not exceed between 8% and 12.5% annually over a specified base quantity. In 2008, the European Union would only apply “with restrictions” paragraph (c) of Article 242 relating to textiles of the Report of the Working Party for the Accession of China

to the WTO, which requires China to restrict exports of those products. On 5 September 2005, China and the European Union signed an amendment to the previous agreement which restricted the access to European markets of articles from the 10 textile categories. Through this amendment, the import quotas were increased to allow the entry of tons of articles from China held up at European ports as a result of the application of the special safeguard mechanisms.

IV. PREFERENTIAL TRADE

It is significant that the various free trade agreements both regional and bilateral signed by the United States and the European Union have granted preferential access to a growing number of developing countries that are exporters of textiles and clothing. Added to this, the extreme complexity of the rules of origin that regulate this sector have a strong impact on the degree to which this preferential access can be utilized to best advantage to increase exports.

Since the eighties, the trade regime of the United States created various programmes intended to stimulate the inbond assembly industry abroad and to levy taxes only on the value-added of the final product (and not on raw materials originating in the United States), the CBTPA Act of 2000 being one of many that were of particular benefit to Mexico and the countries of the Caribbean basin. The US-DR-CAFTA treaty represented a reaffirming of the preferences that the United States had already granted under the Caribbean Basin Initiative (CBI) and CBTPA. Under this agreement products from Central America and the Dominican Republic could enter the United States without tariffs, respecting the rules of origin; in the negotiations it was agreed to include a schedule of scarce items^[3] that allowed the importation of raw materials on the schedule from Members of NAFTA, the African Growth and Opportunity Act (AGOA) and the Andean Trade Preference Expansion Act (ATPEA), to be included as countries of origin. Costa Rica and Nicaragua were granted preferential access as countries of origin in the use of some fabrics in the same manner that Mexico had been permitted under NAFTA, Costa Rica for 2 years and Nicaragua for 5 years. Colombia, whose export markets in this sector have been more diversified, was not so dependent on the preferential status conferred by the United States. Since the formalization of ATPDEA in 2002 the Andean Countries have taken considerable advantage of their preferential access to export to United States markets.

In the case of the US-Chile Free Trade Agreement, all tariffs on both imports and exports of textiles and clothing of both signatories were immediately eliminated as soon as the Agreement came into force on 1 January 2004. Under the same Agreement two quotas were negotiated, one of them with more flexibility on rules of origin than the general regime for a group of textile and clothing products that Chile does not produce. A system of border co-operation was also agreed on to avoid triangulation from a third country.

V. OTHER FACTORS BEARING ON THE COMPETITIVENESS OF LATIN AMERICA AND THE CARIBBEAN

The termination of quotas certainly does not mean free trade in the sector. Both developed as well as developing countries will continue to be equipped with special safeguard and anti-dumping instruments. Tariffs applied to the textile sector and especially to the manufacture of clothing have been relatively high in comparison with those of other manufactured products. The tariff levels in this sector applied in the industrialised countries in the post-Uruguay Round stage are the highest outside those of agricultural products, tripling or quadrupling the levels applied to other industrial goods. Added to this, the tariff cuts forthcoming in this sector have been very modest.

Consequently, the impacts of quota elimination on exports from China could be smaller or less marked than some studies indicate. The main reasons for this conclusion are that these models do not take into consideration elements such as: (i) the industrial structure and the raw material stockpiling strategies of producers continuing to diversify their suppliers' countries of origin; (ii) the protectionist system with its various preferential schedules, including rules of origin which regulate trade in this sector that would allow importing countries to keep on regulating trade once the ATC terminates; and (iii) the cost to industrialized countries of the adjustments that will need to be made in the textile and clothing industry, which could open the door to protectionist policies that invoke clauses on special safeguard mechanisms or anti-dumping measures.

In this respect, it would benefit countries of the region to have a development strategy that enables them to strengthen their industry vertically, that is, not only in the assembly stage but also in the storage of raw materials, design, distribution, and other areas that strengthen the textile and clothing industry as a whole, such as implementing training schemes and improving product quality. Countries should also base their comparative advantage on quality, response time, distribution, etc., and discard advantages to do with labour costs. One option to strengthen competitiveness is through the formation of strategic alliances with other countries in the region such as with some of their greatest competitors in the United States market.

[1] The apparent jump for those months in 2005 are actually a result of the dynamic nature of Chinese imports during stage 3 (from January 2002 to December 2004) of the ATC implementation process, when imports grew from China grew at rates of 29% and 53% in value and volume, respectively.

[2] During the three stages, the United States, the European Union and Canada eliminated only 164 of the 1,271 quantitative restrictions carried over from the MFA. The United States only eliminated 57 of the 758 restrictions and the percentage of restrictions eliminated before stage 4 represented only 7.5% of the volume of its textile and clothing imports. In these stages, those Members chose to integrate products that were: (i) not covered by quotas; (ii) covered by underutilized quotas (quota redundant); or (iii) had low unit costs.

[3] The schedule included fabrics not found in the United States, Central America or the Dominican Republic, whose imports would therefore be permitted from countries belonging to NAFTA, AGOA or ATPEA.