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# Rules of Origin under Generalised System of Preferences as A Market Access Barrier to Indian Textiles and Clothing Exports

## With Special Reference to US and EU Markets

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*Editor:* **Anil K. Kanungo**

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# FOREWORD

Textile and Clothing (T&C) trade represents 5.7 per cent of world exports. In four decades, world T&C trade increased by more than 60 times (actually faster than total goods trade, which grew by 48 times), from less than $6 billion in 1962 to $342 billion in 2001 (in nominal terms). Labour intensive clothing sector has increased much faster than the textile and represents 57 per cent of world T&C trade. In the late 1980s, developing countries overtook industrialised countries in their share of T&C exports, and now account for 50 per cent of world exports of textile and 70 per cent for clothing. As far as India is concerned, EU and USA remained major export destinations for T&C.

In spite of the multilateralism that the WTO regime is expected to promote, market access to export destinations is determined by the regional and preferential trade agreements and the benefits are enjoyed by the countries under other trade programmes like GSP. The study was undertaken to explain the type and nature of the GSP rules of origin and its escalation as provided by the principal donors such as the EU and USA to the Indian Textiles, and also to determine the extent to which donor countries' domestic interests have shaped the rules of origin. The paper has dwelt upon the existent state of the local textiles and clothing sector in India and analysed the implications of EU and US GSP rules of origin on the nature and competitiveness of textiles and clothing sector in India. The extent to which Rules of Origin have constrained the input-output mix of the Indian textiles and clothing sector has been looked into and the study has also considered whether the Rules of Origin under MFA would affect the ability of India's garment exporters to compete in the global market once the MFA has been phased out.

There are no specific methods developed in the past to measure the implication of GSP rules of origin on particular sector. But in this paper, a host of indicators are constructed to analyse the implications of GSP Rules of Origin. In addition to these indicators, certain other tools have been used for the study and are explained at the appropriate sections.

The study covers a time span of five years from 1997 to 2001 for the detailed analysis. Massive data have been analysed to arrive at specific conclusions. In addition, industry visits have been undertaken to understand the practical problems faced by the exporters in complying with the rules under GSP schemes. The industrial visits have covered individual firms and prominent textile clusters such as Bangalore, Ludhiana, Tirupur, Coimbatore, Karur, etc. to various product categories in T&C sector. The paper, we hope, would be useful for policy planning as also for evolving firm strategies. This Institute would be only too happy to host debates and discussions on the issues flagged in the paper.

**PRABIR SENGUPTA**
DIRECTOR

New Delhi
April 2004

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# Rules of Origin under Generalised System of Preferences as a Market Access Barrier to Indian Textiles and Clothing Exports

## With Special Reference to US and EU Markets

*K. Rangarajan*

### Prelude

HISTORICALLY, textiles and clothing (T&C) has played a major role in economic development. Their role in the Industrial Revolution in Western Europe and North America is well known; today they are spearheading industrialisation in the developing world. International trade in textiles and clothing has long been managed through a complex system of quota restrictions. For nearly half a century, world trade in textiles and clothing has been subject to quantitative restrictions, beginning with Japan's 1955 "voluntary restraints " on its exports of cotton fabrics and clothing to the USA, which evolved in stages into the Multi-Fibre Arrangement (MFA) in 1974. The MFA expanded quantitative restrictions beyond cotton products and was extended several times until the Uruguay Round Agreement on Textiles and Clothing (ATC) took effect at the beginning of 1995. Since the establishment of World Trade Organisation (WTO), global textiles and clothing industry has been going through significant transformation driven by phase out of Multi Fibre Arrangement (MFA) under Agreement on Textiles and Clothing (ATC).

The extent to which a country permits imports (Market Access) of textiles and clothing in WTO regime is dependent upon tariff and non-tariff barriers agreed by its members. This apart the Generalised System of Preferences (GSP) also acts as an important trade programme for least developed and developing countries in strengthening their competitive advantage in the developed markets. The GSP is composed of trade preferences granted by developed world to developing countries on a non-reciprocal basis, i.e., without market access

concessions in return. This concept developed within the UNCTAD to encourage expansion of manufactured and semi-manufactured exports from developing countries by making such goods more competitive in developed-country markets through tariff preferences. The GSP reflects international agreement, negotiated at UNCTAD-II (New Delhi, 1968), that a temporary and non-reciprocal grant of preferences by developed countries to developing countries would be equitable and, in the long term, mutually beneficial. To meet its GSP commitment, each industrialised nation determined its own system of preferences, specifying the goods, the margins of preference, and in some cases, the value or volume of goods that would benefit from preferential treatment. Twenty-seven industrialised countries, including the USA now maintain GSP programmes. The main principle of GSP is to provide better-than-MFN (Most Favoured Nation) treatment to imports from qualified countries.

Coupled with dwindling margin, rising importance of new trade policy instruments like rules of origin among the principal GSP donor countries including EU and USA are the major concern for the developing nations like India. Rules of Origin (ROO) have steadily emerged as an important policy issue influencing the market access.

ROO is an important instrument through which wide range of trade issues including trade preferences, quotas and antidumping measures are administered in a country. Since GSP is the only scheme that provides some special market access to the developing nations like India, its ROO provided by the principal donors have significant effect on the beneficiaries. One of the key factors underlying the difficulties in obtaining the preferential access under GSP to the donor country market is said to be the stringency in the GSP ROO. GSP ROO is intended to ensure that the benefit of the preference is provided only to the products, which are manufactured in the preference receiving country. The current GSP schemes have different product coverage and different time-frames. Above all, each GSP donor country has different ROO for different product categories. As a result, a large network of complex GSP rules is prevailing today. The complex GSP ROO also deny the market opportunities for those countries that are not in a position to meet the requirements

even though they are eligible for GSP. In this context, this paper attempts to trace out the implications of the complex GSP Rules of Origin of EU and USA on the export market access of Indian Textiles and Clothing sector.

## Indian T&C Industry

Textiles and clothing industry forms a significant portion of manufacturing base of many developing countries. Textiles industry is one of the main pillars holding the Indian economy. It constitutes about 14 per cent of industrial production, 27 per cent of export revenue and 18 per cent of employment in the industrial sector (*Annual Report 2002-03,* MoT, GoI). In spite of these, India's entire share in the world textiles trade is still maintained at around 3 per cent.

Mills, powerlooms and handlooms constitute three independent sectors of the Indian textiles industry. The mill sector is organised, mechanised and modernised concentrating on the production of yarn whereas the powerloom and handloom sectors have remained technologically backward and stagnant. Almost all the spun yarn made in India comes from the organised mill sector, reflecting the highly capital intensive nature of yarn spinning. Weaving in the mill sector has been gradually suffering due to the competition from the powerlooms and the trend may continue. Most of India's competitors in textiles in the world market have a much larger number of shuttleless looms. The hosiery sector caters mainly to the inner garment requirements.

Further, the analysis of the value chain would help in understanding the weak links of the firms and the country, which may influence their ability to gain from participating in the global market with special reference to USA and EU under the preferential access. The analysis depicted that the strong cotton base has helped the industry to effectively serve the ultimate market however the machinery support required to strengthen this link seems to be weak. Around 50 per cent of the fabric production consists of cotton. Most of the fabric production occurs in the decentralised sectors with the powerloom sector generating 60 per cent. The handloom sector and the hosiery sector produce 36 per cent of the total and remaining 4 per cent comes from the organised mill sector.

*FIGURE 1*

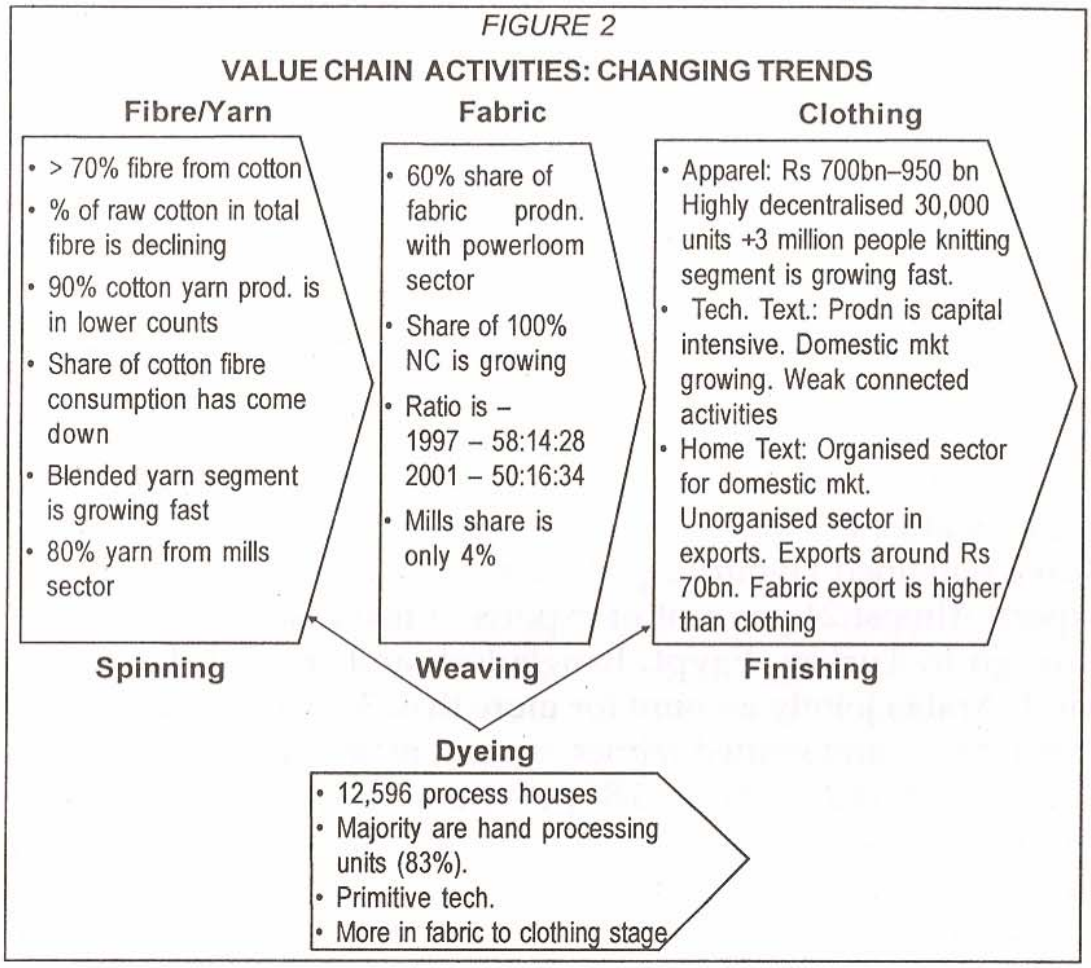
**SECTORAL FEATURES OF INDIAN TEXTILES INDUSTRY**

| Mill | Powerloom | Hosiery | Handloom |
|---|---|---|---|
| • Highly capital intensive<br>• Operates in both spinning and weaving<br>• Uses both natural and man-made fibres<br>• Organised sector<br>• Spinning is the predominant process<br>• Uses spindles, looms and rotors | • Highly decentralised<br>• Caters to the fabric requirements<br>• Uses both cotton and non-cotton yarn<br>• Produces both gray and processed fabrics<br>• Weaving is the predominant process<br>• Mainly uses shuttle looms | • Highly decentralised<br>• Caters mainly to inner garments<br>• Uses both cotton and non-cotton yarn<br>• Knitting is the predominant process | • Highly decentralised<br>• Handloom technology is regionalised<br>• Operates as household units<br>• Hand weaving is the predominant process<br>• Mainly uses all natural fibres |

The textile processing segment of the Indian textiles industry is highly fragmented. It can be divided broadly into four segments, viz. Hand processing units, Hand processing units with certain exempted power processes, Independent power processing units, and Processing facilities attached to composite or semi-composite mills. Most of the independent power processing and hand processing units are located in or near powerloom centres and they bleach, dye, print or otherwise finish fabrics principally for the decentralised sectors.

India is a small producer of technical textiles; the domestic market has increased due to the increase in demand for automotive fabrics from the automobile industry. In home textiles, the market is dominated by the decentralised powerloom and handloom sectors, which supply unbranded cotton goods. The handloom sector is not competitive in products made from finer yarn counts. The powerloom sector dominates production of home textiles made with finer yarn counts such as sheets and pillowcases. A large portion of India's fabric exports is used to make home textiles. India currently exports about 2 billion square metres of fabric annually for the use in bed linen; most of these exports comprise low valued unfinished fabrics destined for the EU markets.

The value chain activities of the T&C industry in India is summarised and shown in Figure 2. The analysis shows that while the numbers of textiles mills in the country increased, the




composite mills have drastically declined. Loomage in the mills has been declining steadily in the recent years while the shuttle-less looms are rising still forming only 6.47 per cent of the total loomage of the mill sector in the country. Powerloom and hosiery sectors are shifting more towards non-cotton/blended yarn whereas mill and the handloom sectors are maintaining lead in the cotton yarn. Fibre yarn output is predominantly with the organised mill sector whereas the fabric is in the decentralised powerloom sector. In the fabric output, share of 100 per cent non-cotton is growing. In the apparel output, growth of the knitted segment is high as compared to the woven segment. Technical textiles and home textiles are the potential export sectors with limited present share. The dyeing and finishing activity in the value chain is a weak link.

## Indian T&C Exports

The exports of textiles and clothing play an important role in developing economy, as it accounts for a major share in the total

exports. It has been contributing about 27-30 per cent to India's overall export trade. China is the leading exporter of textiles to the world (10.2%) followed by Korea (8.1%). India remained at the tenth position with a share of 3.4 per cent. In world clothing exports, China held a share of 18.1 per cent followed by Italy (6.6%). India ranked at 8th position with a share of 2.8 per cent (*International Trade Statistics*, 2001, WTO, p. 154).

Major export destinations of Indian textiles and clothing stood out to be EU, USA, UAE and Russia. USA was the leading importer of silk followed by EU, Hong Kong, Singapore and UAE. In wool, Columbia has emerged as one of the important markets after EU and USA. EU, Bangladesh, Hong Kong and Korea remained favourite destinations for India's cotton textiles export. Almost 24 per cent of exports of manmade filament and yarn go to Turkey, Egypt, Bangladesh and Ireland. UAE and Saudi Arabia jointly account for more than 33 per cent of exports of manmade and knitted fabrics. Second major market for fabrics was EU (14% share). Around 86 per cent of total exports of carpets and floor coverings were accounted by USA and EU. Hence it was seen that in spite of few odds, the export of this industry has shown relatively consistent performance in both US and EU markets. A detailed analysis of the trend in EU and US markets is given in the following sections.

## I. EU-INDIA: TRADE IN TEXTILES & CLOTHING

### (a) Overall Trend

India is a major supplier of textiles and clothing to 15 nations (EU). Exports of these items accounted for 35 per cent of the country's total exports to the EU (*Textile Times*, April-June 2002, p. 11). The dependence of EU on extra-EU markets has risen over the years. The composition of extra-EU imports consists of mainly fifteen preferential suppliers, seventeen restrained suppliers including India and others. In case of India, the share has consistently declined from 6.6 per cent in 1996 to 5.8 per cent in 2000, in spite of corresponding increase in the share of restrained suppliers, which shows that India is losing in the EU market to other restrained suppliers and preferential suppliers. This can be further analysed by segregating the trends in textiles and clothing separately.

*TABLE 1*

TRENDS IN TEXTILES & CLOTHING IMPORTS OF EU

(US$ billion)

| Exporter | 1996 | 1997 | 1998 | 1999 | 2000 | % change (1996-2000) |
|---|---|---|---|---|---|---|
| Intra-EU | 73.90 | 69.54 | 71.67 | 62.08 | 57.31 | -22.4 |
| Extra-EU (100%) | 62.52 | 64.92 | 67.33 | 65.39 | 65.91 | 5.4 |
| Preferential suppliers | 19.07 (30.5) | 19.48 (30.0) | 21.70 (32.2) | 21.14 (32.3) | 20.85 (31.6) | 9.3 |
| Restrained suppliers | 27.09 (43.3) | 28.58 (43.9) | 28.72 (42.7) | 28.60 (43.7) | 29.42 (44.6) | -8.6 |
| Others | 16.36 (26.2) | 16.31 (26.0) | 16.91 (25.1) | 15.65 (23.9) | 15.64 (23.7) | -4.4 |
| India | 4.11 (6.6) | 3.94 (6.1) | 3.86 (5.7) | 3.69 (5.6) | 3.79 (5.8) | -7.8 |

*Notes:* 1. Preferential suppliers (10) are: Bulgaria, Czech, Hungary, Poland, Romania, Slovak, Malta, Morocco, Tunisia and Turkey.

2. Restrained suppliers (17) are: Argentina, Brazil, China, Chinese Taipei, Hong Kong, India, Indonesia, Korea, Macau, Malaysia, Pakistan, Peru, Philippines, Singapore, Sri Lanka, Thailand, and Vietnam.

3. Figures in brackets indicate share of suppliers in extra-EU trade.

*Source: EuroStat* (Cat.: KS-CK-01-502-3A-2).

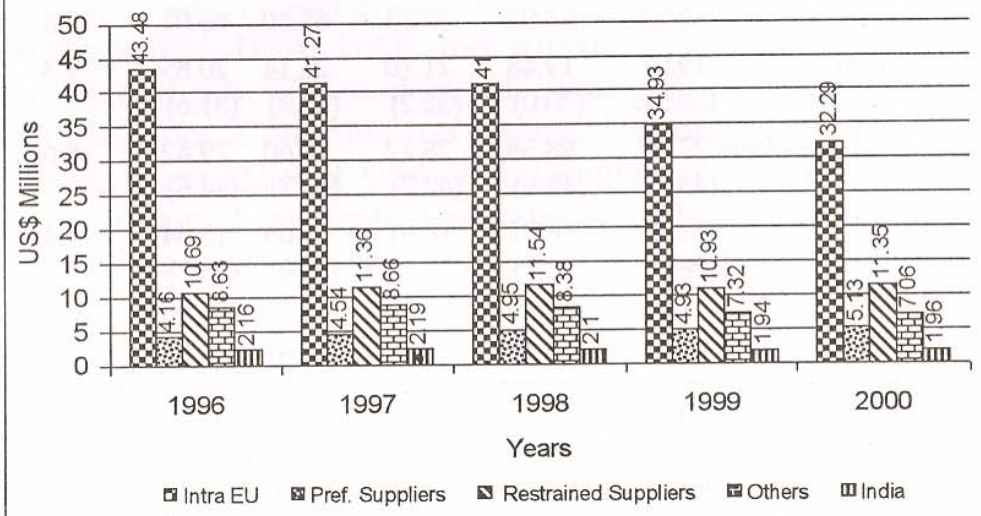
In a nutshell, the import of textiles and clothing indicates that the intra-EU imports have come down recording a negative growth rate of 22.4 per cent during the period 1996 to 2000. However, the extra-EU imports have grown by 5.4 per cent during the same period. Among the extra-EU imports, the preferential suppliers recorded highest growth rate of 9.3 per cent as against the growth rate of restrained suppliers at 8.6 per cent. The other sources of suppliers have experienced a negative growth of 4.4 per cent during the period. In case of India, the imports of EU have come down by 7.8 per cent irrespective of positive growth shown by restrained suppliers.

### (b) Trend in Imports of Textiles

The import of textiles into EU has shrunk from around US$67 billion in 1996 to around US$55 billion in 2000. The intra-EU

import has come down by around 26 per cent during this period. However, the extra-EU import remained at around US$24 billion over the same period. In the composition of extra-EU import, preferential suppliers have improved their market share from around 18 per cent in 1996 to 22 per cent in 2000.

GRAPH 1
TREND IN THE IMPORT OF TEXTILES BY EU




*Source:* EuroStat (Cat.: KS –CK-01-502-3A-2).

Though the share of restrained suppliers has increased from 45.5 per cent in 1996 to 48 per cent in 2000, their value of exports to EU remained at around US$11 billion. Suppliers from the other sources have declined consistently since 1996. In the case of India, the value of exports remained at around US$2 billion but showed a declining growth rate.

### (c) Trend in Imports of Clothing

The import of clothing from extra-EU sources was at around US$42 billion since 1998. Among the sources, the restrained suppliers maintained a share of around 43 per cent closely followed by preferential sources at 37.1 per cent and others at 16 per cent in 2000. Though the share of preferential sources has come down in 2000, they achieved a considerable growth in 1998 and 1999. Similarly, the other suppliers have also stabilised their position since 1997 at around 16 per cent. In the case of India, the share has declined from US$ 1.95 billion in 1996 to around US$1.75 billion in the following years upto 1999, but once again marginally

increased to US$1.83 billion in 2000. Though the restrained suppliers achieved a growth rate of 10.2 per cent during the period 1996-2000, India has recorded declining growth of 6.2 per cent.

*TABLE 2*

**TREND IN CLOTHING IMPORTS OF EU**

(US$ billion)

| Exporter | 1996 | 1997 | 1998 | 1999 | 2000 | % change (1996-2000) |
|---|---|---|---|---|---|---|
| Intra-EU | 30.43 | 28.28 | 30.67 | 27.14 | 25.02 | -17.8 |
| Extra-EU (100%) | 39.03 | 40.36 | 42.46 | 42.22 | 42.38 | 8.6 |
| Preferential suppliers | 14.91 (38.2) | 14.94 (37.0) | 16.75 (39.4) | 16.21 (38.4) | 15.73 (37.1) | 5.5 |
| Restrained suppliers | 16.40 (42.0) | 17.17 (42.5) | 17.18 (40.5) | 17.67 (41.8) | 18.07 (42.6) | 10.2 |
| Others | 5.77 (14.8) | 6.5 (16.1) | 6.8 (15.9) | 6.6 (15.6) | 6.8 (15.9) | 17.9 |
| India | 1.95 (5.0) | 1.75 (4.3) | 1.76 (4.1) | 1.75 (4.1) | 1.83 (4.3) | -6.2 |

*Notes:* 1. Preferential suppliers (10) are: Bulgaria, Czech, Hungary, Poland, Romania, Slovak, Malta, Morocco, Tunisia and Turkey.

2. Restrained suppliers (17) are: Argentina, Brazil, China, Chinese Taipei, Hong Kong, India, Indonesia, Korea, Macau, Malaysia, Pakistan, Peru, Philippines, Singapore, Sri Lanka, Thailand, and Vietnam.

3. Figures in brackets indicate share of suppliers in extra-EU trade.

*Source: EuroStat* (Cat.: KS -CK-01-502-3A-2).

### (d) Item-wise Analysis of Textiles Imports of EU

As has been seen earlier, the overall direction of imports of textiles by EU showed marked improvement by preferential sources and consistent growth by restrained suppliers. However, India as a source of supply recorded a negative growth. This can be further analysed through item-wise analysis of products falling under HS codes 50 to 60. (Annexure 2). Among these products, raw cotton, yarn & fabrics (HS 52) remained as a major item of import, holding a share of 24.7 per cent (as of 2001). Though its share has consistently declined from 28.8 per cent since 1996, it has recorded the highest change of 5.2 per cent in

2000-01. It is followed by manmade filament yarn & fabrics, which held a share of around 19 per cent since 1998.

Among the eleven product items, India was among the Top-5 suppliers in seven, holding the first position in other vegetable textiles fibre (HS 53) and textiles floor coverings (HS 57). In raw silk, silk yarn & fabric (HS 50), China as a single supplier covered more than 60 per cent of the total imports of EU. India also managed to improve its position since 2000. In animal hair, yarn & fabric (HS 51), India's share remained low at around 2 per cent. A major shift in sourcing can be seen in the import of cotton yarn, fabric (HS 52) wherein Turkey (preferential suppliers) emerged as the first ranked supplier, since 1998. Though India managed to improve its exports from 2000, major decline was witnessed by Uzbekistan, which earlier held the Top-5 status. Hence it remained as vulnerable item for India.

In the manmade fibre and fabric segment (HS 54 & HS 55), EU witnessed consistent growth in imports. In both the cases, Turkey as a preferential supplier consolidated its position. Though India showed positive improvement in HS 54, major decline was witnessed in HS 55 to the tune of 18 per cent in 2001. Except Pakistan all the other four suppliers recorded negative growth during 2001 in manmade staple fibres. In textiles floor coverings (HS 57), India remained firm on top recording highest growth rate of 13.1 per cent in 2001 over the previous year. Similarly, in special woven fabrics (HS 58), India has more than doubled its exports since 1997. However, in knitted, crocheted fabrics (HS 60), India's share has declined from euro 41.08 million to euro 28.62 million in 1999 when all the other suppliers, viz. South Korea, Taiwan, Turkey and Switzerland, improved their position.

Thus it can be summarised that India's position in textiles is vulnerable in cotton yarn & fabric (HS 52), other vegetable textiles fibres (HS 53), manmade staple fibres (HS 55) and knitted & crocheted fabrics (HS 60), whereas it was moderate in silk yarn & fabrics (HS 50), woollen yarn & fabrics (HS 51), manmade filament yarn & fabric (HS 54) and special woven fabrics (HS 58). The position was firm in the case of textiles floor coverings (HS 57) and out of focus in the case of wadding, felt twine & ropes (HS 56) and impregnated textiles fabrics (HS 59). Among the competitors, Turkey, Pakistan and Bangladesh pose a major threat more due to their preferential treatment.

### (e) Item-wise Analysis of Clothing Imports of EU

Clothing imports of EU are calculated for the imports of knitted apparel (HS 61), woven apparel (HS 62) and other textiles articles (HS 63). As per the same, clothing imports of EU have grown from euro 38.62 billion in 1997 to euro 54.68 billion in 2001. In the sources of suppliers, Romania and Bangladesh have replaced India and Hong Kong, from the list of Top-5 suppliers to EU. In the Top-5 suppliers of clothing to EU, Turkey, Romania and Tunisia are the preferential suppliers and Bangladesh is a non-restrained supplier. China continued to maintain its position of first ranked supplier with 16.2 per cent share, followed by Turkey with 12 per cent. Romania has remarkably improved its position in 2001 to gain 1 per cent additional market share to reach 6.1 per cent. Bangladesh has emerged as a significant supplier to EU since 2000 wherein its value of exports has shot-up to euro 26.19 billion from euro 18.25 billion in 1999. Though India witnessed a growth in its value, it struggled to increase its market share to 5 per cent in 2002 from 4.9 per cent in 2000.

In knit apparel (HS 61), Bangladesh continued to increase its share from 6.6 per cent in 2000 to 7.0 per cent in 2001. India has also grown in the five years ending 2001, but the growth has been low when compared with both China and Bangladesh. In woven-apparel (HS 62) preferential suppliers, viz. Romania, Turkey, Tunisia and Morocco held more than 30 per cent share. Though India's value of exports declined in late nineties, it has improved in 2001. However, the growth of exports of India in 2001 over 2000 was a meagre 3 per cent compared to 6.6 per cent rise in overall imports of EU in this category. In miscellaneous textiles articles including made-ups (HS 63), though India maintained its share of 12.5 per cent, the rate was the lowest at 3.3 per cent among the Top-5 during the years 2000-2001.

## II. US-INDIA: TRADE IN TEXTILES & CLOTHING

### (a) Overall Trend

The import of US textiles and clothing was around US$49 billion in 1996 which has increased to US$75 billion in 2000 recording a growth rate of around 11 per cent per annum. More than three-fourths of such imports are originating from the

restrained sources consisting of forty-six countries. However, the special arrangement of USA through NAFTA has emerged stronger over the years. The share of NAFTA in US imports has increased from 14.3 per cent in 1996 to 18.5 per cent in 2000. Similarly, the CBI has also become strong since 1999. Though the current share of CBI is only 7.9 per cent, the pattern of growth suggests further firming up of market share by CBI. India as a source of textiles and clothing supply held a share of around 3.8

*TABLE 3*

**TREND IN TEXTILES & CLOTHING IMPORTS OF USA**

(US$ billion)

| Suppliers | 1996 | 1997 | 1998 | 1999 | 2000 | % change (1996-2000) |
|---|---|---|---|---|---|---|
| World | 49.04 | 57.20 | 63.24 | 66.51 | 74.78 | 52.5 |
| Restrained sources | 37.00 (75.5) | 43.72 (76.4) | 48.89 (77.3) | 51.28 (77.1) | 57.51 (76.9) | 55.4 |
| NAFTA Spl. arrangement | 7.00 (14.3) | 9.14 (16.0) | 11.02 (17.4) | 12.49 (18.8) | 13.87 (18.5) | 98.1 |
| CBI – Spl. arrangement | 2.94 (6.0) | 3.93 (6.9) | 4.49 (7.1) | 5.09 (7.7) | 5.90 (7.9) | 100.7 |
| India | 1.89 (3.8) | 2.18 (3.8) | 2.45 (3.9) | 2.56 (3.8) | 2.97 (4.0) | 57.1 |

*Notes*: 1. Textiles & clothing items are those covered by ATC under chapters HS 50-63.

2. Restrained suppliers include 46 exporters: Bahrain, Bangladesh, Brazil, Bulgaria, Cambodia, China, Chinese Taipei, Colombia, Costa Rica, Czech, Dominican Rep., Egypt, El Salvador, Fiji, Guatemala, Haiti, Hong Kong China, Hungary, India, Indonesia, Jamaica, Kenya, Korea Republic, Kuwait, Laos, Macau, Macedonia, Malaysia, Mauritius, Mexico, Myanmar, Nepal, Oman, Pakistan, Philippines, Poland, Qatar, Romania, Singapore, Slovak, Sri Lanka, Thailand, Turkey, UAE, Ukraine, Uruguay.

3. CBI include Anguilla, Antigua, Aruba, Bahamas, Barbados, Belize, British Virgin, Costa Rica, Dominica, Dominician Republic, El Salvador, Grenada, Guatemala, Haiti, Guyana, Honduras, Jamaica, Montsenant, Netherlands, Nicaragua, Panama, St. Kitts, St.Lucia, St. Vincent, Trinidad, Tobago

4. Figures in brackets indicate share of suppliers to total imports of USA.

*Source:* US Department of Commerce, Bureau of Census, extracted from GTIS Database.

per cent till 1999, which has marginally gone up to 4 per cent in 2000. In US imports, all the three major groups of suppliers have increased their share since 1996.

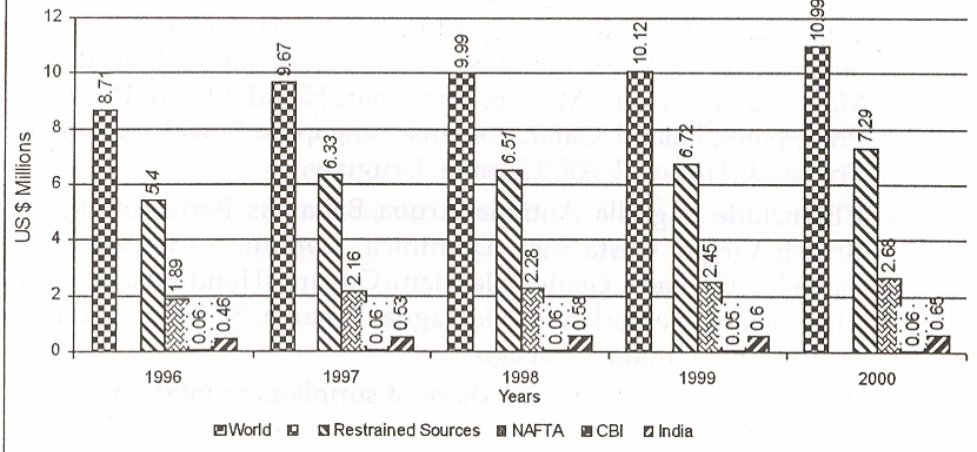
### (b) Trend in the Import of Textiles

Textiles import by USA was US$8.71 billion in 1996, which has grown up to US$10.99 billion recording average annual growth rate of 5.2 per cent till 2000. It constituted around 15 per cent of the total textiles and clothing import of the country. Though around 66 per cent of such imports are sourced from restrained suppliers, the share of restrained suppliers was less than their overall share in the total imports of textiles and clothing by USA. However, suppliers from restrained sources have shown an average annual growth rate of 7 per cent, which is more than the overall average growth rate of textiles imports. NAFTA as a source of supply has grown considerably with an annual growth rate of around 8 per cent. A similar growth was recorded by India also during the period.

### (c) Trend in the Import of Clothing

Clothing import of USA constituted around 85 per cent of its total import of textiles and clothing in 2000 as against around 82 per cent in 1996. The clothing import has grown at the rate of

**GRAPH 2**
**TEXTILES IMPORT OF USA**




*Source:* US Department of Commerce, Bureau of Census, extracted from GTIS Database.

around 12 per cent during the five years ending 2000. The import trend indicates that the sources of supplies are gradually shifting from restrained sources to the specific arrangements under NAFTA and CBI. The combined share of NAFTA and CBI in the clothing imports of USA has increased from around 28 per cent in 1996 to around 33 per cent in 2000. Clothing suppliers from NAFTA have more than doubled in the five years ending 2000.

*TABLE 4*

**TREND IN CLOTHING IMPORT OF USA**

(US$ billion)

| Suppliers | 1996 | 1997 | 1998 | 1999 | 2000 | % change (1996-2000) |
|---|---|---|---|---|---|---|
| World | 40.33 | 47.530 | 53.25 | 56.39 | 63.79 | 58.17 |
| Restrained sources | 31.1 (77.11) | 36.54 (76.88) | 40.92 (76.85) | 42.68 (75.69) | 47.93 (75.14) | 54.07 |
| NAFTA - Spl. arrangement | 5.10 (12.64) | 6.99 (14.71) | 8.74 (16.41) | 10.04 (17.80) | 11.19 (17.54) | 119.41 |
| CBI – Spl. arrangement | 6.04 (14.98) | 7.65 (16.09) | 8.33 (15.64) | 8.88 (15.75) | 9.69 (15.19) | 60.43 |
| India | 1.43 (3.55) | 1.65 (3.47) | 1.88 (3.53) | 1.96 (3.48) | 2.32 (3.64) | 62.24 |

*Notes:* 1. Textiles & clothing items are those covered by ATC under chapters HS 50-63.

2. Restrained suppliers include 46 exporters: Bahrain, Bangladesh, Brazil, Bulgaria, Cambodia, China, Chinese Taipei, Colombia, Costa Rica, Czech, Dominican Rep., Egypt, El Salvador, Fiji, Guatemala, Haiti, Hong Kong China, Hungary, India, Indonesia, Jamaica, Kenya, Korea Republic, Kuwait, Laos, Macau, Macedonia, Malaysia, Mauritius, Mexico, Myanmar, Nepal, Oman, Pakistan, Philippines, Poland, Qatar, Romania, Singapore, Slovak, Sri Lanka, Thailand, Turkey, UAE, Ukraine, Uruguay.

3. CBI include Anguilla, Antigua, Aruba, Bahamas, Barbados, Belize, British Virgin, Costa Rica, Dominica, Dominician Republic, El Salvador, Grenada, Guatemala, Haiti, Guyana, Honduras, Jamaica, Montsenant, Netherlands, Nicaragua, Panama, St. Kitts, St.-Lucia, St. Vincent, Trinidad, Tobago

4. Figures in brackets indicate share of suppliers to total imports of USA.

*Source:* US Department of Commerce, Bureau of Census, extracted from GTIS Database.

In spite of continuous marginal decline witnessed by restrained suppliers along with rapidly progressing supplies under special arrangement, India maintained its share of around 3.5 per cent till 1999 which has marginally increased to 3.64 per cent in 2000. In terms of growth rate also, India's exports have increased to around 62 per cent till 2000 as against the growth rate of 54 per cent by the restrained sources and the overall US clothing import growth rate of 58 per cent.

**(d) Item-wise Analysis of US Imports**

Item-wise analysis of US imports of textiles and clothing covers products of HS 50 to HS 63 of Harmonised System of Classification. As per the data, the products falling under all the categories have recorded a growth of around 29 per cent between 1997 and 2001, wherein the growth rates of textiles (HS 50 to HS 60) and clothing (HS 61 to HS 63) were 4.41 per cent and 33.45 per cent respectively. In terms of textiles products in the eleven HS two-digit categories, India ranked among the Top-5 exporters, in three categories. Among the textiles products, export of textiles floor coverings (HS 57) was the highest with a share of around 23 per cent. In value terms also India exported textiles floor coverings to the tune of US$324 million in 2001 and held the top rank. In cotton yarn & fabric (HS 52), India was the second big source of supply after Mexico in 1997. However, this position got reversed since 1999 wherein India was pushed down to fifth place with exports worth US$134.18 million. US import of cotton yarn & fabrics from India has come down from 10.3 per cent in 1997 to 4.8 per cent in 2001. In silk yarn & fabric (HS 50), India's position was strong in the US market with a share of 33.8 per cent in 2001. Though the export of India has declined by 18.6 per cent between 2000 and 2001, the decline was less than the slide of 19.9 per cent witnessed by the US silk imports during the same period. In rest of the categories (HS 51, HS 53, HS 54, HS 55, HS 56, HS 58, HS 59 and HS 60), India's share was insignificant in the US market.

In knitted apparel (HS 61), the US import has grown by around 1.7 per cent in the five years ending 2001. Mexico with a share of 12.5 per cent followed by China at 8.5 per cent and Hong Kong at 8.2 per cent as of 2001 was the leading source of

supplies to US market. India stood at seventeenth position with a share of around 2 per cent, which is consistently maintained with minor deviations throughout the period under study. In the year 2001, India's growth in knitted garments exports to USA was 6.7 per cent, which was more than the overall US imports growth of the same category.

Woven apparel exports of India constituted around 56 per cent of total clothing exports to USA. India's share of woven apparel exports was around 4 per cent from 1996 to 2001 though it has grown by around 6 per cent per annum in value terms during the same period. Mexico continues to dominate the woven apparel segment followed by China and Hong Kong. Together these three suppliers account for 35 per cent of US imports of woven apparel. In 2001, India's export to USA has come down by 7.4 per cent, which is more than the decline in US imports of 3.4 per cent.

In the miscellaneous textiles articles (HS 63), India continued to perform well. It has increased its share from around 9 per cent in 1997 to 10.2 per cent in 2001. In fact, the US market is also growing positively in this product category, which has led to improved growth by all the top suppliers except Mexico. Though India has achieved a growth rate of 5.8 per cent in 2001, it is below the overall growth in the market which was 6.5 per cent and less than the growth of competitors like China (9.4%), Pakistan (17.7%) and Turkey (6.2%).

In overall exports of India's textiles and clothing, readymade garments & cotton textiles occupy major share. The analysis in this section is summarised as follows:

- EU and US markets accounts for around 55 to 60 per cent of India's exports of T&C.
- India's share of T&C exports in the EU market remained at around 6 per cent though the other restrained suppliers have improved their share. However, in clothing exports the position has improved to some extent than textiles.
- India maintained its lead in floor coverings in the EU market but started losing in cotton fibre, fabric and manmade staple fibre. Similarly, in apparel, Bangladesh and Romania replaced India from the Top-5 suppliers to EU.

- India performed consistently in the US market compared to EU market. It has marginally improved its share in both textiles and clothing exports.
- Preferential arrangements like NAFTA, CBI and PAN European nations have significantly affected India's exports to US and EU markets.

## Market Access and US GSP for Indian T&C Sector

The current GSP schemes have different product coverage and different time-frames. Above all, each GSP donor country has different ROO for different product categories. Under its GSP programme, USA grants duty free treatment to designated eligible articles that are imported from the designated beneficiary developing country provided it satisfies the GSP Rules of Origin which states that the goods must be wholly grown, produced or manufactured of a beneficiary developing country (BDC) to regard as originating in that country. The goods that are manufactured with the imported contents, qualify for the preferential treatment if

- The sum of the cost or value of the materials produced in the beneficiary country plus the direct costs of processing must equal at least 35 per cent of the appraised value of the articles at the time of entry into USA.
- Imported materials are substantially transformed into new and different constituent materials of which the eligible article is composed.

The products eligible for GSP treatment are defined at eight-digit level of Harmonised Tariff Schedule of USA (HTSUS). No article or material of a BDC shall be eligible for duty free treatment by virtue of having merely undergone simple combining or packing operations that does not materially alter the characteristics of the article. However, US GSP ROO allow for full regional cumulation. A regional association contributing to the economic integration of its members may be granted GSP cumulation benefits, which allows the processing to be carried out in any of the beneficiaries within the regional groups counted together to meet the required 35 per cent local content rule. Presently, five associations that are benefiting from this provision

under GSP scheme are ANDEAN, ASEAN, CARICOM, SADC and WAEMU. There are no product specific requirements in the US GSP ROO. The 35 per cent local content requirements remain same for all products at all stages. However, rules are more onerous for those producers who produce fibre or yarn. Thus US GSP rules are relatively more onerous to the products at lower value end.

India is one of the beneficiaries of the US GSP programme since 1976. There has been erosion in the benefits of the trade preferences under GSP to India due to incomplete product coverage, MFN duty cuts and product graduation from time to time. USA provides duty free entry for six handicrafts items when the GSP beneficiary signs an agreement with USA to provide certification that such items are handmade products of the exporting country. The six covered tariff categories are 5701.10.13, 5702.10.10, 5702.91.20, 5805.00.20, 6304.99.10 and 6304.99.40. As per *US GSP Guidebook* (March 1999), 72 T&C items are generally eligible for GSP. The 35 per cent value addition requirement under US GSP may act as a constraint for those beneficiary countries, which are having a little manufacturing base or no recognised regional group as that in the case of India.

## Market Access and EU GSP for Indian T&C Sector

EU was first to implement its own GSP in 1971. The scheme revolves around three key features, namely tariff modulation, country sector graduation and special incentive arrangements. EU GSP scheme allows eligible countries to export to EU at a lower than normal duty rates for the manufactured goods and processed agricultural products with only one GSP regulation for all the products. Under EU GSP, a product shall be considered as originating in a beneficiary country if it has been either wholly obtained or undergone sufficient processing in that country. (As mentioned under Article 68 of the ECCC). When the products manufactured in a beneficiary country partly or wholly from non-originating materials, EU rules require that their non-originating materials be sufficiently processed to confer origin. Further, partial regional cumulative origin is permitted in respect of four separate regional groups of beneficiary countries, which include ASEAN, CACM, ANDEAN and SAARC. Unlike USA, EU allows only for partial regional cumulation.

However, the benefit of the scheme will be phased out for specific sectors of the countries once they reach a particular level of competitiveness. The current GSP programme (2002) divides products into two groups, namely sensitive and non-sensitive products instead of four categories as in previous scheme. While tariff duties on non-sensitive products continue to be suspended, items under the sensitive category will enjoy tariff preferences. The preferential tariff is arrived at by reduction of the flat rate of 3.5 percentage points from the MFN tariff rate. However, for the products of chapter 50 to 63, this reduction shall be 20 per cent.

India is the second largest beneficiary of the EU scheme with a GSP utilisation of over 70 per cent. From 1998, India has been graduated out of GSP benefit for the chapters 50 to 60 along with Pakistan. Currently, clothing sector is enjoying preferential margin of 20 per cent till the end of 2004. Products are classified into "wholly obtained" and "with imported contents" for applying origin criteria. ROO under EU GSP is more onerous for textiles products that are on the higher end of the value chain.

GSP ROO is relatively lenient than other preferential ROO prevailed in both the countries. While US GSP ROO requires 35 per cent of local content, EU needs minimum two technical operations to confer originating status. Low utilisation of preferences is the striking feature of the EU GSP scheme. The US scheme in contrast has a much higher utilisation rate of over 76 per cent in 1998. EU rules are more stringent, comprehensive and discriminatory than US.

## Effectiveness of US & EU GSP for Indian T&C Exports

The effectiveness of the GSP scheme depends on the utilisation rate, product coverage and its utility in total exports of T&C by a country. The indicators used for looking into the effectiveness of the GSP in EU and US markets are (i) market share; (ii) dependency ratio; (iii) GSP product coverage; (iv) GSP utilisation rate; (v) GSP utility; (vi) Import-Export Ratios; and (viii) Relative Competitive Index. These indicators are useful in measuring the effects of GSP ROO on the level of market access. If the rules of the donor countries are more onerous, lesser will be the utilisation rate and the utility rate.

## *I. GSP Utilisation and Utility*

In the context of India, these indicators are calculated and given in Tables 5 and 6, which show a wide gap in the effectiveness of GSP scheme in creating market access into EU and US markets for T&C products. The GSP scheme of EU is attractive both in terms of product coverage and utility compared to US. In the EU market, both product coverage and GSP utility ratio were high at 64 per cent and 51 per cent respectively in 2000. This is also reflected in the utilisation rate, which was 80 per cent in the case of EU in 2000 as against 34 per cent in the case of USA during the same period.

*TABLE 5*

**US GSP EFFECTIVENESS FOR INDIAN T&C INDUSTRY**

| Year | GSP utilisation rate (%) | | Product coverage (%) | | GSP utility (%) | |
|---|---|---|---|---|---|---|
| | All | Excl. HS 50072000 | All | Excl.HS 50072000 | All | Excl.HS 50072000 |
| 1997 | 95 | 95 | 3.86 | 2.08 | 3.66 | 1.97 |
| 1998 | 91 | 88 | 3.75 | 1.84 | 3.41 | 1.62 |
| 1999 | 53 | 88 | 4.40 | 2.08 | 2.34 | 1.81 |
| 2000 | 34 | 83 | 5.01 | 1.98 | 1.70 | 1.64 |
| 2001 | 38 | 84 | 4.74 | 2.15 | 1.81 | 1.81 |

*Source:* Calculation based on data from USITC Trade Data Base.

*TABLE 6*

**EU GSP EFFECTIVENESS FOR INDIAN T&C INDUSTRY**

| Year | GSP utilisation rate (%) | Product coverage (%) | GSP utility (%) |
|---|---|---|---|
| 1998 | 79 | 61 | 48 |
| 1999 | 77 | 64 | 49 |
| 2000 | 80 | 64 | 51 |

*Source:* Calculation based on data from *Eurostat* Trade Data Base as provided in *Textiles Times*, April-June 2002.

The USA virtually excluded most of the T&C products from GSP treatment. There are only 72 tariff lines generally eligible under US GSP during the period undertaken for the study. Even

among these seventy-two products, India exported only forty-two to US market in the last five years ending 2001. This has reflected in the poor product coverage ratio in USA, which was around 5 per cent. Even in these forty-three items where India is availing the GSP benefits, if one product, "woven fabrics containing 85 per cent or more by weight of silk or silk waste other than noil silk" ( HS 50072000) is excluded it gives a different picture. Now the GSP utilisation rate is as high as 84 per cent in 2001, which means that 46 per cent difference in utilisation rate has accrued just because of one eight-digit product among the seventy-two GSP eligible products. However, excluding an item has considerably reduced product coverage from 4.74 to 2.15. Furthermore, it indicates that the product line which accounts for 50 per cent of GSP received in the T&C industry, has turned out to be an empty preference when MFN duty itself became zero. Whatever may be the utilisation rate, real effectiveness of GSP is just about 1.81 per cent of India's total T&C exports to US market.

It is obvious from the above analysis that rules do not matter in availing US GSP, as utilisation rate, product coverage and utility rate are very low. Similarly, the negative effect of the stringency of EU GSP ROO due to inclusion of two-stage processing for clothing is not getting revealed through any of the three parameters taken for the GSP effectiveness analysis. However, one can possibly link the negative effect of ROO in non-utilisation part of India's clothing trade.

### *II. Market Share*

Market share is a best indicator to study India's position in textiles trade in both the markets. It also broadly throws light on how far market access for T&C is hampered by the stringency in ROO. From this point of view, India's market share of T&C products remained almost stable at around 6 per cent and 4 per cent in the EU and US markets respectively throughout the five years till 2001 (Table 7). It is strange that although US market is bigger in clothing segment, India's share is less. This may be mainly due to prevailing high tariff and non-tariff barriers on T&C imports. The table also reveals that India positioned better in both markets for textiles than clothing. However, in both the

markets the effect of GSP ROO on T&C exports is not directly traceable as USA statutorily excludes most of these items from GSP benefits and market share in EU clothing market has not come down. A possible conclusion one can make out of this table is that progressive EU ROO escalation in textiles might have restricted the growth of market share of India in clothing segment.

*TABLE 7*

**MARKET SHARE OF INDIA'S T&C EXPORTS IN EU AND USA**

(Figures in %tage)

| Year | EU | | | USA | | |
|---|---|---|---|---|---|---|
| | T | C | T&C | T | C | T&C |
| 1997 | 8.01 | 5.02 | 5.92 | 5.49 | 3.48 | 3.82 |
| 1998 | 7.68 | 4.85 | 5.66 | 5.80 | 3.52 | 3.88 |
| 1999 | 7.99 | 4.80 | 5.61 | 5.93 | 3.47 | 3.85 |
| 2000 | 7.87 | 4.94 | 5.69 | 5.89 | 3.64 | 3.97 |
| 2001 | 8.01 | 5.00 | 5.74 | 5.49 | 3.59 | 3.85 |

*Source:* Calculation based on data from the *Eurostat* and Bureau of Census, US DoC, as extracted from *World Trade Atlas* Data Base.

### *III. Market Dependency*

One of the most expected effects of the GSP schemes is the high dependency of the exporting country on the donor markets as the schemes provide for preferential tariff benefits. The trade direction of Indian exports of T&C shown in Table 8 substantiates this fact. Further, comparison of India's dependency ratios shows that the dependency of India's export on EU market is higher than that of US market for T&C. However, dependency ratio over a period of time has shown a mixed trend. Therefore, rules have not made any impact on the dependency level of India for T&C in these two markets.

### *IV. Import-Export Ratio and Input-Output Mix*

Import-export ratio is one of the realistic measurements of implications of GSP ROO. As we know, rules always restrict import content and encourage local content irrespective of origin criteria. The GSP rules will affect negatively only when import

intensity of industry is high. Table 9 indicates that import intensity of Indian textiles industry is low. Between 1996-97 and 2000-01 the import-export ratio of T&C has marginally gone up from 9 per cent in 1996-97 to 10 per cent in 2000-01. In order to understand the implications of imported upstream items on the value additions for the export of downstream items, the ratio of import of lower stage is calculated with the next higher stage of exports.

The ratios calculated show that the export of T&C from India is not vulnerable to the imports from the other markets. However, the marginal increase in the ratio of fibre imports to yarn exports and yarn imports to fabric exports needs attention

*TABLE 8*

**DEPENDENCY RATIO OF INDIA'S T&C INDUSTRY ON EU AND USA**

(Figures in %tage)

| Year | EU | | | US | | |
|---|---|---|---|---|---|---|
| | T | C | T&C | T | C | T&C |
| 1997 | 25.33 | 33.00 | 29.80 | 14.52 | 28.32 | 21.90 |
| 1998 | 25.24 | 33.10 | 29.70 | 14.88 | 31.55 | 24.40 |
| 1999 | 27.23 | 35.80 | 32.14 | 14.58 | 31.01 | 23.99 |
| 2000 | 25.07 | 32.80 | 29.61 | 13.21 | 33.78 | 25.30 |
| 2001 | 24.91 | 34.56 | 30.54 | 11.60 | 31.58 | 23.25 |

*Source:* Calculation based on data from Ministry of Commerce, GoI, as extracted from *World Trade Atlas* Data Base.

*TABLE 9*

**INDIA'S IMPORT-TO-EXPORT RATIOS IN TEXTILES AND CLOTHING SECTOR**

(Figures in %tage)

| Ratio | 1996-97 | 2000-01 |
|---|---|---|
| 1. Fibre Import - Yarn Export | 21 | 29 |
| 2. Yarn Import - Fabric Export | 5 | 9 |
| 3. Yarn Import - Apparel Export | 2 | 3 |
| 4. Fabric Import - Apparel Export | 3 | 2 |
| 5. Total Import - Total Export | 9 | 10 |

in the wake of post-MFA implications. This may further shoot up due to the shift in the fibre base from cotton to non-cotton based products where the domestic market is weak and the signs of which are already visible.

In respect of implications of rules, the import-export ratio reveals that rules will be onerous for lower value end products in textiles as fibre import to yarn export ratio is as high as 29 per cent in the year 2000-01. But Indian exports of yarn are only a small fraction of total T&C exports. Given the positive trade balance of 90 per cent for India's trade in textiles, its exports are not vulnerable to ROO norms. However, above aggregated ratios are concealing much more than revealing. On the one hand, we cannot directly link all imports of fibre or yarn to exports of next item in the value chain and, on the other, import-export ratio may be even higher in certain cases of exporters. Second point needs further consideration and elaboration. Hence, input-output mix of textiles industry requires special attention.

Further, it is found that fabricators and producers of articles from silk and wool are relatively more dependent on imported inputs than remaining ones. Their input-output mix is gradually changing due to globalisation. It is evident that two-stage transformation requirement under EU GSP ROO for woven garments has negatively affected fabricators in India. In the case of knitted garments, the picture is completely different wherein the exports of knitted garments to EU market have grown consistently. The input-output mix remained unaffected by the EU GSP ROO and they continued to source their input from domestic market except for accessories in specific cases.

In the case of silk products, producers are facing the problem of satisfying rules under GSP. US GSP requires that 35 per cent local content should be in terms of domestic inputs and direct processing cost. In the case of silk yarn imported from China and converted into fabric in India for export, cost of imports will be more than 70 per cent of appraised value. Hence deny the benefits of GSP. Silk exporters are, however, facing severe problem in complying themselves with the EU rules whenever it specify the import limit of 40 per cent. The data that reported in Table 10 testify this fact.

*TABLE 10*

**IMPORT AND EXPORT OF MAJOR SILK CATEGORIES BY INDIA (HS 50)**

| | 1998-99 | | | 1999-2000 | | | 2000-01 | | |
|---|---|---|---|---|---|---|---|---|---|
| | RS | Yarn | Fab. | RS | Yarn | Fab. | RS | Yarn | Fab. |
| Imports (Rs crore) | 265.4 | 37.0 | 27.2 | 417.8 | 38.6 | 23.4 | 476.2 | 71.2 | 20.5 |
| Landed cost (Rs Lakh/ton) | 9.3 | 7.1 | 12.0 | 8.2 | 6.2 | 9.7 | 10.1 | 5.5 | 5.4 |
| Exports (Rs crore) | 49.6 | 10.5 | 652.4 | 37.3 | 16.3 | 877.1 | 51.1 | 9.4 | 1230.1 |
| UVR (Rs Lakh/ton) | 2.7 | 6.9 | 23.5 | 2.4 | 12.4 | 23.0 | 2.6 | 8.0 | 22.8 |
| I:E ratio | 5.35 | 3.52 | 0.04 | 11.20 | 2.37 | 0.03 | 9.32 | 7.57 | 0.02 |

*Source:* Calculation based on data from *Compendium of Textiles Statistics*, 2001. GoI.

Another important product category examined for this purpose is home textiles. India's export of made-ups constitutes around 10 per cent of total exports of T&C. Most of such exports originate from handloom sector, especially from various textile clusters.

In the case of handloom home textile exports to EU, the GSP ROO has no traceable impact as the transformation criteria has no relevance for handlooms which are predominantly sourced from the local inputs only. Similarly, the preferential margin available to such made-ups could not influence the exports to either EU or USA. Thus, the high cost and high operating cycle involved in handloom home textiles exports could not gain much out of the GSP scheme of EU or USA.

### *V. Third-Party Effects: Cumulative Origin and Donor Content*

Preferential arrangements always encourage trade among member countries and discourage trade with non-members which is generally known as a third party effect or trade diversion. They create trade diversion by manoeuvring rules of origin. Even under the GSP system, rules provide certain provisions, which easily turned out to be disadvantageous for non-beneficiary of the system. There are certain derogations

provided from rule of single country origin in both EU and US GSP schemes. These derogations can create a trade diversion. While EU allowed partial regional cumulation and donor contents, USA allowed only full regional cumulation. India is a not a member of any regional agreements except SAARC. But SAARC is not recognised for cumulation under US GSP scheme. EU granted this facility to SAARC only from the year 2000 onwards. Hence our analysis of effect of cumulative origin or third party effects of rules is only an indicative exercise.

*TABLE 11*

**TRADE BETWEEN INDIA AND SAARC**

(Percentages)

| Countries | Imports | | | | Exports | | | |
|---|---|---|---|---|---|---|---|---|
| | T | | T&C | | T | | T&C | |
| | 2000 | 2001 | 2000 | 2001 | 2000 | 2001 | 2000 | 2001 |
| *SAARC* | 4.44 | 5.19 | 6.28 | 6.77 | 7.22 | 6.41 | 3.29 | 2.93 |
| Bangladesh | 2.13 | 1.43 | 3.86 | 2.54 | 4.65 | 3.79 | 1.94 | 1.61 |
| Nepal | 1.86 | 3.36 | 1.97 | 3.79 | 0.28 | 0.26 | 0.13 | 0.12 |
| Pakistan | 0.25 | 0.25 | 0.25 | 0.3 | 0.02 | 0.03 | 0.01 | 0.02 |
| Sri Lanka | 0.2 | 0.14 | 0.19 | 0.14 | 2.25 | 2.3 | 1.18 | 1.16 |
| Maldives | 0 | 0 | 0 | 0 | 0.04 | 0.02 | 0.04 | 0.02 |
| *World* (Rs billion) | 52.075 | 60.919 | 56.217 | 65.876 | 206.696 | 206.094 | 501.505 | 494.392 |

*Source:* Compiled from the data of Ministry of Commerce, GoI, as extracted from *World Trade Atlas* Database.

The trade between India and SAARC has been provided in Table 11 to measure the effects of cumulative origin. India's trade in textiles with SAARC has not shown any improvement after the cumulation benefit is granted by EU. Further, other sourcing of textiles imports for India is also analysed to know as to what extent import source is diverted due to donor content provisions under EU-GSP.

According to data reported in Table 12, India's major imports of textiles were sourced from China (24%) followed by Australia (9%), Korea (7%) and USA (5%). Silk and wool were the major imported items in T&C. Similarly, technical textiles were also accounted for some of the imports. The EU accounted for 7 per cent of the imports, which mainly originated from Italy for

manmade fibre, high-end cotton fabrics and woollen fabrics. But only fraction of this can be attributed to donor country requirements. So far, we have not come across any case where exporters have used this requirement to get GSP benefits. Perhaps neither cumulative rules nor donor content provisions were relevant for most of the exporters as the import intensity of their products was very low. There is no evidence as such to say that major exporters have relocated the manufacturing facilities from India to other SARRC members or EU to better exploit available cumulation and donor content provisions under GSP schemes. Thus, evidence advanced above clearly indicates that GSP rules have not created any negative effects on non-beneficiaries of the scheme.

*TABLE 12*

**INDIA'S SOURCE OF IMPORTS IN TEXTILES**

(%age to world)

| Country | 1999 | 2000 | 2001 |
|---|---|---|---|
| China | 14.34 | 15.84 | 15.34 |
| United States | 4.38 | 4.82 | 9.86 |
| Australia | 9.05 | 9.5 | 9.45 |
| Taiwan | 8.08 | 8.84 | 8.4 |
| *EU-15* | 8.9 | 7.07 | 7.54 |
| Korea, South | 8.65 | 7.24 | 7.16 |
| Indonesia | 4.1 | 4.61 | 3.95 |
| Nepal | 2.47 | 1.86 | 3.36 |
| Thailand | 4.35 | 3.44 | 3.27 |
| Japan | 2.77 | 2.51 | 3.09 |
| World (Rs billion) | 39.916 | 52.075 | 60.919 |

*Source:* Calculation based on data from Ministry of Commerce, GoI as extracted from *World Trade Atlas.*

## *VI. Export Competitiveness*

The impact of GSP ROO on the export of India may also be traced through the changes in the overall export competitiveness index of India in the respective markets and the world. The Relative Export Competitiveness (REC) Index measures the competitiveness of India's T&C industry in the export market in

comparison with the other industries. The index value indicates the share of exports of that industry to a particular market compared to the average export share of that country in the same market.

The calculated indices show that the overall export competitiveness of India has increased in textiles and declined in clothing over the years. Index values indicate that competitiveness in clothing segment was more than that of textiles in 1990. This trend got reversed in the subsequent years. India's position in textiles was strong in terms of competitiveness in the US market. In the EU market also, India has gained in the textiles segment. However, the competitive strength of India declined in both EU and US markets in the clothing segment. But this cannot be attributed to stringency of GSP ROO as broad comparison says it as GSP neutral.

*TABLE 13*

RELATIVE EXPORT COMPETITIVENESS (REC) OF INDIAN T&C INDUSTRY

| Year | EU | | USA | | World | |
|---|---|---|---|---|---|---|
| | T | C | T | C | T | C |
| 1990 | 4.91 | 2.87 | 9.32 | 2.70 | 4.00 | 4.49 |
| 1995 | 5.92 | 2.30 | 10.52 | 2.50 | 4.83 | 4.33 |
| 2000 | 6.32 | 2.24 | 9.63 | 2.31 | 4.86 | 3.89 |

*Source:* Calculation based on data from *World Trade Statistics*, 2001, WTO.

The value of indices for clothing indicates that India's competitiveness in both the markets remained less than the world average. This raises the doubt that as to how far the EU GSP scheme in clothing has helped India to gain competitiveness. Moreover, the REC value for clothing in EU market, which was higher than that of US market at 2.87 in 1990, has reached 2.24 in 2000, which is less than the US Index. This further strengthens the argument that the export of clothing to EU by India could not gain substantial advantage in spite of GSP benefit available for clothing in EU market.

## GSP ROO, MFA Phase-out and Exports of Garments

The competitiveness of T&C industry can be further examined to see the impact of total MFA phase-out on the Indian

garment exporters and how far the GSP ROO during the MFA period acted as an impediment to such exports. Although India's share of global textiles and apparel exports increased gradually to around 3 per cent, the growth lagged behind that of most other Asian countries, some of which increased their shares multifold in the past one decade. The elimination of textiles and apparel quotas by 1 January 2005 as part of MFA phase-out is likely to generate intense worldwide competition and present significant challenges and opportunities for the Indian textiles and apparel industry, both at home and abroad. The emergence of various preferential trade agreements in T&C sector and GSP schemes also have their influence on the competitive performance of the industry in the world market. Competitive analysis has been carried out hereunder using four indicators, namely quota utilisation level, unit value realisation, productivity level and level of modernisation to ascertain the competitive strength of India's apparel industry in a quota-free global market and the impact of GSP ROO in enhancing or reducing such strength.

## *I. Quota Utilisation*

Most trade in garments is governed by quota restrictions. The quota utilisation level shows the extent to which India is in a position to grab the market when quota is totally phased out. As figures in Table 14 suggest, the utilisation rate is almost 100 per cent for garments in both the markets. Moreover, it also projects that India has untapped potential in garments trade which can be realised once the quota gets eliminated.

***TABLE 14***

**INDIA'S QUOTA UTILISATION IN GARMENTS**

| Year | USA | | EU | |
|---|---|---|---|---|
| | Quota (000'SME) | Utilisation (%) | Quota (000'Pcs) | Utilisation (%) |
| 1998 | 319,906 | 111.10 | 317,900 | 94.49 |
| 1999 | 342,939 | 99.80 | 337,411 | 91.44 |
| 2000 | 371,882 | 109.77 | 358,237 | 100.17 |

*Source:* Calculation based on data from *Handbook of Export Statistics*, 2001, AEPC, India.

*II. Unit Value Realisation*

The above analysis can be further supplemented through the Unit Value Realisation (UVR) of Indian exports in the US and EU markets (Tables 15 and 16). UVR helps in understanding the level of competitiveness in the industry versus other competitors. India was at the seventh position in terms of UVR for textiles and clothing in 1996 and improved to sixth position in 2000. The UVR in clothing was found to be better than that of textiles. India's UVR was the third highest in US clothing imports after China and Hong Kong. It should be noted that India does not qualify for any major GSP benefit in USA in the clothing segment. Hence as far as the US market is concerned, India has to adopt rationalising strategies of production line and bank on its traditional competitive advantages of cost and cotton fibre base to overcome the threat perceptions of post-MFA phase-out.

The GSP of EU may have a considerable impact on India's exports of garments after the MFA phase-out, provided India is not graduated out of the GSP scheme of EU in clothing till that time. The possibility of India's graduation out of the EU GSP scheme is high due to the growing exports of clothing and high quota utilisation in the EU market. Moreover, the present GSP scheme of EU is likely to expire in 2004. Irrespective of such likelihood, the continuation of EU GSP ROO with "two-stage transformation" criterion will affect the garment exports of India adversely. The Indian garment export segment is highly fragmented and dominated by fabricators. The fabricators share in the garment segment is estimated at 72 per cent of the manufacturing capacity.* Given these features of the industry, till MFA phase-out, the exporters will be operating under quota protection wherein the "two-stage transformation" criterion of EU GSP ROO is not causing many problems. This is more so because the exporters are operating only on the middle price range with around 74 per cent of the sub-contracting for the output. With the managed trade era in textiles and clothing to be phased out in 2005, the garment exporters will feel the burden of the "two-stage transformation" to avail GSP benefits in the

* "Structure of the Garment Industry", www.ciionline.org

*TABLE 15*

**COMPARISON OF UNIT VALUE REALISATION WITH COMPETITORS IN US MARKET**

(US$ per SME)

| Competitors–US market | 1996 | | | 1998 | | | 2000 | | |
|---|---|---|---|---|---|---|---|---|---|
| | T | C | T&C | T | C | T&C | T | C | T&C |
| Hong Kong | 1.29 | 5.08 | 4.52 | 1.23 | 5.14 | 4.53 | 1.07 | 4.90 | 4.19 |
| China | 1.43 | 4.37 | 2.97 | 1.54 | 4.74 | 3.04 | 1.57 | 4.84 | 2.94 |
| Sri Lanka | 0.92 | 3.53 | 2.67 | 0.92 | 3.94 | 2.82 | 0.83 | 3.60 | 2.56 |
| Korea | 1.51 | 4.81 | 2.80 | 1.28 | 4.11 | 2.52 | 1.11 | 3.86 | 2.34 |
| Indonesia | 0.61 | 4.02 | 2.47 | 0.58 | 3.82 | 2.02 | 0.61 | 3.94 | 2.26 |
| India | 0.97 | 3.94 | 2.00 | 1.07 | 4.18 | 2.11 | 1.12 | 4.48 | 2.20 |
| Mexico | 0.60 | 3.24 | 1.92 | 0.61 | 3.27 | 2.09 | 0.58 | 3.33 | 2.04 |
| Bangladesh | 0.55 | 2.13 | 1.88 | 0.56 | 2.19 | 1.96 | 0.54 | 2.19 | 1.95 |
| Thailand | 0.90 | 4.39 | 2.23 | 0.77 | 4.33 | 1.97 | 0.74 | 3.87 | 1.86 |
| Pakistan | 0.69 | 3.53 | 1.24 | 0.59 | 3.94 | 0.96 | 0.55 | 3.60 | 0.92 |

*Source:* Calculation based on data from US Department of Commerce, Bureau of Census, extracted from GTIS Database.

*TABLE 16*

**COMPARISON OF UNIT VALUE REALISATION WITH COMPETITORS IN EU MARKET**

(US$ per kg)

| Competitors–EU market | 1996 | | | 1998 | | | 2000 | | |
|---|---|---|---|---|---|---|---|---|---|
| | T | C | T&C | T | C | T&C | T | C | T&C |
| China | 7.12 | 17.71 | 11.35 | 6.47 | 19.00 | 10.45 | 5.59 | 18.23 | 9.21 |
| India | 4.81 | 17.29 | 7.32 | 4.56 | 16.12 | 6.76 | 3.92 | 14.79 | 6.08 |
| Bangladesh | 1.15 | 10.95 | 6.33 | 1.24 | 9.69 | 6.80 | 1.33 | 9.89 | 7.43 |
| Hong Kong | 9.16 | 28.03 | 20.12 | 9.26 | 26.76 | 20.41 | 8.76 | 22.14 | 20.13 |
| Egypt | 4.77 | 14.57 | 6.33 | 5.05 | 16.67 | 7.28 | 4.38 | 16.19 | 6.92 |
| Indonesia | 5.01 | 18.17 | 8.85 | 3.83 | 19.03 | 7.84 | 3.58 | 17.75 | 8.74 |
| Korea | 7.10 | 18.14 | 9.77 | 4.70 | 19.70 | 6.96 | 3.98 | 18.67 | 6.21 |
| Pakistan | 5.38 | 9.64 | 6.36 | 4.44 | 9.18 | 5.37 | 3.96 | 8.09 | 4.85 |
| Sri Lanka | 4.00 | 18.93 | 14.06 | 3.75 | 19.20 | 13.74 | 3.92 | 18.12 | 14.91 |
| Thailand | 5.59 | 21.68 | 9.52 | 5.35 | 21.09 | 9.31 | 5.24 | 18.90 | 10.39 |
| Vietnam | 9.69 | 22.60 | 17.55 | 8.23 | 22.27 | 15.83 | 7.29 | 19.18 | 13.82 |

*Source:* Calculation based on data from *EuroStat* (Cat: KS –CK-01-502-3A-2).

EU. Its current strengths based on cheap and flexible labour and raw cotton may be overpowered by competitors' strengths of integrated production with high rate of modernisation of production lines.

Given the current UVR of India in clothing in EU market, which has come down by around US$3 per kg, the likelihood of serving the niche market after MFA phase-out seems to be a tough task in garments.

### *III. Level of Productivity, Modernisation and Technology*

Analysing the overall competitive strength of the T&C industry in terms of technology, modernisation, costs and productivity can further assess the impact of post-MFA phase-out. This will also help in understanding the influence, if any, of GSP schemes in shaping the industry for the future.

The Indian T&C industry experiences low labour productivity, which is one of the major barriers for enhancing competitiveness in the down-stream activities of the value chain. The productivity level of the industry in major products of garment segment is compared here with some of the competitors in Asia (Table 17). It is measured in terms of number of pieces produced per machine per day in India *vis-a-vis* its competitors. As per the data, India's productivity in the value added products like trousers and ladies dresses are not even half of the productivity of competitors like Hong Kong, Taiwan and Thailand. Even in gents shirts, which is considered to be one of important items of India's garment export basket, the productivity was the lowest at 9.1 pieces per machine per day. Though it is argued that due to flexibility of production line, Indian manufacturers could not achieve specialisation yet the productivity gaps remained very high and could not be leveraged by the labour cost or the net tariff differential of 2.4 per cent as provided under the EU GSP scheme to gain competitiveness.

Low labour productivity and product quality of Indian T&C industry is largely attributable to low technology and modernisation levels. A multi-country analysis of modern textiles equipment use reveals that the technology level in the Indian weaving segment is low as compared with that of other major

*TABLE 17*

**PRODUCTIVITY LEVELS OF APPARELS**

(No. of pieces per machine per day)

| Country | Ladies blouses | Gents shirts | Ladies dresses | Ladies skirts | Trousers |
|---|---|---|---|---|---|
| S. Korea | 14.6 | 17.4 | 08.8 | 17.5 | 15.6 |
| Taiwan | 18.9 | 18.2 | 12.4 | 16.6 | 16.1 |
| Hong Kong | 20.6 | 20.9 | 20.2 | 19.3 | 19.3 |
| China | 10.9 | 14.0 | 07.8 | 13.0 | 06.7 |
| Thailand | 17.0 | 19.8 | 12.2 | 20.5 | 13.1 |
| India | 10.2 | 09.1 | 06.3 | 09.6 | 06.8 |

*TABLE 18*

**LEVEL OF TECHNOLOGY & MODERNISATION IN T&C, 1999**

| Country | Level of technology[1] (Weaving) | Rate of modernisation[2] (Weaving) | Rate of modernisation[3] (Spinning) |
|---|---|---|---|
| India[4] | 0.58 | 1.38 | 31.65 |
| United States | 90.85 | 45.87 | 22.96 |
| Mexico[4] | 29.30 | 12.55 | - |
| Brazil[4] | 26.40 | 8.78 | 15.62 |
| China | 8.45 | 20.29 | 3.36 |
| Pakistan | 5.55 | 3.04 | 16.01 |
| Indonesia | 10.47 | 16.61 | 35.90 |
| Korea | 26.60 | 73.03 | 33.12 |
| Taiwan | 92.61 | 70.54 | 35.24 |
| Thailand | 15.89 | 8.20 | 22.95 |
| World | 13.39 | 11.26 | 19.46 |

*Notes:* [1] Level of technology measured as share of shuttleless looms in total installed looms.

[2] Rate of modernisation as % of new machinery installed during 1990-1999 and total installed capacity as on 1999.

[3] Rate of modernisation in terms of new machinery installed as a % of installed capacity.

[4] Figures pertaining to 1998.

*Source:* Calculation based on data from statistics of ITMF, *International Shipment Statistics* (Zurich), 2000.

competitors. Shuttleless looms, considered as the latest technology with huge production capacity constituted a mere 0.58 per cent of the installed loom capacity of India compared with the world average of 13.39 per cent.

In modernisation (Table 18), measured in terms of new machinery installed over a period of ten years ending 1999, the spinning sector was relatively more modernised than the weaving sector. India was one of the world's leading buyers of spinning equipment during 1990-99 accounting for around 32 per cent of global shipments of new machinery. However, modernisation of weaving sector remained low during the same period. New shuttle and shuttleless looms installed in India's weaving sector during 1990-99 accounted for only 1.38 per cent of total installed capacity.

The evidence provided under competitive analysis suggests that India has untapped potential capacity with poor competitiveness. No doubt, it calls for continuation of GSP benefits even after 2005 to gain some competitive advantage in accessing US and EU markets. As far as GSP rules are concerned, there is no evidence available as such to conclude that they have affected the competitive ability of garment exporters. In this context we can only predict that process criterion imposed by EU rules will possibly reduce competitiveness of those exporters whose exports rely only on GSP benefits.

## Summary

The above analysis may be summarised in conclusion as follows:

- It has been observed that GSP ROO in T&C are relatively lenient than other preferential ROO prevailed in various trade programmes of both the countries. While US GSP ROO requires 35 per cent of local content, EU needs minimum two technical operations to confer originating status and as such is more complicated. Thus, one may conclude that EU rules are more stringent, discriminatory and evolved over a period of time than US. Besides, USA provides general and simple rules for all products, which create less distortions and least documentary cost than EU. ROO escalation in EU for T&C is positive and more visible than in USA. The T&C sector in both countries, have highly protected high tariffs

and numerous non-tariff barriers over other manufacturing sector. This report provides convincing evidences that in the case of EU, ROO under GSP has been framed to achieve trade objectives of the donor countries. In other words, ROO can act as hidden protection to domestic industries of main GSP donors.

- It can be concluded that neither origin criteria under EU and US GSP schemes for T&C nor cumulative origin and donor content provisions in the case of EU GSP have affected the nature and competitiveness of the local and T&C sector in India. It seems that EU ROO is hampering the woven garment fabricators and exporters of silk products who have been denied GSP benefits because of stringency in rules to comply with. This is because the rules have not benefited the woven garment exporters, wherein the single transformation would have enabled the fabricators to source cheap fabric inputs from outside the country for the same product basket. Similar is the case of silk product exporters. However, these results cannot be generalised for the T&C sector particularly in case of USA since product coverage under GSP is just about 2-3 per cent. What follows from the above result is that Indian T&C exporters would have fully enjoyed the GSP benefits if liberal ROO were provided.
- Normally, rules under any preferential arrangements will affect the trade pattern and structure of the parties to that agreement and indirectly on third non-beneficiary countries. However, empirical findings on effects of origin criteria, cumulative origin and donor content provision, do not show any negative implications of developing third country non-beneficiaries of the EU and US GSP schemes. In fact, import intensity of overall T&C sector in India is very low. More importantly neither dependency on EU and US markets for Indian exports for T&C nor direction of sourcing of imports for the same have any significant deviation owing to meet GSP ROO requirements during the last five years. However, our study clearly supports the view that specific rules for T&C under various preferential trade arrangements negotiated by EU and USA have made large impact on global trade in T&C sector.

- Analysis of the domestic T&C industry shows that in the Textile Value Chain, the output of fibre yarn is predominantly with the organised mill sector whereas the fabric is in the decentralised powerloom sector. In the fabric output, share of 100 per cent non-cotton is growing. In the apparel output, growth of knitted segment is high and woven segment is witnessing slow growth. Technical textiles and home textiles are potential export sectors with limited existing share. The dyeing and finishing activity in the value chain is a weak link.
- In the T&C exports of India, EU and USA remained as major destinations accounting for 55 to 60 per cent of the total exports. India's share of T&C exports in the EU market remained at around 6 per cent though the other restrained suppliers have improved their share. However, in clothing exports the position has improved to some extent than textiles. India maintained its lead in floor coverings in the EU market but started losing in cotton fibre, fabric and man-made staple fibre. Similarly, in apparels, Bangladesh and Romania replaced India from the Top-5 suppliers to EU. India performed consistently in the US market compared to EU market. It has marginally improved its share in both textiles and clothing exports. Preferential arrangements like NAFTA, CBI and PAN European nations have significantly affected India's exports to US and EU markets.
- On a relative basis, the garment industry in India is globally more competitive than other industries in the country. But competitiveness in terms of labour productivity or technology level is very poor over competitors like China, Hong Kong, Italy and Mexico. However, as per the data presented in the study, EU or US GSP ROO under the MFA have not affected the ability of garment exporters to compete in the global market.

## Conclusions

To conclude it seems that textiles and clothing industry is in a turbulent environment. This is because, on the one hand, total MFA phase-out by 2005 and rising global integration under WTO pose serious threats and on the other, there seems to be

opportunities in the form of expanded market and quota removal which may improve the position in the near future.

In an extremely competing scenario, GSP will remain as helping window to gain additional competitive advantage over competitors in trade in T&C for country like India. Today overall coverage of T&C products is around 50 per cent under EU GSP and just 2 to 3 per cent under US GSP scheme. Presuming GSP will be extended even after the total removal of quota under MFA, this report insists for accelerated product coverage at least in those T&C products, which are important to developing nations. In order to soften the effects of eroding preferential margins due to ongoing reduction in MFN duties, principal GSP donors like USA and EU must restore the GSP benefits to the level of 1995.

The key issues for developing countries like India are the level of market access under GSP and the extent of cost of compliance with ROO. The present study shows that in the case of fabricators and silk producers GSP ROO under USA and EU has not benefited in increasing their exports. Nevertheless these cases strengthen the argument for liberalisation of rules under EU and US GSP schemes. If the principal donors of GSP want to create a special market access for developing countries, they have to consider the current ROO. The ROO under various GSP schemes have a considerable scope for harmonisation, simplification and liberalisation. UNCTAD should lead these efforts.

On comparison, EU needs to simplify its rules under GSP. Considering the increasing integration of international production, there is a need for single value added criterion for conferring origin status to all products under GSP. Although the rule that 35 per cent local value addition is a feasible criterion to assess substantial transformation of imported inputs, the limit in terms of local materials and direct processing cost, local value added should be calculated as a difference between transaction value minus total imported content. Further relaxation of tolerance limit of 5 per cent import can be allowed for lower end products in a broad industrial category. This tolerance limit will nullify the problem of negative ROO escalation. Within the current framework of EU GSP ROO, a change from two-stage

processing requirement to single stage transformation for T&C seems to be highly beneficial for developing and least developed countries to ensure full advantage from GSP.

In case of US rules, the phrase "*sum of the local value of materials plus the direct processing cost*", needs to be replaced as "*sum of the local value addition as percentage of transaction value must equal to 35 per cent with 5 per cent tolerance for textiles*". Nevertheless, this empirical study convincingly authenticates that there is a great opportunity for principal GSP donors to contribute towards enhancing trade and development of developing countries like India ensuring higher product coverage and simplified rules.

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