CHAPTER ONE

1. BACKGROUND

1.1. OBJECTIVE

The objective of this case-study is to:

(a) present and discuss the impact of changes in both domestic and international competitive environments on the Malaysian textile and apparel industry;

(b) develop a framework for some strategic adjustments by both the Government and the industry by drawing on the experiences of pioneers and forerunners of the industry among the developed and newly industrialised countries.

It is hoped that this study will contribute towards building confidence among those having an interest directly or indirectly in the textile and apparel industry so that together, all parties may confidently work towards sustaining the development of what can be described as a core industry of any country.

1.2. LITERATURE REVIEW

There is a general agreement among authors and researchers that, in the past few decades, the textile and clothing industry has played a significant role in
the industrialisation process of a number of developing countries and in the
growth of their manufactured products. These two sectors are major examples
of the international industrial relocation and of the international restructuring of
the world economy and the presence of multinational corporations (MNCs) has
been a determining factor in that process.

According to a United Nations (1987) study, because clothing assembly is
labour-intensive, developing countries have enjoyed a competitive advantage
vis-a-vis developed countries. In countries such as Germany and the United
States (US), national legislation offering tariff concessions for foreign
processing of apparel has provided an added impetus to the internationalisation
of the industry. The study pointed out that product differentiation is a central
component of the strategies of MNCs, with producers from developed countries
seeking to narrow their product range and to focus on speciality fibres with
higher value-added and on high quality, fashion-oriented products where they
still enjoy some advantages vis-a-vis producers from developing countries.

On the impact of technological change, the study pointed out that developing
countries need to be cognizant of the potentially dramatic impact of
technological change on the future of their textile and clothing industries,
because it would significantly affect the role of those industries in their
development strategies. Certain fundamental technological changes have
occurred that have transformed the competitive environment in which textile
firms from both developed and developing countries must operate - automation may erode significantly the advantage of low labour costs. The study cited the case of several US-based manufacturers of jeans who have closed down their plants in Western Europe and have reduced sub-contracting in Asia because investment in new technologies enables them to achieve higher productivity in the US. The use of micro-electronic-related innovations (MRIs) in assembly are primarily labour-saving and are not justified a priori for most developing countries, with the possible exception of the newly industrialising countries where wages are higher than in developing countries and where more sophisticated equipment could enable them to remain competitive vis-a-vis clothing-producing countries with lower wages.

The study proposed the adoption of the following strategies that for those countries where the labour-intensive side of the industry is beginning to be vulnerable to wage-cost inflation: they should push onto capital-intensive production and higher value-added products; the experience gained in producing "designer label" standards could be extended to the production and marketing of the domestic companies own brands, market diversification to relieve the pressures of protectionism.

Competition and technological progress were identified by a OECD (1983) study, as key factors that have put continuous pressure on the structures of the textile and clothing industry since the Second World-War. This study pointed
out that adjustment to changing conditions of supply and demand, internationally and internally, is a continuous process, which is a product of Government policies and regulations and the responses of economic agents. History and socio-political context result in different government strategies in various countries and to a variety of corporate responses to the challenge of greater competition. However due to the sheer number of players that are involved in decision-making, it is impossible to refer to any single national adjustment path. Moreover constant changes in domestic and international conditions preclude any sweeping generalisations.

Among other areas, the OECD study analysed the evolution of the textile and clothing industry in nine (9) selected countries with the hope that they would throw some light on the mechanisms of "successful adjustment" in the concrete conditions of individual countries and industries. However, the study cautioned that in a rapidly changing world, "success" in any one period can breed "failure" on another occasion. Besides, adjustment, has to be seen in the contexts of developments in other competing industries and adjustment in the rest of the domestic and international economy.

The United States adjustment pattern, in a nutshell, combined protection of a huge domestic market and a large variety of corporate responses trying to take advantage of technological changes in mass production of highly standardised products and of low wage-cost areas within and outside the country.
The United Kingdom (UK), the oldest textile manufacturer, on the other hand has been beset by innumerable adjustment problems particularly after World War 2. Inability of the industry to rationalise due to lacks in finance and managerial capabilities has contributed to a long history of Government intervention aimed at reducing excess capacity, increasing productivity and securing employment. While such measures achieved improvements in efficiency and productivity, it is doubtful if many segments of the textile and clothing industry would have survived without the continuous measures by the Government to protect the domestic market against increasing pressure from imports. Basically, the industry in UK in the 1960s can be described as being production rather than market-oriented. Influenced by the Government’s merger policy, in the 1960s, two important UK man-made fibre producers pursued a vertical and concentric integration strategy in textiles, clothing and trade by establishing outlets through the promotion of mass manufacture of yarns and fabric geared to the domestic market protected against low-cost competition. This mass-market approach was a failure in that it was unable to meet changing conditions, tended to divert attention from the need to specialise, to develop products for new, promising outlets and to turn attention to marketing. In several segments of the clothing industry, poor marketing and fashion performance resulted in the loss of highly profitable markets - both abroad and at home. In addition, the textile sector’s bias towards hardware and productivity resulted in constant excess capacity. To crown the decline in
textiles, was the ultimate loss of ground in the textile machinery market and the poor overall technological performance. This has resulted in a considerable contraction of the industry in recent years.

In a paper discussing the trade policy and foreign investment of the European textile and clothing industry, as part of the OECD Development Centre research programme on "Globalisation and Regionalisation", G. Navaretti (1992) is of the opinion that the European textile and clothing firms followed two strategies (often mutually exclusive) throughout the eighties: improvement of product quality and re-deployment of production to LDCs (Developing Countries). The two options reflect the behaviour of the average firm in Italy (quality) and in Germany (re-deployment). Re-deployment of production or outward processing trade (OPT) is seen as a defensive move of advanced countries attacked by growing flows of imports from cheap labour LDCs. Under this assumption, European producers are expected to benefit from trade barriers since protection provides them with some breathing space and slows down the pace of restructuring including re-deployment. However the paper commented that this is a simplistic view of the restructuring taking place in the textile and clothing industry. The paper points to the fact that in many segments of the industry, particularly for high quality products, European firms re-deploy in order to face competition from other advanced countries rather than from LDCs. Based on a theoretical model developed, the paper shows that under given conditions, in equilibrium, high quality firms will produce at home and
low quality ones will re-deploy, a result that is consistent with the evidence on Italy (quality) and Germany (re-deployment). What can be implied from this is that increasing competition from LDCs should be seen as a process of gradual economic integration between producers in both areas, whereby capital intensive production phases, design and distribution are controlled by advanced countries and labour intensive production phases are carried out in LDCs. Another implication from this theoretical model is that the Multifibre Arrangement (MFA) and trade protection in general is not equally beneficial for protected producers: protection increases the cost of re-deployment, favouring firms with comparative advantage in high quality. In other words, if trade barriers are lifted, re-deployment would be less costly since it would contribute to the improvement in the relative quality of the re-deployers which would strengthen their competitive position vis-a-vis high quality firms firms producing at home. In sum, the paper concludes that trade barriers slow down a process which is beneficial to European producers.

The KIET (1995) study outlined the history of development of the Korean textile and apparel industry, challenges faced at each stage and the strategies adopted by the country. The initial growth of the industry in the fifties was attributed to low labour costs - plant and materials were supplied by foreign aid and the industry grew around a natural generic base since the country produced cotton, wool and silk, strongly backed by the protectionist policy of the Korean Government. In the sixties, production of man-made fibres evolved; towards
the late sixties, fully supported by Government legislation, the industry's shift into export-orientation saw a move towards plant rationalisation and modernisation - resulting in the country joining Hong Kong and Taiwan as one of the "Big Three" as an exporter of textile products right through the oil-shock of the seventies. The next phase saw the country coping with changes in the international trading environment - the enactment of the MFA(1974) and the emergence of other lower-cost producers. To cope with these difficulties, the country relentlessly pursued plant modernisation - the necessary legislation was put in place to allow for the expansion of capacity, replacement of old plants and for the development of technology and human resources. However, in the late seventies as Korea embarked upon the development of its chemical industry, the textile industry experienced wage pressures causing a decrease in exports in the early eighties. In the late eighties, exports hit an all-time high but since 1989, exports have decelerated drastically fuelled by rapid wage hikes, labour shortages and currency appreciation. To counter these problems, the country is investing in automation, plant modernisation, development of high technology besides relocating older plants overseas. These structural adjustments are supported by Government policies - with subsidies in investment and R&D and the encouragement of plant relocation. Notwithstanding the challenges faced by the industry, the KIET study remains confident about the prospects for the industry - the view is that the industry is at a maturing stage where output and export are expected to grow at a decelerated but positive rate for a considerable period of time. The industry remains the
largest industry in Korea in terms of its contribution to value-added, employment and export earnings despite the growth of the electronics, automotive and chemical industries.

On the Malaysian front, the Gherzi study (1990) which was sponsored by the World Bank developed a strategic plan for the industry covering three main areas: marketing, industry restructuring (such as manufacturing, education and training, investment) and policy framework (such as investment support, adjustment of import tariffs). The most significant outcome of this study is the establishment of the Malaysian Textile and Apparel Centre (MATAC). Other than this, there does not seem to be much follow-through regarding the other recommendations of the study, due in part to the demise of the Textile and Apparel Industry Task-Force which was set up following the launch of IMP 1 (1986).

The latest local initiative is the Second Industrial Master Plan (IMP 2, 1996) which is optimistic about the prospects for the industry. Among others, IMP 2 has recommended that the industry move up the value chain, develop innovative fashion designs with brand names, enhance product development with R&D in the areas of dyeing, printing and finishing; improve productivity through automation, flexible manufacturing and technical assistance and encourage the setting up of buying and sourcing houses.
## Table 1: Summary of Literature Review

<table>
<thead>
<tr>
<th>Source</th>
<th>Findings</th>
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<tbody>
<tr>
<td>United Nations Study, 1987</td>
<td>- Developing countries enjoy a competitive advantage over developed countries in apparel manufacture because clothing assembly is labour intensive.</td>
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<td></td>
<td>- MNCs from developed countries have played a key role in the industrialisation of the textile and apparel industry spurred on by national policies.</td>
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<td>- Key strategy adopted by MNCs is product differentiation whereby producers from developed countries focus on the production of speciality fabrics with higher value-added and on high quality, fashion-oriented products.</td>
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<td>- Competitive landscape has changed somewhat with automation significantly eroding the advantage of low labour costs i.e. technology can impact the playing field.</td>
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<td>- For countries losing competitive leverage on account of wage costs, the study recommended a push onto capital-intensive production and higher value-added products, branding and market diversification.</td>
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<td>OECD Study, 1983</td>
<td>- Competition and technological progress are the two key factors affecting the structure of the textile and apparel industry.</td>
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<td></td>
<td>- Adjustment to changes in competitive forces is a product of both Government policies and economic agents.</td>
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<td></td>
<td>- In a rapidly changing world, “success” in any one period can breed “failure” on another occasion. There is no single “successful adjustment” path.</td>
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<td>- The US adjustment - a combination of protection of the domestic market and using technology to gain competitive advantage.</td>
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<td>- The UK adjustment - Defensive protectionist policies were instituted by the Government combined with a vertical and concentric integration strategy aimed at the mass-market adopted at the industry level failed to “defend” the position of the world’s oldest textile manufacturer.</td>
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<tr>
<td>OECD/G. Navaretti, 1992</td>
<td>- European textile and clothing firms essentially followed 2 strategies throughout the eighties - improvement of product quality and redeployment to LDCs.</td>
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<td></td>
<td>- High quality firms will produce at home (Italy) and low quality firms will redeploy (Germany).</td>
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<td>- MFA and trade protection in general is not equally beneficial for protected producers - more beneficial to firms with comparative advantage in high quality.</td>
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<td></td>
<td>- Trade barriers slow down a process that is beneficial to European producers.</td>
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<tr>
<td>KIFT Study, 1995</td>
<td>- Study provides an outline of the development of the Korean textile and apparel industry, challenges faced at each stage and strategies adopted by the country.</td>
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<td>- The critical stage - in the late seventies as Korea embarked upon the development of its chemicals industry - led to wage pressures and resulted in a decrease in exports in the early eighties. Since 1989, exports have decelerated caused by rapid wage hikes, labour shortages and currency appreciation.</td>
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<td>- Strategies currently adopted - automation, plant modernisation, development of high technology and relocation of older plants abroad - fully backed by Government policies.</td>
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<td></td>
<td>- Despite the growth of electronics, automotive and chemical industries, the textile and apparel industry remains the largest industry in Korea in terms of contribution to value-added, employment and export earnings.</td>
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<td></td>
<td>- Study remains confident about industry prospects - views the textile and apparel industry at the maturing stage where output and exports are expected to grow at a decelerated but positive rate for a considerable time.</td>
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<tr>
<td>Gherzi Study, 1990</td>
<td>- This World Bank-sponsored study developed a strategic plan for the country’s textile and apparel industry.</td>
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<td>- The establishment of MATAC represents a spin-off from the study.</td>
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<td>- Lack of follow-through on the other recommendations of the Study can be attributed in part to the demise of the Textile &amp; Apparel Industry Task Force set up following the launch of IMP1 in 1986.</td>
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<tr>
<td>IMP2, 1996</td>
<td>- IMP2 is optimistic about the prospects for the industry.</td>
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<td>- The recommended strategies are all encompassing - requires action to be taken simultaneously on many fronts, strategies including moving up the value-chain, enhancement of R&amp;D, developing innovative fashion designs with brand names to the setting up of buying and sourcing houses.</td>
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The following conclusions can be drawn from the literature review:

(a) The textile and apparel industry is an example of the industrial relocation and of the international restructuring of the world economy and MNCs have played a significant role in these processes.

(b) Competition and technological progress are the 2 key factors affecting the structure of the textile and apparel industry.

(c) Successful adjustments to changes in competitive forces is a product both of Government policies and economic agents.

(d) Technology has the ability to erode competitiveness that is built upon labour-cost advantage; the originators of technology have traditionally been the developed countries who are therefore not to be taken lightly as significant competitors.

(e) Trade barriers that curtail free competition do not necessarily work to the advantage of all textile and apparel manufacturers. As such, the phase-out of the MFA may not be a threat at all!
(f) For countries that have suffered erosion in competitive leverage due to wage pressures, shifts should be made to speciality products, non-basic products that make greater demands on quality and fashion.

(g) It is cost-effective to relocate lower-quality production to lower-cost countries.

(h) Prospects are good for a viable textile and apparel industry provided certain key issues are addressed.

The current case-study will build upon the work that has been done to date on the issue of national “adjustments” to changing internal and external conditions - and attempt to develop a framework for a Malaysian response to such changes. Unlike IMP 2 which has been developed to provide a national blue-print from the policy-maker’s perspective and is all encompassing in the sense that it provides such a broad spectrum of strategies, this study is developed basically with the investor in mind - both existing and potential investors in the textile and apparel industry. This study will provide a quick preview of key issues that are related to the industry and provide a broad framework of key strategic responses.
1.3. DATA COLLECTION

In undertaking this case-study, factory-visits were made to a few textile and apparel manufacturers where field interviews were conducted. The factory visits and field interviews were seen as necessary to gain a bird's eye view of the current developments in the industry vis-a-vis gauge the tempo of the industry, state of technology employed and to obtain the views of manufacturers regarding the prospects for the industry and regarding the kind of assistance that they might require from the Government. A summary of the findings resulting from the factory visits and field interviews itemised as survey findings is included in Chapter 2.

In the selection of respondents, the student was guided by the Malaysian Textile Manufacturers Association (MTMA) and the Malaysian Industrial Development Authority (MIDA). This was to ensure that the small sample totalling eight (8) factories represented a good cross-section of sub-sectors within the industry. Sample size was limited by budget and time constraints. Most of the interviews were unstructured and lasted an average of one hour.

In addition, a large part of the data on which the case-study is based, has been compiled from official documents made available by courtesy of MIDA, a key Government agency involved in the promotion and co-ordination of industrial development of the country.
In order to obtain an overall official picture of the industry and its future from the private sector's perception, the student interviewed the Executive Director of MTMA.

1.4. PROBLEMS AND LIMITATIONS

1.4.1. Due to budget and time constraints, the factory visits and field interviews were limited in number and conducted basically within a limited geographical locality i.e. in the state of Johor which is the hub of the Malaysian textile and apparel industry.

1.4.2. Besides official documents, there is limited literature available on the position of the Malaysian textile and apparel industry. The focus of the key Government agencies involved in trade and industry seems to be on promotion and there seems to have been a neglect to maintain a good database regarding the textile and apparel industry. MIDA's database covers only companies that fall under the ambit of the Industrial Co-ordination Act, 1975 i.e. companies with shareholders' funds amounting to RM2.5 million and/or employing 75 full-time employees. This means that many of the smaller companies, particularly those engaged in apparel manufacture are not included in MIDA's database.

To all intents and purposes, there appears to be a traditional lack of interest in this area of study among local academics and researchers.
The most comprehensive publication regarding textile intelligence available in the market (Textile Outlook International) gives scant coverage to the Malaysian scenario since it concerns the global position of the industry.

1.5. STRUCTURE OF REPORT

Chapter One provides the background to this case-study. Besides explaining the objective of the case-study, the chapter also covers the literature review and data collection methods including some of the problems and limitations of the study.

Chapter Two meanwhile focuses on the structure of the textile and apparel industry in Malaysia and covers aspects such as the development of the industry, industry classification and trade and investment performance. Survey findings are also incorporated in this chapter to provide a complete current overview of Malaysia's textile and apparel industry.

Chapter Three discusses the current issues of interest to the industry. The problems relating to human resource shortages, rising costs and inadequate skills are discussed in this chapter. Other issues covered in the chapter include the lacks in manufacturing technology, Research & Development activities, issues related to raw material sourcing such as the need to increase domestic value-added and linkages, effects of globalisation and other changes in the
international trading environment. The world market opportunities are also defined in this Chapter.

Chapter Four discusses the strategic directions for the industry which is covered under four broad strategies - cluster development, market penetration and development, technology upgrading and human resource training and development - strategies that should be considered for the long-term survival of the industry.

Chapter Five draws some conclusions based on the case-study.