

**Liberalization of trade with China  
in relation to the textile and clothing industry in  
South Africa**

By

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**DECLARATION**

This research has not been previously accepted for any degree and is not being currently submitted in candidature for any degree.

Signed .....

Date.....9/6/2023.....

STATEMENT

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## **ABSTRACT**

The challenge of enhancing competitiveness in a globalizing world is a continuous one, requiring action not only on narrow trade policy concerns but also in a complementary area such as the macro-economic environment to human resource management. The present report offers an overall view of the textile and clothing industries' opportunities and constraints. It proposes liberalization of trade policy with China as well as proper macro-economic environments, regulatory structures support to allow these industries to thrive and become robust by building an effective and efficient supply chain.

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## **Executive Summary**

Globalization both threatens and offers opportunities to South Africa. Although South Africa-EU Trade agreement and African Growth and Opportunity Act (AGOA) presently offer the opportunity for South Africa especially in textile and clothing industry. But the preferences are temporary. Therein the threat! In January 2005, the agreement on textile and clothing will finally phase out all quotas. With quotas gone, the new trade regime will unleash Asian and other highly efficient competitors. Even the tariff exemption for South Africa by AGOA will also end in September 2008. After that, barring an extension of the law, South Africa will have to compete in the U.S. market on equal footing, head-on with the world's best.

Meanwhile the increasing diversity and consumer orientation of the market and the insistence on ability to respond quickly to changes in tastes has led manufacturers and distributors to sharply cut costs and delivery time. These and other technological changes on top of an excess installed capacity worldwide are making global competition in textiles and clothing intense if not brutal. It is thus imperative for South Africa to build a large and technologically robust textile and clothing sector able to replace many imports in the region, increase its share in foreign market and eventually, fend off intensified competition in foreign markets. This requires quick, bold changes in government regulation in order to import skilled-labor, liberalize trade with china, adopt new techniques by firms and attract investment.

South Africa has both advantages and disadvantages in textile and clothing industries. Two major strengths stand out. The region can support the entire pipeline from cotton fibre to finished garments and has many existing world-class producers of textiles and garments. The major weaknesses are:

- Shortage of experienced staff and adequate training facilities.
- Trade barriers make it difficult for firms to create efficient supply pipelines.

- Insufficient range and supply of man-made yarn as well as fabric made from these materials.

The survey results show that manufacturers, above all, feel they:

- Face stiff competition in the international marketplace.
- Have difficulty finding customers due to the cost of marketing.
- Cannot fully utilize their capacity because the labor force is not well training.

Difficulty in obtaining work permit for expatriate is also important constraint. Moreover, the management techniques used in many factories are inadequate and provide little motivation for workers to strive for significantly higher productivity. As for demand by far the most serious constraint in the local market arise due to the avoidance of tariffs by merchants; and, in the international market, due to price competition. Faced with these constraints, can the manufactures have competitive in the market? The results are ambiguous.

South Africa has abundant cotton supplies with mediocre quality but not in man-made fibre. Being the only producer of man-made fibre and filament yarn in the SADC region, South African manufacturers produce a limited range of polyester staple and filament, acrylic staple, nylon filament yarn, which does not satisfy the demand of the manufacturers. Productivity and labor-cost comparisons demonstrate that manufacturers cannot be competitive with those in the Far East and China. South Africa would have to produce at the nearly impossible rate of 34 garments per operator day to compare to China. Nevertheless, the legal prohibition of, and intense union opposition to, piece-rate payments hampers labor productivity. There is a conflict regarding the lead-time, quality and product range between textile and clothing firms. The factory is significantly below the international norm (95%) for on-time deliveries due mainly to port congestion and clearance delays for raw materials.

Having considered the constraints on these industries and their relative competitiveness in South Africa, the analysis makes clear two things:

- No country has an absolute advantage in all stages of production and South Africa is no exception.
- The most competitive pipeline for clothing production will be to use what it does have and source what it does not have.
- On the other hand, being the world's largest producer of textile and cotton clothing and the second largest producer of man-made fibre, China could offer sufficient fibre and textile with acceptable quality and competitive price to South Africa. The problem, however, is that the trade restrictions discourage the South African manufacturers from outsourcing and creating the efficient and effective supply pipelines.

The macroeconomic environment and country-specific policies both constrain and encourage the development of the textile and clothing industries in South Africa. The slow to moderate economic growth do help the development of the industry, but high inflation and real interest rates restrain the growth to some extent.

Beyond these macroeconomic concerns, a country's trade policy, technology and human-resource policies also influence the development of industry. As for trade policy and customs regulations, the salient common problems involve:

- The failure to rebate, suspend, or eliminate tariffs and the value added tax (VAT) on inputs, spares, equipment, and purchased services used to produce exports.
- The apparent failure of South Africa's Customs Service to deduct the value of South African yarn or fabric incorporated in imported textiles or clothing before calculating the amount of duties payable.
- Slow and often corrupt customs services.

- The employment of time consuming import-inspection services to vet cargo beyond their competence to evaluate with adequate precision.

As for human resources, the manufacturers viewed the existing labor regulations as “very important” impediments to their operations. The most frequent complaint was about the tedious and expensive regulation process for firing workers. Another problem is the prohibition of piece-rate pay systems by the labor unions in South Africa. Moreover, the time consuming, frustrating, and often corrupt administrative procedures to obtain work permits for foreign workers daunt industrialists. The scarcity of technicians, supervisors and managers, the frequent and onerous is a serious constraint on competitiveness. In this context, South Africa should seriously consider benchmarking the Mauritius human resource policy and allow the automatic approval of work permits for up to a certain percentage of each factory’s total workforce.

As for support activities, the training of managers, technicians and operators is not enough to meet the demand. Typically, the training that occurs is informal and on the shop floor. Textile and clothing technology and training institutions is not sufficient for the needs of the industry.

In general, the textile and clothing industries in South Africa is still suffering from an inward-looking trade policy. No doubt liberalization of trade would spur their manufacturers to specialize, achieve economics of scale and improve their competitiveness in international markets. The biggest worry of government to push trade liberalization could be the massive job loss. But the low productivity and high production cost would eliminate the industry’s competitiveness, which will end up in less competitive factories closing down and eventually job losses.

The strategy in this paper that will have the greatest effect on the textile and clothing industry is further liberalization of trade with China. The concept of this strategy is to build a competitive supply chain for the textile and clothing industry

in South Africa. As we know, no single country has the resources to perform competitively every part of the pipeline while processing for every possible market. Rather, by abolishing tariffs on equipment, spares and imports used by the textile and garment industries to lower the cost and raise the quality of garments, the manufacturers will be more competitive in both local and export markets, thereby, achieve further economics of scale. Moreover, retailers and wholesalers will sell better quality garments to the market with more competitive price for the customers. This will result in the whole supply chain becoming more efficient in the end-to-end process.

This paper examines the possible influences on the textile and clothing industry if South Africa further liberalizes of trade with China. The result will reveal that there is still large potential to develop the South African textile and clothing industry by addressing constraints within the industry. Drawing on a survey of companies with secondary data support, this paper will argue liberalization with China will have a positive impact on South Africa's textile and clothing industry. There are indications that the restructuring induced by liberalization in these sectors will enable these industries to more effectively exploit its competitive strengths in international markets in the long term.

# **CHAPTER ONE-INTRODUCTION**

## **1.1 Introduction**

By examining the textile and clothing industry background and present situation in South Africa, it is reasonable to say that the industry in South Africa is facing a series of problems. To seek and recommend appropriate ways of solving the present dilemma, a research study regarding liberalization trade with China in the industry will be proposed. The research will adopt the postal survey with collecting secondary data. By conducting this research, we wish to discover the major factors, which could increase the competitiveness of the South African textile and clothing industry in the world markets.

## **1.2 Background**

South Africa is the most economically developed country in the African continent. Having an unparalleled economic foundation, South Africa boasts of fairly good infrastructure and considerably advanced technology, logistics network.

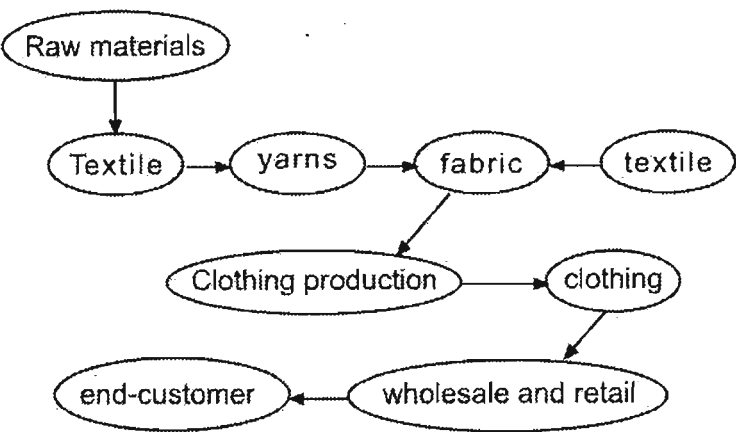
The textile and clothing industry in South Africa occupies an important role within the country's economy. It is the sixth largest the manufacturing sector and the second largest source of tax revenue in South Africa. The South African textile and clothing industries are characterized by producing a very diverse range of products. It has a highly developed textile and clothing pipeline, with a very large number of manufacturing companies in each sector. In total, there are approximately 580 textile production units and 2350 clothing production units in South Africa. Approximately 36% businesses are located in Kwazulu Natal.

Although the free agreement with the EU as well South Africa's compliance with the provisions of AGOA provided the country with certain benefits from the trade, the textile and clothing industry only supply 2% of the country's



exports. (Textile intelligence 2001)

**Figure 1.1** The simplified clothing-textile pipeline



Although the free agreement with the EU as well South Africa’s compliance with the provisions of AGOA provided the country with certain benefits from the trade, the textile and clothing industry only supply 2% of the country’s exports. (Textile intelligence 2001)

South Africa is china’s largest African partner, and this places emphasis on the potential for co-operation between the two powers where economies are complementary. In fact, since 1998 which diplomatic relations had been established, the Sino-South African bilateral economic and trade cooperation was reached. This resulted in a contribution of US\$2.05 billion in 2000, which relates to an increase of 19.1% over 1999. (MOFTEC) However, the textile and clothing trade in the past year, has remained unchanged at the same level.

The purpose of this research is to investigate the further liberalization of trade with China in relation to the development the clothing and textile industry in South Africa. The study links the economic and relative characteristics of the clothing and textile industries, looks at the current trade situation and analysis the drivers and barriers to further develop trade with China in this particular industry. The postal survey, a number of relative Internet websites and trade journals will provide the information.



### **1.3 Motivation**

South Africa has a long history of clothing and textile manufacture for a considerable time. The textile and clothing sectors are important industries in South Africa both from an output and employment perspective. In addition, they provide a ready market for the output of complementary and upstream industries, as well as being an important contributor to the South Africa. With political and economic changes since the 1994 democratic elections, the industry in South Africa moved away from its protectionist past towards an open, integrated economy. The country's textile and clothing industries were previously amongst the most highly protected of South Africa's industries, and are facing major challenges adapting to the requirements that have been brought by international competition and foreign access to domestic markets.

Nevertheless, many textile companies in South Africa have responded to the challenge by outsourcing more competitive supply base outside the country. With import control measures removed and tariff levels reduced, exports are growing as producers take advantage of trade agreements such as the EU's Trade, Development and Cooperation Agreement (TDCA) and the US African Growth and Opportunity Act (AGOA). AGOA in particular has a major impact on the development of textile manufacture in this country. These free trade agreements have created the environment where South Africa can take advantage of the trade.

Amongst all the trade volume, one unexpected result was Sino-South Africa's trade relationship increased continuously. Since the establishment of diplomatic relations between China and South Africa on January 1, 1998, the governments have attached importance to the bilateral economic and trade cooperation. Being the world's leading textile and clothing trade surplus, Chinese fabrics are generally 20-25% lower in price than South African price. (Cotton Incorporated 2002) It is probably viewed as an effective factor for South African companies to secure the export orders within the sub-Saharan region. In addition, despite world textile and clothing trade declined, strong consumer demands still exists in China. To further liberalize Sino-South Africa

trade relationship, hence, will definitely help South Africa to build an efficient supply chain and possibly open an export market for the clothing industry in South Africa in the future.

Past and current researches have focused on South African trade relationship with Europe and USA. There are hardly findings that could relate to the preset study and in particular trade with China. This study seeks to fill this “gap” and thus in particular focuses on the textile and clothing industry.

#### **1.4 Value**

As we mentioned above, the textile and clothing industry in South Africa is facing a series of problems. To seek and identify the factors, which will improve their local and international competitiveness in this industry, should be the major purpose for this research.

Furthermore, after reviewed relative literature and documents, the hypotheses had been concluded which should be further proved--- the textile and clothing industry developments are to a large extent driven by changing South Africa’s international trade environment, especially further liberalize the trade with China.

This research will focus on how to further stimulate the development of the clothing and textile industry, as well lead to attention from government to aware of the develop bilateral trade with China is important for this specific industry. This study will serve as a working document for government organization regarding the trade between China and South Africa.

#### **1.5 Problem statement**

The country’s previous apartheid stance and the sanctions imposed by many countries on South Africa as a result forced its economy to become inwardly – focused and insular. This led industries, including its domestic textile and clothing industry, to be dependent on domestic consumers. With new economic freedom, the domestic textile and clothing arena was force to compete on a global basis. However, overstaffing at mills and a

management's mindset remaining from the past has meant that this change has taken place gradually and not at the rapid rate that it should have.

South African manufacturers are finding it difficult to compete with low priced imports products. Yarns of protectionism have made it hard for South African companies to secure the export orders within the Sub-Saharan. Furthermore, the industry's dominant position is being threatened by a progressive reduction of the tariffs, which have sheltered it from foreign competition.

### **1.6 Objective of study**

The following objectives will assist in solving the problem identified in this study:

- To discover the correlation between further liberalization of Sino-South African trade relationship with the development of the textile and clothing industry in South Africa.
- To discover the leading factors, which probably increase the ability of textile and clothing industry response to the challenge they are facing.
- To recommend to textile and clothing industry appropriate ways of solving the present dilemma.
- Produce a rich, detailed, complete documentary of Sino-South African trade relationship

### **1.7 Hypotheses**

H1: liberalization of trade with China would positively effect the development of textile and clothing industry in South Africa.

H2: liberalization of trade with China would negatively effect the development of textile and clothing industry in South Africa.

### **1.8 Research design and methodology**

This study will be viewed as formal study. It involves precise procedures and data source specification to test the previous mentioned hypotheses. The study will be conducted on a three –tier basis:

- Assessing status quo situation

- Benchmark “to be” situation against other successful case
- Explore the prospect for the textile and clothing industry in South Africa

The data collection will be based on sourcing secondary data and collecting primary data. Survey questionnaires will be posted to the top management in few major textile and Clothing companies. The sampling companies will be chosen from Kwazulu Natal since 36% of textile and 33% of clothing manufacturing units are located in this area. We anticipate a maximum of 10 questions which all closed questions. A five-point likert scales being designed.

In order to obtain a comprehensive data set, the relative Internet web site, trade articles and reports, industry associations and trade publications will also be used to provide the detailed and in-depth secondary data for this dissertation.

### **1.9 Limitations of study**

- The information provide by government would be insufficient due to part of statistics data being confidential.
- Secondary data may be out of data.
- Managers may be biased to answer questions according to their own perspective.
- The primary data collected is based on only one province and could cause deviation and bias.

### **1.10 Structure of the study**

Chapter two- The three theories -Porter’s diamond theory, SWOT analysis and Gap analysis will be reviewed. These theories could be utilized as a sound theoretical foundation to support this paper.

Chapter three- The structure and performance of textile and clothing industries in South Africa and China will be briefly examined as well as the current trade relationship between these two countries.

Chapter four-This session will focus on exploring the strength and weakness of the textile and clothing industries in South Africa by conducting the postal survey combined with collecting comprehensive secondary data.

Chapter five-This session will provide the direction and strategy for the South African textile and clothing industries to become more competitive in the world markets.

### **1.11 Conclusions**

According to research conducted, South Africans spend on average 7 percent of their annual income on clothing. (Textile Industry SA 2002) Low consumer demand and reduced disposable income will lead to fierce price competition. This will result in a decline in local sales that will adversely affect the industry. It is expected that exports of South African textiles and clothing as a result of the weak Rand will increase further that South African manufactures are increasingly breaking into foreign markets.

The South African textile and clothing industry has embraced the General Agreement of Trade and Tariffs (GATT) and the philosophy of trade liberalization and is striving to become more efficient and competitive. In this study there will be a contribution towards the potential for opportunities in this particular industry and in addition promote South Africa's economy.

## CHAPTER TWO-STRATEGY IN A GLOBAL CONTEXT

### 2.1 Introduction

Research projects need to be anchored by a sound theoretical foundation. The major theories to support the study will include:

- **Porter's diamond** will be used to analyze the competitiveness of the nation.
- **SWOT** (strengths, weakness, opportunity and Threat) will be used to classify the internal aspects of the industry as strengths or weaknesses and the external situational factors as opportunities or threats.
- **Gap analysis** will use three questions to indicate the direction and problems of the textile and clothing industries.

### 2.2 Porter's diamond

The literature indicates there is not one single definition for the term of national competitiveness. Earlier definitions relate national competitiveness to macroeconomic variables as exchange rates or government deficits. Or with the availability of cheap labor, as the result of government policies such as e.g. protection, subsidies etc., or finally as a result of management practices and management-labor relations. For Porter none of these definitions is satisfactory. In his eyes, "the only meaningful concept of competitiveness at the national level is productivity". (Porter 1990 p76) Productivity is the basis for national per capita income and therewith the basis for the national standard of living. High standard of living should be the goal of every nation and therefore it depends on the productivity of the local industries and its need for sustainable growth. In order to explain national competitiveness one has to focus on specific industries and segments and how they gain competitive advantage to compete internationally, including trade and foreign investments.

#### 2.2.1. The model of the national diamond

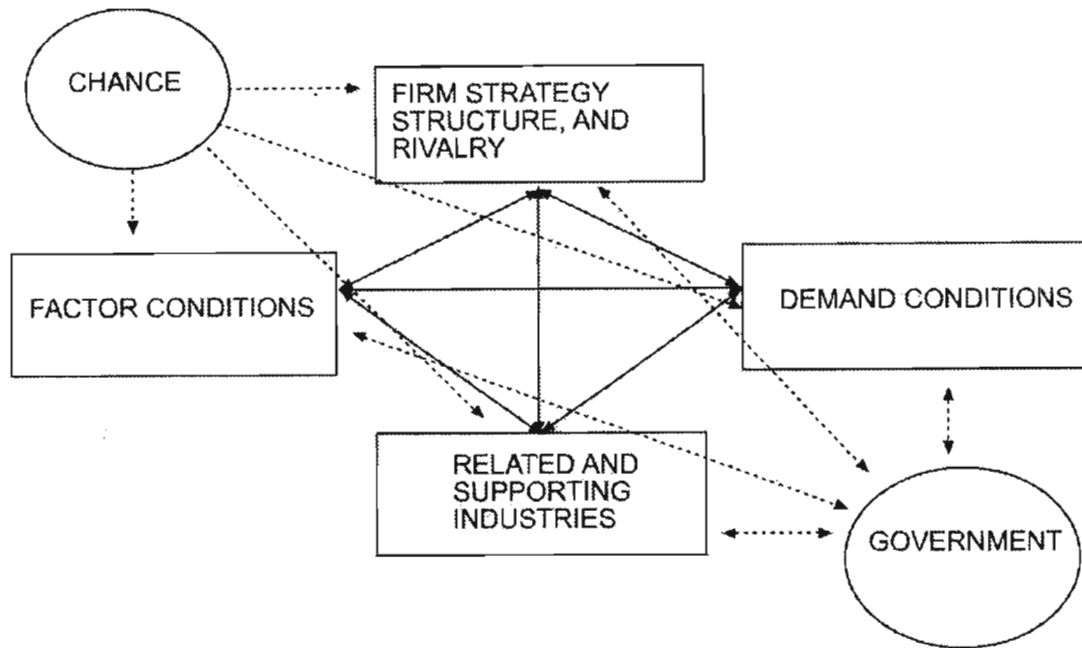
After his four-year study Porter came up with new ideas and explanations why competitive advantage varies among nations, and in the process distanced



him from traditional theories. He suggests, "A nation's competitiveness depends on the capacity of its industry to innovate and upgrade". (Porter 1990 p.73). Companies need challenge and pressure to develop competitive advantage against global competitors, benefiting from fierce domestic rivals, strong local demand and localized process is influenced by culture, history, institutions and economic structure. He contradicts the prevailing thinking that "labor costs, interest rates, exchange rates, and economies of scale are the most potent determinants of competitiveness" (Porter 1990 p.73). The most important issues for gaining and sustaining competitive advantage are innovation and upgrading. Innovation can occur in form of creating a new product, a new production process, finding a market segment that so far has been ignored by others, or by just using an already existing idea for one's own proposed for the first time. A times the path to innovation could be a small investment; sometimes it means great and constant effort and overcoming obstacles. Upgrading of products, processes and other resources are necessary to move ahead of competition and make attempts to stay in front.

The "Diamond of National Advantage" can be described as "a concept intended to capture the key elements of a company's situation that influence its potential international strengths" (Bowman and Fulkner 1997,p.269) or as "a framework for explaining the location of various industries among nations" (Oster 1999, P.109). It suggests that the national home base of an organization play an important role in shaping the extent to which it is likely to achieve advantage on a global scale. It shows which national attributes are important for a favorable national environment.

**Figure 2.1** The “diamond of national Advantage”



Resource: Meyer, R & DE WIT, B 1998, P775

Porter's diamond consists of four determinants:

➤ Factor conditions

According to the traditional economic theory factors of production (labor Land, natural resources, capital, infrastructure) determine the production and trade of the single nation. Emphasis will be on the factors a nation is relatively well endowed with. According to Porter, it is not of outstanding importance which factors of production a nation already inherits, but which factors of production it can create in a short period of time and deploy efficiently.

There are four kinds of factors of production: basic and advanced, general and specialized factors. For creating competitive advantage, it is more important to have advanced and specialized factors. In the age of globalization and international mobility it is easy for companies today to import basic factors (e.g. digital communication networks, engineers) and specialized factors that benefit only a particular industry (special apprenticeships, infrastructure tailored to an industry). These are usually the result of big investment and are more difficult to gain, to use and to imitate. Factors highly specialized to an industry's need offer support to the competitive advantage.



Selective disadvantages in more basic factors can turn out to be advantages. Companies facing a selective disadvantage as e.g. the distance of raw materials to the production facility are forced to innovate in order to compensate the disadvantage and to remain competitive. To become advantages the disadvantages have to meet two conditions: first, they must give companies the chance to innovate in advance of the foreign rivals and second, there must be favorable circumstances elsewhere in the diamond. If there is no challenge at another determinant, e.g. rivalry, companies may be tempted to use the easy path around the disadvantage instead of tackling the problem.

➤ Demand conditions

International competition does not diminish the importance of domestic demand. When the market for a particular product is larger locally than in foreign markets, the local firms devote more attention to that product is larger locally than do foreign firms, leading to a competitive advantage when the local firms begin exporting the product. Not only the size of the local demand is important, so is the character. Highly sophisticated and demanding buyers force companies to meet their high standards. Special or difficult needs can arise from local circumstances, as small flats, hot climates etc. and influence local demand. Products tailored to local circumstances or values may gain international acceptance later. A home demand that provides clearer and earlier signals of demand trends to domestic suppliers than to foreign competitors helps an organization to anticipate future needs. Finally local companies can try to influence foreign demand by using mechanism that transmits domestic preferences to global markets.

A strong and growing local market offers a strong base for a company when going global. In case of maturity local demand may also be an incentive for firms to move to foreign markets.

➤ Related and supporting industries

Another determinant of national advantage is the presence of related as well

as supporting industries. With international competitive suppliers companies lead to a self-defeat, as they do not have real incentives or enough pressure for innovation. Serving global customers means winning global information and being able to communicate those to the local market. Companies can also support their supplier with research and development and help them to enter new markets. Competitive supplying industries will reinforce innovation and internationalization at later stages in the value system. There is no need for all supplier industries to be internationally competitive. Some products and technologies are generalized, as e.g. software.

Related industries can be concerned with complementary products or those with which an organization can use and co-ordinate particular activities in the value chain together. A close relationship between supplier as well as related industries opens the lines of communication and knowledge to companies, a way to constant exchange of ideas and feedback. This relationship should be interdependent.

➤ Firm strategy, structure, and rivalry

Culture aspects and local conditions affect a company's strategy, structure and management, whether a company tends e.g. to be hierarchical or family run. There is no one common global strategy or management theory but various management ideologies. Strategy as well as structure and management style have to converge with those favored in the country. The goals of companies as well as of individuals vary as well throughout the different nations and according to Porter reflect a nation's capital market, whether it is more focus on long run or short-run results. Another aspect for competitive advantage is the national's motivation for work and education, which is influenced by national value systems, opportunities and the prestige of the various industries in a country.

The most important stimulation for innovation and constant upgrading may be the existence of strong local rivals. In general local rivalry is more intense than the global one. It forces companies to move beyond basic advantages of the home country. Vigorous domestic competition pushes companies to increase

efficiency, to innovate, to upgrade. There is no excuse for being beaten by a local rival, as all companies do their business in the same local environment. Often local rivalry gets a personal touch, which leads to even more eagerness between competitors. The more locally concentrated the rivalry, the more intense, and the better. Local competitors will not be able to influence government to their advantage: political actions may harm them as well as their competitors, and benefits are shared equally. Fierce local rivalry can also encourage companies to look to outside markets for growth. Having survived in the fierce competition at the local market the company is well equipped and has improved its ability to compete in global markets.

### 2.2.2 The diamond as a system

The four determinants of the diamond of national advantages are interdependent. Sophisticated local demand cannot be served without skilled human resources. Disadvantages in factor creation will not be eliminated until there is fierce local rivalry. Further the attributes of the diamond are also self-reinforcing, constituting a system, Especially two elements are powerful enough to transform the diamond into a system, “domestic rivalry because it promotes improvement into in all other determinants and geographic concentration because it elevates and magnifies the interaction of the four separate influence”. (Porter 1990,p.86). Intensive rivalry forces innovation which leads to the creation of advance and specialized factors and sophisticated local demand, as buyers know that any of the rivals will satisfy their needs. Further it offers a suitable environment for suppliers and related industries, which also profit from that competition.

Competitive industries furthermore tend to concentrate geographically in the same region. The diamond “creates an environment that promotes clusters of industries” (Porter 1990,p.86) the formation of a cluster goes hand in hand with mutual support and benefits for the whole group. Competition spreads among the various groups of a cluster. A cluster possibly also invites new companies and industries to settle down and offer new information, motivation, ideas and competition. Furthermore, there are two other determinants, which to some extent could affect the competitiveness as

follows:

➤ The role of the government

The government of a nation plays an important role on affecting competitive advantage. There are two basic views: on the one hand, government can be regarded as a friend", a supporter that with policies and regulation directly supports and contributes to the competitive advantage. On the other hand, the view is to leave the market freely to the invisible hand without government intervention. According to Porter, both views are incorrect. The effective role for the government is "as a catalyst and challenger" (Porter 1990 p87) it shall encourage companies to raise and move to higher levels of performance, even if this process maybe unpleasant and difficult. Government, as it can influence all four determinants though a variety of actions, has the responsibility to create a suitable environment for companies by indirectly influencing and modifying the important attributes of the diamond. Governments are often tempted to initiate policies, which have a positive short-run effect on the diamond, because their legislation period is much shorter than it takes companies to adapt and built up competitive advantage from changes in their environment. Typical policies are e.g. arranged mergers and subsidies. Still it is important to focus on the positive effects of policies, which may be unpleasant in the beginning but lead to advantages in the long run.

Porter offers some basic principles for government to support national competitiveness (Porter 1990 p.87):

- Focus on specialized factors
- Avoid intervening in factor and currency markets
- Enforce strict product, safety, and environmental standards
- Sharply limit direct co-operation among industry rivals
- Promote goals that lead to sustained investment
- Deregulate competition
- Enforce strong domestic antitrust policies
- Reject managed trade

Government has to offer companies the opportunities to gain enough strength, ability and advantages within the borders of their own nation to be able to tackle foreign markets from that strong base.

➤ The role of chance

Chance plays another important influence on the national diamond. Not all factors and situations can be influenced by policies and strategies. Random events can either benefit or harm a company's position. Who, for example, comes up with a major first idea? It is also quite common that innovators and entrepreneurs start their first business in the country they live in, and do not seek actively for the most suitable place in the world to stay. It is possible that with their business, they lay down the first stone for a serious cluster in their nation. What starts out by chance may gain substantial economic consequences later.

Other events can be: major technological breakthroughs or inventions, war, dramatic shifts of exchange rate, crash of the stock exchange, price shocks, political decisions of foreign governments.

### 2.2.3 The role of leadership

In the end it depends only on the companies whether they are able to profit from their environment and turn it into competitive advantage. It further depends on the leadership within the company, whether management prefers stability and easy routes around a problem, or whether it is willing to take the risk and move on, overcoming obstacles, investing in research accepting the necessity of change, leading to competitive advantage in the end. Again Porter offers some policies that will support the effort of a company and its management to gain competitive advantage:

- Create pressure for innovation
- Seek out the most capable competitors as motivators
- Establish early –warning systems
- Improve the national diamond
- Welcome domestic rivalry



- Globalize to tap selective advantages in other nations
- Use alliances only selectively
- Locate the home base to support competitive advantage

Following these policies, companies are on the right track to establish competitive advantage.

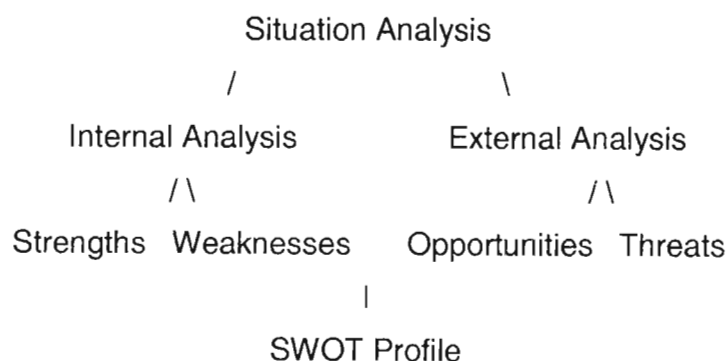
In general, all in Porter's model is not really new. What he mentions to be determinants for gaining competitive advantage in a nation are just general factors every industry is concerned about when examining a competitive environment. But Porter is the one who puts those determinants together in a model, which is shaped as a diamond and launches a new tool in business.

#### 2.2.4 Criticism

Porter's theory of national competitive advantage can be criticized in some way. Porter has gained all his information from case studies from different industries in different nations. He does not offer any empirical or statistical evidence to support his theories. He focuses strongly on developed industries, but what about industries in developing countries. It seems that the basic factors of traditional theories are not as unimportant as Porter suggests. Furthermore he focuses on intensive local rivalry. He might also underestimate the influence global rivalry on today's world market, as enough global players are able to eliminate the existence of smaller local companies. Today's world market is in some industries well separated among a few large MNEs. It is furthermore the question, whether MNEs correspond only to internal or local influences or how far global and external influences are important for establishing competitive advantage. Porter further states that not nations but firms are those, which compete in international markets. So again the examination of competitive advantage has to take place on firm rather than on national level. And as stated before, a lot of business depends on chance; global events can have a strong influence on local markets. Porter's interpretation of the history of industries has to be taken for granted without evidence but is not always convincing that using his model can bring really advantages for a company in the future.

## 2.3 SWOT Analysis

When conducting strategic research for any industry, it is useful to complete analysis that takes into account not only your own area, but your competitor's in the regional and global market and current industry happenings as well. SWOT analysis is one such analysis. SWOT analysis is a tool for auditing an organization and its environment. It is a simple framework for generating strategic alternatives from a situation analysis. It is applicable to either the corporate level or the business units level and frequently appears in marketing plans. SWOT stands for Strengths, Weaknesses, Opportunities, and Threats. The SWOT framework was described in the late 1960's by Edmund P. Learned, C. Roland Christiansen, Kenneth Andrews, and William D. Guth in *Business Policy, Text and Cases* (Homewood, IL: Irwin, 1969). Because it concentrates on the issues that potentially have the most impact, the SWOT analysis is useful when a very limited amount of time is available to address a complex strategic situation. The aim of SWOT analysis is to match likely external environmental changes with internal capabilities, to test these out and challenge how an organization can capitalize on new opportunities, of defend itself against future threats. The following diagram shows how a SWOT analysis fits into a strategic situation analysis.



The internal and external situation analysis can produce a large amount of information, much of which may not be highly relevant. The SWOT analysis can serve as an interpretative filter to reduce the information to a manageable quantity of key issues. The SWOT analysis classifies the internal aspects of the company as strengths or weaknesses and the external situational factors as opportunities or threats. Strengths can serve as a foundation for building a

competitive advantage, and weaknesses may hinder it. By understanding these four aspects of its situation, a firm or industry can better leverage its strengths; correct its weaknesses, capitalize on golden opportunities, and deter potentially devastating threats.

### 2.3.1 Definition

**Strength:** -A company strength is a successful application of a competency or exploitation of a critical factor to develop company competitiveness.

**Weakness:** -A company weakness is an unsuccessful application of a competency or the non-exploitation of a critical factor that diminishes company competitiveness.

**Opportunities:** - An opportunity is an external condition that could positively impact the company's critical performance parameters and improve competitive advantage provided positive action is taken in time.

**Threats:** -A threat is an external condition that could negatively impact the company's critical performance parameters and diminish competitive advantage provides positive action is not taken in time.

### Internal analysis

The internal analysis is a comprehensive evaluation of the internal environment's potential strengths and weaknesses. Factors should be evaluated across the firm or industry in areas such as:

- Company culture
- Company image
- Organizational structure
- Key staff
- Access to natural resources
- Position on the experience curve
- Operational efficiency



- Operational capacity
- Brand awareness
- Market share
- Financial resources
- Exclusive contracts
- Patents and trade secrets

### External analysis

An opportunity is the chance to introduce a new product or service that can generate superior returns. Opportunities can arise when changes occur in the external environment. Many of these changes can be perceived as threats to the market position of existing products and may necessitate a change in product specifications or the development of new products in order for the firm to remain competitive. Changes in the external environment may be related to:

- Customers
- Competitors
- Market trends
- Suppliers
- Partners
- Social changes
- New technology
- Economic environment
- Political and regulatory environment

2.3.2 SWOT profile

When the analysis has been completed, a SWOT profile can be generated and used as the basis of goal setting, strategy formulation, and implementation. The completed SWOT profile sometimes is arranged as follows:

	Strength	Weakness
Opportunity	?	?
Threat	?	?

A preliminary approach for carrying out a SWOT analysis is to list perceived company strengths, weaknesses, opportunities and threats under each of these headings. Ensure that no weaknesses cancel out company strengths and potential threats to the company strengths or opportunities that could arise out of correcting weaknesses. On the above list, highlight key areas of concern or areas that require action. These become the focus for future planning.

This approach is preliminary - as it does not evaluate the relative importance of each issue. A further approach is to locate all the strengths, weaknesses, opportunities and threats into a matrix. A scoring mechanism is also used as an aid to provide clarity to the analysis and assessment. This scoring system is providing straightforward information to indicate that the current or weakness would be positively or negatively affected by an environmental change.

2.3.3 SWOT analysis limitation

While useful for reducing a large quantity of situational factors into a more manageable profile, the SWOT framework has a tendency to oversimplify the entire situation by classifying the firm's environmental factors into categories in

which they may not always fit. The classification of some factors as strengths or weaknesses, or as opportunities or threats is somewhat arbitrary. For example, a particular company culture can be either strengths or a weakness. A technological change can be either a threat or an opportunity. Perhaps what is more important than the superficial classification of these factors is the firm's awareness of them and its development of a strategic plan to use them to its advantage?

## **2.4 Gap Analysis**

In assessing strategies for the future, leaders are usually concerned with understanding the incentive to change—in other words, the extent to which current strategies would fall short of meeting the organization's aspirations and/or obligations. Gap analysis is one approach to assess the need for change.

More usefully, gap analysis is less concerned with the fact that there is a gap between things, than with how to close the gap. Recognition of the fact that a gap exists is only one stage in the process. Having recognized that there is a gap, the manager needs to develop strategic that will close the gap, manage the process of change, and finally, monitor the process to ensure that the same gap does not reappear. The process of gap analysis can thus be portrayed pictorially (Figure 2.2)

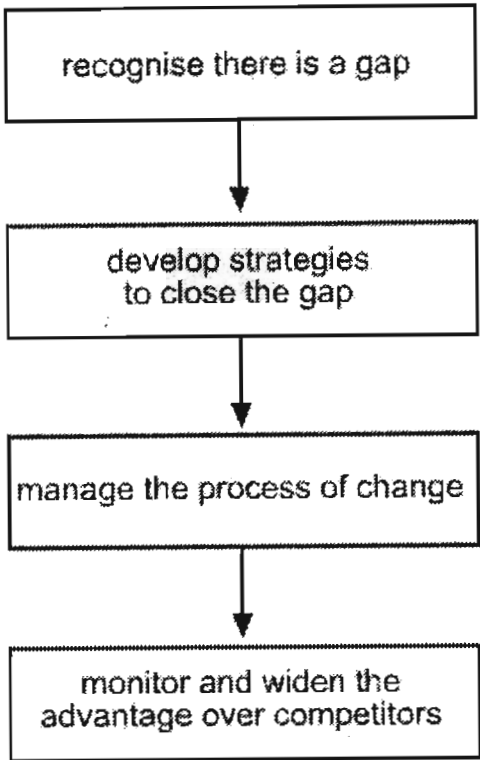
A simple, but very powerful approach to gap analysis centers around three questions:

- Where are we now?
- Where do we want to get to?
- How can we get there?

Those three questions can portray graphically, as shown in Figure 2.3, which illustrates how simple performance gap analysis can be. Used in such a

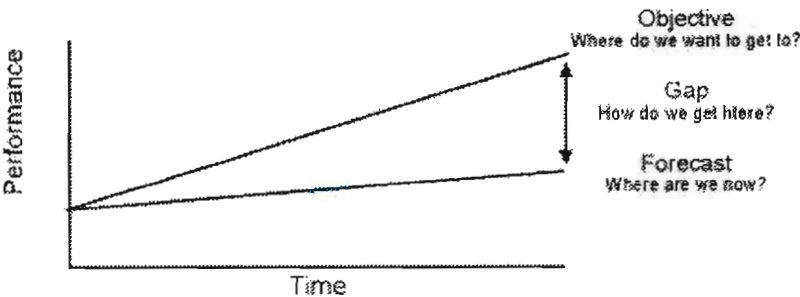
manner, the three questions have relevance in almost every planning and forecasting scenario.

**Figure 2.2** A model of gap analysis



Resource: Ambrosini

**Figure 2.3** Performance gap analysis



Resource: Ambrosini

Their usage tends to frame the nature of the planning and forecasting problem being faced and allows the application of other strategic planning techniques with a purpose and direction.

When gaps are found, three alternative courses of action can be following:

- Redefine the objectives.

The first thing to do when a discrepancy between objectives and forecast is found is to check that the objectives are realistic and achievable. If the objective have deliberately been set at a very high level to stimulate action, it is usually advisable to set less high intermediate objectives. This course of action avoids the problem of the manager perceiving that his actions will not make any significant impact upon objectives, which can lessen motivation.

- Do nothing.

This option is under-utilized by the manager, but should be considered. Reorganization and redirection is commonplace in the business environment but it is clear that people become “change-weary” and that continual change can lead to defensive behavior, increased staff turnover, and decreased levels of satisfaction and lower levels of commitment. Sometimes giving people time to “bed in” to a new structure and new ways of doing things pays greater dividends than another change.

- Change the strategy.

When a gap is found between objectives and forecast and the first two options have been considered and rejected the only alternative is to change the current strategy and develop a new one. Having identified a gap, the manager now used the other strategic tools to analyze the various options available.

Gap analysis is a “first stage” technique that reveals the nature and the size of the strategic problem. Gap analysis frames the problem and informs the manager about the directions in which to look for solutions. Once this direction has been established, other techniques can then come into play. As such, gap analysis is a vital strategic weapon.

## **2.5 Conclusion**

In the session, these three theories have been reviewed. Porter’s diamond theory addressed that a nation can create new advanced factor endowments

such as skilled labor, a strong technology and knowledge base, government support, and culture. Porter used a diamond shaped diagram as the basis of a framework to illustrate the determinants of national advantage. A SWOT starts with an external analysis of the business environment, and then looks at the organization's internal strengths and weaknesses, relative to internal factors such prior performance and also to external factors. The final stage is to combine the analyses to look at opportunities and threats facing the organization and to draw up plans to take advantage of the opportunities and to counter the threats. Gap analysis is one approach to assess the current strategy and the need for change. In chapter 4, we will use Porter's diamond and SWOT as tools to analysis the situation of textile and clothing industries in South Africa as well as to look for the future by gap analysis.

## **CHAPTER THREE-**

### **Structure and performance of textile and clothing industry in South Africa and China**

#### **3.1 Introduction**

The South African economy has historically been based on natural resource industries, and heavy industries linked to natural resources, such as iron and steel, have dominated manufacturing exports (Fine and Rustonjee, 1996; Roberts, 2000). The South African government recently identified textiles and clothing as a priority sector, followed by a policy of export-led growth through incentives and import liberalization. In this sense it is trying to follow the path of Far East and China, which generated these particular industries' growth through trade liberalization.

Against this background, it is therefore interesting and necessary to briefly examine the history and present situation of the textile and clothing industries in South Africa and China as well as the current trade relationship between these two countries.

#### **3.2 Textile and clothing industry in South Africa**

South Africa is a large country with a population of 44 million. South Africa is, at once, a first world and a third-world economy operating side by side. Per capita income statistics may be misleading unless the substantial gap between reasonably well off, middle class, and the masses of poor are taken into account.

The current volatility of global financial markets and realignment of emerging market economies has impacted on South Africa heavily, making the government's ambitious reform and restructuring process difficult. The Asian Financial Crisis hit South Africa particularly hard, as Japan and Taiwan are



South Africa's two large trade and investment partners. As a direct result, the South African Rand lost 25 percent of its value against the dollar since January 1998. South Africa is experiencing an economic slowdown, which began in the 3rd quarter of 1997.

South Africa has severe unemployment, officially estimated at over 30%, but, realistically, most recognize it at 50-60%. The country's previous apartheid stance and the sanctions imposed by many countries on South Africa as a result forced its economy to become inward-focused and insular. This led industries, including its domestic textile and apparel industry, to be dependent on domestic consumers (primarily Woolworth's – the South African equivalent to Marks & Spencer) until sanctions were lifted some 10 years ago. With new economic freedom, South African retailers began sourcing worldwide to improve their ability to compete with a large influx of commodity- type imported apparel from Asia. When South African retailers began looking for a more competitive supply base outside the country, the domestic textile and apparel industries were, in turn, forced to begin to try to compete on a global basis after years of, in effect, protectionism. Over-staffing at mills and a management mind set remaining from the past has made this process a challenge. While reducing the number of company employees is necessary to increase competitiveness, this has proved difficult in a country with strong unions and an exceptionally high rate of unemployment.

Employment in South Africa is governed by a minimum wage of Rand 192/week (US\$28) or \$112/month minimum. However, most textile workers receive wages between US\$200-\$250/month. Wages, working conditions and workers' rights are closely guarded by strong unions which operating mostly in urban areas. Some companies (small entrepreneurial companies and foreign investors) are setting up operations in decentralized zones (Decentralized Zones have been set up by the South African government in rural districts to encourage development outside of major urban areas. Union does not govern Employment in those zones) to take advantage of the lack of union activity in those areas, thereby giving employers a chance to negotiate wage rates below minimum by as much as 50%.



### 3.2.1 The textile sector

The textile production chain consists of distinct levels of processing in which raw material is made into yarn, which in turn is made into fabric (either knitted, woven or not-woven) from which various articles are made, including clothing. South Africa produces both dry land and irrigated cotton, averaging about 175,000 bales over the past five years, 240,000 bales (53,000 MT) in 1999/2000, mostly 1 3/32 inch. This is supplemented by imports of 138,000 bales (30,000 MT) from Zimbabwe, Zambia and Mozambique. The industry is uncertain about the impact on cotton supply from Zimbabwe due to the political and farming disruption caused by its current leader. Total cotton fiber consumption is estimated at 345,000 bales (73,000 MT). (Simon Roberts & John Thoburn) South African mills are compelled to buy South African fiber first and can import cotton with a permit only once that supply has become exhausted. Prices paid to growers are typically about the level of the 'A' index (implicitly higher than other growers in the region). If local spinning capacity is expanded, spinners would likely demand access to competitively priced fiber, which, in turn, may lead the South African government identifying alternative farmer support schemes. Yarn capacity in South Africa is 66,000 MT, about 2/3 cotton and the remaining third poly/cotton blend. In 1999, fabric production in South Africa was about 165 million square meters of knitted fabric, plus 180 million square meters of woven cotton fabrics; plus 235 million square meters of synthetic fabrics (spun and continuous). South Africa imported less than 8,000 MT of woven cotton fabrics in 1999. The low levels of fabric imports are despite industry assessments that Chinese fabrics are generally 20-25% lower in price than South African fabrics.

The SA textile sector developed against the background of conditions similar to those discussed in relation to the clothing sector and evolved a similarly highly diversified structure. While this is becoming simplified today, the aggregate level of specialization remains low. Of 20 separate product types, which are listed by the Textile Federation, the largest category was yarns (listed by 12 companies), followed by knitted fabrics (6 companies), curtaining, furniture and upholstery fabrics (5 companies) and toweling (3

companies). Production increase into 1997 before falling sharply (Figure 3.1), and employment has fallen over the decade (Figure 3.2). Capacity utilization has been falling since the mid-1990s, mainly due to weak domestic demand. Poor performance in 1998 and 1999 has also been attributed to the East Asian crisis, which led to cheaper imports from countries in that region.

Figure 3.1 Index of real production

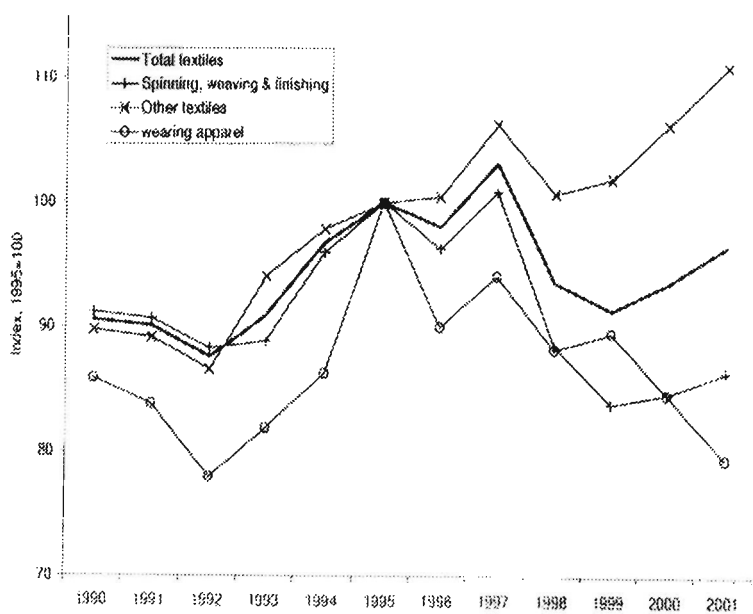
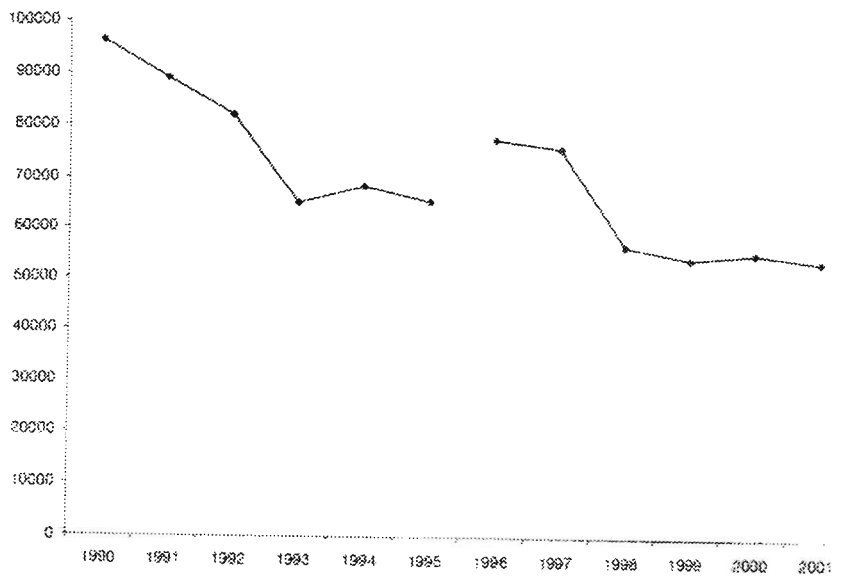


Figure 3.2 Employment



Source: Statistics South Africa  
 Note: Break in series: data for the former 'homelands' were only included from 1996.

In general, there are four main pointers could be used to describe the current trends in textile industry.

- Most companies were in the process of becoming more specialized. This trend was an informally coordinated one and encompassed specialization both by raw materials (from natural fiber to the other), by process and by product range (from a wider to a narrower range of yarns). The reason for this change is try to achieve greater economies of scale in the production to meet the world market.
- Greater specialization entailed a trend away from apparel and toward non-apparel textile. In fact, apparel textile output's share of capacity had been halved since 1996 and was now being mostly outsourced to smaller mills. The industry yarns/fabrics tended to be associated with higher margins, more security of demand, longer run lengths; less finishing work and less left over inventory.
- Within apparel textile production for export, there was a strong tendency for direct exporting to be preferred over indirect exporting. Partly, this was again for reasons concerning economies of scale due to the indirect export demand were considered mostly too low to justify investment in new special yarn or fabric developments.
- Output is more concentrated by company than in the clothing sector and there is also a generally more concentrated ownership structure. Very little vertical integration between textiles and clothing exists, but the levels of foreign ownership have been increasing and now run at around a third of larger firms.

### 3.2.2 The retailer sector

There is an extremely high level of concentration within the South Africa retailer sectors and correspondingly with high levels of buying power which increased during the 1990s. The combination of very high levels of buyer power, seriously heightened price competition and the availability of an import option have led to two main changes in the conditions faced by clothing manufacturers in the domestic market. Firstly, both volumes and margins have come under severe pressure. As the discounter-led competition has

been heightened, many retailers have had to work on lower margins. Secondly, with the notable exception of Woolworth's, leading retailers took most of their long-run business offshore. Offshore sourcing is normally for longer runs because it is cheaper and easier to find supplier for them and because it is here that the major price advantages of offshore sourcing can be gained. In addition, the long run items normally have longer lead times and can therefore be sourced over longer distances. Thus local manufacturers were left with a higher proportion of short runs with short lead times, This trend was partly amplified by tendency toward product proliferation in the domestic women' wear market.

A relatively unusual feature of the South Africa clothing retail scene is that, of the seven leading retailer, two (Pep store and Edgars) have in-house local production facilities, while another (Foschini) sources a large majority of its intake through an own organized network of near delicate CMTers. South Africa retailers were sourcing through at least 11 distinct channels, which separately divides to imported intake and domestic intake (Table 3.1)

Besides a general shift toward imported sources of intake, South African retailers had generally abandoned exclusive supply relations with full manufacturers, and were making more use of design houses and "opportunity buys" than ever before. Design houses were being used more frequently because a number of former suppliers (especially for women's wear) had converted themselves from full manufacture to this role. Mainly amongst retailer in lower market segments there was a trend to use full manufacturers not only as for manufacturing but also as design house, importers and finishers.

**Table 3.1** South Africa retailers sourcing channels

Imported intake	<ul style="list-style-type: none"><li>• SA specialized importers and importer/wholesalers</li><li>• Agents in the Far East and India</li><li>• Global sourcing agencies</li><li>• SA full manufacturers' importing operations</li><li>• International licensees (For branded goods without local licensees)</li></ul>
Domestic intake	<ul style="list-style-type: none"><li>• SA full manufacturers (with/without own CMTers)</li><li>• Design houses and their CMTers</li><li>• Word-of-mouth "opportunity buys" (over-runs, cancelled orders, other retailer's stock, etc)</li><li>• In-house manufactures</li><li>• Own-organized CMTers</li><li>• Local licensees (For branded goods)</li></ul>

Resource: DTI

3.2.3 The clothing sector

The South African clothing industry first developed to a size approaching its present one only during the 1960s, during which decade it almost doubled in size. This followed a period of relative slow growth coinciding with a gradual extension of import substitution measures. Prior to the 1960s the industry was based largely in the Johannesburg area with a secondary concentration in Cape Town. As a consequence of new apartheid status imposing limits on the use of African labor in urban areas, the industry contracted in Transvaal and expanded in Durban and Cape Town, which soon became its single main center. Partly because most of the country's leading retailers were also headquartered in Cape Town, the industry there came to be oriented toward the larger retail chains.

The main instrument of import substitution was an extremely complex system of protection with liberal use both of formula and specific tariffs. There were approximately 2000 separate clothing and textile tariff rates by the 1980s and many of them apparently introduced to give protection to individual firms. As a result of this system, aggregate levels of specialization within the sector was extremely low and the distribution of production capacity between women's, men's, and children's and between fashion/fancy and basic product lines corresponded more or less directly to the overall pattern of national demand. Competition was restricted and levels of efficiency were almost certainly below the international standards.

There was also a significant level of new foreign investment in this period- particularly by Taiwanese companies into low-wage and larger regional areas. While most Taiwanese investments were of an SME type and aimed at domestic market production, there were also a series of larger ones aimed at export proportion by companies that were already quota holders in Taiwan. From 1991 onwards foreign investment began to dominate the employment picture in decentralized areas, both because of its own gradual rise and, because when the RDP subsidies expired-many SA owned companies closed or returned to the urban areas.

South African clothing companies can be characterized in one of 4 categories:

➤ *Medium-sized, urban-based companies with organized labor.*

These companies are heavily dependent on domestic customers but have the longest experience in exporting. Despite devaluation of the Rand in recent years, wage increases have out-paced devaluation, increasing their cost of production. These companies are the most technologically up-to-date.

➤ *Larger-scale urban-based with organized labor for large-scale production.* Capacities make these companies most likely to meet the U.S. volume requirements. They have a more



collaborative approach to labor relations and customer relations, giving them a source of strength.

- *Small entrepreneurial companies working outside formal labor and tax structures.* These companies have been typified as places where 'everybody wants to work but nobody knows how'. Generally, these companies are seen as assets to the industry with a cost-effective labor resource. The challenge seen by the industry is how to capitalize on these companies without spoiling them.
- *Trans-national companies.* These companies are largely Hong Kong entrepreneur and Taiwanese owned and based in the decentralized regions to take advantage of low cost labor. Chinese companies working in these areas are focused on larger scale operations and have set up companies using Chinese management and working practices including payment on piecework basis. Wages in these areas are typically 50% those in the industrial areas of Cape Town, Durban and Johannesburg.

Beginning with the negative developments, this sector has undergone a substantial real decline in output since the political transition- a real decline, moreover, almost twice as great as domestic market shrinkage. Output rose in nominal terms by almost 17 percent between 1995 and 2000, but in real terms declined by 19.6 percent. Total clothing production was officially estimated at 200 million units in 1999 (Many industry experts believe that figure is much higher). Sophisticated consumer demands but lower overall consumption levels characterize the South African clothing market. Import values still exceed those of exports in textiles and footwear, while clothing manufacturers have maintained a fairly equal balance by value. Imports in 2000 amounted to around R1bn, while exports amounted to approximately R1.3bn. Clothing production volume currently exceeds that of textiles. Major export categories include men's woven and men's knitted cotton shirts.



After declining figures following the 1998/99 recessions, the local market was slow from 2000 as retailers felt the impact of changing spending patterns with introduction of the lotto, legalized gambling and increasing cell phone expenditure. Furthermore, South African manufacturers are finding it difficult to compete with imports of large quantities of “commodity” type products at low price points. Further cheap supplies, from Asia in particular, make it hard for South African companies to compete in the export market in these product categories. Even within the Sub-Saharan region, South African companies are finding it difficult to compete in getting export orders since companies in Lesotho and Mauritius have greater capacities and productivity. On average, apparel manufacturers have less than 100 employees, making it hard for them to achieve economies of scale for commodity garments. South Africa recognizes that they will need to focus their marketing efforts on securing orders from medium-sized companies and orders for more specialties garments.

On the other hand, total employment remained almost constant. This apparently paradoxical development is consistent with a process of informalization in the industry’s traditional urban centers. Employment registered in enterprises declined by over 20 percent in the six years prior to 1995 but in the following six years further declined by over 40 percent. There are around 200 enterprises, a majority of which was former Association members-went “underground” in order to reduce their variable costs. Similar processes took place, on a reduced scale, in Western cape and in Guateng.

### **3.3 Textile and clothing industry in China: a general overview**

China’s resurgence as a major textile and clothing exporter has changed the landscape of world textile and clothing trade. In 1950, China was a significant textile exporter, but inward-looking policies under central planning led to gradual erosion of China’s market share. China was unable to exploit its vast labor resource by specializing in labor-intensive exports. By 1970, China accounted for less than 14 percent of total textile exports originating in developing economies and less than 5 percent of total clothing exports from

developing economies (Chinese Customs statistics). However, in the last two decades or so, the most remarkable relocation seems to have occurred among developing economies, especially in Asia. The market share lost by the newly Industrializing Economy has been entirely captured by China, ASEAN and South Asia. This occurred in a period of about two decades, but most of the shift occurred from the mid-1980s when China's exports began to surge dramatically. This surge should attribute the economic reforms beginning in the late 1970s, which provided a strong impetus to the sustained growth of textile and clothing exports. As China's exports surged, the dominance of the newly Industrializing Economy in the world textile and clothing markets began to decline. While the growth of the newly Industrializing Economy share in the world textile market was continued to increase, their share in the world clothing market has dropped sharply. The newly Industrializing Economy accounted for more than 70 percent of clothing exports originating in developing economies up to the 1970s. By 1996, however, this market share had fallen to 18 percent. The dramatic decline in the importance of the newly Industrializing Economy in the world clothing market reflects the fact that clothing is more labor-intensive than textile. As real wages increase and labor skills upgrade, the newly industrializing Economy has therefore lost much of their comparative advantage in clothing while maintaining it in textiles. Accelerating the process of structural adjustment in the newly Industrializing Economy is the opening up of the Chinese economy, which has become attractive to export-oriented foreign direct investment from the newly Industrializing Economy. A large part of newly Industrializing Economy's clothing production has moved to China. In addition, a large proportion of China's textiles and clothing exports continue to be re-exported via Hong Kong. This has facilitated China's access to overseas markets.

By 1988, China's share in the world textile market had peaked, having increased to 22 percent of total textile exports originating in developing countries, or 7 percent of world textile exports. As for clothing exports, China's market share has continued to increase.

### 3.3.1 Changing structure of production and exports

Textiles and clothing have been the spearhead of China's industrialization. According to official statistics, the share of clothing in industrial output has increased in recent years. Until recently, China's textile and clothing industries had been dominated by the state sector. With the freeing up of the rural economy, township and village enterprises began to play an increasingly important role in the textile and clothing industries. In the ten years from 1990-2000, their share in national textile output and 98 percent of clothing output. As township and village enterprises grew more rapidly than other sectors on average, they contributed the bulk of incremental output. There are several reasons why township and village enterprises have grown more rapidly than state-owned enterprises.

- Wage costs in rural China are generally considerably lower than in urban China where most state-owned enterprises (SOEs) are located. Given the labor-intensive nature of textiles and clothing, this gives township and village enterprises a considerable cost advantage. These enterprises are more flexible in their wage policies. In the past they have attracted a large number of skilled workers whom have taken up employment with township and village enterprises.
- Township and village enterprises are more accountable for their own management. In contrast, their state counterparts often face a "soft budget" and tend to lack incentives to improve efficiency.
- Township and village enterprises are more responsive to market condition. They are more adaptive and innovative in meeting market demand.

Because of these qualities, these enterprises have become dominant in China's labor-intensive manufactured export. For example, 90 percent of China's clothing exports in 1992 were produced by township and village enterprises. The share of these enterprises in textile and clothing exports is likely to have increased in the past four years, but comparable statistics are not available. Overall, township and village enterprises produced more than

one-third of China's total exports in 1992. By 1997, this share had increased to 36.4 per cent (Editorial Board of ACTE 1998).

Due to the strong resumption of international market demand and low base for last year's export, China's export of textile goods and garments rose sharply. According to the statistics of the customs, the export amount of such goods grew by around 49%. The characteristics of the textile and clothing industry's exports are as follows:

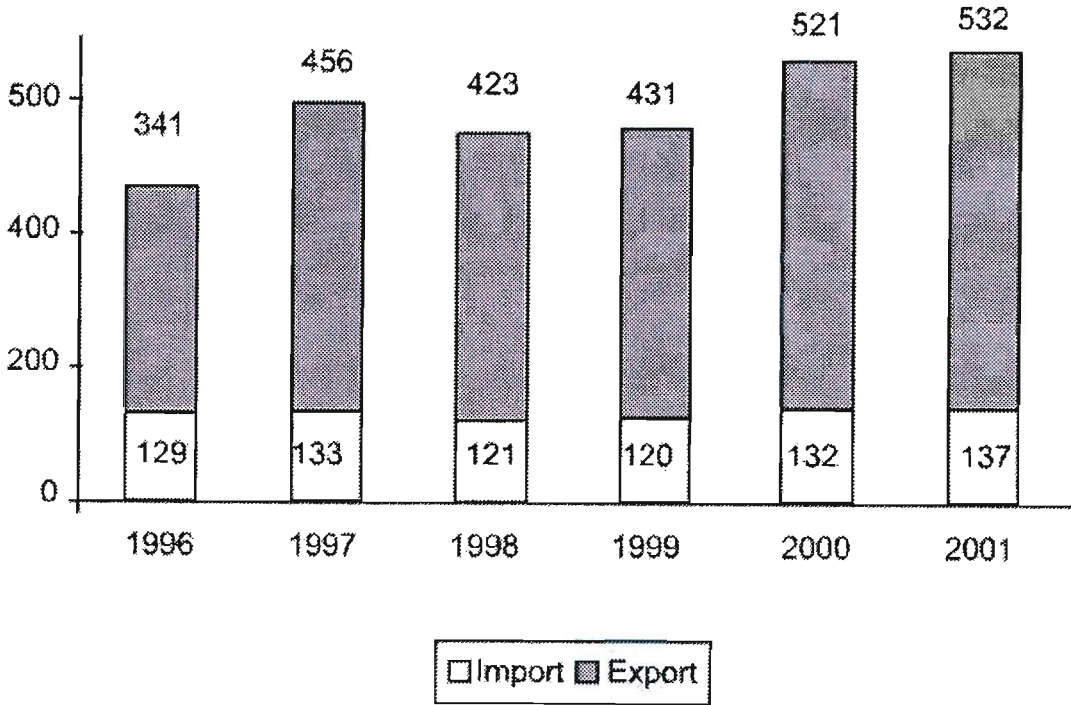
- China's textile and clothing production is heavily concentrated in the coastal regions. Exports are even more concentrated. The top 8 provinces together accounted for about 90 percent of total textile and clothing exports. The geographical concentration of textile and clothing exports is higher but follows a similar pattern.
- China's experience of export expansion by small enterprises is not unique. The small and medium-sized enterprises have all played an important role in China's export-oriented growth.
- The export price for cotton yarn and cotton cloth continues to decline while that for other products has seen somewhat pickup. The amount of man-made fiber yarn and cloth rose by 44% and 24.4% respectively.
- The exports of Chinese textile machinery is also undergoing rapid growth with an estimated increase of 20 percent thanks to the state's taxation policies and improved production. China's homemade textile machinery will be more popular this year, with sales climbing to 12 billion Yuan (US\$145 million) and exports hitting US\$200 million, according to "China Materials News."

### 3.3.2 Current Situation

China has become the world's largest manufacturer and exporter of textiles and garments in the world and Chinese textile industry remains the main force in foreign trade. The total import and export volume of textiles and garments reached an amount of US\$67 billion, which was an increase of 1.57 per cent compared to 2000. (Figure 3.3).

Among the total volume of import and export in 2001, the import volume suffered a decrease of 1.2 percent or US\$ 13.72 billion. On the other hand the export volume realized US\$ 53.28 billion in 2001, increasing by 2.31 per cent compared to the previous year. This indicates the importance of the WTO accession for the Chinese textile exporters, who are seeking new markets for their products. Japan has become China's top market for textiles. Exports grew last year by 38.9% to Japan. But, there are also other countries, that have enlarged their export/import relations with Chinese textile exporters, such as South Korea (50.36%), Southeast Asian countries (56.93%), the European Union (32.14%) and the U.S. (32.1%).

**Figure 3.3** Textiles Import and Export Of China  
(US\$ 100 million)



Source: cntextile.com

Chinese textile manufacturers have been going through a lot of changes in recent years to be competitive and attractive for its exporting countries. In 1997 the total output of the Chinese textile industry reached 714.9 billion Yuan. This sector then employed 10 million people in about 45,600 textile-manufacturing companies. It exported textile products worth US\$45.6 billion. In 2001 the number of enterprises decreased to 20,846, where 3,241



enterprises are state-owned and 17,605 are township and village enterprises. About 7.6 million people are now employed in this sector. A strategic restructuring of the last years as well as the East Asian crisis in the 1997 was related to the worldwide economic stagnation, which had a negative effect on the Chinese textile industry itself and their exports. The rising domestic raw material prices in the last few years also lead to a drop in demand on textile products both national and international. To overcome the negative effects of lesser export demand and overproduction caused by the worldwide stagnation, Chinese government and textile producers had to look for ways out, which meant restructuring. This led and is still leading overall to gradual transformation of a former centrally planned economy to a market related one.

Following China's WTO accession, China's textile industry is altering in a completely new manner. On 1<sup>st</sup> January 2002 phase 3 of the ATC (agreement on textile and clothing) will commence eliminating 51% of textile quotas. From 2005 China's textile market will be opened to all WTO members; China itself can distribute its products to other overseas markets. This will correspondingly affect the South Africa textile market as well.

### **3.4 South African Trade summary**

#### **3.4.1 Trade policy**

South Africa has progressively opened its market since 1994. As a matter of government policy, the South Africa government is aiming for still further market liberalization in order to increase trade and develop more competitive domestic industries. Tariff rates have generally declined and other non-tariffs have been reduced.

Although South Africa has reformed and simplified its tariff structure to comply with its WTO commitments, South Africa's tariff schedule remains complex and can create uncertainty for businesses that frequently import goods. The complexity of the system often makes it necessary to employ facilitators to assist with importing. South Africa's import tariffs have two categories-most-Favored-Nation (MFN) and General. The MFN rates are applied to most commodities imported from the WTO members. Other imports are subject to

the general rates. The dutiable value of goods imported into South Africa is calculated on the F.O. B. price in the country export. The rates on exports from the Chinese are: 0-40% on the clothing products, 0-20% on toys, 0-20% on electrical equipment, 0-30% on footwear and free for watches and clocks. (China Statistics) Apart from customs, tariffs, imports are subject to a 14% value-added tax (VAT). VAT is payable on nearly all imports. However, goods imported for use in manufacturing or resale by registered traders may be exempt from VAT. The valuation of imported goods for VAT is based on the F.O. B. value plus 14% of that value, plus any non-rebated customs duty.

The government's worry of reduction of import tariffs is the massive job losses once the cheaper imports flood into South Africa market. But not everybody in the clothing and textile industries is against the erosion of trade barriers. Actually, there are many manufacturers who want to be able to import product inputs cheaply. At a meeting in 1999, Sactwu, the clothing Federation of South Africa (Clofed) and the South Africa textile federation were "unable to obtain a mandate for calling on government to support a freeze in the tariff phase-down in terms of our WTO obligations" wrote former Clofed President, Bernard Richards, in the 1999 annual report. There is also some evidence that tariff barriers have not been directly responsible for all job losses. In a report published in March 2000, the International Monetary Fund (IMF) reported that employment had tended to fall less in sectors whose tariffs had been deducted the most. The IMF found that:

*The footwear sector employed 33 000 people in 1990 and was protected by an import tariff of 47%. Protection for the sector continued through the 1990s and in 1998 the tariff was reduced to 34%. Despite tariff protection, employment fell to 22 000 in 1998, or by 5% a year. On the other hand, the chemical products sector employed 64 000 people in 1990 and was protected by an import tariff of 29%. By 1998 the tariff had been reduced to 5% but employment had grown to some 68 000, or by 1% a year.*

Resource:IMF

This implies tariff protection may not be the effective way to reduce the unemployment rate. The textile and clothing industries in South Africa have



been under siege for few years, it has to be forced to rationalize and modernize. The South African government recently identified textiles and clothing as a priority sector. Trade policy in textiles and clothing has been an important element of the “government structure” shaping the territoriality of clothing value chains. The trade liberalization in these industries is predicated to lead to enlarge the current trade base and benefit the local manufacturers, which had more choice to outsourcing the materials and the distribution to distribute the goods.

### 3.4.2 Trade pattern and partner

South Africa's trade in manufacturing is the leader in trade performance, which separately accounted for 58.53% in exports and 84.32% in imports in 2002. (DTI). The statistics shows that US is the world's largest importer, as well as South Africa's second largest trading partner, for both merchandise and manufactured goods. South Africa's largest trading partner for both merchandise as well as manufactured goods is the UK, and the third most import market is Germany. (Table 3.2)

**Table 3.2 SA main trading partners by country**

Imports 2001		Exports 2001	
Germany	32,137,685,316	U.K.	21,412,470,114
U.S.A.	25,815,410,560	U.S.A	20,098,001,450
U.K.	18,289,997,448	Germany	169,965,821,409
Sadui Arabia	14,897,669,817	Japan	10,935,171,512
Japan	14,686,038,063	Netherlands	9,639,299,406
China	9,085,955,441	Belgium	6,891,865,444
Iran	8,841,594,279	Italy	6,648,625,711
France	8,125,281,911	Mozambique	5,718,733,124
Italy	9,047,161,224	Zimbabwe	5,383,076,470
Australia	6,038,290,692	Zambia	48,925,837,459

Resource:SARS

For textile and clothing industries, South Africa has a large potential to increase its exports dramatically although it is still a very small player in world markets accounting for less than 0.1% of world exports. Only around 10% of total outputs are exported to overseas market. (SA Statistics). Analysis of the trade data of textile and clothing industry shows that the developed countries dominate the top export destinations and imports most come from the developing country.

Approximately half cotton man-made and woven trousers, knitted shirts and woven suit export to USA, followed by EU. No doubt, these increases are partly contributed to companies taking advantage of concessions granted under AGOA and South Africa-EU Agreement. Oppositely, about a third of South African imports of textiles and clothing originate from developing countries. China dominates, followed by Malawi. India and Hong Kong also maintained their share of export in South Africa.

#### 3.4.3 Trade relationship between China and South Africa

Since the establishment of diplomatic relations between China and South Africa on January 1, 1998, bilateral economic and trade cooperation has been attached great importance by the two governments. To promote its development, the two governments signed a series of cooperative agreements in the field of economy and trade. In May 1996, South Africa and China concluded a MFN Agreement, which commits both countries to granting the other "MFN" treatment. Such agreements range from the agreement on investment protection, the agreement on joint committee for economy and trade to agreements on economy, trade and technology cooperation.

South Africa is China's largest African trading partner. 27% of the total trade between China and Africa is conducted between the two countries. In 1999 bilateral trade was around 1.722 billion dollars, which was a record high. Trading volume after two years of stability is up. Among it China exported 861 million dollars, which was a decrease of 0.7% and imported 861 million dollars that increased of 24.6%. China mainly exports to SA products like electrical machinery, shoes, clothes and accessories, textiles and light industrial

products, pottery and glass, plastic and rubber and travel kits and bags. What China import from SA are iron ore, diamond, crude oil, copper, primary plastic, aluminium, coal, paper pulp, paper.

**Table 3.3** Bilateral Trade from 1991 to 2002  
(in hundred million dollars)

year	Total	Import	Export
1991	0.15	0.02	0.13
1992	2.44	0.89	1.55
1993	6.58	2.46	4.12
1994	9	3.6	5.4
1995	13.2	6.3	6.9
1996	13.5	6.8	6.7
1997	15.7	7.8	7.9
1998	15.58	8.67	6.91
1999	17.22	8.61	8.61
2000	19.04	9.94	9.1
2001	18.12	9.09	9.023
2002	18.74	14	4.74

Resource:MNTEC

However, bilateral trade in recent years, especially export from China to South Africa, has just remained at the same level. It has rapid growth in 1990s and only took 6 years to reach 1.57 billion dollars in 1997 from the 14 million dollars in 1991. But since 1998, the bilateral trade has been lingering between 1.5 billion and 1.7 billion dollars. Direct reasons for it can be concluded from the side of South Africa where the economy was brought to a halt by Southeast Asian crisis and the weak performance of currency. Moreover, many exported goods are not quality controlled by Chinese SME. These exported-products not only lead to low-price sale but also ruin the Chinese products reputation in South African market. Considering the quality, it is

reasonable to say that South African entrepreneurs will hesitate to place the order from China even if the price is cheaper.

The South African government also put a deterrent on the road to liberalize the trade with China. South Africa is one of the countries that take anti-dumping measures against the products from China. The South Africa board on tariff and Trade has initiated anti-dumping or countervailing investigation and impose duties on a variety of Chinese-made products including woven fabrics (Table 3.4) South Africa has viewed China as non-market economy and used substitute country for the determination of the real value.

**Table 3.4** South Africa’ s Anti-Dumping Duties

Country/ Customs Territory	Product	Date of imposition
China	Woven fabrics of polyester staple fibers	28/02/92
	Towels and facecloths	28/02/92
	Hoes	12/11/92
	Spades, shovels, rakes forks	02/12/93
	Garden picks	11/10/96
	PTFE tape	18/10/96
	Aluminum hollowware	07/02/97
	Indigoblue	16/05/97
	Underwear	08/05/98
	Float glass	28/05/99
	Flat glass	28/05/99
	Blankets	18/06/99
	Acetaninophenol	18/06/100
	Bolts and nuts of iron or steel	06/08/100
	Garlic	20/10/00
	Stainless steel hollowware	15/12/2000
	Door locks	25/01/2002
	Blanketing in roll form	08/02/97

Source: Hong Kong Trade Development Bureau

As a result, the commons and differences between these two countries can be concluded as follows:

Commons:

- Both countries are developing countries, which applying export-oriented trade policy to spur the entire economy.
- Textile and clothing industries are belong to traditional industries for both countries; their performance could possible have a considerable impact on the country's economic development.
- Both countries have abundant labor resource to meet the labor-intensive clothing industry as well as supply a large consumer base.
- Both countries are member of World Trade Organization (WTO), all the relatively tariff regarding the textile and clothing industries and bilateral trade deals should apply to these two countries.

Differences:

- China produces sufficient raw material like cotton and man-made fibre. China is one of the largest cotton producing and consuming countries. It accounts for more than 20 percent of world production. China's WTO accession also will have a significant impact on the world cotton market; South Africa produces cotton but not sufficient, therefore they should either import from SADC or overseas.
- There are numerous township and village enterprises (TVE), which produce wide-range clothes accessory to supply the clothing manufacturer. Most of them are small but are more adaptive and responsive to meet the variable market demand with lower cost. Comparing, South Africa's accessory suppliers offer limited products with higher price. This industry, unlike textile and clothing, is rather variable and not easy to be captured in the short-term.
- Productivity and labor-cost comparisons demonstrate that South Africa's manufacturers would have to produce 34 garments per operator day to be competitive with China. (Peter and Musa,2001:8)

Considering the current 15 pieces per operator day, it is mission impossible!

- In order to survive in today's intensive market competition, the textile and clothing enterprises should have a qualified workforce to support and develop. The well-trained workers account for 50-70% of the total employees in China's small and media enterprises. However, there are plenty low-skilled labor caused by the economy transformation from a mining-based to a manufacturing-based economy in the mid-1990 in South Africa. Training is the only way to solve this problem.

### **3.5 Conclusion**

In this session, the textile and clothing industries both had been overviewed in South Africa and China as well as the current trade relation. Nevertheless the bilateral economic and trade cooperation has been established and further developed between these two countries, the trade constraints in textile and clothing industries were still high. The massive job losses due to cheaper imports and made-in-China products of poor quality could be the two main constraints to hamper South African government to further liberalize trade with China.

From the above analysis, it is reasonable to say both commons and differences exist between these two countries in textile and clothing industries. Those differences can be regarded as the industry's disadvantage. By overcoming those disadvantages, It could help the industry to gain the competitiveness in the entire supply chain.



## CHAPTER FOUR-THE WAY FORWARD

### 4.1 Introduction

For any industry, to explore the potential and plan the future, it is necessary to understand the current problem and strengths. Gap analysis is one approach to assessing the need for change. It is conducted by answering three simple questions. The solution concluded should be the way to close the **gap** (How do we get there?) between the objective (where do we want to get to?) and current situation (where are we now?)

In this chapter, the analysis of the current situation was based on the collected primary and secondary data. To collect the primary data, a survey which using questionnaires had been posted to the top management in 25 major textile and Clothing companies mainly located in KwaZulu-Natal. The questionnaire was constructed to reveal the practices and problems associated with

- Purchase and reception of inputs
- Human resources
- Current and expect trade relation with China

In order to obtain a comprehensive data regarding the impact of the macroeconomic, political, fiscal policy on textile and clothing industry, the relative internet web sites, trade report, and trade publications have also been used for collecting secondary data. This report also benefited from an extensive review of the literature and diverse statistical sources.

### 4.2 Where we want to get to?

A key strategy of the South African government to urge economic development and lower the unemployment rate is to target some industries, which roots on broad and intensive consumer-base in local market, as well as capable to share certain world market. The clothing and textile industries were



identified as among the best to target, because of the critical stage they are in and threats from cheap and illegal imports, but more because they fit the kinds of industries that can bring significant benefits in the short-run for the country's economic development. To achieve this, South Africa's textile and clothing industries should implement the following objective through government support:

- To promote the growth and development of textile and clothing manufacturers to produce high quality goods that are domestically and internationally competitive.
- To select competitiveness strategy and implement necessary changes in business and manufacturing processes and equipment.
- To create sustainable growth and profitability through creativity, flexibility, responsiveness and innovation.
- To become the core industry in the South African economic structure.
- To become major textile and clothing exporter in the world market with reliable quality and well-know brands

### **4.3 Where we are now?**

All factors from internal and external to any industry affect their competitiveness. Overcoming these constraints is important not only for individual firms and country's national industry, but also for the country to develop competitive garment-delivery pipelines. This part provides an understanding of the importance of each constraint in textile and garment industry with Porter's diamond theory, highlighting those constraints that may require to be overcome.

#### **4.3.1. Porter's diamond as a tool**

- Factor condition

### Infrastructure

A positive aspect of South Africa's capital stock is its impressive infrastructure, particularly if we compare it with the standards of other developing countries." (Mohr:1998;141) In general, South Africa has a distinct advantage in the region with its advanced physical infrastructure in terms of electrical supply, wide-reaching roads, port facilities, transportation services, logistics and banking industry. The only area, which faces difficulties at times, is water supply. Water supplies are especially critical in fabric production, yarn dyeing, and garment washing which are essential processes for the garment delivery chain. This problem needs to be addressed as a matter of urgency. In addition, the international transport costs in South Africa is an obstacle to trade. Indeed, the international transport costs to and from South Africa are almost 50% higher than the average for developing countries. (Naude 1999:22-23)

Insufficient capital in South Africa also is an important problem. According to the report from the firms, most firms had problems with short-term capital and in others long-term capital or both. The most critical problems were for local firms who could either not obtain financing overseas, or could not obtain finance locally at reasonable rates. In addition, locally owned firms would have trouble obtaining pre-shipment financing. In some, the pre-shipment financing was only for imported raw materials and not for the local value-added input. With a slowdown in the South African economy and a reduction in orders for the textile and apparel industries from domestic customers, the banking sector has witnessed deterioration in margins, declining revenues, bank loan defaults and bankruptcies. As a result, the banking industry has sharply reduced its exposure in the textile and apparel industries, making it more difficult for the middle market to obtain bank financing.

### Raw material

Raw material is the largest component of the manufacturing cost of textile and clothing. The raw material for yarn is either fibre in the form of staple or man-made chemicals that are extruded to form filament yarns. The staple fibre can

be either natural fibre, such as cotton wool or silk, or man-made fibre such as rayon, polyester, and acrylics. Most fibres and yarns are commodities; and the prices paid vary little from supplier to supplier but are subject to variations over time due to shifts in demand and supply. Some specially yarns and fibres have limited markets, often command premium prices, and are frequently made-to-order. For most natural fibers, prices are set daily in public commodity markets for current or future delivery.

Cotton is the fibre most used for textile production in the world. Acrylics, polyester and PP/HDPE are the most frequently used man-made fibres. Until 1970 cotton was still a relatively minor crop in South Africa, but since 1974, the area under cotton production increase more than threefold. Notwithstanding this, production rarely meets demand and on average South Africa only supplies about 50% – 60% of its annual needs from local production. Cotton produced in the Republic of South Africa (70% under dry land & 30% under irrigation), on average, compares very favorably with that produced in the rest of the world - although on a much smaller scale. Man-made fibre production in the region, however, does not satisfy the demand and some import man-made specialty fibers, such as rayon, are not even produced in South Africa. Not only this fabric-related constraint referred to the absence of local production of materials such as cotton, lycra or certain other more “technical” fabrics, also to the absence of relevant weights and/or global standard constructions to meet the special requirement from overseas market.

Furthermore, the cotton users are required to buy all the local cotton supply before import permits are granted (Jafta and Jeetah 2001:36). As a result, spinners do not always use the proper grade cotton. This may cause them to use good cotton where an inferior grade would do, resulting in higher costs. It may also cause problems in blending and dyeing, resulting in quality problems. The market is further restricted in that import orders must arrive in 12 equal monthly shipments (Jafta and Jeetah 2001:37), which imposes storage and financing costs on the spinners.

Man-made fiber production requires large capital investment; thus, only a few suppliers exist worldwide. South Africa is the major supplier in SADC region.

But the suppliers in China benefit from much larger economies of scale than those in South Africa, except in nylon filament yarn, and, as a result charge generally lower prices. Despite the additional transportation costs, man-made fiber products from China can be cheaper. For example, the C.I.F. price for dyed acrylic yarn used in Botswana was reportedly \$4.86/KG for South African yarn and \$4.16/KG for Chinese yarn (Rubin 2001a:16) South African manufacturers produce polyester staple and filament, acrylic staple, nylon filament yarn, and polypropylene filament yarns. The range is limited. The supplies are insufficient for even domestic South African consumption (Jafta and Jeetah 2001:39)

Except for the raw material mentioned above, clothes accessory is also a major component of clothing industry. As the modern fashion clothing style needs those accessories to decorate and distinguish, clothing accessory has become part of "raw material" for the clothing industry. The range of accessories is very wide and it can be divided into two items: basic accessory such as zip, elastic, drawcord, toggle, satin and so on; fancy accessory such as crochet lace, suede panel, embroidery sticker, Chinese tie, leather tie and so on. There are only around 30 companies, which major in producing those basic accessories in South Africa. According to the survey data, most clothing manufacturer import the fancy accessory from overseas countries like Taiwan or China. Some manufacturers source these accessories by the local agency. Some large manufacturers even set up their agency in China or Taiwan for outsourcing the necessary accessory. The reason for those clothing manufacturers sourcing from overseas is not only because the overseas price much cheaper than local supplier, also because only few accessory options offered by suppliers. Conversely, In China there are a larger number of SME's that producing all kind of basic and fashion accessories for the clothing industry with 3-4 times cheaper prices than South Africa's suppliers. However, most manufacturers complain about delays caused by custom inspection and excessive tariff rate, which increase the inputs cost.

Textile and clothing equipment are also necessary parts for these industries. Except Taiwanese companies, most South African manufacturers import their equipment from overseas, mainly from Germany. However, manufacturers

suddenly found it far more expensive to buy and maintain their machinery. "The cost of every spare part has gone up", says Laments Frank Greenblatt, the managing director of Svenmill, one of the largest textile producers, "our repair bill is 40 percent higher than anticipated".

### Labor/Skills and technology

The most important resource for any industry is people. South Africa has a fairly large population, which means it has a great number of potential workers. However the main problem is a lack of skilled labor in the workforce. In fact, the largest part of the population falls into the unskilled category, which is also the faster growing category. The transformation from a mining-based to a manufacturing-based economy in the mid-1990's meant that low-skilled labors were not skilled enough to participate in the new manufacturing-based economy. This problem was further exacerbated by government legislation. Apartheid didn't provide basic education for all; much less development of skills and training for the largest section of the workforce and today's government is still trying to redress the balance by raising the level of education, training and human development. The factors mentioned above, excluding wages, costs South African textile companies 4% of the wage cost and another 1% of employment cost, in total constituting another 1% of turnover. Furthermore, the nature of South Africa's laws, although conceptually desirable, is unfortunately incorrectly balanced in favor of the trade unions. It therefore necessitates considerable additional expenses in the pursuance of counter-balancing and administering the cause and effects of these agreements. The payment of a multitude of levies to trade federations, employers' bodies, and training boards and export councils adds cost in addition to other employment expenses, such as pension funds and medical aids. Table 4.1 Shows these levies make an unfavorable comparison if measured against other SADC countries.

Labor relations tended to surface in almost every manufacturer surveyed as a constraint than any other issue. The aspects of labor relations most commonly mentioned by respondents were the perceived inflexibility system and labor



costs. Inflexibilities system encompassed everything from the nature of the procedures it was necessary to observe in order to, for example, obtain a dispensation for overtime or for the hire of contract workers, through the time-demanding nature of the laid-down arbitration process to the overall institutional architecture governing the sector's dualistic labor market. In addition, other social benefits affect labor costs, e.g., sick-leave allowances, maternity benefits, and vacation entitlements. The current study did not collect comprehensive data on these social charges in South Africa. A systematic study would be beneficial and help policy makers who may want to review national policies in light of their effect on labor-cost competitiveness.

**Table 4.1** Labor costs comparison

	<b>Labor cost</b> (New hire) (\$/month)	<b>Labor cost</b> (5 years experience) (\$/month)
Malawi	19.5	32
Lesotho	69	105
Mauritius	66.15	149.75
Swaziland	93.46	117.26
Botswana	100	178
South Africa	213	283

Source: ABSA

No doubt, new technology also acts as the most essential role for textile and clothing industries as any other industries. Technological change, especially, has been far more dramatic in the textile industry. These changes concern both the replacement of manual with mechanized and automated operations, as well as the increase of speed with which a particular process is carried out. In 1975, a typical loom for fabric production could produce 8.3 square yards of fabrics per loom hour, by 1997 loom productivity has gone up to 34.7 square yards per loom hour. High capital investment is required for such equipment. In clothing production, the technological improvement such as laying out and cutting material also undoubtedly has brought significant productivity gains.

Therefore, it is reasonable to say that South Africa has to keep up with international technological developments and training in many industries including textile and clothing industries. However, one of the consequences of

modern, highly developed technology is that it requires a sophisticated, well-trained labor force to install, operate and maintain the specialized equipments, which were scarce resources in South Africa.

Productivity and innovation

After raw materials, labor is the next largest component of a textile or clothing product’s cost. The actual time spent, the labor cost per hour, the number of defects requiring rework, and the number of products that are rejected after final assembly or processing effectively determine the labor cost per garment. No matter whether for the export markets or local markets, labor cost per unit is one of the critical factors for cost competitiveness in garment manufacturing. Productivity and labor cost comparisons demonstrate that manufacturers in South Africa are not competitive with those in the Far East and South Asia (Table 4.2) South Africa would have to produce at the nearly impossible rate of 34 garments per operator day!

**Table 4.2** Productivity and labor cost comparison for men’s casual shirt

	Pieces per Operator Day	Productivity Rank (1=highest)	Monthly Salary (\$)	Monthly salary Rank (1=lowet)
Malawi	10.5	8	26	1
Lesotho	18	4	87	7
Swazilad	15	6	105.4	8
China	20	1	150	11
South Africa	15	6	248	13
Thailand	19.8	2	n.a.	n.a.
Taiwan	18.2	3	n.a.	n.a.

Sources: SADC country reports  
 Note: Monthly salary figures for Thailand and Taiwan are unavailable. Productivity data are shown for comparison only.

Although SA garment manufacturers have a big advantage, in that they have no quota for the EU and the United States markets. This combined with the duty-free privileges available under Lome/Cotonou and AGOA gives SA suppliers a potential cost advantage of 30% over South Asia and 45% over



China (Biggs et al. 1996:67). This advantage, however, will not last forever. The agreement on textiles and clothing (ATC) under which countries and regional trading groups impose quotas on textile and clothing imports will expire in January 2005, the South Africa-EU agreement will expire in 2008. These imply that SA will no longer be competitive with China if the low productivity still were maintained.

Garment manufacturing is labor intensive. Improving labor productivity, therefore, improves the industry's competitiveness. Paying operators by the piece is a recognized method of increasing labor productivity in garment manufacturing. It is common in high productivity garment-manufacturing countries such as the United States and China. It reduces the need for supervision and gives the workers immediate and meaningful feedback on whether or not they are meeting production targets. In South Africa, only one manufacturer reported using piece-rates at all. The rest cited labor regulations and union prohibitions against piece-rates as reasons for not paying piece-rates.

Two misunderstandings concerning the use of piece-rates result in it having a bad reputation. The first is that the use of piece-rate-pay systems forces the workers to work harder. In fact, it encourages worker to work not really harder, but smarter, as the workers will earn more if they produce more. The second misunderstanding is that piece-rates are a way to pay workers less than the minimum wage. In fact, in most countries where piece-rates are widely used, workers on piece-rate must be paid the minimum wage. To be fully effective, however, labor laws must allow workers to be easily dismissed if they do not produce enough to earn the minimum wage after a specified period such as three months. Piece-rate pay gives individual operators the incentive to meet the target times, as well as to receive immediate feedback on whether or not they are meeting the targets. The combination of proper training with piece-rate pay for operators is essential for obtaining the best possible labor productivity in garment operations. However, most traditional textile and clothing firms typically use low-skill, low-wage labor without training, which are not able to achieve the high productivity.

- Local rivalry

The history of the textiles industry in South Africa is not very long. In the early 1940s, the production of blankets, rugs and sheeting was the principal activity for textiles, which accounted for 90% of demand. In the ensuing years after the initial expansion of the industry, it has grown considerably in size, range and sophistication of its products. The South African market demand increasingly reflects the sophistication of first-world markets. The textile and clothing industries cover the whole range from manufacturing of fabrics such as cotton and nylon to manufacturing of finished clothing and the sale of clothing.

The total value of textile production was almost R10 billion. Textile manufacturers have benefited from high levels of tariff protection, which allowed them to sell textiles, which were more expensive than world market prices to local clothing manufacturers. Frame is South Africa's largest vertical integrated textile manufacturer, consisting of 13 divisions, covering a large spectrum of textile manufacture, from short staple to worsted spinning systems, processing cotton and cotton blends, as well as fine wools and blends thereof, into world class yarns. However, it still has to respond to use better equipment to boost productivity and reduce costs due to the import competition.

The total value of clothing production was almost R10.2 billion. South African clothing manufacturers are pleased that the textile manufacturers are losing government protection because this reduces the cost of manufacturing clothing. Local firms have to compete with a flood of imports mostly from low cost Far Eastern producers. Only a small number of local manufacturers such as Seardel, Rex Trueform and Shakur Olla dominate the current clothing manufacturing market. Seardel is the largest clothing manufacturer in South Africa and supplies men's, women's and children's apparel foundation garments and household textiles to larger chain stores. Many of the smaller firms in the western cape have been forced out of the market by cheaper imports.

The total value of retail sales was approximately R25.7 Billion. In fact, the clothing retail sector in South Africa is extremely concentrated. The following table (Table 4.3) outlines the structure of the industry. The local retailers needs to ensure that their product range offers consumers perceived value for money including cheap copies of high fashion designs. They also need the manufacturers to respond quickly to changes in demand however lead times of over six months are not unusual. Many retailers such as pep and Edgars also own factories in order to control their source of supply. The clothing sales not only have been affect by the competition between chain stores and from other retail store, also affected by the growth in the use of mobile phone and buy the national lotto.

**Table 4.3:** Leading South African clothing retail chains

Group	Chain	No. of stores
Eedcon	Edgars	198
	Sales house	100
	Jet	107
	Smiley's Warehouse	49
Pepcor	Pep Limited	1201
	Ackermans	211
	Stuttafords	11
Wooltru	Woolworths	120
	Truworhs	200
	Topics	170
Specialty	Mr Price	260
	Hub	10
	Milady's	163
Foschini	Foschini	330
	Markhams	180
	Exact	85

Resource:DTI

- Related industries and suppliers

The relationship between clothing producers and textile mills is after beset with accusation from the clothing manufacturers that the textile mills are inefficient. It takes long lead times (both for fabric development and for production of already developed fabric) and often the cause for their delays in

production and poor quality. Clothing producers, under time pressure from retailers, argue that their failure to operate Just-In-Time (JIT) strategies is in large part due to inefficiencies and delays upstream in the supply chain. The conflict between textile manufacturer and clothing manufacturers absolutely exists:

“The choice of fabric is minimal. There is no innovation in the fabric area here. They don’t even copy. They are very insular. They don’t benchmark themselves. It’s an attitude of “you lucky people, you will get the fabric on time”.

Resource: Peter and Musa, 2001:8

In response, one textile mill admits that his industry has a reputation for later deliveries, but argues the clothing manufacturers are naive about the process of fabric production, which is far more complex than that of clothing. To complicate matters further, stringent demands of the retail industry are leading to a more direct pipeline relationship between the textile mill and the retailer. Textile mills often must gain approval from the retailer before the fabric can be passed on to the clothing manufacturer for example. Or the retailer especially points out the fabric must be produced from a certain textile mill when they placed the purchase order with the clothing manufacture.

Probably one of the most salient features of textile-clothing industries around the world, and indeed the South African industry is no exception, is the dominance of the retail sector in the pipeline. Almost all of the retailers sourced nationally. That is to say, rather than simply in the vicinity of that manufacturer, each manufacturer that retailers procure throughout the whole country, South African domestic suppliers are located in three centers: KwaZulu-Natal, Western Cape and Gauteng. On average retailers stated that 52% of suppliers were in KZN, 35% in the Western Cape, and the remainder in Gauteng. Most leading retailers tend to be quite concentrated. Although most retailers have a fairly high number of suppliers, a high percentage of sales are sourced from a few leading suppliers. On average 18% of sales were sourced from the top supplier, and 35% from the top three suppliers (DTI Clothing Sector Report). The retailer builds a relationship with a particular supplier, who is ultimately responsible for delivering the agreed upon

garments. Retailers are fully aware, that not all suppliers manufacture in – house. It is quite clear that the smaller supply bases and closer relationships with suppliers is affecting the nature of communication and making it easier to offer feedback to suppliers. But the biggest gap between retailer expectations and manufacturing performance is in the area of delivery reliability where retailers are far from happy with their suppliers.

The relationship between suppliers and retailers is still very uneven, however, as retailers often dictate all commercial term and the manufacturer are often under mark-up and margin pressure. An indication of this powerful imbalance is manifest in the net return in clothing manufacture as compared to retailing. Comparing with 4 percent returns to clothing firms, retailer returns are estimated at 150 to 210 percent. The explanation for this is quite simple: retailers control the consumer market. The five largest retailers in this country account for around 70 percent of total clothing sales. Given this high concentration, the clothing manufacturers are inevitably dependent on the business of a few, very large, retail chains. This gives the retailer power to set prices and make stringent demands on quality and delivery date. Some clothing manufacturers have opted out of the control from retailers, and entered the retail end of the market themselves. This is a risky option for most manufacturers. If they fail in retailing, closure is their likely fate, as other retailers would be unlikely to re-approach the firm. Some clothing firms argue that the retailing industry is destroying its own domestic supply base. However, much of the downward price pressure really emanates from increasing competition from East Asian producers such as China and Thailand. It is necessary to recognize that the future of global sourcing will probably become to buying agents for retailers active in all clothing producing centers of the world, to source the cheapest and highest quality garments for local consumption. The challenge for local manufacturers is to produce seasonal, high value-added garments that can compete with the East Asians on price and quality.



- Local demand

The market is extremely tough at this moment, and has been shrinking. Most of the respondents felt that general market conditions in the clothing retail sector were poor at the moment. At the same time, 50% felt that their chain was losing market share. Within these tight market conditions, price is becoming increasingly important as the basis for competition. This is very much in line with findings in 1996, which showed that KwaZulu–Natal clothing manufactures were increasingly being forced to sacrifice profit for turnover in order to remain competitive (Harrison and Dunne 1998). At the same time, customers from across the income spectrum are demanding greater “value for money”, that is lower prices without a sacrifice of quality. At the upper end of the market particularly, design, fabric types and quality are all becoming increasingly important, alongside direct cost concerns. This trend was already apparent in 1996, and seems set to become one of the driving pressures in the clothing sector (Harrison and Dunne 1998).

All these market phenomena are attributed partly to general economic condition and partly to growing levels of competition from imports. By far the most serious, in the opinion of the manufacturers surveyed, the most important constricts on local demand was with importers who avoided tariffs. This problem affects both the garment and textile industries because reducing demand for locally made garments often reduces the demand for locally made fabric. Competition from imports is a problem for three reasons.

#### Lack of effective customs protection

Customs is simply unable to enforce the regulations and impose duties on imported garments. Although this is a serious problem and needs to be addressed, more diligent customs enforcement on imports could create problems for manufacturers using imported raw materials and accessories. While demanding better enforcement against competing goods, they expect more liberal treatment for their imports. In our survey, the South African customs procedures have been considered as “lengthy or cumbersome customs procedures”.



### Failure of local firms to supply the demands of the market

Consumer preference is changing. South Africa's consumer no longer demand standardized products, but rather products that will distinguish their wearer an identity from the masses. Moreover, increasingly sophisticated consumers are demanding increased variety of product choice. This is leading to shorter product seasons, more rapid product cycle turnover and smaller lot sizes. However, most clothing companies may not be able to respond to these rapidly change and supplying enough products for local customers. Responding to local shortages, importers bring in what customers want, while, in many counties, local manufacturers have apparently not discovered the market in which they have a competitive advantage over importers. Since tariffs on clothing and textiles products are going to continue to decrease, local producers must find ways to compete locally if they wish to stay in that market. The primary advantage they have in the local market is access to timely information about what local consumers want. Rather than make excuses about why they cannot compete, manufacturers should find ways to develop proximity to this changing market as a competitive advantage.

### Low consumer buying power

Low consumer buying power results from the general state of the economy and can only be solve by raising the national income and ensuring it is equitably distributed. In addition, national lotto and cellphone have become the two major spending for most South Africans, which apparently eliminates the buying power on clothing spending.

- The government

Fully developed textile countries in Europe and the Americas are still being protected by quota systems and moderate duties. Asian countries protect themselves with high duties and secondary taxes, while their governments give generous subsidies for input materials and value-added processes. Conversely, South Africa's textile industry gets no help other than good wishes from its government. There are no South African government financial

assistance programs to help exporters' products become more competitive against foreign competition. Some assistance is available through support at trade shows. The South African government is reluctant to initiate any programs, which might be construed as anti-competitive under the GATT due to anti-dumping claims made by the U.S. government against South African steel producers.

The government in the 1950s to support infrastructure development projects through medium and long-term development project financing established the Industrial Development Corporation (IDC). The IDC has specialists in the textile and clothing sector who have few textile-related projects presently underway. The Export-Import Bank of South Africa, formed in 2000 to support more short-term financing of capital goods, also has textile and apparel specialists, but to date, has no active programs. The Credit Guarantee Insurance Corporation operates as a private-sector export trade credit insurer, supported by the government. This body insures debtors outside South Africa on behalf of South African exporters (similar to the GSM credit program in the U.S.). As their activity has focused mainly on the European and Australian / New Zealand markets, they are not equipped to manage exposure in the rest market. Under the terms of this program, the product must have 70% South African content.

While it is understandable that South Africa does not have the financial resources to pay subsidies, it has, if willing, the same opportunities as other countries to use non-monetary policies to help our industry to fully mature. There is a misguided perception amongst the Department of Trade and Industry that the South African textile industry has achieved a level of development, where we are ready to export and be capable of surviving the most severe onslaught any textile producing country has ever had to endure. In addition, government regulation often raises the cost of production and limits output. Trade unions in South Africa have a great deal of power. The labor law is designed to protect the employee, making it is difficult to fire workers who perform badly. This can also lead to increased inefficiency among employees.

- Chance

Perhaps the greatest opportunity for South African textile and clothing manufacturers currently is taking advantage of AGOA. It provides an opportunity for South African exporters to open the USA market. In addition, the South Africa-EU trade and development Agreement also offer the opportunity for exporters.

#### Africa Growth and Opportunity Act

The Africa Growth and Opportunity Act (AGOA) is a non-reciprocal unilaterally determined trade regime offered by the USA to Sub Saharan countries. AGOA, which is part of the Trade and Development Act 2000, opens the U.S. market for exports with preferential access for a period of eight years ending 2008. AGOA being a unilateral declaration of preferences, and the US president having the right to determine import sensitivity of products, its renewal beyond 2008 remains subjected to circumstances that will prevail at that time.

To benefit from the quota-free and duty-free preferential access to the U.S market, sub-Saharan African countries must fulfill two conditions under AGOA. The first is political, mandating that countries must meet political, human and work rights criteria. Occasionally, countries cannot engage in activities that undermine U.S. national security or foreign policy interests. Certain governments unofficially express serious concerns about economic interests, or be used for arm-twisting in future WTO negotiations. The second is legal and bureaucratic, requiring countries to put in place a customs visa system officially approved by the U.A customs authorities to address trans-shipment risks and to guarantee compliance with the rules of origin and ensuring documentation.

AGOA's rules of origin are far more stringent than those of EU-ACP agreements. AGOA provides that, with certain very specific exceptions, to benefit from the quota-free and duty-free access, apparel assembled in sub-Saharan Africa must be from fabric wholly formed in sub-Saharan Africa must be from fabric wholly formed in sub-Saharan Africa from U.S or sub-Saharan

African yarn. Indeed, AGOA promotes increased trade and economic co-operation between the United States and eligible sub-Saharan African countries. This legislation represents a solid, meaningful and significant opportunity, which could result in billions of dollars in new trade and investment flows between the US and Africa. Moreover, it provides an opportunity to promote investment particularly for oversea industrialists to invest in the region for the production of textile fibers, fabrics and clothing, using quota free and duty free access to the American market from Africa as the strongest incentive.

*Textile and Apparel Benefits:*

- Lifts all existing quotas on textiles and apparel products from sub-Saharan Africa.
- Extends duty/quota free US market access for sub-Saharan African apparel made from yarns and fabrics not available in the US.
- Extends duty/quota free treatment for apparel made in sub-Saharan Africa from US yarn and fabric.
- Extend duty/quota free treatment for knit-to shape sweaters made in sub-Saharan Africa from cashmere and some merino wools as well as apparel produced in sub-Saharan Africa from silk, velvet, linen and other fabrics not produced in commercial quantities in the US States.
- Extends duty-free and quota free US market access for apparel made in sub-Saharan Africa with African/regional fabric and yarn. Such imports however, are subject to cap (limit) ranging from 1.5% to 3.5% of the multi-billion dollar US apparel import market over an 8-year period. Sub-Saharan African apparel imports made with African fabric/yarns currently total about \$250 million. Under the cap, these imports could increase to \$4.2 billion over a period of 8 years. Normal MFN duties would be levied on apparel (regional fabric) imports over the cap.
- Promote investment in sub-Saharan Africa's poorest countries through a special provision in the cap which allow sub-Saharan African countries with an annual GNP of \$1,500 and below to use third country fabric inputs for 4 years. This special investment incentive for the poorest sub-

Saharan African countries is aimed at providing a market stimulus to economic development for areas with little existing industry.

- Provides an average 17.5% duty advantage on apparel imports in the US market. This would provide sub-Saharan African countries with a competitive advantage over many other major suppliers.

#### EU-South Africa Free Trade Agreement

The EU-South Africa Trade, Development and Cooperation Agreement are a comprehensive aid and cooperation agreement governed by WTO rules on Free Trade Agreements (FTA). The agreement requires the removal of customs duties on “substantially” all trade over a maximum period of 12 years. The agreement provides for the EU to remove duties on imports from South Africa on approximately 95% of its tariff lines over a period of 10 years from implementation (1 January 2000). In return, South Africa will be required to remove the duties on around 86% of its imports from the EU over a period of up to 12 years in a few cases. However, South Africa’s tariff cuts will mainly occur in the second half of the 12-year transition period, i.e., between 2006 and 2012. This will give the South African government more maneuvering space to protect and nurture sectors like textiles and clothing.

#### 4.3.2. SWOT analysis

Since the textile and clothing industry is complicated and multi-faceted, it is difficult to generalize about it as a whole. A comparative advantage in one production factor, such as labor cost, does not necessarily result in an important comparative advantage in all production stages. Each production stage, however, is important since a manufacturer can only compete successfully as part of a competitive pipeline. The perspective adopted in this part is to evaluate the role of the pipeline in these industries, which is based on the whole country. This part revealed major strengths and weakness of the South Africa’s textile and clothing supply chain. Analysis of these shows South Africa still has significant potential for developing in these industries if the major weakness can be overcome.



The table below 4.4 and 4.5 will conclude the Strengths and weaknesses for South Africa’s textile and clothing industries briefly:

Table 4.4 Strengths and weakness of the textile and clothing industries

Strengths	Weakness
Inputs	
1) Abundant, good quality cotton	1)South African cotton users must consumer domestic cotton before they are allowed to import cotton; Ginning quality is not consistent
2) Man-make fibre available in South Africa	2) South africa is the only producer of the mn-made fibres used for apparel in SADC;The variety of what is produced is limited; The total supplyu of man-made fibre does not meet the demand-raw fibre imports alone is 10% cinsumption
3) Cotton is ofter conveted to yarn and favrics in the countries in which it is grown	3) The capacity for yarn and gabric production is low and much of the cotton grown is exported; The capacity that does exist is under utilised, mainly because of financial problems; The products are limited in range; South Africa textile manufacturers have poor on-time delivery performance
4) Abundant labour resource gives comparative advantage in this labour-intensive industry	4)Poor training and skills results in poor productivity; labour costs are much higher in most countires than in other SADC competitors and China; Restrictions on labour mobility within South Africa
5) Relatively cheap electric power	6)High depencence on overseas suppliers for machine parts, accessories, and miscellaneous supplies
6) As industry has reached critical mass istockists carry most parts and supplies locally; and many are manufactured locally	
(logistics)	
1) Geogtaphic proximity of yarn, fabric and garment producers reduces transport costs, lead tines and pipeline inventories	1) delays in clearing goods at boarders
2) Durban and cape town are major ports with frequent sailings and reasonable rates to all major markets and from main supply destinations	2) Durban is congested and has frequent loading and unloading delays; Durban's ad valorem wharfage fees rais the cost of handling
3) South Africa has good, resonablely priced telecommunications, and internet services	
4) Many South Sfrican retailers have implemented world-class merchadising, and sourcing systems, including quick response programs	4) Distribution systeins in the region are still antiquated, slow and expensive; Most retailers in South Africa are far behing in implementing modern retailing systems



(policy and trade relations)	
<p>1) South Africa have attracted investors in textile and clothing sectors</p> <p>2) AGOA has made all the countries in SADC potentially able to export garments duty- and quota-free to the United States</p> <p>3) All the countries in SADC can export duty- and quota-free to Europe under the South Africa-Eu agreement</p>	<p>1) High crime making it risky and confusing for foreign investors to come to invest</p> <p>2) Under AGOA, South Africa must source fabric and yarn immediately only from other AGOA-eligible countries or the U.S. to be able to benefit from AGOA preferences</p> <p>3) The agreement expires in 2008</p>
(Others)	
<p>1) long history of garment and textile production in the region</p> <p>2) Many world-class producers of fibre, yarn fabric, and garments exist in the region</p> <p>3) English is a common language, which facilitates labour mobility, intra-regional linkages, and marketing to Europe and the United States</p> <p>4) South Africa have advanced design and product development facilities</p>	<p>1) Much of the textile and clothing industry was developed under protected or embargo trading regimes and management is weak in international marketing skills, and world-class manufacturing techniques</p> <p>2) The movement of labour in South Africa is highly restricted</p> <p>3) Lack of training adequate training facilities limits the ability to develop skilled technicians, supervisors, and middle-managers</p> <p>4) A general lack of design and product development skills</p> <p>Impact analysis for textile and clothing company</p> <p>Environmental change (opportunity and threats)</p>

**Table 4.5 SWOT**

envirmental charge opportunities threats	technological change	increasy globalization of industry	sophiscated MKT demand	trade agreement with major world MKT	political stability	unstable currency	+	-
<b>Strength</b>								
* strong infrastructure & communication system	+1	+1	+1	+2	+2	0	+7	0
* availability of natural fibre	+1	+1	+2	+3	0	0	+7	0
* abundant labour force (but unskilled)	-1	+1	+1	+2	0	0	+4	0
* well - established mechandising & sourcing system	+1	+2	+3	+1	0	-2	+7	-2
* moderate investment climate	+1	+1	0	+3	+3	-3	+8	-3
<b>Weakness</b>								
* inadequate finacial resource	-1	-1	-1	-1	0	-2	-6	0
* poor education & training progrem	-2	-1	-2	-1	0	0	-6	0
* lower productivity & high relative wage	-2	-3	-2	-2	0	0	-9	0
* lack of marketing skill technical management	-2	-3	-2	-2	0	0	-9	0
* high dependece on expensive overseas suppliers for mechineparts & accessories	-1	-2	-2	-1	0	-2	-6	0
<b>Envirmental impact score</b>	<b>+4</b>	<b>+7</b>	<b>+7</b>	<b>+11</b>	<b>+5</b>	<b>0</b>		
* impact	-9	-10	-9	-7	0	-9		
* score	-5	-3	-2	-4	+5	-9		

The positive (+) score denoted that a strength that textile and clothing industry possesses and would help it take advantage of, or counteract, actions arising

from an environmental change or offset weakness. The negative (-) score denoted that strength would be reduced by the environmental change or a weakness would prevent the industry from overcoming the environmental change or a weakness would prevent the industry from overcoming the problems associated with environmental change. From these scores, “moderate investment” has the highest score, whilst “lack of management skill” and “low productivity” have lower scores. This indicates that the “moderate investment” poses strong advantages in the changing environment and “low productivity” and “lack of management skill” have weak advantage. From the analysis, the weaknesses such as low productivity have remained as a weakness in the changing environment. An overall indication of the textile and clothing industries’ position, given the changes it faces, is shown by the environmental impact score” at the foot of the table, the textile and clothing industries in South Africa is facing challenges in the future.

#### **4.4 How do we get there?**

The macroeconomic environment and regional and country-specific policies, regulations and institutions both constrain and encourage the development of the textile and clothing industries in SA. Although all the case is diverse, the guiding criterion is that any solution must change the environment to allow and encourage firms to become increasingly efficient and world-competitive, able to turn the threat of globalization into an opportunity.

##### **4.4.1 Macroeconomic environment**

Macroeconomic performance-the rates of growth, investment, inflation and real interest and the official versus secondary-market exchange rates-varies widely in SA. Although the South African government has implemented a series policies to create a stable economy environment, but the high inflation and fluctuated exchange rate still have negative repercussions for trade and investment, including for the textile and clothing industry. As per Tsikata’s (1999) study, “South African exports are highly sensitive to real exchange rates, world demand, and trade policy. The short-run exchange-rate elasticity



is 0.8”, that is, a 1% increase in the real exchange is associated with a 0.8% increase in exports. He also concluded “real exchange rate-based competitiveness is a pre-requisite for a developing (especially low-income developing) country to become a successful exporter of manufactured goods. South African government, therefore, have to adjust the macroeconomic policy, leading to stable real exchange rate. Nevertheless, this topic is not the major problem we considered.

#### 4.4.2 Tariff, taxes and Customs regulation

The regulations applying to imports and exports are contentious topics with diverse, strong interests lobbying and perhaps bribing to guarantee, modify, thwart or circumvent their implementation. As a result, policy sometimes becomes a mythical system supplanted by a practical code with unintended consequences hobbling rather than aiding industrialists (Hors 2001: 16). In other cases, policy can have inadvertent undesired results harmful to industry.

The South African economy has, for the past two decades, undergone a gradual process of trade reform, aimed at ensuring efficiency in resource allocation. There is a growing body of literature that shows the trade policy is more important in terms of its distributional effects than it is directly on growth. The leading rationale behind this premise is that resources are re-allocated from one sector of the economy to another as the economy is opened up to international competition. The trade policy of Mauritius is a very good example of success which by lowering the import protection to enable resource to flow from the countries faster and cheaper than theirs (Box 4.1). Compared to Mauritius’s trade policy, the survey we conducted in South Africa shows the trade policy in South Africa is outdated with limited openness. The common problems involve:

- The failure to rebate, suspend or eliminate tariffs and the value added tax (VAT) on inputs, spares equipment and purchased services used to produce exports.

- The apparent failure of South Africa's custom service to deduct the value of South African yarn or fabric before calculating the amount of duties payable.
- Slow and often corrupt customs services.
- The employment of time-consuming inspection services to vet cargo beyond their competence to evaluate with adequate precision.

#### **Box 4.1**

#### **Trade Incentives**

A key to Mauritius's export success

All raw materials, accessories, spares and production equipment for the textile and garment industries enter Mauritius duty free. Mauritius has also declared the whole island an export-processing zone so that an investor merely has to obtain a site and the required local government licenses to be able to apply for a certificate as an export processing zone manufacturer. Originally, such producers received a 10-year tax holiday, but the government now applies a uniform 15% income tax on all manufacturers.

Elimination of tariffs brings many advantages, pre-shipment inspections and the associated costs become unnecessary. Customs can drastically reduce how often cargo is physically inspected (the Mauritius customs authorities, using risk analysis, inspect just 3% of cargo containing textiles or clothes as opposed to 25% of other cargos) as a consequence, most cargo for the textile and clothing industries can be released immediately.

In addition to these fiscal measures, Mauritius has mitigated the impact of the surge in oil prices in 2000 by completely removing "the VAT on electricity consumption (and clothing) the customs duty exemptions granted the central electricity board to Rs 100 million yearly. As a result, the rate of increase in electricity tariffs has been limited to 20% on average, instead of 32% " (Mauritius Ministry of Finance 2000: 18). The VAT on water was also scrapped.

The silent and common problems involve 1) the failure to rebate, suspend or eliminate tariffs and the value added tax (VAT) on inputs, spares, equipment, and purchased services used to produce exports; 2) the apparent failure of South Africa's customs service to deduct the value of South African yarn or fabric before calculating the amount of duties payable; 3) slow and often corrupt customs services; 4) the employment of time consuming import-inspection services to vet cargo beyond their competence to evaluate with adequate precision.

Resource: Peter and Musa 2001:8

It is often argued that though South Africa's nominal tariffs are average by middle-income country standards, the existing effective rates of protection are high. It is important to note that nominal protection is an important indicator of the import protection level that creates a wedge between the local and international prices while the effective rate of protection indicated the efficiency of resource allocation in the economy. However, according to the report of IDT, relatively high effective rates of protection are found in textile and clothing industry.

South African customs authorities are supposed to deduct the tariff on importation, which are used to produce the final goods. In fact, the authorities require importers to pay full duties. Moreover, South Africa's trade tariff structure still remains cumbersome with some 47 ad valorem tariff bands, and over 7000 lines (DTI). The structure of the tariff schedule, especially in textile and clothing industry, may have an important bearing on efficiency. A highly dispersed and cumbersome tariff structure may mean uneven protection and gains from openness may still be limited. Thus, although South Africa has reduced the tariff rate on textile and clothing industry, the large number of different tariff means the system is not only unwieldy to administer, but is also not very transparent. In addition, it is likely to send a confusing message to South African exporters and importers.

Delay and unreliability in the delivery chain can doom a factory desiring to gain or keep international customers, especially in textiles and clothing industries. When deciding on the frequency of physical inspections, the customs authorities must understand that inspections and consequent delays and unpredictability impose costs and have adverse implications for manufacturers and the nation. Deliveries are delayed, factories are left idle and clients get scared off. According to the survey results we conducted, 65% of manufacturers are expect to import inputs from China or 25% manufacturer are already experiencing this trade relationship with China, however, the "customs regulation" and "relatively high tariff" are two *import constraints* that hinders developing trade with China.

In summary, the South African government should adjust the current trade policy on textile and clothing industry. Only a lower and uniform tariff rate is likely to create higher efficiency and lower the production cost in the industry. It will ease the importation of inputs that are necessary for international competitiveness of firms. From a political economy point of view, it is relatively easy for government to give this immediate attention



#### 4.4.3 Labor regulations and work permits

Most manufacturers viewed the existing labor regulations as deemed "*important impediments*" to their operations and capacity utilization. The most frequent complaint was about the tedious and expensive regulatory process for firing workers,. For some employers, however, their answers were limited by their vision. For example, though piecework rates, which are used for inspiring higher productivity for individuals or teams, are widely used to spur productivity in the clothing industry in Asia, it is very rare in the factories in South Africa. Not surprisingly, the manufacturers in general did not complain about the restriction, which prohibit wages based on piecework. Few even pay significant productivity bonuses, much less piecework rates despite the efficacy of such systems.

Without exception, most employers experience "*very important constraints*" due to shortages of properly trained staff for the textile and clothing industries. As a consequence, when a country's rules and administration for the issuance of work permits to expatriates are cumbersome, unpredictable and sometimes thoroughly corrupt, the efficiency and profitability of factories declines and with that the country's attractiveness for investors. South Africa is deemed the country where work permits are difficult to get. Such restrictions on the issuance of work permits including interfering with and delaying the employer's choice of recruiting supervisors, management team are critical in the textile and clothing industries. In fact, the people they want to recruit are the key personnel on the factory floor. Without dynamic, well-trained floor supervisors, productivity and quality droop threatening the industry's viability. Moreover, the approval of work permits is fraught with corruption and unjustified delays. Though governments need to promote employment and training for their citizens, they must also respect the industrialist's need to choose, without grave hindrances, a good management team. Indeed, the current rules governing the employment of expatriates hinders the regions' stability to benefit from underutilized or unemployed skilled, technical and managerial talent available in SA. Mauritius has an effective guest-worker program for overcoming specific skill shortage. They import well-trained workers and supervisors mostly from China. Although it presently raise the

production costs, it nevertheless increases the productivity and could improve productivity for the whole industry in the long term.

#### 4.4.4 Manpower training incentives

There is very little formal training of skilled personnel, technicians, supervisors and managers occur in the textile and clothing industries in South Africa. Typically, the training that occurs is informal and on the shop floor. Even where the training facilities exist, only 40% of respondents deemed that the courses offered are sufficient for the need of their industry. The “lack of appropriate training institutions “ is considered a barrier to provide the proper skilled labor.

Under the skills Development levies Act of 1999, a levy-grant system has been introduced under which each employer has to pay 1% of total payroll (From 1 April 2001) to fund skills development. The South African Revenue Service collects the skill levies. Twenty percent of this revenue is paid into the National Skills Development Fund for training of the unemployed; the rest is paid to the sector authority for disbursement. Firms who already train their employees are entitled to reimbursement of expenses. There is no restriction on training at foreign institutions (Jafta and Jeetah 2001:24 and 26). Such levies help to offset the daunting costs of in-factory training; compensate for the tendency by many managers to underestimate the value of training new technology and managerial systems; overcome the notorious fear by managers that, if they invest heavily in training, they will lose because others who invest nothing benefit by luring away the newly trained workers; encourage other parties to respond to the increased demand by setting up training schools. With a training levy, those who train are reimbursed, in large part, by those who only employ, but never train, skill workers justice! And the entrepreneurs like the idea.

#### 4.5 Conclusion

In this session, the major strengths and weaknesses, which textile and clothing industries are facing, have been explored by conducting the postal

survey combined with collecting comprehensive secondary data. Analysis of those data shows South Africa still has significant potential for further developing textile and clothing industries. Rather than stifled in a small-protected market, The South Africa government should change the trade environment with China to allow and encourage the textile and clothing industries to become increasingly efficient and world-competitive, able to turn the threat of globalization into an opportunity. The more detail strategy will be discussed in next secession.

## CHAPTER FIVE—CONCLUSION AND RECOMMENDATION

### 5.1 Introduction

Globalization both threatens and offers opportunities to South Africa. For the textile and garment industries, South Africa has both advantage and disadvantage as we discussed above. The single strategy, which will have the greatest effect on the textile and clothing industry, is ***further liberalization of the trade relationship with China***. The core concept of this strategy for the textile and clothing industry is to build a competitive advantage in supply chain. The strategy will do that by allowing industry to do what it does best and source what it does poorly. Indeed, it is also the basic and core reason why international trade happens between countries. In reality, no single country has all the resources to perform competitively in every aspect for every possible market. Nor should they try. Rather, by eliminating, even abolishing, tariffs on equipment, spares and inputs from China and adjusting the support activities will facilitate achievement of economies of scale and improved competitiveness for the textile and clothing industry.

### 5.2. Conclusion

South Africa has both advantage and disadvantage in textile and clothing industries. South Africa produces cotton, which can be utilized to make yarn, fabric and clothing; it has relatively cheaper electricity and abundant labor ideal for labor-intensive clothing market. Some firms have accumulated significant experience in international marketing and earned a reputation for reliability and quality. Such firms are able to guide a whole chain of suppliers to properly satisfy customer. Finally, the major industrial cities are located in ocean ports with good shipping facilities to principal overseas markets.

Besides national macroeconomic environments, proper regulatory structures and policy also support and facilitate the development of industry. However, problems exist too. South Africa has a huge shortfall in fabric production, necessitating big

imports. Productivity is also low compared with the Far East, accompanied with high wage. Managerial, supervisory and technical skills are in short supply; and formal training institutions appropriate for the industry are few and offer but a subset of the required courses. Moreover, the management techniques that used in many factories are inadequate and provide little motivation for workers to strive for significantly higher productivity. However, South Africa's industrialists often endure adverse regulations and fiscal policies that:

- Hamper their choice of a management team and the use of expatriate technicians.
- Delay customs clearances for raw materials, spares and equipment.
- Grossly complicate and slow down the process of setting up a functional company.
- Protect communication and electricity monopolies that charge excessive rates for poor service, and imposed taxes that are never or very belatedly refunded to exporter.

Any industry cannot survive in isolation without considering the final consumer target market. Price and product quality are also important to build their competitiveness in present market. Price is the cost to the purchaser. Developing a price-competitive pipeline means lowering costs all along the supply chain. Price competition is related to production cost since a manufacturer must charge a price that will ensure long-term profitability. Lowering production costs requires:

- Increasing volume to gain economies of scale.
- Lowering of cost of inputs and increasing input usage efficiency.
- Specialization.

The above analysis has presented that those barriers in textile and clothing industries impede the manufacturers from using the most cost effective suppliers.

Product quality refers to the design, level of embellishment, type of finishing and packaging and overall degree of workmanship. It refers the consumers' perception of the relative quality of one article to another. In competitive terms, it is subjective and is determined by the customer. Quality competition has become a marketing issue. The manufacturers need to obtain the information about market needs and how much the market can afford. One major barrier to manufacturers competing on quality is the availability of yarn and fabric and accessory. The yarn, fabric and accessory used influence the consumer's perception of a garment's quality. If a manufacturer cannot get the right yarn, fabric and accessory, he most likely will not achieve the targeted quality. As discussed in the last chapter, the yarn and fabric available from local manufacturers is insufficient. Meanwhile, due to the cotton users need to use up the local cotton before import, the textile mill do not always use proper grade cotton. This could cause serious problems in the supply chain, resulting in quality problem of garment. Moreover, the range of accessory available locally is extremely limited. 90% of manufacturers surveyed had problems with sourcing fancy accessory locally and 64% of them had experience of sourcing accessory from China and Taiwan. But they also admitted the price of Taiwanese products usually higher than price of China products as well as limited options. Barriers to importing yarn, fabric and accessory and using these materials to make garments for local and foreign market must be eliminated if these industries are going to compete successfully on quality.

In general, the South African government should benchmark Mauritius's successful model: the abolition of all intra-SADC and external Most-Favored – Nation (MFN) tariffs and value-added taxes on goods used by the textile and clothing industries. South African government should at least adopt a liberalization trade policy to eliminate the trade barriers with China in raw material, equipment, and clothes accessories and adopt the easy approval system of work permits for up to a certain percentage of each factory's total workforce. In addition, relatively custom reforms would eliminate many



bureaucratic inefficiencies e.g., the need for pre-shipment inspection, the delays and demurrage charges incurred while clearing goods through customs, and the need for bonded warehouses. This also would facilitate improve efficiency for supply pipelines and simultaneously enhancing import substitution, economies of scale, and better management process. In the end, with an easy trade policy, fast customs clearance plus a guaranteed right to choose managers and technicians, are not only benefit the entire industry's development, also send a clear message to the investor: welcome!

## **5.3 Recommendations**

### **5.3.1. Macroeconomic environment**

High inflation, high real interest rates and an overvalued currency are an unfriendly environment for facilitating industry development. The South African government must slow down the high inflation, reduce real interest rates and liberalize foreign exchange.

### **5.3.2 Policy and regulatory framework**

- Tariffs taxes.

Although some large textile mills have become internationally competitive, the remaining mills would benefit from increased competitive pressures to either improve their productivity or risk closing down. South Africa therefore, should immediately eliminate all tariffs on trade with China in raw materials, accessories and productive equipment used in the textile and clothing industries. This tax reduction will also enable the South African government to abolish pre-shipment inspection on the above goods and reduce the frequency of customs inspections at the ports and interior frontiers for such goods and the consequent delays and expenditures for warehousing of goods awaiting release by the customs authorities. This will slash and make more predictable the transit time for raw materials to reach factories, a critical consideration given the stress international clients put on timely deliveries.

- Taxes on consultants.

If South Africa 's textile and clothing industries are to compete internationally, they must be able to implement world-class technology and business practices. To facilitate this, the concept of trade in services should be extended to include professional services such as consultancy, testing, management outsourcing, product design, and marketing services.

- South African Customs' interpretations of tariff policy.

Pending the abolition of tariffs on inputs and spare parts used by the textile and garment industries, the South African Revenue Service should verify that, in practice, the value of South African fabric used to produce imported clothing is deemed non-dutiable.

- Customs reform.

In part related to corruption, the undue delays in customs' clearance of imports imply costs and risks for both manufacturers and their clients and deter sales. Since the pervasive corruption in many of the customs services within the region subverts policy, reduces governmental revenues, and encumbers business activities, governments must strive to combat such practices by:

- Reducing excessive tariff rates to lessen the incentive to bribe.
- Monitoring to more readily detect malpractices.
- Simplifying and computerizing systems to make vigilance against corruption easier, and applying more consistently the economic and criminal penalties allowed within the law to deter both bribe giving and taking.

### 5.3.3 Human resource policy

- Training levies.

As part of long-term effort to reduce dependence on expatriate personnel, the South Africa government should apply a 1% or 2% training levy on total salaries to create a fund to reimburse manufacturers for expenses incurred for formal training conducted in in-factory schools and other local or foreign industrial training institutions.

- Training needs.

South Africa should also arrange to study systematically the needs and availability of training in the region for the textile and clothing industries so as to

plan to create, strengthen or expand regional training institutions and technology centers to overcome deficiencies.

- Facilitation of work permits for expatriates.

Since South Africa needs to promote the entire country as an attractive destination for investment while also encouraging advanced technical and managerial training for the local worker, South Africa should adopt regulations for expatriate labor in such a way so as to advance both goals simultaneously: stimulation of investment and better training. Since the cumbersome, slow impractical and sometimes corrupt approval of work permits is a serious deterrent to investment and the efficient operation of the textile and clothing industries, South Africa should adopt quick and transparent systems to issue the work permit. To achieve both the above goals, we suggest all the textile and clothing factories would have given the automatic right by government to hire skilled-labor from China up to 5% of their total workforce subject to the payment of a fee.

- Piece-rate pay systems.

The South African government should benchmark and legalize piece-rate pay systems to improve the whole industry's productivity so long as:

- Workers are guaranteed the minimum wage set for the industry.
- Employers have the ability to dismiss workers who do not produce the equivalent to earn the minimum wage during a period of three months.

#### 5.3.4 Marketing policy

- Cotton markets.

Even Chinese cotton and fabrics are generally 20-25% lower in price than South Africa's cotton and fabric, South African mills are prohibited from importing cotton until the local cotton have been used up according to the South African policy. To achieve cost advantage and quality assurance, cotton lint markets absolutely

need to be liberalized. A more effective solution would be to develop local cotton auctions where cotton prices are set in local currency for current and future delivery. This would enable cotton buyers and sellers to establish prices based on local and overseas supply and demand and mediate the local value of adjustments for quality.

#### 5.3.5 Infrastructure

- Electricity.

Eskom should maintain a supply of relatively cheaper and reliable electricity to textile and clothing factories.

- Transport costs.

The transport commission should undertake a study of the transportation infrastructure and freight costs that are particularly important to increasing trade in fiber, textile and clothing. Improving the transportation infrastructure and lowering freight costs should be treated seriously.

- Telecommunications.

Protecting local telecommunications companies by laws upholding their utter monopoly and, hence, their suppression of modern and cheap Internet technology for telephony and fax services is extremely costly to both nations and their manufacturers. Government must, therefore, liberalize these activities and permit competition, thereby allowing companies the same advantages as their international competitors have.

#### 5.3.6 Technology and Information

- ISO 9000 Promotion.

Other than all the ways to improve the entire quality in textile and clothing industries as above mentioned, governments should actively promote quality as an objective and encourage firms to seek ISO 90000 certification. Government should consider a quality award to encourage quality awareness.

- Data gathering.

The lack of timely, specific information about the activities and performance of the textile and clothing sectors in South Africa is a serious barrier to rational policy making. There is hardly any information regarding the trade relationship between China and South Africa since the establishment of diplomatic relations in 1998. It also makes it difficult to assess the potential to increase production and meet market demands. The government should sponsor a regular, comprehensive program to gather this data and publish it on its web site. Such information will not only help government to follow up the actual consequence after the policy has been executed but adjust it if it is necessary, also help investors and investment promotion agencies to encourage investment in viable facilities in South Africa.

- Labor costs.

Labor cost is a key element in the labor-intensive clothing manufacturing. The available data is neither comprehensive nor up-to-date. As a result, the government should sponsor a study of the labor cost in the clothing and textile industries. This study should cover a large sample of manufacturers and produce detailed wage profiles by industry segment, employee category, and length of service; labor regulation; social charge such as training levies, pension and national health contribution and the use of piece-rates and other productivity related payment schemes.

- Informal clothing markets.

Government needs to undertake detailed studies of informal markets in clothing and textile in South Africa. These studies will include not only the nature and volume of the products sold, but also an analysis of how these products are distributed. Supplying these informal markets is a significant opportunity for small and medium enterprises and these studies are an important way to support their development.



- Trade-fair attendance.

China holds different kind trade fairs regarding the textile, clothing, equipment and accessory industries every year. To most South African manufacturers, the most efficient way to get all kind of product information and human resource information at one time is through attending trade fairs. The Chinese embassy should assist South African textile and clothing entrepreneur to get the business visa and invitation ticket to attend the trade fairs as quickly as possible.

## **5.4 Possible strategies in short-term and long-term**

### **5.4.1 Short-term strategies**

As mentioned above, from the WTO Agreement on Textile and Clothing (ATC), which expires in 2004 to AGOA, those agreement provides South Africa with a near term advantage over major producing countries that are limited by quotas and tariff-free access to USA market. They are regarded as an incentive for foreign investment. After 2008, in which year AGOA will expire, South Africa will find itself in head-to-head competition with such exporting giants as China, Taiwan, and Hong Kong. South Africa only has fewer than four years to establish herself as a strong competitor in world markets. South Africa manufacturers should further explore the U.S. market and try to build the customer loyalty in knit shirt and trousers products, which are the largest categories imported from South Africa by USA. The manufacturers can concentrate on these basic clothing items that are not generally subject to seasonal demand and easy to meet the quality standard.

### **5.4.2 Long-term strategies**

Companies that hope to be successful in the long run will need to prepare themselves for the phase out of ATC and the possible end of AGOA and its special benefits after September 30,2008. Potentially successful companies will master the learning curve for basic garments quickly and use their knowledge

and skill to develop a business and marketing plan than that will extend for beyond more than eight years.

Ultimate success will depend on a number of factors. In the first instance, South African manufacturers must be able to offer a quality product produced in a timely manner by an efficient, educated and well-trained workforce. Knowledge and understanding of the market is the second prerequisite for long-term success. In any event, success in clothing manufacturing is a continuing challenge as consumer taste change and fashion evolves. Government should provide manufacturers with an open door, but the success will be determinate by what they do after they walk through that door.

### **5.5 Summary**

In conclusion of this above, this is no doubt that the textile and clothing industries in South Africa are less competitive in world markets. In this paper, we argued that in order to be more competitive, the South African government should:

- Eliminate barriers to trade with China in textile and clothing industries.
- Amend laws to simplify approval for recruiting skilled labor.
- Establish consistent policies for investment and regulation that will encourage investment.
- Provide the seeds for the development of training, technology and marketing where the firms does not have the resources or is unable to co-ordinate these developments themselves.

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