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# The Implications of ATC-Liberalisation on the German Textile Industry

## - Summary & Recommendations -

The Implications of the Liberalisation within the ATC Framework  
(Agreement on Textiles and Clothing) on the German Textile Industry and Textile  
Employment – with Special Emphasis on China's Accession to the WTO

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# The Implications of ATC-Liberalisation on the German Textile Industry

## - Summary & Recommendations -

### A) The Change of German Textile Industry

#### Smaller - but fitter

Over the past decades the German textile industry<sup>1</sup> went through deep structural changes. Driving forces behind these changes were a continuous increase in competition resulting from imports, weak domestic demand, high domestic labour and other costs, a speeding up of fashion and product cycles, as well as the rise in technical textiles that have developed into an important growth market.

As a result, today’s textile industry is a modern, future-oriented sector, deeply integrated into the globalised economy and whose increasing exports contribute significantly to the industry’s overall turnover. Many German companies developed strategies enabling them to successfully compete in a more demanding environment and to secure both production and employment. Other companies, however, have a large part of the adjustment still ahead of them, particularly in sub-sectors that - for decades – benefited from protection through import quotas.

The extent of the structural change of the German textile industry becomes most obvious when looking at the reduction in employment. Between 1970 and 2000, textile employment fell from 496.000 to 121.500. The number of textile companies fell from 2.400 in 1970 to 1.085 in 2000.

This reduction continued during the 1990s. Between 1996 and 2000 alone, almost 17.600 jobs were lost in the textile industry. Two thirds of this reduction incurred within textile finishers, cotton weavers, producers of pullovers and home textiles. Non-woven producers and weavers of silk/synthetics, however, created new jobs. However, as employment fell in Germany, new jobs were created abroad, where the German textile industry is estimated to employ about 60.000 people, i.e. half as much as German domestic textile employment.

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<sup>1</sup> The term „textile industry“ does not include the clothing or chemical fibre industry, unless explicitly referred to as textile and/or clothing / chemical fiber industry.

Similar reductions took place in the number of companies, with the closure of almost 100 production sites between 1996 and 2000. Only rope-makers and non-woven producers did set up new sites. Production has also been declining strongly, although it was accompanied by a steady rise in productivity that – since the early 1990s - increased faster than the production declined. However, the volume of investment has been decreasing in overall terms.

### **Different Speeds in Preparing for Increased Competition**

Different sub-sectors of the textile industry adjusted and restructured in different ways and at different speeds. As a result – and in depending on their specific characteristics - sub-sectors are prepared differently for the ATC quota removal.

- Some sub-sectors were able to successfully compete over the past years and are better prepared for an increase in competition than other sectors: non-woven producers, home textile producers, weavers of silk/synthetics and manufacturers of knitted fabrics. All of those sub-sectors increased their turnover between 1997 and 2000, especially through a strong increase in exports. Some of them did create new employment or at least were able to minimise job losses at a low level.

The strengths of these sub-sectors is their intensity of capital and know-how, a strong or increasing focus on the growth market of technical textiles, customer orientation and flexibility, as well as in some cases low import competition from Asia. Therefore, prospects for non-woven producers and weavers of silk/synthetics look rather good, as do those for producers of knitted fabrics, but to a slightly lesser extent. This is also valid for the home textile industry, and particularly for its carpet/floor covering producers, whereas its “Textilkonfektionäre”, i.e. makers-up of textiles need to be more sale- and marketing-driven rather than production-driven. Particularly, home textile producers need to reduce their strong dependence on the German market by significantly increasing their exports to the EU and beyond.

- A much less encouraging situation exists for wool spinners and wool weavers, knitwear producers (hosiery, pullovers, etc.) and – to a lesser extent – for the textile finishers. All those sub-sectors did not only see their turnover significantly reduced over the past years, but also their employment and number of production sites – sometimes even dramatically such as in the case of wool spinners and wool weavers. Only textile finishers and hosiery were spared from deep reductions in their turnover.

The problems of those sub-sectors as well as their vulnerability vis-à-vis the ATC quota removal are very different from each-other. Wool spinners and wool weavers, for example, will hardly be concerned by the quota removal, but suffer from changing consumption patterns in Europe. However, the finishing industry strongly depends on the clothing industry as a customer which will feel the impact of the quota removal. The knitwear industry is strongly protected by quotas, but will itself turn to importing final products as well as input materials. The same is true for textile finishers, who will import even more input materials than they already do today, in order to finish them in Germany. The removal of quotas will significantly increase the choice in international sourcing. In addition, all four sub-sectors will have to increasingly relocate parts of their production particularly to Central and Eastern European countries (CEECs) in order to lower costs and to follow their customers. This adjustment process will lead to further declines in production, number of companies and employment. On the other hand, textile companies will be able to secure long-term production and employment in Germany, being more flexible, using their technical know-how as well as a fashion- and customer-orientated marketing.

- The strongest pressure to adjust to ATC quota removal is likely to be felt by cotton spinners and cotton weavers. Their key products will remain protected by quotas until 31 December 2004 and in many cases the necessary structural adjustments have not taken place. Quota protection may have contributed to the fact that the decline in turnover, number of companies and jobs has not been very strong over recent years. Building on an expansion of its already healthy export business, cotton spinners could even achieve a slight increase in turnover.

In addition to the continuing quota protection, cotton spinners and weavers strongly depend on the knitwear and clothing industries which will feel the impact of quota removal. A reduction in demand from these customers is therefore rather likely. This means that cotton spinners and weavers need to take the necessary measures quickly. The most urgent task is to pull out of mass-production of standard quality goods and/or to relocate such production e.g. to the CEECs. Cotton spinners and weavers should also increasingly focus on producing small quantities in order to enter the market in a flexible manner with different and ever changing yarns and fabrics. To achieve this aim, investing in computerisation and logistics are as important as investing in creativity, design, qualified personnel and marketing. In addition to further increasing exports companies will need to relocate more to CEECs in order to follow their clients that have already moved their production to these

countries. Some companies will also have to reduce their own production in favour of import business and/or turning into converters. Losses in production, number of companies and employment will undoubtedly accompany this process.

### **Exporting and Partial Relocation – a Matter of Survival**

Today’s German textile industry is characterised by a high and rising export share<sup>2</sup> reaching 35%. Export shares are particularly high in the non-woven sector (55%), followed by spinners, threads, knitted fabrics and weavers. The past few years show that in many cases increases in exports partially compensated for losses in turnover made from sales in Germany.

However, in spite of rising exports shares the textile industry – and some sub-sectors in particular – still strongly depend on the German market. In terms of the industry’s sales this market is shrinking and a further decline can by no means be excluded. For many companies an increase in their export business will therefore be a matter of survival, in order to prevent drastic declines in total turnover. The significant rise in export turnover in most sub-sectors demonstrates that companies have not only realised the importance of increasing their export business, but also that it is entirely feasible to do so.

This is of paramount significance for the future of the industry. Whereas in 2000 a quarter of EU textile exports to third countries came from Germany, German exports grew slower than those of other EU countries (1990-2000), reducing the German share in total EU exports to third countries by a third. As exporters of other EU countries face the same market access barriers in third countries, this development indicates that German companies have more difficulties penetrating third markets than their European competitors.

Furthermore, German textile exports are heavily dependant on the “processing markets” of Central and Eastern Europe. These markets will be shrinking due to the trend towards “local sourcing” in these markets, as well as due to ATC quota removal. German companies will therefore need to start quickly to diversify their export markets and particularly to enter and develop far-away markets.

For many companies relocation of parts of their production especially to the CEECs will become a matter of survival, too. Whereas foreign investments of the German textile industry are still at a low level – particularly compared to the clothing industry -, this is going to change however over the coming years.

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<sup>2</sup> Export share = share of export turnover in total turnover.

In addition to reducing costs - especially for standard products and mass production that will come under pressure after ATC quota removal – the aim of entering/developing foreign markets will become the main motivation for foreign direct investment. Already today, relocation to the CEECs has become a matter of market entry/development for many companies, to be able to satisfy local demand through local production. The trend towards “local sourcing”, whereby local clothing manufacturers use locally made input-materials instead of importing them from Germany, means that textile manufacturers will lose their customers if they don't follow them with their own local production.

Market entry/development will also be the main motivation for direct investment in further-away regions where traditional export activities are not sufficient to build up a durable presence in these markets. For example, the latest investments of German companies in China aim to supply the Chinese market, rather than to reduce production costs. Direct investments to serve regional markets will also gain momentum, particularly where groups of countries join together form free trade areas.

One important factor that could push German companies – in the medium term – to relocate their production sites to the CEECs is the increasing shortage of qualified personnel in Germany. A “wearing-out” of the tissue of personnel could significantly accelerate the process of relocation.

Foreign direct investment and relocation will not, however, lead to the disappearance of the German textile industry. They will rather be part of overall company strategies that keep the creative, capital- and know-how-intensive parts of production in Germany, while relocating labour-intensive steps as well as production of standard quality goods. As such strategies will become a matter of survival, the weak cushion of many companies' own financial resources – and particularly the smaller ones – creates a serious problem. Given the tendency of many larger banks to reduce their credit lending and due to the planned changes through “Basel II”<sup>3</sup> many companies could be driven out of the market.

### **Training, Research and technical textiles**

To secure long-term textile production and employment in Germany, the industry needs well-qualified personnel as well as a sufficient number of motivated trainees with development potential. The still widely held image of an industry

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<sup>3</sup> The term "Basel II" describes the current discussion on changing the rules for own capital requirements. Many fear that Basel II would lead to a situation where smaller companies would

with bad future prospects means however that it is hard to find qualified personnel and trainees, particularly for technical activities. As this negative image does not coincide anymore with the reality of a modern, international industry, company managers, employee representatives, textile associations and trade unions need to work on developing a positive image which is closer to today's realities. Moreover, investing in training programmes and continuous training as well as adapting the training to the globalised nature of the actual work are key conditions to remain competitive in Germany and on foreign markets.

Continuous investment in product development and process innovation is another pillar of the increasingly high-tech-oriented German textile industry. With its excellent research institutes and a high level of company expenditures reserved for research and development (R&E), Germany has a competitive advantage particularly in the area of technical textiles. This advantage needs to be fully exploited, in order to continuously renew the lead in innovation vis-à-vis international competitors.

Today, technical textiles represent already 32-40% of the German textile industry's total turnover, compared to 5-8% in the 1980s. The growth of technical textiles will continue in the future, even though on a slightly lower level. Hence, the German textile industry has a good starting point to further develop this segment and to enter/develop international markets.

technical textiles have so far been a successful way to escape from the tough and often ruinous competition in traditional textiles, and to keep production and employment in Germany. To ensure this role also in future – and especially in view of the ATC quota removal – Germany will have to offer a favourable economic environment that stimulates innovation, guarantees the availability of qualified personnel and maintains a solid network of research institutes.

## **B) The German Chemical Fibre Industry**

The German chemical fibre industry is the largest producer of chemical fibres in the EU and its companies are among the most competitive world-wide. As part of the textile industry, chemical fibre manufacturers were subject to deep structural changes leading to a cut by one half of the workforce over the past 10 years, although turnover and production remained relatively stable despite some fluctuations from year to year. Due to changes in ownership structure, today the sector is strongly European and international.

The structural changes are due to a re-focussing on core activities, a partial withdrawal from standard products in favour of specialities, the rationalisation and modernisation of machinery, and due to some reductions in production capacity. In addition, the sector had to adapt to the reduction of the German and European clothing industry as a user of chemical fibres. This loss, however, could be largely compensated by a higher use of chemical fibres in technical textiles, which today are the largest customers of the chemical fibre industry.

With an export share of 67% the chemical fibre industry is heavily export oriented, posting a big export surplus. On the other hand, the industry strongly depends on the Western-European market absorbing 70% of the exports. This dependency, however, has been reduced over the past 10 years, demonstrating the industry's efforts to geographically diversify their exports. Interestingly, the share of exports going to Central and Eastern Europe has tripled between 1990 and 2000. This trend is going to continue as many of the German customers of the chemical industry – particularly weavers – will increasingly relocate parts of their production to Central and Eastern Europe and as a result local production of technical textiles will increase there as well.

For some time already, the main problem of the chemical fibre industry has been its over-capacities. Despite an overall reduction of capacities across the EU over the past years, this problem has not changed fundamentally. The inclusion of the very strict EU codex for the chemical fibre industry into the multi-sectoral EU state aid Code may lead to a less strict control of state aid, which in turn could hamper further capacity reductions. Another problem is that considerable new capacities were created e.g. in Asia from where fibres are exported to the EU – often at very low prices. In the past, state aid or dumping practices often accompanied such exports.

The growing import pressure particularly from Asian developing countries is accompanied by an increase in the quality of imported goods, as modern machinery and know-how is easily available due to global exports of western machine tool manufacturers. Even if German industry benefits from a lead in innovation and high productivity competitors are catching up particularly in the area of standard quality products that are still produced in Germany.

As there are no ATC quotas apart from those for synthetic and artificial fibres, access to the German market is currently free from such trade barriers. This means that ATC quota removal at the end of 2004 will have no significant direct effects on the chemical fibre industry. However, indirect impacts will be felt by those companies whose major customers are in the clothing sector, as the latter will be hit by the abolition of quotas. While technical textiles will help to cushion further losses in sales to the clothing industry, a re-orientation of their production on technical end-uses will be almost impossible for many chemical fibre manufacturers.

### **Recommendations**

Regarding the future, the structural adjustment in the chemical fibre industry has by no means come to an end, and further declines in production and employment are to be expected. Apart from the need to drastically reduce capacities, the focus will have to be on company mergers, rationalisation and especially on concentration on niche markets and speciality products. Particularly the withdrawal from standard/commodity products has not yet made much progress and therefore needs to be accelerated. Given the growing competitiveness of many Asian and other suppliers the future of the German/ European chemical fibre industry does not lie in standard products. Instead, it lies in high-quality products and technically sophisticated specialities, that require equally sophisticated production processes, extensive know-how and highly qualified personnel. This adjustment will have to be accompanied by a further increase in exports and a reduction in today's dependence on the European market, through expanding exports to remote regions such as China.

## C) The Impact of Quota Removal on the German Textile Industry

### Quota Analysis

A large number of the remaining quotas on textile products are not binding on trade (only the removal of binding quotas can be expected to have an impact on trade, output and employment). In 2000 there were 156 textile quotas (down from 257 in 1995) in the EU of which only 27 (17%) were binding (defined as imports exceeding 80 % of the quota level) and only 8% of the quotas were strongly binding (imports greater than 95% of the quota level).

The clothing sector is subject to a higher number of quotas (283 in 2000) and a higher proportion of these are binding – 36% were binding in 2000 with 20% of the number of quotas strongly binding.

The impact of the removal of these binding quotas will depend upon the importance of the constrained countries in EU and German imports. If they comprise a small share then even a substantial increase in imports from these countries will not cause major disruption to the market. Our analysis of the EU market identifies just two textile categories (category 3 – woven fabrics of synthetic fibres ; category 39 – table, toilet and kitchen linen ) as being sensitive to quota removal<sup>4</sup>. In 2000 German imports of this category from countries subject to binding quotas comprised 0.65% of total imports of textiles in Germany from third countries and 0.27% of total (intra+extra EU) textile imports. German exports to other EU countries of category 3 products accounted for 3.4% of German textile exports to the EU. The value of German imports of category 39 from countries subject to binding quotas comprised 5.7% of total imports of made-up textile articles in Germany from third countries and less than 1% of total (intra+extra EU) made-up textile imports.

Hence, the analysis suggests that quota removal at the end of 2004 is unlikely to have a significant direct impact upon the overall market for textiles and made-up textiles in Germany.

The situation is somewhat different regarding the importance of the clothing sectors which are identified as being sensitive to the removal of quotas due to a large share of currently constrained imports from suppliers. German imports of clothing in the key categories (5 – Jerseys, pullovers etc ; 10 – gloves and mittens ; 13 – underwear, knitted or crocheted ; 18 –underwear other than knitted

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<sup>4</sup> We identified categories sensitive to quota removal as those where there were binding quotas and the share of countries subject to binding or strongly binding quotas in total imports exceeded certain threshold levels (see methodological approach below).

or crocheted; 21 – Parkas etc ; 29 – women’s and girls suits ; 31 - brassieres and 68 – babies garments and accessories) comprised 26% of total German imports of clothing from third countries. Such products also accounted for 22% of German exports of clothing products to the EU in 2000. It should be noted that of these categories, 10, 18, 21 and 68 were integrated in 2002. Thus, the impact of clothing quota removal in 2004 will be limited to just 4 categories.

This suggests that if the removal of quotas in 2004 does have an impact it will be felt most strongly in the clothing sector with little direct impact expected on the textile sector. For textiles producers in Germany the main impact will come not directly from the removal of textile quotas but there may be an indirect impact from changes in demand from clothing producers in the EU, where the removal of quotas may have a more profound impact upon competition.

### **Product Differentiation and Relative Quality**

The extent of the impact of quota removal will be further conditioned by the degree of substitutability between the products exported by quota constrained countries and the products produced in the EU and those supplied by other non-constrained suppliers. The degree of substitutability will be determined by the extent to which different countries specialise and are efficient in the production of different products and the extent to which quality differentiates products from different countries. Thus, if quota constrained countries have specialised in producing different products within the quota categories or are producing a different range of qualities then the impact of quota removal will be dampened. If imports from quota constrained countries are more similar to imports from other suppliers to the EU market than to the products provided by domestic suppliers then the impact of quota removal will fall more heavily on other third country suppliers.

Analysis of current trade structures suggests that the main competitors for German produced textiles on the EU market are other EU countries and the US and that countries subject to ATC quotas currently compete directly with Germany in products which comprise a relatively small proportion of German exports to the EU. This will dampen the impact of quota removal of German producers.

Competition from lower wage suppliers is more intense for German clothing than for German textiles producers. Thus, for example, just over one half of German exports of clothing products to the EU are products which are exported by China to the EU, whilst for textiles the level of similarity is less than one quarter.

In addition, Germany appears to be specialised in the production of high quality textile and clothing products. For only 3 (categories 4 – shirts and T-shirts ; 12 - panty-hose and tights and 13 – underwear, knitted or crocheted) out of the 34 categories analysed (those with binding quotas in 2000) do German export products appear to be of lower quality than the average product imported into the EU. For many textile categories the pursuit of higher quality appears to be compatible with a fairly broad based market approach (in the sense that quality competition is associated with a higher volume of exports than imports). For clothing, however, the scope for effective quality competition may be more confined to particular niches in the market, since high quality of German and EU products is associated with imports entering in greater volume than exports.

### **Model Results**

A specific modelling exercise which looks at the textiles and clothing industries in the context of the overall economy suggests that in an enlarged EU the removal of quotas at the end of 2004 will, after a medium-term period of around 7 years, reduce output of textiles by 4.4% in Germany and output of clothing by 6.4% relative to a situation in which quotas are maintained<sup>5</sup>. These simulated changes in output are likely to be at the upper bound of actual changes since our detailed analysis of the extent to which quotas are actually binding suggests that the crude treatment of the quotas that is possible in the model will overstate their true effects. The impact on the CEECs is much larger, the model suggests output declines of 4.5% in textiles and 12.9% in clothing.

About half of the fall in textile output in Germany is attributable to the removal of clothing quotas in the EU and in other locations that use German textiles as inputs into the production of clothing such as the CEECs.

The relatively small impact of quota removal on domestic output in Germany reflects that some of the impact is felt by other suppliers to the EU market, particularly, the Central and Eastern European countries and the Mediterranean region. There is also a decline in imports from the US. Similarly, on the export side, German exports to the US fall as they bear some of the impact of quota removal in the US. On the other hand, German exports to countries such as India and China increase, albeit from a very low base, as incomes in those countries rise and as output of clothing increases which demands some textiles inputs from Germany.

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<sup>5</sup> This decline is exclusively due to the quota removal which takes places *in addition* to any other cause of decline. The same is true for the decline in employment (see below).

The results from the model can be interpreted as showing that the more effectively German producers differentiate their products in terms of design, quality, reliability and so on, the more able they will be able to effectively counter increasing competition from low labour cost suppliers of textiles and clothing.

### **Recent German Performance in the EU and Overseas markets**

Two key features seem to characterise recent German performance in the textiles and clothing sectors. On the one hand import penetration has been rising more slowly than in other EU countries whilst on the other hand German exports to overseas markets have been rising more slowly than the exports of other EU members. In fact, for textiles as a whole German imports were lower in 2000 than in 1990. Exports to the EU have fallen and exports to the rest of the world have been relatively sluggish. The German share of EU exports of textiles to third countries fell by a quarter between 1990 and 2000, from 36 to 27%.

Germany is very highly represented in neighbouring markets ; Central and Eastern Europe and the Balkans, but has a very small share of EU exports to key markets in North America and Asia. For example, in 2000

Italy provided over 30% of EU exports to the US and Canada whilst Germany provided just 15%. This is important if, as recent research suggests, the main markets offering prospects for export growth are the large markets of the US, Japan and China. Conversely, further liberalisation of textiles and clothing trade is likely to adversely affect German exports to the CEECs.

Germany appears to be exporting lower quality products to the large North American and Asian markets compared with the quality of Italian exports to these markets.

### **The importance of the CEECs and the impact of enlargement**

Trade with the Central and Eastern European countries (CEECs) is an important aspect of the German textiles and clothing industries. In 2000 47% of German exports of textiles went to the CEEC countries and almost 24% of German imports of clothing in 2000 came from these countries. Germany is much more heavily involved with the CEECs than other EU countries. Clearly, this reflects, in part, location and historical ties, but it implies that any policy changes which have a specific impact on the CEECs will have a disproportionate effect upon German textile and clothing producers.

A key change which will affect the CEECs will be accession to the EU. Margins of preference for German suppliers will fall as these countries adopt the common

external tariff. On the other hand, as the modelling exercise shows, if enlargement leads to an increase in the size of the clothing sector in the CEECs there will be an increase in demand for German textiles (the model simulation suggests that enlargement will increase textiles output in Germany by about 2%) although competition in clothing will increase (a slight decline in German output in the model simulation).

At present the rules of origin under the EU’s free trade agreements with the CEECs help lock the CEECs into using German textiles and may encourage outward processing activities due to the difficulty of actually proving consistency with the origin rules. After enlargement these rules of origin will become redundant and there may be an impact on the location choices for German firms which send textiles for processing overseas. Possibly, the European countries that did not take part in the EU enlargement might gain some importance. Furthermore free trade agreements between the EU and Russia, the Ukraine and Balkan countries might play an important role in firms’ decisions.

#### **D) Strategies of Third Countries to Prepare for 2004**

Many of the countries that are constraint by ATC quotas hope to benefit from the quota removal and to expand their exports. For a number of countries – and particularly for China – this will be the case. On the other hand, today’s quotas offer export countries a guaranteed share in their export markets where they are protected from their (Asian) competitors. Once quotas are removed this protective function (which is actually much appreciated by many countries) will cease to exist. Hence, after 31 December 2004 access to the EU market and buying decisions of European importers (retailers, wholesalers, clothing and knitwear manufacturers, etc.) will be determined by market forces instead of availability of quotas and licenses. As a result, the current market shares of the various supply countries will change.

According to estimates from EU retail and industry China will be the main “winner” of quota removal. Countries that have already lost market share, such as Hong-Kong, South Korea, Thailand, Taiwan, Malaysia and the Philippines are expected to loose market share in the future, except for chemical fibres (Korea, Taiwan, Thailand, etc.). Also, Laos, Cambodia, Bangladesh and Indonesia are likely to lose market share to China. Vietnam will only be able to survive if it becomes a WTO member soon. Part of the “losers” could also be Sri Lanka and Turkey, although both of them have largely moved out of the mass market and are therefore in much less direct competition with China. India and Pakistan are

also likely to lose market share in the EU to China, but they are expected to compensate through market share taken from smaller supply countries.

In view of the expected changes, many quota countries are preparing for quota free competition after 2004. Both India and Pakistan have developed ambitious plans to remove the weaknesses of their textile- and clothing industry in order to fully benefit from quota removal. They intend to considerably increase their exports over the next 5-10 years and to improve both the quality and the fashion content of their products as well as their ability to supply within short deadlines.

Similar plans exist in almost all of the larger supply countries. Particularly countries such as Bangladesh fear that they will not be able to survive – particularly vis-à-vis China – if they don't invest in their textile industry (spinning and weaving). In China, an ambitious Five-Year-Plan focuses on the modernisation of its industry and the creation of a complete textile-fibre-to-clothing production chain. Countries such as South Korea see their future in textiles. Korea already started implementing an ambitious, partly state funded programme aiming at a slow withdrawal from clothing manufacturing and the build up of a powerful textile industry, including technical textiles. However, with the exception of Korea and China many countries have already run into difficulties implementing their plans. In many cases, realising the sometimes very ambitious plans will therefore take more time than originally expected.

## **E) Overview of the Methodological Approach**

The study is based on a combination of quantitative and qualitative analysis.

The empirical-qualitative analysis identifies the main characteristics of both the German textile industry and the chemical fibre industry, analyses recent developments and trends, and assesses the individual sub-sectors' ability to compete in a more demanding environment. Moreover, the most significant supply countries are analysed with respect to the economic/industrial strategies they adopted to prepare for ATC quota removal. This analysis is complemented by assessments of the German import and retail sector regarding the likely impact of quota removal on import flows into the EU and on price developments. In addition, an overview is provided on how the Italian textile industry is preparing for quota removal.

On the one hand, the analysis is based on detailed assessment of available studies, publications from industry associations and international institutions,

statistical data and other relevant publications. On the other hand, the study is also based on an analysis of a large number of targeted interviews with experts and key actors of the textile industry and textile trade policy, in Germany and beyond. Interviews were conducted among others with representatives of German and European textile peak associations and branch associations as well as with trade unions. Many interviews also took place with work council representatives, managers and CEOs from the textile and chemical fibre companies, from German importers and retailers as well as with representatives from the Italian textile- and clothing industry. Finally, interviews were conducted with embassies of selected countries in Brussels and Geneva, with representatives of the WTO, the European Commission and the German Ministry of Economics.

The empirical-quantitative analysis is based on three observations. The impact of quota removal under the ATC on German textile producers will depend upon:

- i) the extent to which quotas are currently constraining trade,
- ii) the importance of constrained imports in total imports, and
- iii) the extent to which products from constrained suppliers compete with products produced in Germany.

If quotas are not binding then their removal cannot be expected to have any economic impact.

If countries which are subject to binding quotas provide a small fraction of total imports then, even if quota removal leads to a large expansion of trade from these countries, there will be little disruption to the market as a whole. The extent to which Germany produces different products within the textiles sector and the degree to which products produced by Germany and constrained countries are differentiated by quality, design and reliability will dampen the impact of quota removal from constrained import suppliers.

This project has looked in great detail at the extent to which quotas under the ATC are binding. Unlike other studies we considered each quota category separately and defined quotas to be binding if imports exceeded 80% of the quota level. A further distinction was made with strongly binding quotas being those where imports exceed 95% of the quota level. This allowed for a precise identification of which suppliers in which categories were subject to binding quotas. We then proceeded to analyse the importance of the constrained suppliers (those subject to binding quotas) in EU and German imports of each category.

We identified categories sensitive to quota removal as those where there were binding quotas and the share of countries subject to binding or strongly binding quotas in total imports exceeded certain threshold levels. We used a synthetic index to bring together these different threshold levels such that key categories were those where i) either bound imports exceeded 30% of external imports and strongly bound imports exceeded 20%, or ii) if bound imports exceeded 40% of external imports and strongly bound imports were more than 10%, or iii) if strongly bound imports exceeded 30% of the total.

The analysis then applied various commonly used measures to assess the extent to which products sold by Germany on the EU market were competing with products from constrained suppliers in the rest of the world. Firstly, we applied the similarity index to compare the structure of EU imports of textiles and then, separately, clothing from Germany and from third country suppliers such as China. This was then complemented by the construction of measures of revealed comparative advantage to show the extent to which products in which Germany appears to be an efficient supplier to the EU market were the same as the products in which, say, China appears to be an efficient supplier to the EU market. We then looked at some standard measures of the quality of German exports to the EU relative to that of other suppliers to the EU and whether competition within each textile and clothing category appeared to be quality based or price based. A combination of the obtained information, allowed us to make conclusions concerning the number and importance of quota categories which may be sensitive to the removal of quotas and the extent to which product differentiation and differences in quality will dampen the impact of any changes on German producers.

Finally, we used an established economy-wide general equilibrium simulation model to directly quantify the impact of quota removal on trade, output and employment in the textiles and clothing sectors in Germany.

The model covered a range of sectors and countries and regions in the world economy. The model was able to show the extent to which quota removal affected not only domestic suppliers but also non-constrained suppliers in the rest of the world. The more detailed analysis of the quotas and of product differentiation, described above, proved to be useful in interpreting and understanding some of the results from the model, and in particular led to the conclusion that the more German companies succeed in differentiating their products the lesser the impact of the removal of quota and protection of the home market on German industry and the greater the ability to exploit opportunities from liberalisation overseas.

## **F) Recommendations**

In view of the abolition of ATC quotas, but also due to an expected increase in competition *independently* of quota removal, companies, employees and the government will have to take measures to ensure long-term textile production and employment in Germany. This should be done on the basis of the following recommendations .

### **1.1. A Change in Company Strategy**

In the light of an increase in imports and a trend towards shorter fashion- and production cycles, the German textile industry will have to face stiff competition. In order to survive and to secure long-term domestic production and employment, many companies will have to –sometimes drastically- change their strategy. The most important challenge is the necessity to abandon supply-driven strategies in favour of sales- and demand-driven production and distribution strategies.

#### **1.1.1. Market-driven Strategy Secures Sales**

Many suppliers are still producing standard quality goods, to ensure full use of capacity. Some parts of the textile industry are also heavily dependent on the clothing industry and the domestic market. As a result they are more vulnerable to increased imports from developing and other countries.

Possible solutions:

- Reduction of dependency on clothing industry can be achieved through product and sales diversification, e.g. through familiarisation with technical textiles.
- Increase of product quality and focus on other product lines, that face less competition from overseas; adoption of strategies aiming to become the price-leader in a given product range.
- Development of more fashionable products in terms of colours, colour combinations and patterns, as well as specific fibres, fibre- and yarn combinations and functionality.
- Development of many and smaller sized fashion lines. Italian producers produce some 8-12 lines per year.
- Active product marketing with focus on fashion, trends, and formality, that go beyond pure functionality.

### **1.1.2. Flexibility increases Competitiveness**

Many companies produce a large quantity of similar goods and are not able to respond to specific client demands. In the light of increased market and fashion trends and an increased fashion conscience among consumers, companies have to react quickly to customer demands in order to sell their products.

Possible solutions:

- Refocus of machinery from mass production to production of smaller quantities; investments into computerisation and logistics, in order to respond to smaller client demands and to facilitate positioning in niche markets.
- Development of an efficient sales network. This service can be offered in addition to the goods and can guarantee shortened delivery time.
- Development of close and sustainable employee management strategies (especially in the area of house- and hometextiles, that heavily rely on close contacts with distribution networks.). Therefore, companies should jointly develop patterns, designs and brands and should co-operate marketing efforts, as well as exchange electronic data through networks.
- Close co-ordination of working-time and flexibility agreements with employees and employee representatives to guarantee production and distribution. Companies should use so called “working-time accounts” and embark upon a joint-analysis of training programs.

### **1.1.3. Co-operation Creates Synergies**

Co-operation agreements amongst textile companies are still not a common features. As a result companies are unable to capitalise on cost reduction, increased flexibility and joint-pursuit of market opportunities. Italian companies have shown for decades that co-operation is one means of maintaining a competitive edge. This lack of co-operation is an important “Standortnachteil” (competitive disadvantage) of German companies.

Possible solutions:

- A change in the existing mentality, so that co-operation agreements are not only seen as possible add-ons that can be used in times of exceptional need, but rather a necessity. Co-operation agreements should be incorporated into every-day management strategies as part of a company’s national and international competition strategy.

- Proactive search to conclude long-term co-operation agreements with “friendly competitors” that produce on the same level of the production chain. Such agreements can enhance production lines and can be used to produce large orders, that the company could not have mastered on its own due to limited capacities and/ or insufficient supply or stock of raw material.
- Co-operation of companies on different levels of the production chain, enable companies to jointly develop product lines and to react quickly to changing market trends as well as specific customer demands.
- Close co-operation alongside the textile production chain can include upstream and downstream production (manufacturers of machinery, large industrial customers) and can lead to the development of new products and production processes, – especially in the area of technical textiles.
- Co-operation agreements to streamline training and continuous training programs. Companies that produce in only one part of the production chain can thus offer their employees comprehensive training regarding production know-how and technical knowledge along the whole production chain. Companies should also develop training agreements amongst several companies within the same region.

#### **1.1.4. technical Innovation is the Key to maintain a Competitive Edge**

Not only technical textiles, but also home- and clothing textiles are in need of continuous production and production process innovation, to stay competitive and to successfully defend niche markets. German companies are often taking the lead amongst their competitors and benefit from advanced innovation and know-how. But not all companies are sufficiently innovative to survive in a highly competitive market environment.

Possible Solutions:

- Continuous efforts and new investments in Research and Development (R&D) to produce new products, product uses and production processes. This will enable companies to explore market opportunities and production processes especially in the area of technical textiles and textile finishing.
- Modernisation of machinery and logistics to distribute innovative products and production procedures.

### **1.1.5. Export Is Crucial**

The high and ever increasing export quotas<sup>6</sup> of the German textile industry are proof of the increasing importance of trade with third countries. In the light of decreasing domestic turnover in many sectors and increased competition through imports, full exploitation of export market will not only become a necessity but a question of survival for many companies.

Large parts of the German textile industry, however, are still too dependent on the domestic market and are only slowly increasing their export quota. However, there is a large potential to increase exports, even within “difficult” export markets. Other EU countries, such as Italy have been able to access those markets, while the accession of China to the WTO offers some very concrete possibilities to enhance access to the Chinese market, as China will slowly decrease textile tariffs to 5-12% until 1.1.2005.

Possible solutions:

- Company strategy should be extended to include European and global export potential and to pursue those whenever possible.
- Development of an elaborate international marketing and sales network. This should include importing knowledge on other cultures through targeted hiring of employees originating from target markets.
- Focused training including language and cultural management courses of employees dealing with export market related issues.
- Co-operation agreements amongst companies on the same level of the production chain, but with different products (i.e. creation of so called “company pools”) to join forces when entering third country markets. The creation of such “company pools” could be facilitated through Gesamttextil, and regional textile associations and could be financed through public funds. Those company pools can serve to:
  - Exchange export related experience dealing with market access problems.
  - Create joint export initiatives and to develop market access strategies.
  - Contract consultancies that support and prepare export initiatives.
- Use international trading companies to buy expertise and know-how to gain market access and set up a distribution network in the target countries.
- Pro-active use of existing, but not sufficiently used, export tools, such as:

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<sup>6</sup> Export quota = Share of export turnover (exports) in total turnover.

- Increased participation of export and foreign trading fairs, especially by making use of the possibility to jointly set up information stands.
- Use of services of the Chamber of Commerce.
- Use of country reports or services offered by the office of foreign trade information (Bundesstelle für Aussenhandelsinformationen -BfAI).
- Use of the economic department of the German embassies or consulates.
- Organisation of seminars on target markets and market access problems and exchange of views amongst company heads of export. This could be facilitated through Gesamttextil.

#### **1.1.6. Partial Relocation Secures Production and Employment**

Foreign Direct investment and relocation of company production have played a minor role, apart from some exceptions. Full domestic production in many cases is no longer profitable in the light of increased imports, more cost effective production requirements in third countries, relocation of customers into neighbouring countries and in the light of the necessity to access new markets.

Possible Solutions:

- Development of market driven company strategies to maintain or enable competitive domestic production (see above: “Market driven strategy secures sales”).
- *Partial* relocation of production into neighbouring countries with lower wage levels, especially regarding less capital intensive production processes and the production of standard quality goods.
- Maintaining capital and know-how intensive production within Germany, including product development, design, marketing and distribution. This would safeguard internationally competitive domestic production and employment.
- Investment in efficient logistics and training programs, to effectively coordinate domestic and international production/ distribution.
- Reinforced FDI in distant regions, to open up markets and to serve the needs of customers that have previously moved into these regions.

### **1.1.7. Growth through Technical Textiles**

Technical textiles have been an area of growth and this trend is expected to continue in the future. The development of technical textiles has proven to be successful in safeguarding domestic production and employment. Therefore, technical textiles are considered to be of prime importance and more companies should consider partial or complete reorientation of their production in that direction.

In doing so they will have to consider the following:

- Continuous product and process innovation – based on R&D efforts – are the key requirements to maintain a leading edge. High expenditure on R&D for technical textiles can be 2-3 times the cost of R&D expenditure on traditional textiles, but is justified due to higher returns per item sold and higher turnover, resulting in increased cash-flow.
- Investment in training and efforts to keep qualified employees are key to production of innovative products and successful marketing of those products.
- Companies should increase co-operation and should enter the market through product systems rather than separate product lines. This can cut high development costs and reduce time spent on tiresome government approval measures.
- The high export potential of technical textiles has to be fully exploited. Markets with growth potential lie in Eastern Europe, the US, Japan and in Asian developing countries with existing industrial production, especially China. These markets have to be accessed at an early stage, because competition will increase through the influx of international competitors.
- German producers of technical textiles will have to relocate abroad, in order to meet large client orders, e.g. to fulfil orders of the car industry in China, including just-in-time supply.
- Relocation of production of more simple technical textiles, e.g. to Eastern Europe will become an essential part of many a company’s policy, since competition on prices and international competition within the area of technical textiles is bound to increase. In the area of standard quality technical textiles, German manufacturers will increasingly rely on co-operation agreements with Eastern European or Asian manufacturers, in order to stay competitive on prices.

- The increasing number of EU-Directives and regulations in the area of environmental protection and employment will lead to the development of a European market for technical textiles. German companies will have to anticipate this development in view of product development and production, marketing and distribution strategy in order to access markets and niches early enough. Gesamttextil and its member associations can support such strategies.
- A high degree of legal environmental requirements and the administrative transposition of such regulation can prevent especially small companies from becoming involved in the production of technical textiles. Given the large degree of SMEs this can have a negative effect on production and employment in Germany. Associations, trade unions, and companies will therefore have to pro-actively seek dialogue with political decision-makers to safeguard domestic production and employment.

## **1.2. Qualified Employees are needed to Secure Production**

Despite the changes within the German textile industry to become a more modern and innovative, high-tech oriented industry in many areas, many companies still suffer from a negative image of their sector. This image mainly consists of not offering a future perspective for long-term employment. In the medium to long-term it is feared that this image will lead to a reduction of the number of qualified employees, which would have a detrimental effect on the sector as a whole, since qualified employees are the backbone of its competitiveness. We have suggested a number of remedies and action points to prevent that companies have to relocate or stop production as a result of a lack of qualified employees:

### **1.2.1. Modern Industry Profile to Improve Image**

Without an improvement of the industry’s image, the recruitment situation will not improve and will jeopardise production in Germany.

Possible Solutions :

- Definition of an up-to-date industry profile, based on a clear description of today’s industry, its future outlook and of the required employment needs and practices, working conditions and typical recruitment requirements.

- Active communication of this profile in contacts with educational institutions, professional advise offices, political decision-makers at local, regional and national level, as well as in contacts with the media.
- Direct-marketing efforts in dealing with educational institutions, the local and regional press and job fairs. This should be done in close co-operation with companies, employee representatives, employees and trainees. Companies should also organise “open days”, where they can provide young potential trainees with hands-on experience.
- Companies should use the Textile Internet Portal that is currently developed, and which will transmit the industry’s profile to a wider audience.
- There should be a study on the effectiveness, feasibility and financing requirements of a large and widely-based image campaign, as well as on the content and possible communication tools of such a campaign.

### **1.2.1. Improve Professional Training**

In order to recruit qualified employees with a potential for future development, and in order to provide young employees with future career perspectives, efforts have to be made to improve in-house training and training within professional training schools. The dual education system, based on professional training schools (Berufsschule) has guaranteed high quality training, but is also in need of reform.

Possible answers:

- Adapt the industry’s image used by the Berufsschule to the changing realities of today’s textile industry. The emphasis should lie on conveying a future orientated image of the sector on the basis of the above-mentioned profile.
- Adapt the curriculum of the Berufsschule to today’s requirements, especially with a focus on practical learning, but maintaining a broad education that will teach students to become “thinking human-beings”, who can manage increasingly complex work assignments. Students should also obtain *active* language and media skills, that surpass basic computer skills, as well as intercultural skills.
- Increased co-operation between companies and the Berufsschule to develop specific training programs that correspond to the company’s and the trainees’ needs.

- Enforcement of in-house training, especially in those companies that have not trained young trainees in the past years. The focus should lie on the requirements of an international business, e.g. through international education and co-operation agreements, language courses etc.
- Creation of training co-operation agreements between several companies from different levels of the production chain, in order to transmit (technical) know-how along the textile chain.
- Creation of a “Fund for Professional Training”, which co-finances training programs. This fund could be financed through a mandatory contribution from all companies covered by collective agreements. The set amount of the contribution could be negotiated between the social partners. Such a fund could facilitate trainee recruitment of small and medium sized companies.
- An overview of “best practices” of training and in-house training measures. Such an overview could be done by Gesamttextil and would help companies to improve their own training programs.
- Extension of the virtual Training Network (virtuelles Bildungsnetzwerks ViBiNet). ViBiNet will include the complete technical knowledge of the industry.

### **1.2.3. Safeguard Education through Creation of Textile University Networks**

Textile education is threatened to suffer from a decrease in educational institutions that focus on textiles, despite Germany’s wide-ranging and decentralised education system. This is the result of a decrease in students and higher educational institutions, which in the past have partly suspended textile education. As a result students often have to travel far to reach existing education facilities.

Possible solutions:

- Early marketing and information campaigns on university degrees on textile management.
- Adapt content of textile management degrees to international outlook of the industry. This can be done by concluding co-operation agreements with foreign universities, that lead to internationally recognised degrees (Bachelors/ Masters), work-placements abroad, and teaching in English etc.
- Enhanced co-operation between the existing textile universities to exchange knowledge and to avoid inefficiencies.

#### **1.2.4. Maintain German R&D network**

Germany has a highly regarded and efficient R&D network, consisting of numerous textile related research institutes. A continuous effort to improve research activities, also within the framework of company financed research programs, is an important safeguard of Germany’s competitive edge. This is especially true in the area of technical textiles, which is responsible to a large degree for R&D efforts in the textile industry.

We recommend:

- Research should continue to be done out of Germany and should continue to be co-financed through government funding. A reduction in government funding in the light of less funding provisions, could jeopardise the industry’s competitiveness through innovation.
- The research focus should increasingly lie on developing research tailored to the company’s needs, especially to the needs of SMEs. Companies are already able to participate in project selection of the Forschungskuratorium (textile industry research committee). This opportunity should be used by individual companies.
- Companies should show more interest for research programs and research based results. SMEs are often not aware and are often not actively seeking information or advise on research results. Sources of information such as virtual databases and information services are not used sufficiently. Trade associations could help to lift obstacles and barriers by providing information to their member companies.
- Some Länder (federal states) have set up cost-efficient information and advise centres. These centres provide companies with information on research and how to apply it in practice. Such centres should be available in all regions with a large number of textile companies, or be centralised with the help of Gesamttextil.
- Companies should continue to use basic research results. They should then be applied to company specific research projects that are exclusively financed by the companies. Research based on public funding can thus serve as a catalyst for company specific research.
- Co-operation between textile research institutes and other research institutes (chemical, machinery, construction) should be reinforced to develop new

potentials for use of textile products, especially in the area of technical textiles.

- Co-operation should not only be reinforced with non-textile research institutes but also with users of textile products that are found outside the traditional textile industry sector. Contacts and exchange of information can be facilitated through Gesamttextil and individual textile trade associations, this includes the possibility to establish multi-disciplinary, issue specific working groups.
- The EU’s 6<sup>th</sup> framework programme for Research and Development will allow for more direct and less bureaucratic access to European funding. Gesamttextil and the Forschungskuratorium will therefore be able to better promote European textile research and the use of new possibilities.

### **1.3. Improvement of the Political and Economic Environment**

To assist the textile industry and its employees to prepare for the impact of ATC quota removal, the German government has a number of options to improve the framework conditions in Germany, the EU and beyond. This includes in particular the creation of an economic environment that facilitates business and innovation and secures the “Standort Deutschland” for professional training and research. In addition, international conditions need to be shaped in a way that allows German companies to enter and develop new markets and to do business both as importers and exporters in an environment that is fair and free of trade barriers.

#### **1.3.1. Market Access - a Matter of Survival**

Increasing exports and entering/developing new markets in- and outside of Europe will become a matter of survival for German textile companies and their employees. However, high tariffs and non-tariff barriers in countries such as the USA and many developing countries hamper the expansion of export activities. As the responsibility for external trade policy lies with the EU, the German government will have to ensure at EU-level that the industry’s market access interests are adequately taken into account in European trade policy.

There are several options:

▪ Support for the EU market access strategy:

For several years already, this strategy aims at negotiating improvements in reciprocal market access with third countries that are subject to EU import quotas. First successes were achieved with regard to Ukraine, Sri Lanka and – with reservations – Pakistan. However, countries with particularly interesting markets, such as India, are hesitating to dismantle their high market access barriers. As the ATC quotas – which serve the EU as a key incentive to convince third countries to open up their markets - will soon be abolished, the EU must be much more offensive in its quest for open markets. Therefore, the German government should strongly support that the EU considerably improves its offer for improved access to the EU market, such as:

- A substantial increase in quotas that are actually binding;
- A retroactive application of quota increases as of 1 January 2000;
- A removal of all quotas that are not or only slightly binding;
- A political statement that there will not be an excessive increase in anti-dumping measures after 31 December 2004.

Bilateral and inter-regional free trade negotiations also offer opportunities to improve export conditions for German textile companies.

- Therefore, the current EU-negotiations with Mercosur-countries should be used to reduce these countries' import barriers particularly for textiles.

▪ Capitalise on the WTO Trade Round:

The new WTO round of trade negotiations offers the best chances for reducing and abolishing trade barriers on a global scale. The German government should therefore support the following objectives:

- Reduction and - where possible – abolition of industrial tariffs.
- Particularly deep cuts in high tariffs and tariff peaks – which are numerous in the textile and clothing sector – without exceptions for individual sectors or products. The focus should be on the USA as well as on developing countries.
- Developing countries should be subject to the same market access commitments as industrialised countries. Longer implementation periods should be avoided and - where necessary - be linked to the level of development of a given country.

- An offensive approach to the concept of „graduation“ in the framework of the negotiating group Trade & Development. The aim should be to operationalise the GATT provisions of the „Enabling Clause“, to be able to distinguish between more and less advanced developing countries and to adapt their commitments to their respective level of development.
- Strengthening of the WTO Anti-dumping- and Anti-subsidy agreements, in order to prevent a protectionist abuse of these instruments. Especially developing countries increasingly use such measures in an often intransparent manner – much to the disadvantage of German and European exporters.
- An offensive approach to the issue of trade and environment, to prevent a protectionist abuse of environmental standards, but also to allow the EU to set adequate levels of environmental protection in Europe.
- Active use of the negotiating group Trade & Development to discuss trade instruments that *promote economic development* by offering *additional market access* provided the core ILO Conventions<sup>7</sup> are respected.
- Preventing a watering down of the TRIPS Agreement on the protection of intellectual property, including its provisions on patents that are of key importance for technical textiles.
- Concrete financial donations for technical assistance from the EU and other industrialised nations at the next WTO Ministerial conference. The aim should be to enable developing countries to implement the provisions of the TRIPS Agreement and other WTO obligations.
- Respect of the WTO rules on public procurement. The aim should be to ensure that e.g. producers of technical textiles are subject to the same conditions in public procurement tenders abroad as local companies from the respective country.
- Conclusion of the WTO-Round within three years in order to ensure that the implementation of its results does not start later than 2006.
  
- Reinforce tools at national level:

The existing export tools that are used to support German companies should be fully exploited and reinforced. Recommendations:

  - Support for participation in international trade fairs. In the past, this tool has proved to be effective and it should be continued. In order to increase

<sup>7</sup> ILO Convention No. 29 and 105 (forced labour), No. 87 and 98 (freedom of association), No. 110 and 111 (non-discrimination), No. 138 and 182 (child labour).

the number of participating companies, the government could rethink its selection criteria e.g. regarding the practical value of joint presentation stands. This could be done through dialogue with Gesamttextil to ensure that government funds have a maximum impact.

- The funding of trade fairs on technical textiles (e.g. “High-Tex from Germany”) have shown to contribute to the recent export successes in technical textiles. Trade fairs in this product area, which has proven to be of key importance for the German textile industry, should be carried out in regular intervals.
- The reports of the Federal Office of Export Information (BfAI) should be widely distributed, noting however that they need to be more focussed on practical company concerns. One very good example is the recent BfAI-report („Markt in Kürze“) on technical textiles in China.

### **1.3.2. Avoid Safeguard Measures on China**

The Chinese WTO accession protocol provides other WTO members with two possibilities to restrict textile and clothing imports from China after the ATC quota removal in late 2004, provided the imports threaten to cause injury to the industry of the importing country.

On the one hand, until 2008 all ATC products can be subject to quantitative limitations for a maximum period of one year. On the other hand, until the end of 2013 the protocol’s product specific safeguard clause allows for an extension of existing quotas for up to three years and possibly beyond. It is therefore the latter that allows for a possibility to restrict imports for longer periods even after the removal of ATC quotas. It can be expected that not only many developing countries will make use of this possibility, but also the USA, not least as there will be presidential election in the US in 2004. This could encourage the EU to follow suit by introducing safeguard measures, particularly as EU enlargement could lead to a “protectionist” majority in the EU Council of Ministers.

However, such import restrictions should be avoided because:

- safeguard measures would be ineffective as they could easily be circumvented by shipping goods through China’s neighbour countries. As the ATC quota removal will also remove the possibility to monitor EU imports from China’s neighbours, there won’t be an effective mechanism to stem such circumvention.

- safeguard measures could encourage China to retaliate with new non-tariff measures that would hit German textile exports.
- textile safeguard measures could provoke China to adopt retaliatory measures in other sectors of key importance to the German export business. This would be against the overall interest of the German economy.

#### **1.3.4. Reassessing Origin Rules**

EU textile origin rules are constructed in a way that the anterior processing steps get an advantageous treatment in a preferential area: clothing articles have to be manufactured using input materials from within the preferential area in order to be eligible for tariff preferences. If these rules were loosened, one would expect an overall negative effect on some sub-sectors, such as spinners. Other sub-sectors could however benefit from changed rules, such as textile finishers or home textile manufacturers, but also weavers. Depending on how the rules are changed, these sub-sectors could import input materials with a higher degree of processing and nevertheless obtain preferential origin through high added-value processing and/or finishing.

Possible solutions:

- The German Ministry of Economics, peak associations from the textile and clothing industries as well as trade unions should jointly discuss/assess the advantages and disadvantages of changing the rules. Particular attention should be paid to where the industry’s future lies and which sub-sectors can be expected to form the pillars of a future textile industry in Germany.
- To commission a study that analyses the effects of today’s origin rules on the various sub-sectors of the textile and clothing industries, as well as the possible implications of changing these rules, taking into account different options for change.
- Based on this study and the outcome of the above mentioned discussion among stakeholders, the German government should support (in Brussels) either a change of the origin rules or the current status quo.

### **1.3.5. Risks and Opportunities of Environmental Protection**

Environmental protection creates risks and opportunities for the German textile industry. The opportunities consist in the ability to be recognised as an industry that produces in an environmentally friendly way, even in those parts of the industry that strongly depend on the use of chemicals. In addition, the textile industry produces products *for* the environment, i.e. ecological-textiles to be used in air and water protection measures, or to avoid ground erosion, etc. However, the environmental efforts of the industry are little known by the public – particularly abroad.

Possible solutions:

- Trade fairs that focus on ecological textiles. This could also be done as part of trade fairs on environmental technology, where the textile industry could present its products.
- Modification of the selection criteria for public procurement at federal or regional level. The selection criteria should reflect environmental concerns like environmentally friendly production processes; such criteria should also be used in EU-wide public procurements as well as by other EU countries, to benefit not only the environment, but also environmentally friendly companies.

However, environmental requirements can also pose a risk to German textile companies, if they make production unprofitable or if they increase the price of - or even prevent - the installation of new machinery. High environmental standards can slow down growth and even lead to relocation of production, especially in the area of technical textiles and textile finishing. This is particularly true for SMEs. This would be neither beneficial for the environment, nor for the companies concerned and their employees.

Possible solutions:

- To maintain production and employment in Germany, textile industry associations, trade unions, companies and relevant ministries should ensure a regular dialogue on a regional and federal level. This dialogue should be used to establish and implement workable legislative solutions.
- Administrative bodies should be briefed at the regional level, to implement environmental protection requirements in a less bureaucratic way, focusing on safeguarding a high level of environmental protection without leading to unnecessary costs and administrative burden for the individual companies.

- Environmental policy should focus on offering economic incentives to introduce environmental standards rather than focusing on detailed legal requirements.

The implementation of the above-mentioned recommendations through policy-makers, companies and employees will considerably improve the prospects for the German textile industry. The recommendations should help to secure competitive production and employment in Germany and to integrate the industry into a wider regional context in order to fully exploit its export potential. The German textile industry combines all the necessary conditions to achieve this goal.

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