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Garments exports, job creation, and growth in Pakistan: The way forward

About the project

Funded by: IGC

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Impact:

The studies on the garments sector led to a series of reforms by the Government of Punjab including the formation of the Quaid-e-Azam Apparel Park and introduction of training at the Punjab Skills Development Fund for skills specific to the garments sector. Based on the seven areas of reforms identified by the study, sub-committees were formed under the guidance of the Chief Minister of Punjab. The findings of the work also contributed lobbying efforts and the eventual granting of the GSP plus status. The work has been presented to the senior most policy makers at the provincial and federal level including the State Bank of Pakistan.

This policy brief is based on the report "Implementing Policies for Competitive Garments Manufacturing" and is authored by Dr. Ijaz Nabi (IGC and CDPR) and Dr. Naved Hamid (IGC and Lahore School of Economics). The policy brief has been written by Dr. Ijaz Nabi.

In brief

- Pakistan's uncompetitive garments sector has led to relatively low value products being offered to the international market.
- While many firms are adopting technology and innovation to compete globally, a number of impediments prevent firms from reaching the scale necessary to accelerate job creation and growth.
- Some reforms have been implemented with success, but key areas such as trade policy and customs procedures continue to pose a burden.

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Weak export performance is a major contributor to balance of payment crises that slow job creation and economic growth in Pakistan. The textiles and readymade garments industry has the potential to significantly improve overall export performance and create jobs for the million-plus new entrants into the labour market every year.² Garments currently account for half of Pakistan's exports, 30 percent of value added in large scale manufacturing, and 40 percent of industrial employment.

To help make Pakistan's garments exports more competitive, the International Growth Centre (IGC) commissioned several studies to assess the performance, growth potential, and hurdles faced by firms in the readymade garments sector – the highest value-addition, least energy intensive, and highest job-creating segment of the textiles industry. Following are key findings from the research:

Lack of competition results in low value products

The 2013 study, "A Comparative Analysis of the Garments Sector in Pakistan"³, found that a lack of competitiveness has resulted in the garment sector supplying low value products to international markets. To come to this conclusion, the study built a profile of garments manufacturers in Pakistan based on a survey of 234 randomly selected firms from Karachi, Lahore, Faisalabad, and Sialkot (all major industrial centers) and compared it to similar firms in Turkey and Bangladesh.

Researchers gauged the relative quality of garments manufacturing across the three countries based on indicators of competitiveness such as product mix, diversity of export destinations, expertise of the work force, cost of production, functioning of regional manufacturing clusters, and effectiveness of government policy.

While Pakistani firms have shown good growth in recent years, they lag behind comparator country firms on many important indicators of competitiveness. Pakistani firms are consequently focused on the low-price segment of the market with insufficient export diversification. Using the global value chain framework⁴, the study shows that most Pakistani garments manufacturers supply low value products to retailers, brand manufacturers and brand marketers with only a few having the capability of design manufacturing. For the large number of small firms this is due to the high cost of upgrading technology and, in turn, poor

access to formal finance to do so. The agglomeration benefits of cluster formation, that might increase capabilities of firms located in Karachi, have not been realised due to poor law and order that increases transaction costs. The severe energy crisis has also not helped. Strengthening capabilities will be vital to becoming part of the value chain of a global garments market that is estimated at \$133 billion, growing at 12 percent annually and with China poised to vacate its share of 26 percent of the market.

How successful garments manufacturers operate, and what they need to improve

A follow-up study, "Garments as a Driver of Economic Growth"⁵ conducted detailed interviews with 20 knitwear and 13 woven garments manufacturers located primarily in Karachi and Lahore. This provided rich insight into the growth path of firms, the critical turning points, and the entrepreneurial ingenuity that enabled firms to take advantage of opportunities. It also revealed the biggest policy constraints to improving exports as perceived by firms. Analysis of the interviews shows that garments is a modernizing industry connecting educated, aware Pakistani entrepreneurs with rich consumer markets through well-established brand names. Many firms produce to global standards, some have developed niche markets, and a few have advanced design capabilities. Information technology is used extensively to overcome connectivity hurdles and reduce turnaround time. Resourcefulness and ingenuity have enabled successful firms to mitigate the economic and political risks perceived by importers in placing orders with Pakistani manufacturers.

There is a strong belief among successful firms interviewed for the study that Pakistan could increase its global garments share manifold and make a significant contribution to exports and employment. However, it is stressed that the success of a few firms is not enough to realise the scale effects of a modern garments industry. That will require committed policy intervention to enhance the international competitiveness of the sector as a whole. The areas that need policy attention are: Customs procedures, the skills gap, government incentives and policy consistency, law and order, facilitating buyer visits, and negotiating market access.

Policy implementation: Where it worked and where it struggles

A third study, "Implementing Policies for

¹ Pakistan Country Director, International Growth Centre and Chairman of the Board of Governors, Consortium for Development Policy Research

² "The Textiles and Garments Sector: Moving Up the Value Chain", Ijaz Nabi and Naved Hamid, IGC/CDPR Policy Brief,

³ "A Comparative Analysis of the Garments Sector in Pakistan"³, T. Husain, K.Z Malik, U. Khan, A. Faheem, N. Hamid and I. Nabi. IGC Pakistan, LUMS and Consortium for Development Policy Research. April, 2013

⁴ "The governance of global value chain", Garry Gereffi et al. Journal of Political Economy, 12(1), 2005.

⁵ "Garments as a Driver of Economic Growth: Insights from Pakistan Case Studies", Naved Hamid and Ijaz Nabi, IGC Pakistan and Consortium for Development Policy Research, March, 2013.

Garments Manufacturing"⁶, tracked the policy process to assess the influence of analytical work in changing policy. It also assesses the impact of one of the recommendations of the earlier study (improve market access) on export performance and expands the case studies to include firms in Sialkot, a cluster of innovative firms manufacturing sportswear not covered in the previous research. Firms' assessment of the policy implementation process was recorded in additional interviews conducted in all three of Punjab's industrial clusters: Lahore, Faisalabad, and Sialkot.

The Punjab Chief Minister's provincial growth strategy, 2013-18⁷, stressed the importance of export-led industrialization for employment generation and drew upon the studies cited earlier that argued for a large role of garments in achieving that objective. Keen to engage in the rollout of a comprehensive program to support garments manufacturing in the province, the Chief Minister chaired a meeting⁸ of senior Punjab policy makers, civil servants, garments manufacturers, and researchers affiliated with the International Growth Center (IGC) and the Consortium for Development Policy Research (CDPR). During the meeting, the recommendations of the previous IGC/CDPR studies were endorsed and the Chief Minister announced a steering group headed by Chairman, Planning and Development, to oversee the implementation of policies in each of the recommended areas that were further fine-tuned as: market access, trade policies and customs procedures, skills, energy, and cluster formation. Five sub-committees were formed to roll out the policies.

Did the roll out work? Following the subcommittee implementation of market access reforms that strengthened federal compliance to the European Union, Pakistan was awarded the GSP plus status in December

2013. As a result, Pakistan's garments exports to the EU grew much faster (11 percent annually) than exports to the rest of the world (1.5 percent).⁹ Progress is also satisfactory on cluster development as Quaid-e-Azam Apparel Park takes shape. Along with improved market access, this will promote Chinese investment in Pakistan's garments manufacturing through the China-Pakistan Economic Corridor (CPEC). On skills, the Punjab Skills Development Fund is developing training programs tailored to the needs of the garments industry. While there has not yet been substantial improvement in the energy situation, large investments are being made in power generation in Punjab which will bring about significant improvements in the coming months.

Less impressive is the progress in the critical area of trade policies and customs procedures. Imports of raw materials remain heavily regulated, duty drawbacks are cumbersome, and customs procedures continue to be a burden. The anti-export bias in exchange rate management is worsening with the continued appreciation of the rupee.¹⁰ One step in the right direction, however, is the recent easing of access to raw materials for garments manufacturers and better customs procedures in CPEC special economic zones.

The need to address the difficulties faced by garments manufacturers in the area of trade policies is critical but lies in the federal domain. Provincial governments – even Punjab with its strong political affiliation with the federal government – will need to find ways to work with Islamabad to improve the overall policy environment for garments manufacturers so that the sector can realise its full potential for export growth and employment generation. This includes better macro-economic management to avoid balance of payments crises that shrink the policy and fiscal space to support growth.

⁶"Implementing Policies for Competitive Garments Manufacturing" Naved Hamid and Ijaz Nabi, IGC Pakistan and Consortium for Development Policy Research, 2017.

⁷"Punjab Growth Strategy 2018: Accelerating Economic Growth and Improving Social Outcomes", Government of Punjab, Planning and Development Department, March 2015

⁸Punjab Chief Minister Secretariat, July 2013.

⁹Zara Salman, "Has GSP plus status improved Pakistan's garments exports?" <https://devpakistan.com/2017/05/24/has-gsp-plus-status-improved-pakistans-garments-exports/>.

¹⁰Hamid, Naved and Mir, Azka Sarosh. "Exchange Rate Management and Economic Growth: A Brewing Crisis in Pakistan", The Lahore Journal of Economics, 22: SE (September 2017): pp. 73-110.