Re-emergence of the Hosiery Industry in India - The Post Quota Experience

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Abstract: The International trade in Textiles was regulated by Multi-Fibre Agreements (MFA) under General Agreement on Trade and Textiles (GATT), until the formation of World Trade Organisation (WTO) in the year 1995. The MFA controlled textile trade through quota restrictions (QR). After the formation of WTO, it was decided to phase out QR gradually over a period of ten years from 1994 to 2004. During this period the textile industry of the member countries, especially the developing countries who exported textile and clothing to developed countries underwent major changes. The hosiery industry in India too underwent major changes. This article assesses the performance of the hosiery industry in Tirupur, an export hub of India after the dismantling of quotas. It makes an attempt to identify the problems of this industry that needs to be addressed in order to enhance its competitiveness in the post quota regime.

Keywords: Post quota regime, FDI, FTA

I. Introduction

The textile industry in India is a strong and vibrant sector contributing largely to India’s economic growth. The sector contributes about 14% to industrial production, 4% to the gross domestic product (GDP), and 17% to the country’s export earnings [1]. Abundant availability of raw materials and skilled workforce has given India a competitive edge in textile exports. The international trade in textiles was governed by the MFA (a system under which a country could import from a particular country only up to the limit prescribed by QR) until the formation of WTO. With the phasing out of the quota regime, the sector was exposed to open competition. The purpose of this article is to assess the situation after the removal of QR with particular reference to hosiery industry in Tirupur. India’s textile exports comprise of cotton textiles, readymade garments, hosiery, manmade textiles, technical textiles etc. Out of these the hosiery segment contributes significantly to India’s exports. An assessment of this industry’s performance over a period of 10 years (2005-2014) that followed the dismantling of quotas would throw light on the emerging pattern of trade and the areas to be revamped to enhance the industry’s competitiveness. Since there was no organized data exclusively on the hosiery industry, the information was gathered through discussion with the entrepreneurs and Secretaries of industry associations in Tirupur. Regarding the secondary sources the case studies and articles on Tirupur published in business magazines, newspapers and websites were taken as the base for this article.

II. The hosiery industry before Quota Removal

Tirupur and Ludhiana are the two prime centres for knitwear production in India. While Ludhiana focuses primarily on woollen knitwear, Tirupur is actively engaged in the production and export of cotton knitwear. This small town situated in the Coimbatore district of Tamilnadu accounts for nearly 3% of India’s export trade and 80% of India’s total hosiery exports [1]. The town was performing exceedingly well under the quota regime and was granted the status of ‘Town of export excellence. Competition was nonexistent before quota removal and therefore the structure of this industry was simple. It had assured but limited global market. Cotton knitwear production comprises of several processes such as knitting, dyeing, bleaching, printing etc. The firms here operated as small scale units specializing any of the processes mentioned above. Therefore the industry was highly fragmented and there were around 7010 units operating like this. (A Diagnostic study on cotton knitwear in Tirupur available online at http://www.smeclusters.org/pdf/creports/tirupepr.pdf). This had resulted in high degree of subcontracting relationship between them. This unique structure had minimized the need for vertical integration and at the same time given the advantages of flexibility of operations, savings on the costs of space, machinery and labour. The export orders in Tirupur were generally procured from buying houses that acted as the buyer’s agent. The orders thus received were processed and exported to the foreign buyers who would then sell them in their own brand names. This pattern of operation had made Tirupur a job working centre rather than a brand exporter. Government support was available to this industry in the form of protective policies, concessions, subsidies and export promotion measures to nurture this industry [19].
While the above structure had given the impetus to grow and flourish in a protected environment it had also created problems that went unnoticed under the quota regime. For example the high level of outsourcing had prevented the industry from undertaking large scale production thereby restricting scale economies. Likewise the practice of producing according to buyer specifications had barred the firms from indulging in serious marketing activities. Further it had made R&D redundant, which severely hampered innovations. All this turned out to be major drawbacks in the post quota regime. Consequently there was a need for this industry to quickly restructure itself.

Tirupur’s export performance during the quota regime is presented in Fig-1. While both volume and value curves show an increasing trend during the period 1987-2000, the trend is not the same after 2000 indicating the setting in of uncertainty in the growth trends. The phasing out of the quota system began in 1995 and reached a significant level by 2000. The above trend indicated the possibility of a turbulent situation after 2005 if not addressed effectively.

**Fig. 1: Tirupur’s Export Performance under Quota Regime**

![Graph showing export performance under quota regime](image)

*Source: Compiled from data provided by TEA and other sources*

### III. Measures taken to restructure the hosiery industry

In order to gear up for the new environment, several measures were initiated collectively by the government, industry and the firms. The government de reserved this sector from Small Scale Industry (SSI) to facilitate large scale production. It also allowed 100% FDI into this segment to boost investments and technology transfers. Apparel parks and fashion institutes have been set up by the government and industry associations such as Tirupur Exporters Association (TEA) and South India Hosiery Manufacturers Association (SIHMA).

The government introduced Technological Upgradation Fund Scheme (TUFS) to upgrade technology. To undertake large scale production firms are moving towards vertical integration and TUFS is being fully utilized to upgrade technology. The government has taken initiative to sign Free Trade Agreement (FTA) with European Union. Presently EU levies an import duty of 9.6 % on garments and 5% on other textile items from India [3]. This is expected to end as soon as the FTA is signed. As a step towards diversification, the industry is seriously considering the option of moving to synthetic fabrics. The fact that EU is a major hub for synthetic fabrics adds to Tirupur’s fortune. The exporters here are of the opinion that if the government signs Free Trade Agreement with Europe, Canada, Israel and other countries, the industry has got the potential to double its exports in the next 3-4 years. In an effort to combat competition new markets have also been explored. Countries like Japan, South Africa, Israel, South America and Brazil were identified as potential markets and garment are being exported to these countries. Japan and Brazil are considered to be high potential markets as there is huge demand for T-shirts there. So far India’s exports to Japan account for only 4% with China being the major exporter to Japan[18]. The Indo-Japanese Comprehensive Economic Partnership Agreement (CEPA) signed is expected to boost exports from Tirupur. TEA has taken initiative to create a brand name for Tirupur’s products in the international market.

### IV. The Post Quota Developments

Initially after the dismantling of the quota system, the town experienced an upward trend and exports went up from Rs.6500 crores in 2004-05 to Rs 8000 crores in 2005-06. But it started showing signs of decline...
subsequently. It decreased from Rs 11000 crores in 2006-07 to Rs.9,950 crores in 2007-08, a decline of around 7%, it further went down to Rs.9500 crores in 2008-09, recording a 5% decline over the previous year (Data provided by TEA). Although the appreciation of rupee against dollar, slowdown in the economic activities of U.S and European Union were all cited as reasons for the decline, the major reason was, Tirupur’s garments becoming expensive in the international market after quota removal due to increased cost of production. Some of the big overseas buyers moved out of Tirupur to Bangladesh due to this [4]. Around 60% of Tirupur’s exports were to EU and 30% to US, the regions where quota restrictions were in force [5]. Therefore countries with lower production costs such as China and Bangladesh started gaining an edge over Tirupur in those markets. Tirupur’s export performance in the post quota period is presented below in Fig 2.

Fig. 2: Export performance of Tirupur in the post quota regime

![Export performance of Tirupur in the post quota regime](image)

Source: Compiled from data provided by TEA and other sources

In the years that followed 2008-09, the industry started showing signs of improvement though not in a big way. Despite its higher cost of production, the exports increased from Rs. 9,500 crores in 2008-09 to Rs 17,817.08 in 2013-14. Between 2012-13 and 2013-14 it recorded an impressive growth of 30% in rupee terms (Data provided by TEA and other sources).

The main reason for the industry’s revival was the fading competition from Bangladesh and China in the years that followed quota removal. Bangladesh, the second largest garment exporter in the world after China, steadily gained market share due to its cheap labour. The estimated monthly wages in Bangladesh was as low as $40 for a worker, against an estimated $200 in India and $150 in China.[9] Further, Bangladesh had zero duty access to the European Union under the General System of Preferences. This made Bangladesh goods cheaper by 10% [6]. However the industry crisis that resulted out of a major fire accident at a factory near Dhaka brought to light the country’s non compliance with safety standards. Following this many western buyers shifted their sourcing destinations to other countries like India and Vietnam. Further the Bangladesh government raised the minimum wages to $68 per month pushing down the profit margins by 1%-2% [10]. In China too, there was a raise in minimum wages which pushed the production costs up by 15% to 18% [11]. Further the recovery of US economy from recession and increased purchasing power in EU helped to lift the gloom upon Tirupur. The problems encountered by the two major competitors, Bangladesh and China have put Tirupur in a strategically competitive position. The exporters in Tirupur are keeping their fingers crossed as to the decision the western buyers would make following the tragic accident in the textile factory in Bangladesh. Tirupur still retains its image for quality and perfection and international brands like Walmart, H&M, Carrefour, C&A, Tommy Hilfiger and Marks & Spencer source from Tirupur. If at all they were to shift out of Bangladesh it would be a major boom to the industry.

V. Areas to be revamped

Though the international environment is conducive for the industry, it is plagued by domestic problems that add to its cost of production. Tamilnadu has been experiencing severe power crisis and it has taken its toll on this industry. The acute power shortage has forced many units to run on generator sets which cost Rs 18-19 per unit compared to the grid rate of Rs 6.50[13]. Though investments have been made in windmills it could not be
utilized properly due to poor grid connections [14]. In an effort to find a long term solution to this, the industry has invested in renewable energy sources such as solar, power and windmills. Investments in wind energy projects that can generate up to 1200 MW have been made so far[15]. The central and the State governments have also invested in wind energy in Tirupur. Some of the units have jointly invested in solar power plants too. But it is not happening in a big way due to heavy capital and technology requirements[17].

Another factor detrimental to this industry is the inadequate infrastructure to handle effluents from the dyeing units. The effluents are let out into the Noyyal river polluting it to the maximum. Therefore strict emission norms were implemented by Central Pollution Control Board (CPCB) on dying units. The firms were asked to install Effluent Treatment Plants (ETPs) to avoid environmental pollution. The WTO regulations also insisted on complying with environmental standards. But many hosiery units were unable to do it owing to higher technology costs. Eventually the Madras High Court ordered the closure of several dyeing units for not achieving zero liquid discharge [7]. This forced several manufacturers to send the fabrics to processing houses in other states like Karnataka and Gujarat. Due to this processing costs went up from Rs.80-90 per kg to Rs.120-140 per kg [8]. Though the court order was revoked later it was a major blow to this industry. As an aftermath the industry quickly invested in Effluent treatment plants. According to TEA sources, the industry has both Individual Effluent Treatment Plants (IETPs) and Common Effluent Treatment Plants (CETPs). About 500 dyeing and bleaching units are attached to 18 CETPs, and another 154 units have their own ETPs. They have successfully achieved zero liquid discharge (ZLD). But still there are several units which could not invest in ETPs due to higher costs. The industry opines that the only permanent solution to this could be the discharge of treated matter into sea, a project that would require huge capital investments.

Besides, the town which was once known for cheap labour is now experiencing labour shortage. The downturns had made many workers move out of this sector. The sector now depends on migrant workers from other states. Due to this, there is high level of congestion in the town and the living conditions of the workers are pathetic. This has put additional pressure on the factory owners who have to provide housing, water, and medical facilities to their recruits.

The factors discussed above have made Tirupur’s cost of production 10% higher than Bangladesh [12]. The problems discussed above are pertaining to infrastructure which requires huge capital outlay. Though there have been investments from government and industry into infrastructure projects they are inadequate in terms of the requirements of this industry. Under such circumstances channelizing Foreign Direct Investments (FDI) into this segment could help to improve the situation. Though the government has permitted FDI into infrastructure, the inflows are poor due to political, legal, commercial and regulatory reasons. There has been no FDI in Tirupur even though the Government has permitted 100% FDI in knitwear. At this juncture the FTAs that are being proposed can be used as an instrument to pull FDI into Tirupur’s hosiery industry. Across the world FTAs have been used as an instrument by the developing countries to attract FDI. These full fledged trade agreements are considered to be a positive sign of trustworthiness of the host government [16]. FTAs drive FDI flows through different channels. One is that FTAs remove export regulations by lowering trade barriers to facilitate the movement of products between parent firms in source countries, and foreign affiliates in host countries. Other positive effects of FTAs on FDI could arise from other conditions negotiated in the FTA to divert financial resources to host countries. Hence, countries targeting an increase in FDI inflows from a particular source country or region could seek to implement FTAs as a viable tool to achieve their aim. Following this norm when FTAs are being signed, India can have suitable provisions in them to attract FDI exclusively into the hosiery segment in Tirupur. There is lot of scope for renewable power projects in Tirupur due to its geographical location and climatic conditions [20]. Renewable energy power projects and effluent treatment plants need superior technology. Boosting FDI from EU and Japan which are technologically advanced would certainly help to ease the problems of this industry.

VI. Conclusion

The hosiery industry in Tirupur has come a long way in exports. It reached greater heights under the quota system. When it was decided to dismantle the quota system, the industry realised that the rules of the game would soon change. Therefore it started restructuring itself even before the quota system ended. The government, industry and the firms actively played their role in the restructuring process. But they could not do much when infrastructure bottlenecks emerged as a major problem. They pose a serious threat to this industry as they result in higher costs of production thereby eroding the competitiveness of this sector. Seeking FDI for the hosiery industry in Tirupur through FTAs could be a possible solution to enhance the industry’s competitiveness.

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