STUDY ON DEVELOPMENT STRATEGY FOR UZBEKISTAN CLOTHING INDUSTRY

By
Nuriddin N. Tursunov

THESIS

Submitted to
School of Public Policy and Management, KDI
in partial fulfillment of the requirements
for the degree of

MASTER OF PUBLIC POLICY

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ABSTRACT

Textile industry in Uzbekistan has a high but so far not fully realized potential. It has considerable competitive advantages both on the world and national markets through possessing local raw materials. High potential of textile industry development could be one of the "growth points" for the entire national economy. However, government policy aimed at paramount export of cotton fiber and minimization of its processing and export of ready-made products leads to considerable risk for the national economy due to wide range of instability of the world prices for cotton fiber, especially during the periods of their drastic downfall[1]. Export of ready-made products may soon encounter serious problems of high competition on the world markets due to liberalization of international trade and ban of quotas. Cheaper textile from countries – competitors (China, Turkey, Indonesia, etc.) may not allow to increase export as well as domestic sales of textile manufactured by Uzbek enterprises but simply reduce the achieved volumes. Therefore, this study examines the major factors influencing the purchasing activity of the population for better understanding of the differences and similarities in preferences of the various groups of cotton apparel consumers. Moreover, this research focuses on general review of the commodities produced by Uzbek companies and other countries-competitors –major players in apparel market. Namely this analysis is based on the examination of:

- knitted wear produced in Uzbekistan and those of other countries producing the world's most demanded garments; and
- consumer preferences divided by groups.

There is a need in a comprehensive strategy on improvement of textile industry competitiveness that will cover all technological stages of its production.

This research clearly shows that in spite of the cost advantages, Uzbekistan companies still fail to command a sufficient level of recognition in domestic and overseas markets. Thus this research paper provides with a comparison between Uzbek textile and clothing industry, represented by SJSC "Uzbekengilsanoat", and clothing industries of China, India, Pakistan and Turkey, which are the most desirable textile and clothing manufactures in low-end segment in the world.

Based on findings, the paper offers recommendations, on how SJSC "Uzbekengilsanoat" enterprises may improve their product characteristics and hence achieve a greater success throughout the world.

[1] Textile industry in Uzbekistan: development prospects. Center for Ecoomic Research, Uzbekistan, 2005.

Study on Development Strategy for Uzbekistan Clothing Industry

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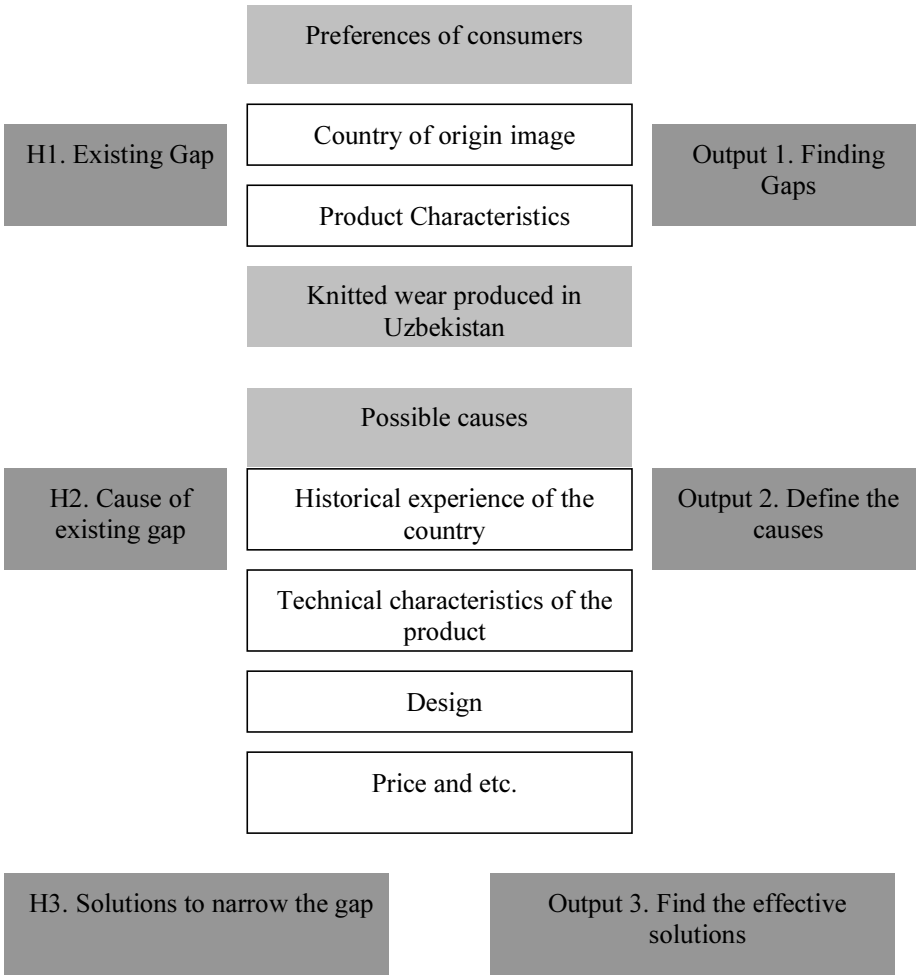
I. Introduction

1.1. Objective of Study

The main objective of the study is to investigate and identify main factors influencing the competitive advantage in textile industry and develop effective solutions to help Uzbekistan knitted wear manufactures successfully compete in domestic and world markets. The term "knitted wear" will be used synonymously with "clothing and apparel" throughout the paper.

1.2. Hypothesis

Figure 1. Developing Hypothesis



This study is aimed at discovering of a significant gap between the Knitted wear produced in Uzbekistan and those of the world's most desirable manufacture countries and consumer preferences. Finding the evidence of its existence enables us to define the cause of the gap and even solve the problem.

1.3. Methodology and Data Used

To get clear understanding of Uzbekistan textile industry we used various methodologies and methodological tools including:

- macroeconomic analysis while determining the light industry's impact on economic growth in Uzbekistan;

- comparative analysis methods and methods of analogues upon comparing opportunities and strategies for light industry development in the Republic compared to other countries;

- various statistical methods on processing data.

Using information, data and statistics, this research is based on both historical and modern points of view.

The results of marketing research study conducted in Uzbekistan (2007) were used as the basis for this paper. To ensure the accuracy of results, both studies have been carried out carefully and well-devised recruiting and briefing steps prior to actual fieldwork. The detailed scope of studies is shown below:

Study on determination of the major factors influencing the purchasing activity of the population

Methodology: In-depth interviews (Qualitative research), online questionnaire and drop-off survey (Quantitative research)

Target countries: Uzbekistan.

Sample size: N=40

Target respondents: all low and middle income knitted wear consumers

II. Literature Survey

Recent years have witnessed a growing intensity of competition in virtually all areas of business, whether at home or abroad, in markets upstream for raw materials, components, supplies, capital and technology as well as in markets downstream for consumer goods and services [Henderson 1983; Wind and Robertson 1983]. This has resulted in greater attention to analyzing competitive behavior and competitive strategies effective under different environmental conditions. Typologies of generic competitive strategies or "strategy types" have, for example, been proposed [McGee and Thomas 1986; Miles and Snow 1978; Porter 1980] and empirically tested [Dess and Davis 1984; Galbraith and Schendel 1983; Hambrick 1983a,b; Miller 1986; White 1986]. Levels of performance associated with these strategy types have been examined, as also their organizational characteristics and the type of environmental conditions under which different types of competitive strategy are most likely to be pursued [Asnoff 1965; Bain 1956; Barney1986; Conner 1995; FitzGerald & Arnott 2000; Palepu 1985; Parrish, Cassill and Oxenham 2004; Peteraf 1993].

The clothing industry, due to its low barriers of entry, is one of most highly competitive manufacturing sectors in the world [Standards and Poor's 2004]. As obstacles to trade among nations have declined due to improved transportations systems, technology transfer and government cooperation, the industries have seen a rapid increase in globalization and competition. A common marketing trend seen throughout the 1970s was price competition as a means by which firms would

compete for sales. Such measures, however, were found to lower margins, create a lack of customer loyalty, product imitation and inadequate profitability.

The word “strategy” itself, has been around for a long time. Managers now use it both freely and fondly. It is also considered to be the high point of managerial activity and almost everyone thinks that they know what strategy is. However, if we ask what the word “strategy” means to them, the range of replies is surprisingly varied. For someone the term “strategic” is no more than a synonym for “important”; for others it may be a plan of action and for the third group it might be a blueprint for success. More considered replies are likely to reveal different shades of meaning within this broad range. But what does it really mean?

One of the earliest definitions of “strategy” comes from the ancient Greek writer Xenophon (Cummings 1993: 134): “Strategy is knowing the business you propose to carry out”. The definition stresses that “strategy” requires knowledge of the business, an intention for the future, and an orientation towards action. This definition also emphasizes the link between leadership and strategy formulation. Xenophon saw strategy as a direct responsibility of those in charge, not as a spectator sport [Macmillan, Tampoe 2000].

Kenneth Andrews (1971) defined strategy as: ‘The pattern of major objectives, purposes or goals and essential policies or plans for achieving those goals, stated in such a way as to define what business the company is in or is to be in and the kind of company it is or is to be’.

Kenichi Ohmae (1983: 92) defines strategy as: ‘The way in which a corporation endeavors itself positively from it’s competitors, using its elative strengths to better satisfy customer needs’. This definition addresses both the competitive aspect of

strategy and the need to build capabilities. It also explicitly mentions customers and the satisfaction of their needs as a driver of strategy.

According to Charles Baden-Fuller and Martyn Pitt, strategy formulation in real life is rarely separated from implementation. The history of the individual and that of the organization are inextricably linked, and both color diagnosis and action. In their book ‘Strategic Innovation’ they have tried to explain the industry setting. They have typically found that industry analysis, apparently so clear in some text books looks quite different inside organizations and there is often considerable disagreement about matters such as: market definition, market size, share of competitors and relative cost positions.

The most dominant strategic management paradigm in recent years is known as the competitive strategies model (Hambrick, 1990). Exemplified by Porter's (1980, 1985, 1990) work, this approach addresses the issue of how firms compete within their product markets. Porter identified two competitive advantages that provide a firm with a defensible position: lower cost and differentiation. The lower cost advantage is defined as the ability to more efficiently design, manufacture, and distribute a comparable product than the competition. Products with unique and superior value--in terms of quality, features, and after-sales service are examples of the differentiation competitive advantage. Pursuing one of these advantages will make a firm's product or service unique, and is strongly recommended, so the firm is not "stuck in the middle" (Porter, 1990), where, by pursuing both competitive advantages, neither is achieved.

Porter also believed that before a company decides which strategy to adopt, it must know its competitive scope: “the breadth of its target market, the range of products it wishes to produce, the distribution channels, the type of buyers and

geographic areas it wants to serve and the related industries it will be competing in" (Hunger and Wheelen [2001] p82).

The cost leadership strategy is aimed at the broad mass market and requires actions like cost minimization in Research & Development, service, sales force, advertising and so forth. By doing this, the company will sell its product for a smaller price than its competitors, but still achieve reasonable profit. This also creates an entry barrier for new market entrants, as it would be difficult for them to match the low cost of the existing producer. (Hunger and Wheelen [2001] p.83)

The differentiation strategy is aimed at the broad mass market as well, but at this time creating a product which must be perceived as unique by its customers, for example through design, image, technology, customer service, dealer network and so on.

The strategy aims to gain customer loyalty and therefore making the buyer insensitive to a high price. This again will also make entry into the market more difficult for new entrants (Hunger and Wheelen [2001] p83)

Hunger and Wheelen (2001, p.83) argue, "differentiation strategy generates higher profits as it creates a better entry barrier. Low cost strategy however, creates increases in market share".

The vast majority of research on competitive strategy, especially relating to generic strategy types has, however, been conducted in relation to businesses in the U.S. Less interest appears to have been focused on examining the extent to which these findings are generalizable to markets outside the U.S. To assume that such typologies are universally valid without explicit investigation is, however, analogous to the adoption of a pseudo-ethic approach in cross-cultural attitudinal research [Triandis 1972; Pike 1966]. This widely criticized approach was founded in the

assumption that attitudinal scales, intelligence and personality tests developed in the U.S. would provide unbiased measures of attitudes, intelligence or personality in other countries [Gordon and Kikucki 1966].

Yet, both empirical findings and anecdotal evidence give reason to believe that differences may occur in competitive strategies from one country or region of the world to another. Companies of different national origins or organizational types may, for example, pursue different competitive strategies due to different management philosophies, or goals and objectives. Companies may also use different strategies to penetrate overseas markets due to differences in the competitive market environment. Market characteristics, such as the stage in the product life cycle, rate of market growth, technological change, patent protection, the flow of imports or exports, may also vary from one country to another, thus impinging on the choice of competitive strategy [Macmillan, Tampoe 2000].

III. International Experience and Modern Trends on Clothing Industry Development in Foreign Countries and Uzbekistan

3.1. Historical development of cotton textile and clothing industries and their role in the economies of the countries

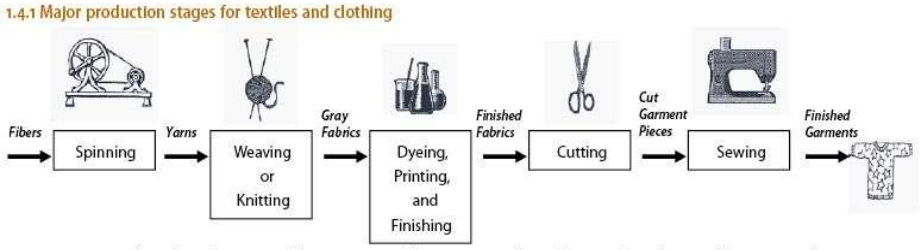
The textile and clothing industries have had a critical part in the industrialization process in a wide range of countries, over a period for two centuries. The history of development in textile industry was started in Britain as the spinning and weaving machines were invented in that country. High production of wool, cotton and silk over the world has been boosted the industry in recent years. Though the industry was started in UK, still in the 19th century the textile production passed to Europe and North America after mechanization process in those areas, further to Japan in the

first half of the 20th century, and to Hong Kong, South Korea, and Taiwan in the 1950s. The sector played at least four important roles in these countries' economic development. Firstly, it absorbed large magnitudes of unskilled labor. Secondly, it produced goods that satisfied elementary needs for large segments of the domestic population. Thirdly, despite of low investment requirements, it served to build capital for more technologically demanding production in other sectors; and Fourthly, it financed imports of more advanced technologies by generating export earnings. Many developing countries, especially low-income ones, believe that the industry can play a similar "bootstrapping" role for them today, and on this basis, they promote its development and its links to the global market. The extent to which the hopes such policies express are realistic depends, of course, upon whether the assumptions lying behind the successful experiences of Japan and the NICs remain valid.

For the last two decades, textiles and clothing have been the second most dynamic products in world trade after electronic and electrical goods. Developing countries have contributed significantly to this growth, and this sector continues to play a vital role in their economies on account of inherent and evolving comparative advantage. It is a sector that offers good prospects for diversification away from traditional commodity exports, for entry into the area of manufactures, for absorption of large pools of labor, for crossing the great divide between the rural and urban sectors, and for generating foreign exchange. Also, the economic performance of the sector has important implications for socioeconomic issues, such as equitable distribution of income, employment opportunities for women, development of small- and medium-scale enterprises, spillover to the informal sector, integration of remote regions into the global economy, promotion of rural development and poverty alleviation [Hayashi 2005].

Before turning to historical development and recent issues in textiles and clothing, it is important to note briefly the industrial structure. Viewed as an integrated whole, the value chain in textiles and clothing consists of the following five production stages (Figure 1.4.1): (i) spinning of fibers into yarn; (ii) knitting or weaving of yarn into gray fabric; (iii) dyeing, printing, and finishing of fabrics for clothing production; (iv) cutting of fabric into clothing parts; and (v) assembly or sewing operations (combined with accessories like buttons and zippers) to create finished clothing.

Figure 2. Major Production Stages for textile and clothing



Source: USITC. 2004. *Textiles and Apparel: Assessment of the Competitiveness of Certain Foreign Suppliers to the U.S. Market* (2 volumes). Publication 3671. Washington, DC. January. Available: http://www.usitc.gov.

England

The historical development of textile and clothing industries in England started with Industrial Revolution. The era known as the Industrial Revolution was a period in which fundamental changes occurred in agriculture, textile and metal manufacture, transportation, economic policies and the social structure in England and may be defined as the application of power-driven machinery to manufacturing. It had its beginning in remote times, and is still continuing in some places. The changes that occurred during the period from 1760 to 1850, in fact, occurred gradually. The year 1760 is generally accepted as the "eve" of the Industrial Revolution.

The textile industry had some special problems. Prior to 1760 the manufacture of textiles occurred in the homes, by people who gave part of their time to it. It was a

tedious process from raw material to finished product. In the case of woolen cloth, the wool had to be sorted, cleaned and dyed. Then the wool was carded and combed. Next, it was spun into thread which was woven into cloth. Subsequent processes were performed upon the cloth to change the texture or the color of the woolen cloth. Many of these stages of production were performed by women and children. The supply of raw material for the woolen industry was obtained domestically. In the cases of silk and cotton, the raw materials were obtained from foreign sources, such as, China, the West Indies, North American and Africa[2].

The manufacture process in textile industry was organized complicatedly and with the gross inefficiency. It took four spinners to keep up with one cotton loom, and ten persons to prepare yarn for one woolen weaver. Spinners were busy, but weavers often had to be idle for lack of yarn. Differences existed from one locality to another; generally, a merchant employed putters-out to distribute the raw materials to spinners and weavers who were scattered throughout the countryside.

The situation started to change in 1733, since John Kay, a Lancashire mechanic, patented his flying shuttle. Weaving could then be done more quickly, but it was still delayed until yarn was available in more abundance. In 1771, Richard Arkwright's "water frame" was producing yarn. About the same time, James Hargreaves (1778) patented a spinning jenny on which one operator could spin many threads simultaneously. Then in 1779, Samuel Crompton combined the jenny and the water frame in a machine, known as "Crompton's mule," which produced quantities of fine, strong yarn. The yarn famine had come to an end[3].

The changes that took place in the textile industry must certainly center about the inventions and their inventors, though not necessarily be limited to them. These

[2] Montagna, A.J., “The Industrial revolution”, http://www.yale.edu

inventions that were perfected and employed led to tremendous change in the world of work. The days of the Domestic System were gone, yielding to the new ways of the Factory System. These factories which were to spring up throughout the countryside were large, dusty, poorly illuminated and ventilated, and dangerous. The employment of women and children was commonplace and desired, they were paid lower wages than their male counterparts. Working conditions in these factories were not subject to much regulation.

In the period of 1780-1860 further mechanization occurred in textile processes. In 1784, a machine was patented which printed patterns on the surface of cotton or linen by means of rollers. In 1894 Northrup produced an automatic loom, and when the power loom became efficient, women replaced men as weavers, although there were still hand weavers in the paisley shawl trade as late as in 1850s. By 1812 the cost of making cotton yarn had dropped nine-tenths, and by 1800 the number of workers needed to turn wool into yarn had been reduced by four-fifths. And by 1840 the labor cost of making the best woolen cloth had fallen by at least half[4].

The subsequent history of the industry, from the mid-1970s onwards, can be seen in part as a series of attempts by the big groups – some of which became even bigger through further acquisitions – to find a viable place in the world market.

With hindsight, it can be seen that the strategy of scale, standardization and vertical integration was flawed. First, it proved impossible for UK-based manufactures, even with modern equipment, to compete on price in commodity yarns and fabrics with low-cost foreign suppliers. Second, some biggest companies as Courtaulds' aimed to become the Hong Kong of Europe, supplying standard fabrics throughout the Continent, were based on the assumption, that Western Europe would

[3] http://mars.wnec.edu/~grempel/courses/wc2/lectures/industrialrev.html

become an integrated, homogeneous market, similar to that of the US. But indeed, the European market remained more diverse and more fashion-orientated than the US, and less conducive to standardization. Third, those companies underestimated the difficulties involved in managing a vertically integrated group; the policy of forcing all group companies to buy fibers and yarns from in-house suppliers led to poor quality and loss of market share. With the partial exception of some large Japanese manufacturers, no other textile company in the world has followed a similar strategy; in the US, for example, as in most of Continental Europe, the manufacture of fibers and fabrics is the hands of separate companies, and that structure remains. Another mistake according to Owen (2001) was to choose the wrong machinery, especially for the new weaving mills. One experienced observer, after examining the equipment that had been installed at the Skelmersdale mill, could see "no possibility of manufacturing profitably on those machines in current or probable future trading conditions" [Ormerod 1996].

Specialization and internationalization, these British examples be suggested, are the keys to survival. Companies are supposed to decide which parts of their business, if any, can be internationally competitive, and do everything possible to reinforce them. Specialization might mean opting out of apparel-type fabrics to concentrate on high-performance textiles. This is the strategy pursued by Allied Textiles, once one of the leading Yorkshire manufacturers of worsted fabric for clothing; this company, having pulled out of the fashion sector, now makes such products as coated fabrics for airbags, waterproof breathable fabrics, and fabrics for high-visibility clothing[5]. Another interesting case is Dawson, the Scottish knitwear group, which, after an unhappy experience with diversification, has converted itself from a mini-

[4] Rempel, G. "The Industrial Revolution", http://www.ecology.com

conglomerate into a cashmere-based business, with the Ballantyne brand as its flagship.

What we have seen, then, in the British textile industry over the last three decades, is a slow and painful process of adjustment to the realities of the world market, with several false steps along the way. While the story is not all gloom, performance has clearly been less good than in Germany or Italy. What did German and Italian manufacturers do right, that their British counterparts got wrong?

Owen (2001) states, that there are two important differences, which apply to both Continental countries, that they did not have a Lancashire-type problem – a huge cotton sector with capacity far in excess of likely demand – and they did not face the problem of low-cost imports as early or as severely as the British industry did, because of the Commonwealth connection. In addition, German and Italian textile manufacturers benefited hugely from the rapid expansion of intra-European trade in the 1950s and 1960s – a process in which British firms, partly because of Britain's delayed entry into the Common Market, participated to a much smaller extent.

Japan

In contrast to the shipbuilding, iron manufacturing, and railway industries, which developed in response to the "needs of government," the technology of the textile industry was developed to meet the "needs of the people." Specifically, the industry developed by supplying good-quality cotton cloth at low prices to people who had been "half naked," according to the record of a British traveler in Japan immediately after the opening of the country [Takeuchi 1990]. This development was accompanied by a revolution in materials, wherein linen was replaced by cotton, a change that was reflected in the dyeing process as well. Besides dark blue and brown,

[5] Textile Outlook International, March 2001

woven fabrics of striped patterns using dyed yarns were produced, and these diversified and enriched the market for cloth.

Clothing was expensive and therefore used and mended carefully. Old bits were stitched together to form new pieces, and quilted waterproof winter coats were made by sewing with thick threads so many times that the original piece could no longer be discerned. There was a big demand for used clothing; indeed, each entertainment district in today's Tokyo previously had a market for used clothing, and a used-clothing network covered the country. The markets and routes of those days have become the distribution bases and routes for today's ready-made apparel (Nakagome 1982). In short, the technological changes that took place upstream were smoothly channeled downstream to create fertile new fields of trade expansion.

Regarding production, only spinning, which demanded a high input of labor and skill, was mechanized and modernized, as power spinning was 20 times more efficient than manual spinning. Weaving, however, was left to traditional technology (Ishii 1986). Modern technology was transferred only in the spinning division partly because Western weaving machines could produce only broad cloth, while the demand in Japan was for narrow cloth. Thus, modern technology did not eliminate traditional technology; rather, both shared interdependent or mutually supplementary relations, and, for these reasons, the textile industry and its technology became stable and could be developing into a national industry.

As mentioned, power spinning was more efficient than manual spinning, but the switch was not made without a careful consideration of what technology would best suit the existing needs and conditions. The mule spinning machine was the first to be imported, but it was replaced with the ring spinning machine in less than 10 years. The ring machine was imported not only because it was the most advanced, but also

because it required fewer skills and could be operated by low-waged women workers. The mule machine required skilled manual labor, traditionally that of only adult males; and it took a long time to form such skills. How significant the skill-saving was could be seen in the fact that productivity in Japan even with the highly efficient ring spinning machine was only one-fourth to one-eighth the productivity of a skilled British worker operating a mule machine. This great difference led to widespread adoption of the ring machine.

Although the development of the spinning industry owed much to the efforts of private individuals, men like Shibusawa Eiichi (1840-1931), initial technology transfer was made by the government. The government-operated model spinning plants were, however, short-lived. Both of them were poorly managed, and a fiscal crisis of the new government was an impetus for their sale to the private sector. Where the government succeeded, was successful substituting its own products for imports (which had accounted for 30 per cent of Japan's total imports), and later got started producing goods for export.

Nevertheless, this partial success was overshadowed by the government's failure in terms of business management. For example, in the spinning industry, the government set up 10 small plants (each with 2,000 spindles, that is, a set of 4 machines, each with 500 spindles) in various places in Japan. The 10 plants were part of an anticipated 255 plants that, if it was established throughout Japan, would make possible the complete replacement of imports with domestic products. However, these first 10 plants did not succeed. The total number of plants established by the government reached only 17, and when, about 10 years later, the government withdrew its support, only 3 factories managed to survive. These three ones evolved into the two large textile concerns of Toyobo and Kurashikibo [Hayashi 1990].

A simple comparison of Japan and India reveals there was no restriction on expansion and development in the Japanese cotton industry, in contrast with the situation in Great Britain and India (Yonekawa 1981). There were only economic limitations. Thus, for example, in the Japanese cotton industry, there was a 24-hour, 2-shift (day and night shifts) operation system in effect, and the high profits earned from this system were reinvested. Before 1911, no legislation existed to protect the workers.

This, then, enabled Japanese enterprises, the initial scale of which was much smaller than that of the spinning shops in Bombay, to catch up rapidly.

According to Kato (1979), a shift from the mule to the ring spinning machine was carried out simultaneously in Japan in all large factories, contrary to the situations in England and India, where both types were in use. In India, there was the big factory at Tata that converted to the ring at an early stage but in India as a whole, the mule spinning machine was in the majority and the ring machine was auxiliary one.

The question regarding types of spinning machine relates to the problem of management. Tata was exceptional because, from the beginning, it was opposed to the proxy management system (foreign-owned, locally managed enterprise system); whether we may point to that as the reason for Tata's early conversion to the ring spinning machine is uncertain, but it does appear that India's proxy system by nature was passive toward technological change. Indeed, the switch to the ring spinning machine in India was slow, and, in comparison to owner-managed operations, the proxy system was not sensitive to technological change [Hayashi 1990].

On the other hand, when Japan was making frantic late-comer efforts to master the new technology to replace imports with domestic products, because (1) the ring spinning machine required fewer skills to operate and (2) domestic demand was

mainly for low-count yarns, the ring spinning machine was most suitable: it was not only the most advanced, but it was also the best suited to the market and working conditions in Japan at the time.

When the large-scale factories, specialists in spinning low-count yarns, started also to produce woven fabrics - at the time of their entry into the Korean and Chinese markets - a development in the technology of cotton mixing was introduced; this change was accomplished through minor operational improvements in the functioning of the ring machine for spinning middle- and high-count threads and for weaving. The technology of mixing had thus developed into Japanese specialty.

The important aspect of this development was that, rather than an unconditional or blind transfer of the most advanced technology, the selection of a technology was made based on rational judgment in terms of skill-formation costs and marketability.

The Japanese textile industry today no longer depends on natural fibers. Although natural fibers are useful and sometimes indispensable, they have lost the importance they had before the war. Hand-woven linen, cotton, and silk cloth made of only natural fibers have become extremely high-caliber craft work.

Most of the leading textile companies in Japan today have been engaged in the research and development of chemical fibers since World War II, when Japan could not import raw materials, and have thus diversified into the chemical industry, as well as in other sectors of new technology. Japan's technological stock has prepared it to enter the most advanced fields of technology; indeed, although most Japanese are not aware of this, vinylon (polyvinyl alcohol fiber) was invented in Japan. Furthermore, the trading companies that specialized in raw cotton and cotton products have become general trading companies, serving technology has been transfered as a part of their activities.

South Korea

Cotton spinning was one of those first industries in South Korea faced the challenge of industrial adjustment in the 1970s, well before, shipbuilding, autos or electronics.

The successful historical development of this industry started in early 20 century. The first large-scale cotton spinning mills succeed on the Korean peninsula were under Japanese colonial rule from 1910 to 1945. Later in 1945, the Japanese textile factories reverted first to the American Military Government, and then, to the South Korean government with establishment of Republic three years later. Japanese spinning mills in the colony, which were large scale and labor-intensive, created for Koreans small opportunity for higher administration or investment experience, but plenty of experience as workers and even low-level managers. According to Shoemaker (1946), a leading US official in the southern part of Korea at the time of liberation in 1945: “The most important industry, by far, is textile manufacture. Japanese techniques in this field were as advanced as in the world, and textile workers were well trained.” Some features of the colonial textile enterprise survived liberation, such as the scale of plant and the prominent role of the state in financing.

As Korea got control at the mills from 1946, it started to build its textile industry on the formerly Japanese-owned base of plants and machinery. According to one survey report, 220,000 spindles were at the plants of Kanegafuchi, Toyo, and the Chosen Spinning plant in Pusan in 1945. The Korean-owned colonial era Kyungbang plant outside of Seoul reported 30,000 spindles [SWAK 1968]. Soon after, the industry recovered from the Japanese exodus in the late 1940s, the Korean War (1950-1953) destroyed mills and dispersed workers in Seoul and Taegu, the centers

of the industry. According to Ministry of Commerce and Industry estimated: lost of industry during the war was 64 percent of its plant, and 67 percent of its machinery. Funding for reconstruction from the United Nations, and local site properties on recovery in import-substitution industries contributed to a remarkably fast recovery. The government report referred 121,000 spindles in operation by 1953, and nearly 475,000 spindles in place by 1960, about twice the scale of the industry fifteen years earlier[6].

Smaller producers were frustrated by the mills equipped with 30,000 to 60,000 spindles and achieved economies of scale through mass producing of cotton yarn and fabrics. Thus concentration distinguished the industry already from the years of reconstruction with eight major spinning firms accounting for 85 percent of the nation's operating spindles by 1959. McNamara (2002) states that dependence on support from abroad also marked the formation of the industry, with the early firms not only built on the base of the former Japanese properties, but also relying on foreign aid for plant reconstruction, imported technology, as well as for imports of raw cotton.

By that time Korean spinners recognized that they have to integrate production from the outset in order to produce not only cotton yarn, but cotton cloth and thus, avoid middlemen such as independent weavers and converters, so they decided to develop weaving industry by investing capital in weaving machines[7]. These early mills also attempted to manage suppliers, production, and sales within their own related firms, replicating an integrated business group dynamic on a smaller scale. The one of the main purposes of investing in weaving machines was to stretch the

[6] Ministry of Commerce and Industry, Republic of Korea, "General Survey and Rehabilitation Programs of Industries in the Republic of Korea," (Washington, DC: National Archives, 1953), pp.41-42

[7] TPH 1957, Sec. I, pp. 15-16

production line from yarn to fabric, rather than contracting out to smaller, independent weavers in Taegu and Pusan, and in 1959 sixteen member mills of Spinners and Weavers Association of Korea (SWAK) accounted for all of Korean's yarn production, but also for about 70 percent of fabric production [Gallagher 1959]. This initial effort at capturing more profitable phases of textile production would persist as a familiar strategy at the Korean mills. Unlike their Japanese predecessors, vertical integration of spinning and weaving distinguished the Korean industry with estimates that the mogul spinners were weaving as well with up to one-half of total yarn production [Donaldson 1958].

The initial process of serial production took place among firms, at least combining spinning and weaving at the same time. Such efforts to capture profits down the line of textile production resulted in integrated textile plants as well as oligopoly, and high debt ratios. Extensive credits available for plant development distinguished early growth in the Korean industry, and spurred a competition for those funds in effort to extend production to capture a share in an expanding market. Availability of financing from state banks such as the Korea Development Bank and state-controlled commercial banks for larger enterprises with an established base of technology further encouraged concentration and highly leveraged capital investment[8]. Loans to textile firms by commercial banks amounted to about South Korean Won (KWN) 11 billion in 1957, 13 billion in the next year and KWN 15,9 billion in 1959, ranging between 27 and 34 percents of all loans for manufacturing in

[8] A SWAK report of March 1957 citied total bank loans of 11.1 billion kwan for member mills, as against a paid in capital of only 1.08 billion kwan; Reconstruction Bank credits for textile manufacturing accounted annually for 30 percent of its total funds for manufacturing in 1957, and 20 percent for the next two years. The bank committed about 9.7 billion kwan to the industry in 1957, 13.2 billion kwan the next year, and 14,7 billion kwan in 1959, just as commercial banks under government control and partial ownership devoted a major share of their manufacturing credits to textiles.

those three years[9]. Additional recourses were brought beyond the local market by foreign aid from the joint Korea – US Combined Economic Board and the International Cooperation Agency of the US, but here also the mills had to compete to gain credits and to balance expansion of plant with projected demand.

By 2004, the Korean textile industry enjoyed a global market share of 3.1%, ranking fifth in the world behind the EU (32.3%), China (29.7%), Turkey (3.9%) and the U.S. (3.8%). In the US$453 billion of global market, Korea' share was US$14.2 billion, compared vs US$146.2 billion for the EU, US$134.7 billion for China, and US$17.6 billion for Turkey. . The nation ranks fourth in polyester production, the most widely used synthetic fiber, and 15th among world's producers of cotton yarn.

As we come to Korean "ready-to-wear" clothing industry, it started to develop in 1975, providing momentum for an emerging fashion/apparel industry. By the 1980's, as Korea's GNP increased and more women entered the workforce, this industry began to evolve into one offering customer's choice in styles and fashions. Into the mid-90's, Korea's apparel market was firmly established as one of its most important markets, growing over 15% per year, with annual sales of US $15 billion by 1996. Today South Korea is a highly competitive market both in the quality and price of its textile and cloth products. Although domestic consumption for clothing here has continued its decrease since 1999, since the second half of last year, according to "Textile Korea 2005 Annual Report & Forecast" published by the Korean Federation of Textile Industries (KOFOTI), it began to turn around and show improvement, thus allowing a 4,3% increase in its fashion market in 2006. It is discovered that the local market consumption recorded a 5,3% decrease as a result of

[9] Bank of Korea, *Josa Weolbo* 14, 11 (Nov. 1960): 40-41

weak consumption, weak competitiveness of the textile industry, and increasing overseas production in the clothing industry[10].

During the last two decades, textiles and clothing were the second most dynamic products in world trade after electronic and electrical goods. Developing countries contributed significantly to this growth, and this sector continues to play a vital role in their economies on account of inherent and evolving comparative advantage. It is one sector that offers good prospects for diversification away from traditional commodity exports, for entry into the area of manufactures, for absorption of large pools of labor, for crossing the great divide between the rural and urban sectors, and for generating foreign exchange. Also, the economic performance of the sector has important implications for socioeconomic issues such as equitable distribution of income, employment opportunities for women, development of small- and medium-scale enterprises, spillover to the informal sector, integration of remote regions into the global economy, promotion of rural development and poverty alleviation [Hayashi 2005].

Today, clothing industry is providing one of the most basic needs of people and holds importance; maintaining sustained growth for improving quality of life. It is also hard to overstate the significance of the employment and incomes that accrue to female workers, often new entrants to the labor force. Without these jobs, there would be little alternative formal employment of young female workers in manufacturing. The opening of the formerly closed economies of South Asia and the transitional economies of Southeast Asia would not have been as rapid, had it not been for the growth of a strong export-oriented industrial lobby based in the clothing sector.

[10] (2005), "Annual Report," *The Korea Federation of Textile Industries (KOFOTI)*,

It is wrong to think that, in the changing international division of labor that is now under way, all the prizes will go to the developing countries. They, too, have had difficult adjustments to make, especially those which are in the mid-way stage between developing and developed status.

Take the East Asian tigers, Hong Kong, Taiwan and Korea. These countries built up large textile and clothing industries during the 1960s and 1970s, building close relations with customers in the US and to a lesser extent in Europe. Now wage costs are at a level which makes clothing production uneconomic, and companies in these countries have been obliged to shift production to mainland China and other lower-cost locations.

What we are seeing, then, throughout the developed and developing world, is a continuing search by manufacturers of textiles and clothing for the strategy which best suits their circumstances – their history, their acquired capabilities, their domestic market situation. If there is a common theme, it is the importance of focus – doing the things you are best at, and abandoning or outsourcing the things that other people can do better. But these very general prescriptions still leave companies with difficult strategic choices.

There are already signs that, for reasons of cost and convenience, the growing production of clothing in, say, the Czech Republic, is stimulating new investment in fabric in that country. Some observers believe that, although there will continue to be a large number of textile and apparel exporting nations, an increasing share of world trade will be concentrated in the hands of four "mega-powers" – China, India, Mexico and Turkey – which will provide a one-stop service covering all stages in the value chain , from fibers through textiles to clothing. However, because of

fragmentation, small countries that are competitive with low labor costs or highly skilled sewers, and have low trade costs because of smooth customs operations and good infrastructure, are likely to survive and may even thrive in the (almost) quota-free trading environment.

For some Asian countries, the textile and clothing industry has become the leading source of manufactured exports and, indeed, total merchandise exports. Over 80% of the merchandise exports of Cambodia (85%) and Bangladesh (83%) are clothing. For Sri Lanka (55%), Nepal (51%), and Laos People's Democratic Republic (42%), clothing exports are also by far the largest item in merchandise exports. For Pakistan, 70% of merchandise exports are in textiles or clothing [Hayashi, 2005].

3.2. Textile and clothing industry in Uzbekistan and the role of FDI in its development

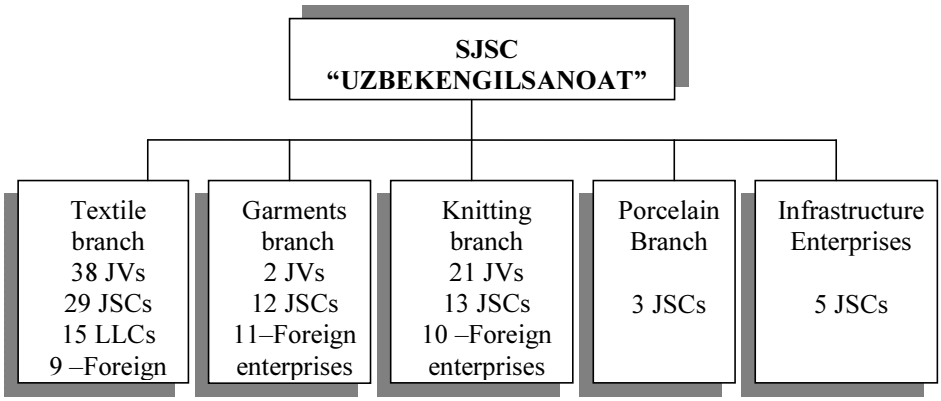
Uzbek textile industry has very deep and rich history. Uzbekistan is well known as a country which lays on the ancient "Silk Road" and famous for its garments throughout the world. During Great Silk Road period, the most expensive fabrics were in high demand in many European and Asian countries. However, Uzbekistan did not develop cotton-processing industry until 1920 and started formation of the industry only during the industrialization period of former USSR. The very first real industrial garment factory was built in Tashkent in 1924. Before World War II, garment factories in Samarqand, Bukhara, Kokand, Tashkent, Urgench and Andijan were put into operation. During and after the war a number of garment factories were built in Chirchik, Karshi, Namangan and Khiva.

Knitting sector started its development in early 1930-40s. During this period, a number of large textile mills were built and produced 80 million square meters of

fabric. Production of cotton fabric increased 89 percent during 1940-1960. Having such a growth rate, Uzbekistan could have become a leading textile manufacturer, but it was decided in the 1960s that Uzbekistan would specialize in cotton growing only. Development of the textile industry had been preserved and constructions of plants were stopped. So the idea of turning Uzbekistan into the textile hub of Soviet Union did not materialize.

However, the situation changed after Uzbekistan gained its independence in 1991. In mid 1990s, Uzbekistan stabilized its macroeconomic situation and began reforms in the textile sector. During these reforms the branches of production of silk and footwear had been separated and the significant part of the Light and Textile Industry enterprises was inherited by the State Joint-Stock Company "Uzbekengilsanoat".

Figure 3: Structure of SJSC "Uzbekengilsanoat"



Source: SJSC "Uzbekengilsanoat"

Alone the period of 1995-2000, 9 large textile mills were built and put into operation. Presently, the Company incorporates more than 133 enterprises of textile,

garments and apparel, and porcelain branches, and over 50 of them are joint and foreign enterprises[11].

Before Uzbekistan gained independence, there was no private ownership and all textile mills were government-owned. Only after 1991, during aforementioned reforms, Uzbekistan began to switch to market economy and allowed the private ownership. Private textile mills began operating after 1995, because private entrepreneurs made up their capital and realized the potential in textile industry. Almost all of the enterprises were privatized and turned into joint stock companies, but the Uzbek government is still the main shareholder. SJSC "Uzbekyengilsanoat" manages all government shares in these textile mills. However, the Uzbek government is trying to continue its privatization process and offering its shares to foreign investors. Presently, Uzbekyengilsanoat is acting on behalf of the Uzbek government and trying to help textile mills induce foreign investors, obtain hard currency from the government, and promote the industry development. It is shifting its role from supervisory functions to industry promotion.

The current share of textile and clothing industry in Uzbekistan though reaching 20 % in the total volume of national industrial production constitutes merely 3.0 % of GDP. Low share of textile industry in GDP results from low share of ready-made production in the sectoral structure that generates value added. Less than a quarter volume produced in the sector is the output of clothing, knitting and hosiery industries. The main volume falls on production of cotton fiber (cotton ginning); that is 1.4-1.5 % of GDP and about 10 % of the total production volume is exported as raw cotton without extra processing (Appendix. Tables A - C). As a result, the main

[11] As of September 1, 2005: total number of enterprises – 133. SJSC "Uzbekengilsanoat" has its share in the charter capital of 40 joint-stock companies, owning from 2,8 up to 25 percents of stocks, and being also the co-founder of a number of joint-ventures in which the foreign investors own the majority of shares. Other 93 enterprises are the associated members of the Company.

share of products made from raw cotton, sold at low prices, is typical for production with low degree of processing.

Table 1. The share of textile industry in GDP

Textile industry	1991	1996	2000	2001	2002	2003	2004	2005
(excluding cotton processing)	8,5	3,6	2,2	2,3	2,4	2,5	2,8	3,0

Under current conditions, substantial share of cotton fiber undermines badly the development of raw material base of national textile industry, thus reducing the amount of ready-made products (cloths), impeding increase of its production volumes and employment generation.

At the same time the positive trends of textile industry growth, the gross output of textile industry in 2005 was 1,7 times higher than in 2000, enabling an increase of industry's input to GDP up to 3,0 percent.

Table 2. Growth rate of textile and clothing industries

(*percentage as to the previous year)*

	2000	**2001**	**2002**	**2003**	**2004**	**2005**
Textile Industry	15,5	12,1	7,7	5,5	3,7	3,5
Clothing Industry	41,9	15,2	32,0	25,8	7,0	13,3

However, due to indirect influence of allied industries on GDP , the gross input of textile industry to GDP in 2005 amounted 7,6 percent.

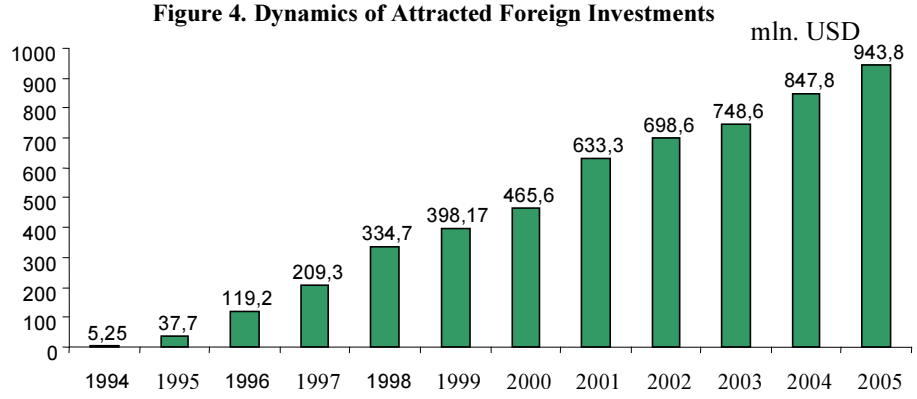
Table 3. Gross input of textile industry in GDP, *(in percents)*

Textile industry influence to GDP	**2000**	**2001**	**2002**	**2003**	**2004**	**2005**
Indirect influence through allied industries:	3,6	2,8	3,8	3,5	4,3	4,7
raw material and equipment supplying industries	2,7	2,9	2,8	2,5	3,1	3,3
textile industry production,	0,9	0,9	1,0	1,0	1,1	1,1

consuming industries						
Direct input of textile industry	2,2	2,3	2,4	2,5	2,8	2,9
Gross input of textile industry in GDP	5,8	6,1	6,1	6,1	7,1	7,6

Foreign investment plays an important role in development of the textile industry in Uzbekistan. The first foreign investment law was adopted in mid-1991 and it was the first step towards foreign contacts promotion. Due to the reasons explained in previous chapter, foreign investment, which moved quite cautiously in the early 1990s, expanded significantly in 1994 and 1995. Starting from this period the volume of foreign investments attracted into the industry has comprised over US $900 million. Most of the investments were directed into modernization and replacing old outdated equipment making the project sizes very large.

Figure 4. Dynamics of Attracted Foreign Investments



Source: SJSC "Uzbekyengilsanoat"

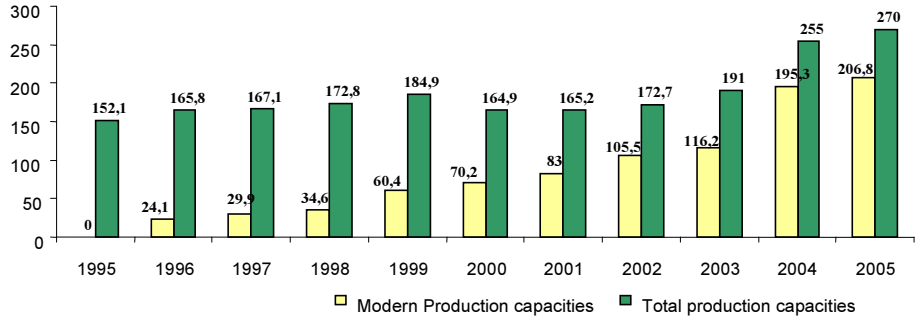
Since 2003 the construction of modern textile complexes including finishing, knitting and garment lines is underway. Projects are mainly implemented at the expense of direct foreign investments[12]. These projects already have allowed to install the significant additional dyeing and finishing capacities (over 40 thousand

[12] More than 60 projects have been implemented and more than 50 joint ventures have been established with the partners from Germany, Switzerland, Japan, Turkey, the USA and other countries.

tonnes) in the Republic, enabling to carry out dyeing and finishing processes in line with the modern requirements for production of qualitative garments and apparel.

The implementation of aforementioned activities, aimed towards domestic textile industry development, resulted in increase of overall cotton fiber processing capacities of the Company for almost 180 percents.

Figure 5. Cotton Fiber Processing Capacities



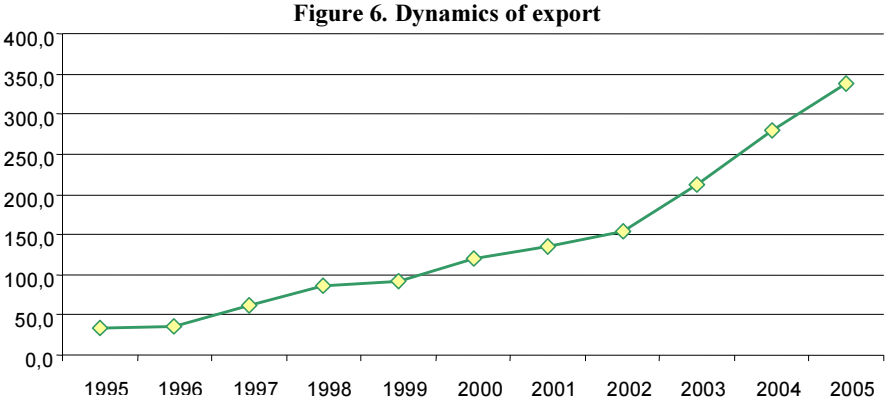
Source: SJSC "Uzbekengilsanoat"

At the same time, the trend shows the continuous increase of the share of up-to-date equipped enterprises. Thus, the number of newly established enterprises with foreign capital, which specialize in processing raw cotton up to finished consumer products has shown a significant increase. In 2003 only two of a number of newly established modern enterprises specialized in manufacturing finished products, in 2004 their number reached seven whereas in 2005 nine enterprises started to operate.

Gradually, with increase of production capacities, the share of domestic processing of cotton fiber has increased from 13 percent in 1994 up to 28 percent in 2005. Comparing to the previous years, when exports of semi-finished textile products, such as yarn and gray fabric, comprised almost 100 percent, the enterprises recently managed to increase the export volume of garments and apparel considerably, the share of which in total amount of exports comprised 12 percent in 2005. Currently over 60 enterprises of SJSC "Uzbekengilsanoat" export their

products in Europe, the USA, Canada, Asia and CIS countries, their number is constantly growing and the volume of exports has shown a significant increase from US $7.7 million to US $338.7 million.

Figure 6. Dynamics of export



Source: SJSC "Uzbekengilsanoat"

In 10 years (1995-2005) alone from the time the first JVs have been put into operation their share of exports in the total amount of actual exports of "Uzbekengilsanoat" has increased from 17 percent up to 85 percent.

At the same time, with the purpose of further development of textile industry, it is expected to conduct a modernization and reconstruction of old enterprises and establish new ones with the complete cycle of production up to finished goods with high added value.

In order to implement this goal, the Cabinet of Ministers of the Republic of Uzbekistan, early in 2005, has adopted the Resolution "On measures for attraction the investments into the textile industry of the Republic". The Resolution approves the State Program on Attraction of Investments into the Textile Industry for the Period of 2005-2008.

The Program embraces 100 projects throughout of the Republic, envisaging the attraction of the investments in amount of US $1.5 billion for modernization, re-

equipment and complete reconstruction of the enterprises, as well as for establishment of new enterprises with a complete production cycle. It is expected that implementation of those projects will produce a gradual increase of the share of domestic processing by the most up-to-date equipment and technologies up to 50 percent of the total volume of cotton fiber grown domestically. In other words, Uzbekistan will double the share of domestically processed fiber against 2005.

Successful implementation of the objectives set in line with the Program on Attraction of Investments will allow domestic enterprises to increase the volume of production and quality of products considerably.

3.3. Clothing industry and market analysis

A. Industry analysis

Attractiveness of Uzbekistan clothing industry for foreign investors is secured by availability of steady and vast stocks of raw materials, specifically, high quality cotton fiber, low costs for energy resources, qualified and relatively inexpensive labor resources, advanced network of communications, developed system of banking and legal services, availability of vast sales markets of textile products and apparel.

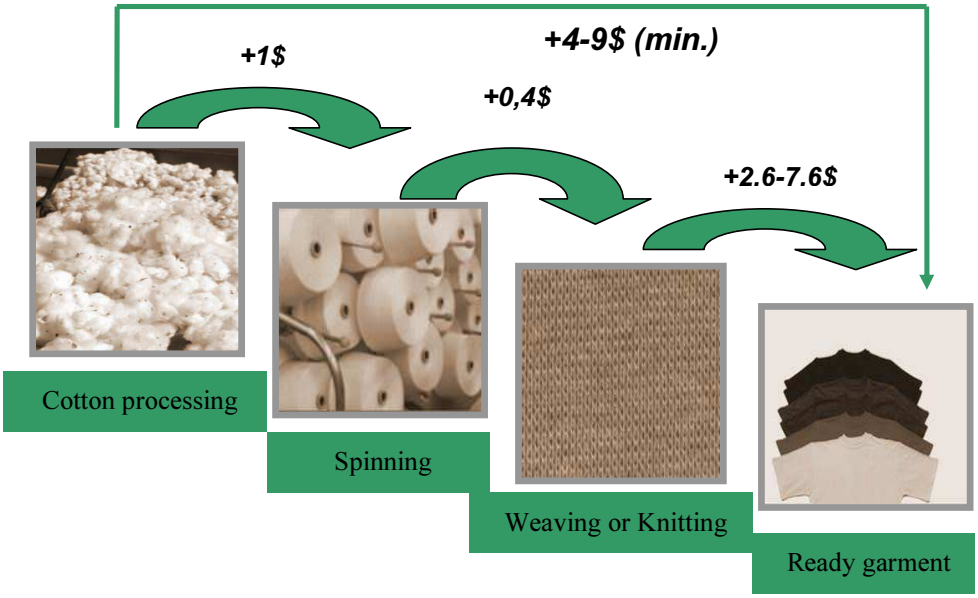
Among other attractive advantages for investors are support and special favorable conditions created by the Government of the Republic. These conditions include stable legal framework for economic activity of enterprises, simplification of procedures of licensing, registration and certification, but primarily, wide range of various privileges, preferences and guarantees for foreign investors, which are secured by the legislation.

According to Decree of the President of the Republic of Uzbekistan dated April 11 2005 for the purpose of the further improvement of investment climate in the country, wide formation of private foreign direct investments, starting from July 1

2005, textile sector enterprises with direct private foreign investments *are exempted from income tax, property tax, tax on development of social infrastructure, ecology tax, single tax for micro-firms and small enterprises, and compulsory payments to the Republican Road Fund*[13].

Moreover, during recent several years, the national legislation regulating activity of foreign investors has been constantly improved to enable maximum attraction of foreign investments into the projects worth deep processing of cotton fiber and fostering domestic production of finished goods. The main reason of this decision can be vividly viewed on the example of one of the Uzbekistan enterprises, where the highest added value is created by processing of the cotton fiber into the finished product.

Figure 7. Created added value by processing cotton fiber into the finished products



[13] Decree of the President of the Republic of Uzbekistan dated April 11, 2005 №UP-3594, "On additional measures on stimulation of attraction of private foreign direct investments"

One of the recent acts of that kind, which lays out a ground for considerable improvement of the investment climate in textile industry, is the above-mentioned Resolution of the Cabinet of Ministers of the Republic of Uzbekistan "On measures for attraction of investments into the textile industry of the Republic" dated January 27th 2005. According to this governmental decision, the enterprises included into the Investment Program are granted a number of additional significant privileges to support the modernization. Moreover, various privileges are prolonged till 2009 for those, specialized in production of garments and hosiery products, and those exporting the major share of produced finished goods, to facilitate the delivery of auxiliary materials and equipment not produced domestically, etc.

Moreover, enterprises, included into the Program and undergoing re-equipment process, are additionally exempted from the payment of customs duties (except for the customs registration fees) on imports of technological and auxiliary equipment, technological accessories and spare parts for industrial needs, subject to results of the expertise to be conducted by the Council under SJSC "Uzbekengilsanoat" for each case. It is expected that this measure of state support will lead to significant reduction of costs.

Enterprises importing chemicals, dyes, accessories and other auxiliary materials not produced domestically are exempted from payment of customs duties for another 4 years due to prolongation of the existing privilege.

A significant benefit is granted to the enterprises with foreign investments when they purchase the main raw material – cotton fiber. Existing legislation provides enterprises a 15 percent discount from the price set at the Liverpool Cotton Exchange and permission to purchase cotton for a hard currency. At the same time, if

enterprises have full production cycle (by processing the entire volume of cotton fiber into the finished goods as an end product) and the export share is not less than 80 percents of the total production, they receive additional 5 percent discount, thus making a total discount equal to 20 percent of the Liverpool price.

Currently, the majority of newly established enterprises producing the finished export-oriented goods are undergoing the process of consumer market formation and establishment of partnership with foreign companies, dealing with retailing of the textile products. With regards to this matter, the provision of an exclusive right to set the maturity date of letter of credit up to 90 days, given that use of such type of payment is confirmed, became an important aspect of financial activity. Taking into consideration relative remoteness of domestic producers from the markets of potential distribution, application of the given privilege enables to simplify significantly and speed up the procedure of payment settlements of the textile enterprises – exporters, as well as to set more flexible terms of shipment for external markets. At the same time, commercial banks of the Republic are recommended to issue the short-term credits (up to 180 days) to the enterprises of the textile industry, including credits in foreign currency, for production and distribution of the export-oriented goods.

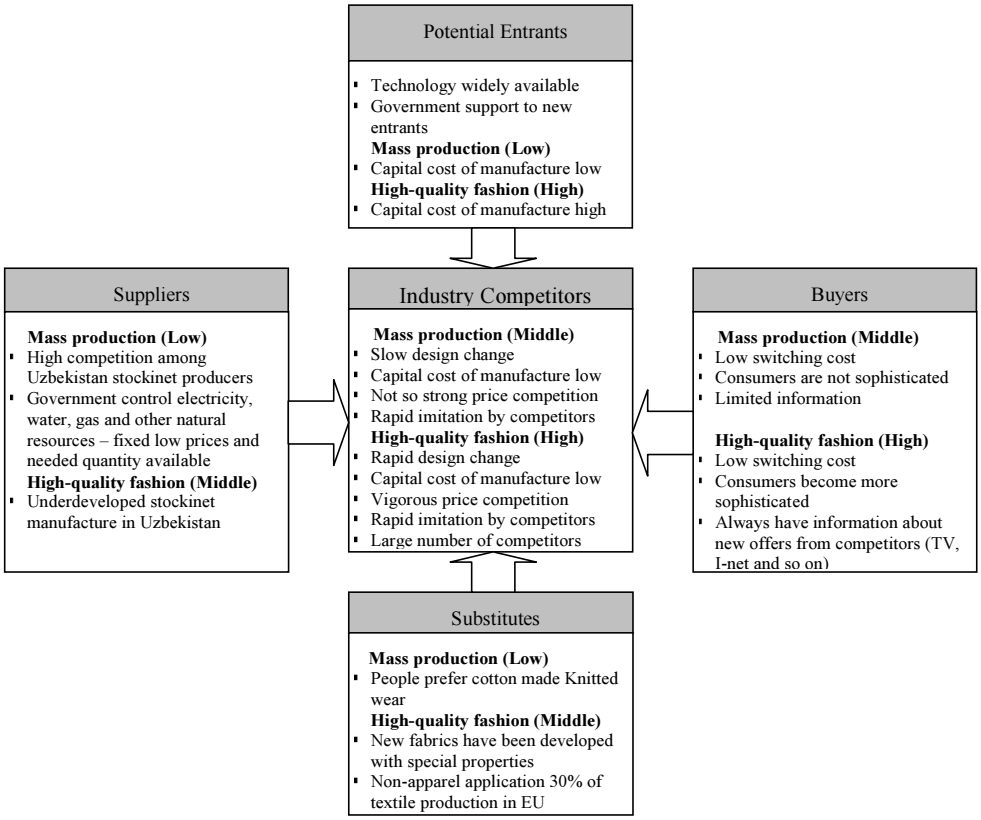
Furthermore, till January 1, 2009, exporter-enterprises enjoy the exclusive right to purchase semi-finished textile products (yarn, fabrics, knitted cloth and cotton-spinning wastes) for hard currency (with zero rate charge of VAT) in the domestic market. This right is considered to be exclusive and exceptional because, according to local legislation, all financial transactions and payments within republic should be made in local currency.

Recent governmental decision determined that sale of cotton fiber to enterprises

with foreign investments is to be conducted with indication of the amount of VAT in the wholesale price, providing reimbursement of the VAT when selling the finished products abroad.

The above-mentioned privileges and other numerous preferences extended to the enterprises in the textile industry and particularly to those implementing deep processing of raw material up to finished products, are aimed at creation of the most favorable conditions for opening the potential of the industry, improvement of its investment climate and ensuring further dynamic growth.

Figure 8. Five Forces Analysis of the Knitted Wear Industry



Industry Competitors.

The clothing sector is at the same time a labor-intensive, low wage industry and a dynamic, innovative sector, depending on which market segments one focuses upon. In the high-quality fashion market modern technology, design, high degree of flexibility, research and development (R&D) are important competitive factors. The high end of the fashion industry uses relatively well-paid human capital intensively in design and marketing. The major players on this market are Turkey, Italy, France, US and others.

The other major market segment is mass production of lower-quality and/or standard products such as T-shirts, uniforms, white underwear etc. Some developing countries in this market have special advantages that set them apart from the competition. For instance, Cambodia has a reputation for good labor standards resulting from its bilateral textile agreement with the United States. Mexico and several African and Caribbean countries also enjoy special trade benefits in the US market.

Uzbekistan enterprises are also currently serving this market and their major competitors on domestic and foreign markets are Turkey, China, India and Pakistan.

Substitute products. On the product side, new fabrics have been developed with special properties, both for apparel and for industrial uses. The effect has been to make the textile industry more research-intensive than in the past, and to create new market opportunities for manufacturers in high-cost countries. What are known as technical textiles, for non-apparel applications, now account for nearly 30 per cent of textile production in the European Union, and the proportion is growing.

Bargaining power of suppliers. Both textiles and clothing are closely related technologically. Textiles provide the major input to the clothing industry, creating vertical linkages between those two ones.

The enterprises united by SJSC "Uzbekengilsanoat", in total have significant capacities for production of wide range of cotton yarn and fabrics. In 1995- 2005 alone, overall cotton fiber processing capacities of the Company's enterprises have increased from 152 thousand tons up to 255 thousand tons.

Despite the obvious progress there is a challenge being faced by Uzbekistan enterprises, serving fashion market. This challenge is due to the relatively high import dependency of ready-made garments and knitted wear on interim goods and accessories**.** Uzbekistan, unlike other competing countries, does not have adequate manufacturing capacities for the production of accessories and modern fabrics for clothing. These deficiencies affect the domestic production of ready-made garments. As a result, both textile enterprises and local population have to rely on imported fabrics for tailoring.

Today, preparation of industrial garment with accessories and ornaments takes 7-10 days in China, India and Turkey, As for Uzbekistan, this process can take up to 20-30 days since local accessories are not available and printing/embroidery consumables are imported mainly from Turkey or the United States. Uzbekistan also depends on imported equipment spares, lubricants and chemicals; a dependency, which causes higher production costs because of current import regulations, transit time, transportation, etc.

Potential Entrants. There are low barriers to entry in the Uzbekistan cotton textiles and clothing sector, whereby many players can enter the sector and strongly threaten the existing players. As for the high end, since investment requirements are

larger and equipment costlier, the sector seems empty, whereas a bulk of the players are in low end products, thus barriers to entry for the industry can be considered to be low.

Bargaining power of buyers. Due to termination of the Multi-fiber Agreement and the consequent cancellation of world quotas, competition in the world market is intensifying. Costs remain the driving factor in the post-quota world but now the advantage will be greater as retailers are bound to raise the bar higher on the responsiveness and flexibility from their suppliers. As a result, only those producers who supply low cost products with high quality could emerge as winners.

The retail market has become more concentrated, leaving more market power to multinational retailers. These ones have market power not only in the consumer market, but perhaps more importantly they have considerable buying power. In addition, high-volume discount chains have developed their own brands and source their clothing directly from the suppliers, whether foreign or local.

Indeed, the retailers in the clothing sector increasingly manage the supply chain of the clothing and textiles sectors. This development probably started with the establishment of shopping malls such as Wal-Mart in the United States in the 1970s. Wal-Mart insisted that suppliers implemented information technologies for exchange of sales data, adopted standards for product labeling and methods of material handling.

Despite the numerous strategic challenges posed by those developments, they also represent opportunities for companies of all sizes in all industries to create new sources of competitive advantage that will enable them to participate in and even to shape how industries evolve in the future. On the other hand, those same challenges also threaten to erode the longstanding competitive advantages of companies that are

either slow to react or unable to mount an effective response. Thus, to survive and prosper in the new millennium, the need to build and sustain competitive advantage will be greater then ever.

B. Market analysis

The world textile and apparel industry encompasses a large number of products and markets. A product-and country-specific competitive assessment may be conducted to evaluate a country's risk exposure, taking into account competitiveness factors such as:

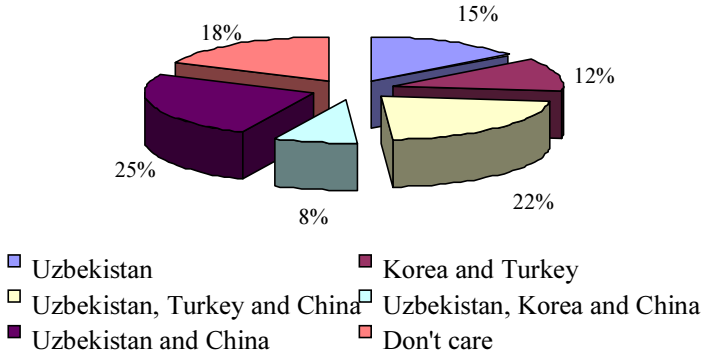
- Preferential trade agreements provided to regional suppliers;
- Wage and non-wage labor costs;
- Labor productivity;
- Infrastructure (access and costs of electricity, water, communications, and local transportation);
- International transportation cost and lead times; (lead time= the amount of time between the placing of an order and the receipt of the goods ordered. A span of time required to perform an activity. In a logistics context, the time between the initiation of a process and its completion).
- Corporate tax rates;
- Customs procedures;
- Access to competitively priced raw materials, yarns, and fabrics;
- Political and economic conditions; and
- Access to foreign capital and management and marketing expertise.

Domestic market analysis through the marketing research

During the last decade several marketing researches have been done in textile garments market. In this paper we would like to stress out the main findings based on relationship between customer satisfaction, behavior and major factors affecting them.

The analyses of preferences of respondents toward country of origin of knitted wear showed that the most popular knitted wear among 15% of respondents is Uzbekistan made. 12% of respondents respond that they usually buy knitted wear from Korea and Turkey. Other 22% prefer knitted wear from China, Turkey and Uzbekistan. 8% buy products manufactured in Uzbekistan, Korea and China, 25% manufactured in Uzbekistan and China, and rest 18% don't care about country of origin at all.

Figure 9. Preferences of consumers in country of origin of knitted wear

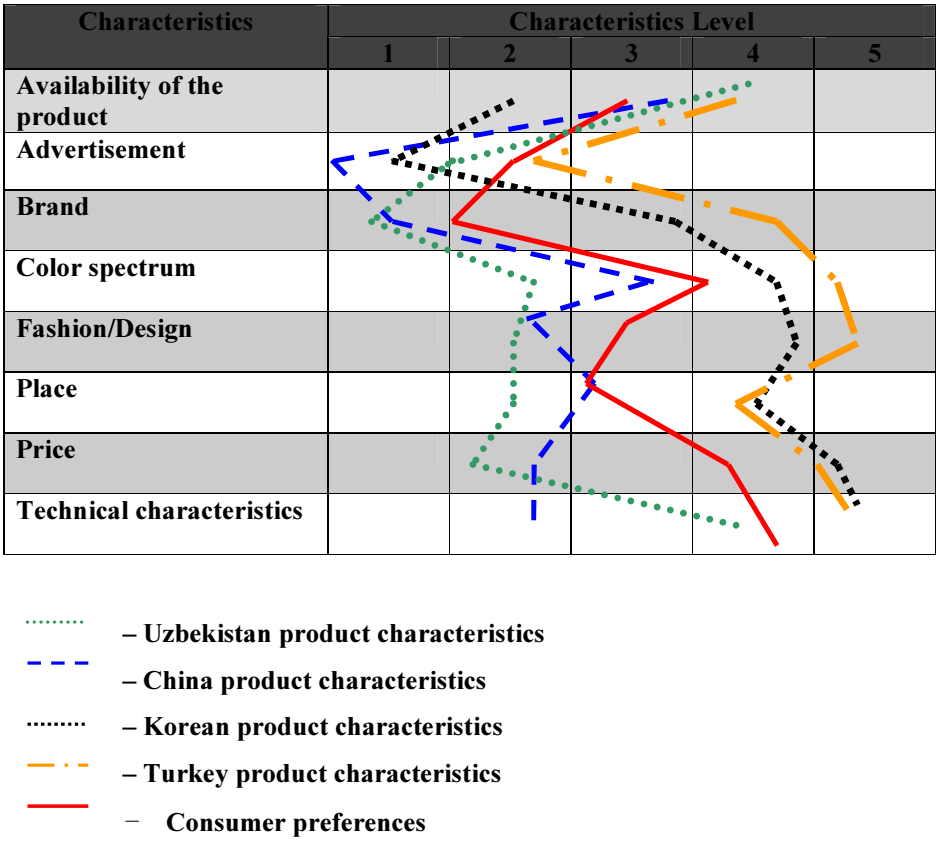


It's obvious that product made in Uzbekistan is already popular in local market segment for low and middle income people, but competitors are very strong, and in order to compete with them successfully manufactures have to know preferences of consumer in product characteristics. In other words they have to know which factors of the product are influencing consumers' purchase behavior, and what consumers thinking about the Uzbekistan product according to those preferences in factors. As survey results show the most important factors for Uzbekistan consumers in the

knitted garment are price, color spectrum and technical characteristics, followed by design, place and brand.

As next step we determined the mean in characteristics of Uzbek, Chinese, Korean and Turkey knitted wear based on summarized opinion of respondents and its combination with preferences in the same characteristics in the following figure.

Figure 10. Comparison of consumer preferences in knitted garment characteristics and their opinion about characteristics of existing on domestic market knitted wear.

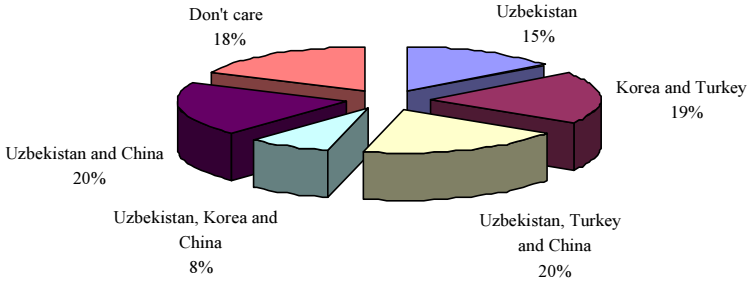


As it is shown on the figure, Uzbekistan products have good technical characteristics, but the color spectrum doesn't meet consumer preferences, and the advertisement activity has to be improved.

Being out of step with global fashion trends is another problem of Uzbekistan textile industry. Due to lack of close contacts with global markets, Uzbek textile manufacturers cannot follow evolving fashion trends and move up the market. They mostly cater to cultural and national traditions of domestic market and can only produce for exports based on disappearing fashions.

One more factor negatively affecting consumer satisfaction is place. In today's contingent economy, some of yesterday's retail stars are dimming while others are burning brighter than ever. According to the conducted research when it comes to buying clothes, 20% of female consumers say they shop at specialty stores, up 5.5 points for the 2000. When men are factored in, the shift is even stronger. Compared with last year, 24% of male respondents, an increase of 6.3 points, say they prefer to shop in specialty stores (8).

Figure 11. Preferences of consumers in country of origin of knitted wear

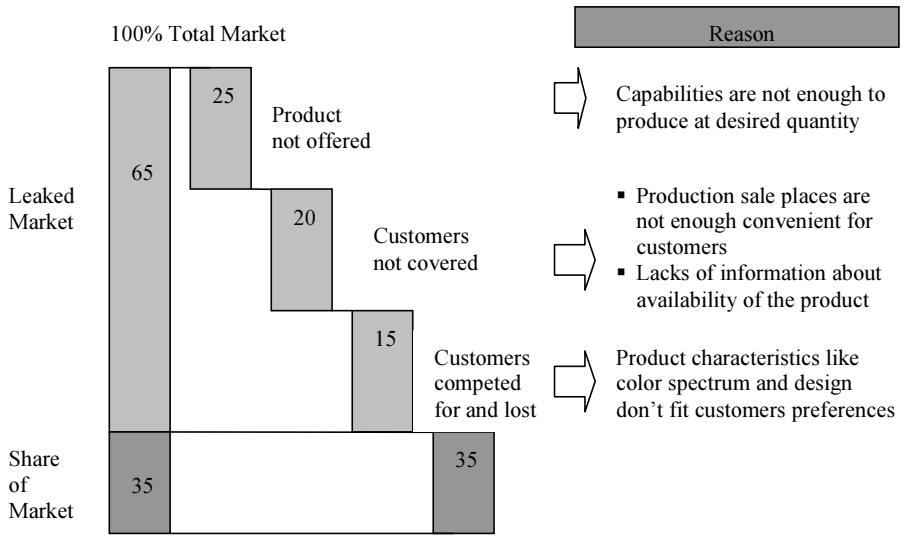


It is obvious that today's consumers are redefining the value to include functionality, as they start asking: "what can the clothing do for me?" Thus, manufacturers, brands, and retailers have come to offer and consumers have come to expect clothing with added functional value. There is one more issue to be mentioned here. Many companies rely on product returns as a proxy for consumer satisfaction. But this feedback, though a helpful indicator, comes after product development

decisions have been made, and usually, after large manufacturing orders already have been placed. Consequently, a question is being raised: does the quality in clothing matter and will consumers pay more for it? Quality in apparel can be defined by the way an item fits, how it is sewn together, how well it launders, or its durability. In essence, quality is in the eye of the beholder. Research on consumer attitudes and shopping behavior indicates that quality is essential in an industry that depends on product styling and quick inventory turns to achieve profitability. Yet the research suggests that while consumers demand a certain standard of quality, they are growing less inclined to pay a premium for it (4).

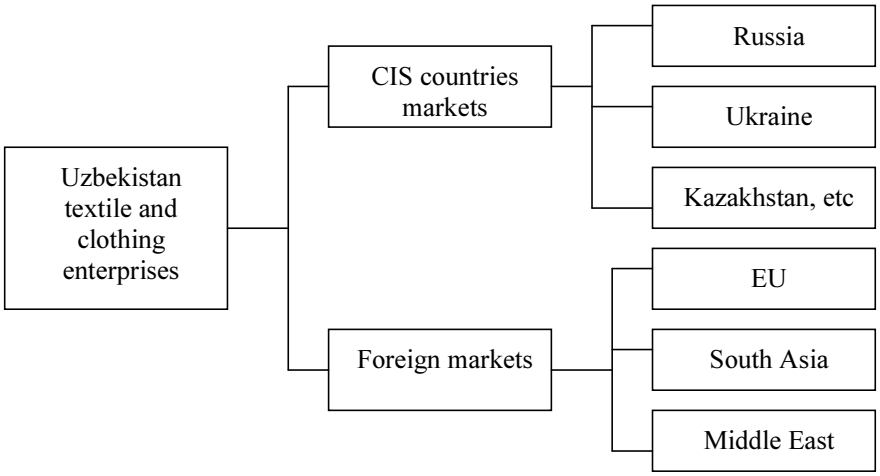
The conventional belief that consumers will pay more for higher-quality apparel is being challenged. Consumers in Uzbekistan have been questioned about their willingness to pay more for higher-quality clothing, and the results have been similar to the trend in apparel prices deflationary. For instance, in 2000, 89% of consumers were willing to pay more for higher quality, compared with 80% today.

Figure 12. Market Leakage Analysis



Foreign market analysis. The main export destinations of Uzbek enterprises can be conventionally split into the following: (I) exports into the foreign countries and (II) export into the Commonwealth of Independent States (CIS) countries. Exports to the foreign countries, in turn, can be divided into the following three regional markets.

Figure 13. Main export destinations of Uzbekistan enterprises



First – Western markets are the exports-oriented towards the countries of the European Union, whose share accounts for 25.6% of exports into the foreign countries, and 17.8% of total exports of the republic.

This market is characterized by high solvent demand, but at the same time the countries of this region themselves have a well-developed production and retail systems of various textile and clothing products, in a number of cases being the leaders in technical equipment and trendsetters. Even though requirements for qualitative features of products, orientation to consumer demand, following trends in this market along with price indicators (flexibility) seems to be the most important factors of success.

Even though Uzbekistan has some advantages (refer to next chapter), domestic producers will face the following problems and challenges:

− Large share of transport costs due to non-existence of direct access to maritime ports;

− High technical requirements for trade in European Union (requirements for quality, certification of products, labeling, package of goods, complexity of procedures of access to market, non-existence of direct contacts with minor wholesale consumers).

This sets the current composition of exports to Western markets. These are mainly raw materials, including cotton fiber, yarn, and fabrics. The ratio of ready-made product exports is not large.

Second – Asian markets including the countries of South Asia, namely Japan, South Korea, China, India, Vietnam, Malaysia, Singapore, whose share accounts for 10% of exports to the foreign countries, and 6.8% of the total exports of the Republic.

This group of countries represents rapidly developing economies featured by the aspiration to their due place in the world market of goods. Competitive advantages of these countries include their geographic location on the crossroads of trade routes, high potential demand for the goods by the virtue of the number of their population, low labor costs, and development of new manufactures on these underpinning by bringing in foreign investments.

The most promising of them is the export of raw commodities and materials, as it is actually recorded in the statistics. Compared with Western markets, composition of Uzbek exports is represented in a greater variety in the Asian markets. This includes cotton fiber, silk, yarn, fabric and other textile products.

Trade and exports to these markets could be diversified. Uzbek companies could compete with the products of these countries in cost and quality indicators, yet large transportation element in the cost of goods make the delivery to these countries practically non-competitive. Besides, if raw materials are purchased from Uzbek exporters by partners from these countries, then the enterprises of the Republic do not have sufficient skills in independent advancement of a wide nomenclature of products.

Certain difficulties are caused by language barrier, mentality, weak knowledge of institutional-legal aspects of market access.

Third – Southern markets, including Near and Middle East, like Iran, Israel, Turkey, Afghanistan, United Arab Emirates, Saudi Arabia and Egypt, being the group of countries, account for the largest share in the exports of Uzbekistan – 21.6% of exports into the foreign countries and 16.1% of the total exports of the republic.

Southern markets demand the great diversity of the textile goods made in Uzbekistan. Along with raw materials, semi-processed and ready-made goods are also supplied to these countries. These include cotton fiber, yarn, fabric and other textile products.

Afghanistan market is very promising for the textile industry of Uzbekistan. However, the advancement of Uzbek goods is restrained by the absence of effective transport communications. Access to southern ports through Iran may completely change the composition of exports into the countries of the South, as well as of the East Asia, and Southeast Asia enables to take advantage of the full investment potential of Asian international financial institutions, financial resources of UAE and Saudi Arabia, technologies of Israel, industrial products of China, Turkey, and other countries.

The serious obstacles are faced by Uzbek exporters to enter the market of the non-WTO member-countries, such as Iran, where regulatory functions are implemented primarily not by tariffs but by the system of taxes, permits, and percentage rates of bank financing.

The factors affecting exports certainly include the aspiration of the countries to protect their markets and support domestic producers as well as rather high level of current tariffs. Uzbek producers have to compete with countries that enjoy favorable trade agreements with duty-free or low-duty export of their goods to the largest markets of Europe and USA[14]. For Uzbekistan's exports to such markets, custom duties constitute 14-18% of the amount of contracts. Cotton yarn, fabrics, ready-made garments and knit-wear exported by Uzbekistan to the EU, for example, suffer from customs duty at 4.2%, 8.4%, 9.6% of the total cost, respectively [UNDP 2006]. On the other hand, imports from some countries, such as Turkey, Syria, Egypt, Nigeria and Pakistan, are free of duty[15]. Ray (2006) states, that in India, average rate of the current tariffs is 15-25 %, whereas in Egypt, according to Australian Government Department of foreign affairs and trade (2005), it's over 25%, in Vietnam [VietNamNet Bridge 2006] – 12-20 %, and in Korea - 12%.

The analysis of geographic distribution of exports shows that the CIS countries account for 31.5%, including more than 95% to Russia, Ukraine, Kazakhstan, Tajikistan, Turkmenistan, Azerbaijan, and Belarus.

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[14] Thanks to North American Free Trade Agreement, Mexico has duty-free export to American market. Hence the ready-made garments from this country have prevailed over Chinese goods. Due to Caribbean Initiative and Trade Preference Act the same advantages have been granted to Dominican Republic, Salvador, Guatemala, Honduras, Jamaica, Bolivia, Ecuador, and Peru.

[15] According to so-called Lom Conventions (the first one was signed in 1975) almost all goods from seventy countries of Africa, the Caribbean and the Pacific were granted duty-free access to EU markets. The same agreements have been signed with 12 Mediterranean countries. EU Commission has also stated about a set of trade preferences for Pakistan.

A distinct feature of the exports in this direction is also the most diverse composition of deliveries, which includes virtually entire range of Uzbek exports. Along with raw materials (cotton), semi-processed and ready-made goods are also supplied to these countries. These include cotton fiber, yarn, and fabric and other textile and clothing products.

This is facilitated by technological compatibility, similar requirements for quality, production cooperation, and collaboration of enterprises in the production of goods and services, long-term trade and partnership ties, established itineraries and schemes for delivery of goods, well-developed scheme of forwarding and banking services.

Competition is beefing up the requirements for the goods of CIS markets as well. Currently foreign trade operations between the CIS countries are carried out in the free trade regime when the goods originating from CIS countries and delivered thereto are not subject to tariff policies.

Figure 14. SWOT Analysis of Uzbekistan textile enterprises in domestic and foreign Market

	Domestic market	**Foreign markets**	**CIS countries markets**
Strengths	▪ low cost and high quality product ▪ government support ▪ growing popularity of Uzbek product	▪ low cost and high quality product ▪ already developed retail chain by many Joint Ventures	▪ low cost and high quality product ▪ technological compatibility ▪ similar requirements for quality ▪ production cooperation, and collaboration of enterprises in the production of goods and services ▪ long-term trade and partnership ties ▪ well-developed scheme of forwarding and banking services ▪ free trade regime
Weaknesses	▪ weak distribution	▪ language barrier	▪ weak distribution

	chain ▪ existing capabilities are not enough to satisfy market demand	▪ mentality ▪ weak knowledge of institutional-legal aspects of market access ▪ high level of current tariffs	chain ▪ existing capabilities and technology are not enough to satisfy market demand ▪ underdeveloped stockinet manufacture for fashion market
Opportunities	▪ growth in market demand ▪ growth in population income	▪ high solvent demand	▪ high solvent demand
Threats	▪ growing competition ▪ most of current favorable conditions created by the GOU (exemption from tax and duty payments) are expiring in 2011 ▪ New entrants to the industry	▪ most countries themselves have a well-developed production and retail systems of various clothing products ▪ growing technical requirements for trade (especially in EU) ▪ large share of transport cost ▪ growing competition from the countries enjoying FTA with duty free or low-duty export ▪ development of substitute products ▪ increase in tariff rates	▪ growing competition from China, India and Turkey ▪ countries may start their own manufactures ▪ existing free trade regime may disappear ▪ growth in high fashion market with rapid design change

IV. Assessment of Uzbekistan Textile Competitive Advantages in Internal and External Markets

4.1. Factors Influencing Competitive Advantage in Textile and Clothing Sectors

It is very difficult to derive a certain conclusion about competitive advantage of any country in textile and clothing industry in comparison with others. Such advantage depends on many factors, but the most important among them are the

economic environment, the structure and managerial skills of enterprises, the costs of production, the quality of products, the efficiency of marketing, flexibility of manufactures. The main determinant of economic environment is the overall infrastructure of a country (public policies, administration, human resources, banking, transportation, industrial structure, etc) and it differs in each country, in accordance with its development level. For example, efficient transport infrastructure, reliable and competitive modes of transport and efficient customs procedures for maintaining a competitive edge in the highly competitive textile and clothing markets are very important. The reliability of transportation infrastructure and efficiency in customs procedures complements each other in minimizing transit periods for shipments involved in international trade and can make geographically remote locations more internationally competitive. Even if long transit periods can be overcome to some extent by preferential market access arrangements, long transit periods can essentially eliminate from international competition the offshore centers that are either geographically remote from the buyer's markets or nearby centers with poor transportation infrastructure. The countries with a well established and smoothly functioning system in all these areas can easily gain comparative advantage over other countries as it leads to more efficient production. Industries in countries with open markets are regularly more used to international competition, and therefore more competitive, than in those countries protecting their industries against imports. But the competitiveness of an industry can also be affected by exchange rate changes, which may not have been caused by anything to do with this particular sector [CRPM 2005].

The structure of enterprises and their managerial skills not only vary among different countries, but also within one country. While in the traditional textile and

clothing producing countries where exists a full chain of textile and clothing production (fibers, yarn, fabric, finishing, made-ups, clothing, and accessories), production in many developing countries is very much concentrated on a few products only, and raw materials have to be imported. Such kind of cases can be found in most African countries, in Latin America, and sometimes also in Asia (for example Bangladesh and the Philippines). Great importance also applies to the existence of a textile machinery industry in the same country. The advantages of regional proximity and close cooperation in the development of modern technology and machinery for the production of textiles and clothing seem to be evident. Managerial skills of enterprises are primarily based on individual capacities and, therefore, vary even among companies within one country. This contributes to the development and existence of companies with different competitiveness in the various markets. The level of skills in a country is, however, also an expression of the management culture, more or less advanced in the different countries. The comparative advantage of developing countries in the assembly process, i.e. the sewing process, based on low wages, does not necessarily transfer into a comparative advantage in the management of the entire supply chain when all services- related dimensions are taken into consideration. Efficiency in managing the entire supply chain is required, including in design, fabric procurement, and logistical skills in transportation, quality control, and property rights protection, export financing and clearing of trade formalities. The danger is that badly running businesses will perish before they have a chance to prosper. Mr. Goodstone reckons that without better bosses, the mass-produced garment business in Central Europe will be "dead in five to ten years"[16]. The new trend in Central Europe is for investment by firms from

[16] Washington Post, "China ready to Take On All Competitors and Markets"

other outsourcing locations in places such as China, India and Turkey. Firms there are eager to gain an edge on their rivals by moving closer to the customer. Turkish entrepreneurs, for example, have bought textile factories in neighboring Romania, Uzbekistan and Kazakhstan, installing new management there. That takes advantage of local labor costs, and brings big productivity gains.

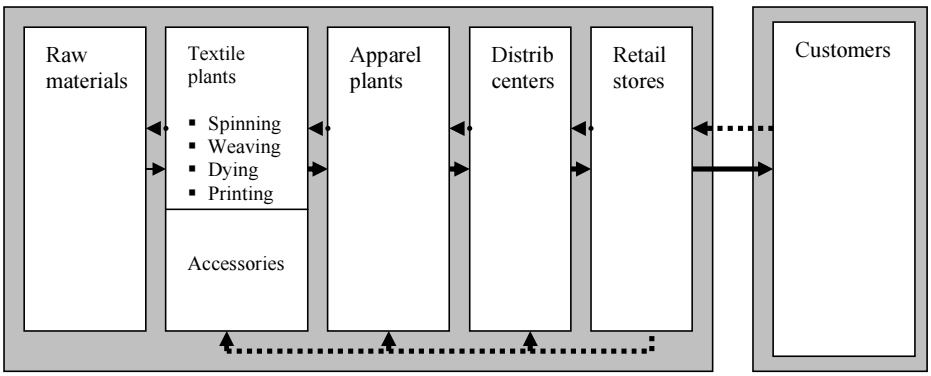
As the clothing sector productivity highly depends on a high input of labor, labor costs represent the most important cost factor in this case. Design and quality of products are other factors which are influencing competitive advantage of the sector. As in the case of production technology, where a continuous process of innovation and modernization takes place at all levels and in most countries, same in this field, permanent upgrading is essential for achieving, maintaining and improving competitiveness. There are large differences in levels of design abilities, product innovation, product quality, and the share of branded products, between European producers of textiles and clothing and those in most developing countries. But much progress has been made in recent years, particularly in the advanced export oriented developing countries such as Hong Kong, South Korea and Taiwan. As upgrading and innovation of processes, materials and final products have been developed as a basic instrument for the EU industry to remain competitive, so this is also true - albeit at a lower level - for developing countries. Recent reports talk of the efforts of clothing producers, for example in Bangladesh and Thailand, to move steadily toward high-value, sophisticated items, such as high-quality suits, jackets, branded jeans items etc.

Recently not less important factor of comparative advantage became the development of efficiency in the marketing of products. Already, most developing export oriented countries have to make efforts to find markets for their products.

Waiting for customers to come is no longer sufficient to increase exports. Marketing strategies have to be developed and applied, if the industry of a country wants to survive the more intense competition of the future. Experience in this field of most developing export oriented countries including Uzbekistan is rather limited.

The textiles and clothing sectors can be seen as a supply chain consisting of a number of discrete activities. Increasingly the supply chain from sourcing of raw materials via design and production to distribution and marketing is being organized as an integrated production network where the production is sliced into specialized activities and each activity is located where it can contribute the most to the value of the end product.

Figure 15. The supply chain in textile and clothing industry



Source: Nordås H.K.,(2004) *The Global Textile and Clothing Industry post the Agreement on Textiles and Clothing,* WTO, Geneva, Switzerland

When the location decision of each activity is being made, costs, quality, reliability of delivery, access to quality inputs and transport and transaction costs are important variables. The supply chain in the textile and clothing sector is illustrated by Figure 1. The dotted lines represent the flow of information, while the solid lines represent the flow of goods. The direction of the arrows indicates a demand-pull-

driven system. The information flow starts with the customer and forms the basis of what is being produced and when. It is also worth noticing that information flows directly from the retailers to the textile plants in many cases. The textile sector produces for the clothing sector and for household use. In the former case there is direct communication between retailers and textile mills when decisions are made on patterns, colors and material. In the second case textile mills often deliver household appliances directly to the retailers.

4.2. Analysis of Competitive Advantages of Major Countries Competing with Uzbek Textile Manufacturers on Domestic and the World Market

Quota protection, under Multi Fiber Arrangement (MFA), predictably discouraged its beneficiaries in both developed and developing countries from improving their competitiveness. The chickens of their inattention have come home to roost, as many now see their market shares being gobbled up: China's share of the US$350 billion global textile market is expected to rise from its current 20 percent to a maximum of 60 percent in the coming years.

Predictably, a protectionist outcry has arisen against the one exporting country that has done everything necessary to be competitive and no longer dependent on low wages or quota protection. Today, China finds itself the target of post-quota protectionist efforts in countries - developing as well as developed - whose governments and industries failed to prepare for post-quota market challenges. Renewed protection will only perpetuate dependence on unsustainable market interventions - at the expense of both consumers (who must pay higher prices) and workers (whose wages and productivity are lower, and job fewer).

China's competitive advantage resides principally with its cheap labor, but this is by no means the country's sole strong point. Though China's labor certainly is cheap compared to developed countries', wages have been rising rapidly. Labor shortages have appeared as economic growth spreads prosperity; many workers are returning to their countryside homes as farm incomes rise. Wage rates (and overall labor costs) in clothing industry are already significantly higher in China than in Vietnam, Cambodia, Bangladesh, India, Sri Lanka, and Indonesia.

The Chinese textile industry's competitive advantages lie elsewhere. First, Chinese workers are much more productive, probably because they are better-educated, better-motivated, and have better health status, given the legacies of the socialist state. Second, Chinese factories benefit from economies of scale, given the large production base and domestic market afforded by the country's huge population. Third, China's large, diverse, and increasingly integrated industrial base means that many materials required to make clothing are locally available, avoiding the added costs, risks, and longer delivery lead-times that imported inputs impose on other countries. Fourth, China's geographical location, close to Japan, South Korea, Taiwan, and Hong Kong, allows it to readily import advanced equipment and high-tech textiles for its finishing industries. Fifth, the predominantly Hong Kong- and Taiwan-based manufacturers in the global industry may have language and cultural advantages managing Chinese workers, and thus may be willing to invest more in China. Sixth, China has also invested heavily in its physical infrastructure, allowing speed of delivery of both imports and exports. (China's currency, pegged to a now-declining US dollar, is not a significant factor in its cost competitiveness; the undervalued Yuan raises the cost of imported inputs, on which manufacturers rely heavily [Lim 2005]).

Another competitor of Uzbekistan in textile market is India, which according to India Brand Equity Foundation (IBEF) report contributes about 25 per cent share in the world trade of cotton yarn. Being one of the largest exporters of yarns in international market, India accounts for 22 per cent of the world installed capacity of spindles. Its textile industry contributes about 22 per cent to the world spindleage and about 6 per cent to the world rotor capacity installed. It has second highest spindleage in the world after China with an installed capacity of 38.60 million [IBEF 2006].

India has a natural competitive advantage in terms of a strong and large multi-fiber base, abundant cheap skilled labor and presence across the entire value chain of the industry ranging from spinning, weaving, and made-ups to manufacturers of garments. India's textile industry comprises mostly small-scale, non-integrated spinning, weaving, finishing and apparel-making enterprises.

Another competitive advantage of India is ability to contribute to the design, not only in preparing samples and prototypes, but also in translating concepts into varieties of finished designs, as well as introducing designs of their own. Several Indian firms have their own design departments and in the last five years have begun to work closely with overseas designers and/or agents. It is estimated that increased specialization in higher value-added goods contributed to a 46% rise in Indian cotton-made exports to the US in 2003. Survival depends on efficiency, flexibility and responsiveness [Soko].

The Indian textile engineering industry, which is able to produce at competitive prices sophisticated machines of higher speed and production capability, gives Indian textile manufactures one more competitive advantage.

In fact, in the last six years, an estimated US$ 6.7 billion has been invested in the textiles sector, aided by the Technology Upgradation Fund (TUF) scheme. The TUF

scheme expires in March this year (2007) and the quotas on China will be lifted in 2008. Hence, companies will continue to add capacities over this year. Also, according to CRISIL, the sector is likely to rise over US$ 3.5 billion from the capital markets in the next few years[17].

In addition to this, Indian industry has consistently remained flexible in terms of production quantity and lead time. While typical production runs are governed by fabric color minimums, India presents the possibility of producing quantities as low as to a few hundred pieces. According to Devangshu (2003), this capability is especially critical in an unpredictable market where retailers and brands are looking to source ever-smaller quantities of product, increasingly closer to the season.

The dominant markets for India's textile and apparel exports are the US and EU, which together accounted for nearly 87 percents of exports in 2005.

Notwithstanding their strong competitive advantages, China and India first have to tackle their internal problems if they are to take full advantage of the post-MFA milieu. For all its much-vaunted economic success, China remains saddled with serious problems - closed financial markets, massive bad debts, an underdeveloped service sector, little transparency and pressing problems of rural poverty - that pose significant economic risks. Al-though Indian textile exports could grow by more than 15% now that quota restrictions have expired, translating this potential into reality will depend on whether New Delhi has the political will to accelerate economic reforms, especially the removal of barriers that dissuade foreign direct investment and smother competition.

Pakistan is one more competitor of Uzbekistan. For the last 59 years, Pakistan has used its low-cost labor as a competitive advantage in textile industry and was

[17] http://www.crisil.com

considered as the best in terms of cost-vs-quality equation. But recently this competitive advantage has been taken over by countries like China, Bangladesh and Sri Lanka that are not the best cotton-producing nations, but, as in the case of Bangladesh, buy cotton from Pakistan and convert it into value-added products at a lower cost than its competitors [Abbas 2006]. Thus, if the cost advantage is no longer there, what other competitive advantage Pakistan has?

A producer of cotton and man-made fiber and the largest yarn exporter in the world, Pakistan has a strong and modern weaving industry and a fledgling processing and apparel sector. It also has in place the kind of vertically integrated supply chain that will be an essential ingredient to success in the post-quota world. Having invested more than US $5 billion in upgrading existing plants, and adding new capacities and new products, Pakistan's textile industry believes it has now the necessary scale and product quality to compete with the countries like China and India[18].

Diverse geography and strategic location vs. Uzbekistan is one more competitive advantage of Pakistan.

Turkey, another contender in the textiles market, is focusing on producing high value-added products and becoming a leader in the field of fashion and design. Turkey regards itself as having competitive advantages in fashion, design and production quality, and is proud of its prompt production and delivery times.

Two segments dominate Turkey's textile and clothing industry:

- The spinners and weavers that use high quality domestic raw materials to produce textiles. These firms keep market standards high with original designs.

[18] (2005) Material wealth, http://www.fdimagazine.com/news/fullstory.php/aid/1141

- Apparel manufacturers, which use a combination of domestic and imported cloth to produce finished non-branded goods. These include non-branded firms who market their products through 3rd party retail chains. Non-branded products currently make up the majority of the industry's domestic and export sales.

As regards the technology level of the industry, textiles and clothing industry is an outward-oriented industry, using modern technology, and competing in the export markets. The main reason behind the good performance of the textile and clothing industry is the increase in modern machinery imports and new investments in recent years. It has a powerful and diversified textile machinery base, a developed finishing industry with some 400 finishing entities equipped with modern facilities, existence of developed side industries with 115 zippers, 300 buttons and metal accessories, 10 hangings, 100 labels, 8 stiffening materials, 50-60 quilted materials and 10 fiber companies. The Turkish clothing industry consists of over 40,000 establishments, most of which are small. 1,000 out of the 40,000 companies accounted for 50-60% of the market. Most of these companies have their own brands and in-house designers[19].

Many of Turkey's leading manufacturers maintain top global reputations. To maintain this quality, well-known local brands, such as Beymen and Vakko, train their design staff in European fashion capitals. This facilitates exports and also allows apparel firms to directly compete in the domestic market against foreign brands.

As the crossroads of Europe and Asia, Turkey is not only a local player of the clothing and textile industry, but also the main domain of supply for Russia and Caucasian region countries - Middle East - North Africa region and the Central Asian republics. But the main export market is still remains EU, followed by the US. According to government data, 63.7% of the country's total textile and clothing

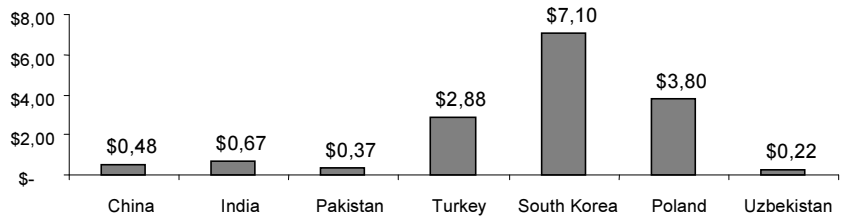
exports are to the EU and 11.6% are to the US market. Within next 10 years, Turkey expects the Chinese market to be as important as the US, EU and Japanese markets to Turkish textile exporters[20].

4.3. Analysis of Competitive Advantages of Uzbekistan Textile and Clothing Industry

Textile and garment suppliers from Uzbekistan have the advantages as well as disadvantages on the market. The main advantage is an existence of raw material base in Uzbekistan, especially high quality cotton, which gives an opportunity for further development and expansion of textile manufacture. Uzbekistan produces more than 1 million tons of cotton fiber per year, but only a fraction of that is used by domestic textile enterprises. Closeness of raw materials sharply reduces transport costs and time for delivery to enterprises.

Not less important advantage Uzbekistan has in labor cost, which is also cheaper than in such rival countries as Pakistan 1.6 times, India 3 times, China 2.1 times, Turkey 10 times and South Korea 32 times.

Figure 16. Clothing Industry Labor Cost Comparison (as of 2004)



Note: Labor costs in Europe comprise around 21-35$/hour, in the USA – around 16$.
Source: 2004 data from http://www.wernertex.com/

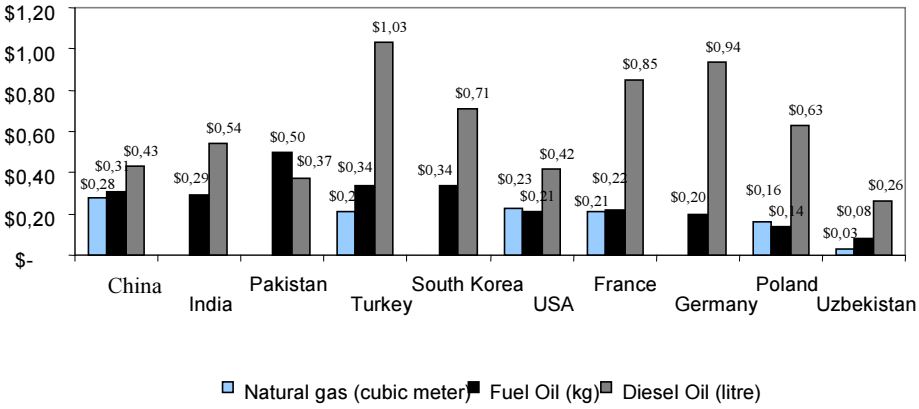
[19] Textile and clothing sector, http://www.turkey-now.org/db/Docs/A-%20Textile%20May%202006.pdf

According to US Department of State (2005), literacy rate in Uzbekistan is almost universal at 98 percent, and workers are generally well educated and trained. Even most local technical and managerial training does not meet international business standards, but foreign companies engaged in production report that Uzbek workers learn quickly and work effectively. Foreign firms find that younger Uzbeks, untainted by the Soviet system, work well at all levels.

Besides it, as Uzbekistan has lease crude and natural gas, it has some advantage in resource cost over rival countries as China and Turkey. For example, 1 cubic meter of natural gas in Uzbekistan costs US $0.03. In Turkey, France and USA it is between US $0.21 and US $0.23, while in China the cost is US $0.28.

A kilogram of fuel oil in Uzbekistan costs US $0.08, while in China, India, Turkey, South Korea the cost is between US $0.29-0.34, in the US $0.20, in Western Europe US $0.23 and in Pakistan US $0.50.

Figure 17. Energy Cost Comparison (as of 2004)

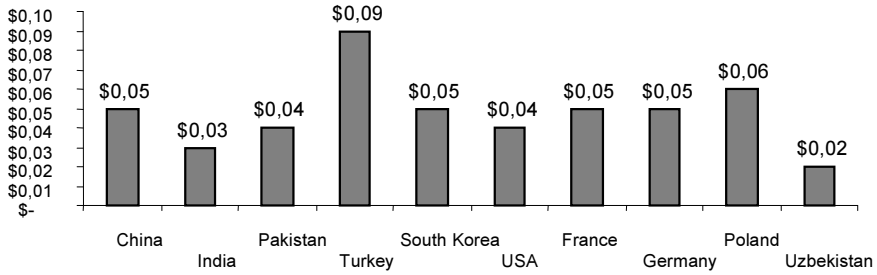


Note: Data on natural gas in India, Pakistan, Korea and Germany is not available
Source: International Energy Agency "Key energy statistics 2004"

[20] (2005), Turkey changes tack, *http://www.fdimagazine.com*

The cost of electricity in competing countries varies from US $0.03 to US $0.09 per kWh while in Uzbekistan it is US $0.03.

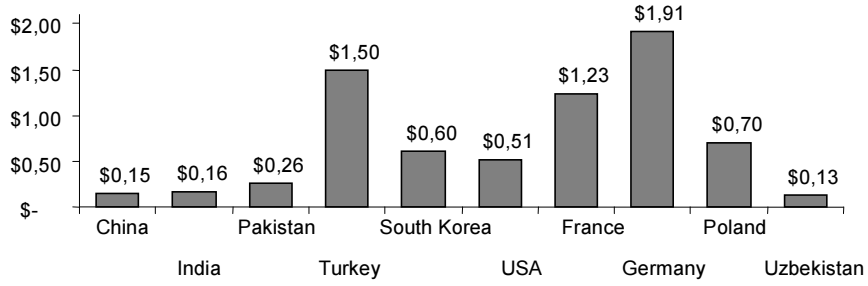
Figure 18. Electricity Cost Comparison (as of 2004)



Source: International Energy Agency "Key energy statistics 2004"

The cost of water in Uzbekistan for industrial needs constitutes US $0.13 per cubic meter, while in China it is US $0.15, in India US $0.16, in Pakistan US $0.26, in USA US $0.51, South Korea US $0.60, Turkey US $1.50, Western Europe US $1.23-1.91. While the water use in textile industry is not so large, low water price still provides some additional competitive advantages to the industry.

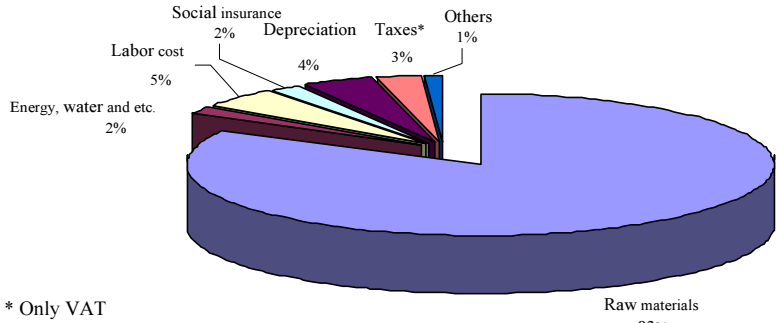
Figure 19. Water Cost Comparison (as of 2004)



Source: International Energy Agency "Key energy statistics 2004"

All above mentioned cost advantages give an opportunity to Uzbek enterprises to decrease their operating expenses and thus increase their profits.

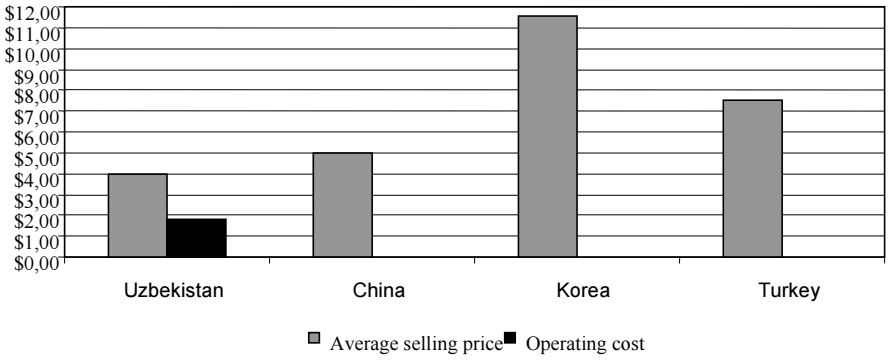
Figure 20. Average expenses on Knitted wear manufacture in Uzbekistan



* Only VAT

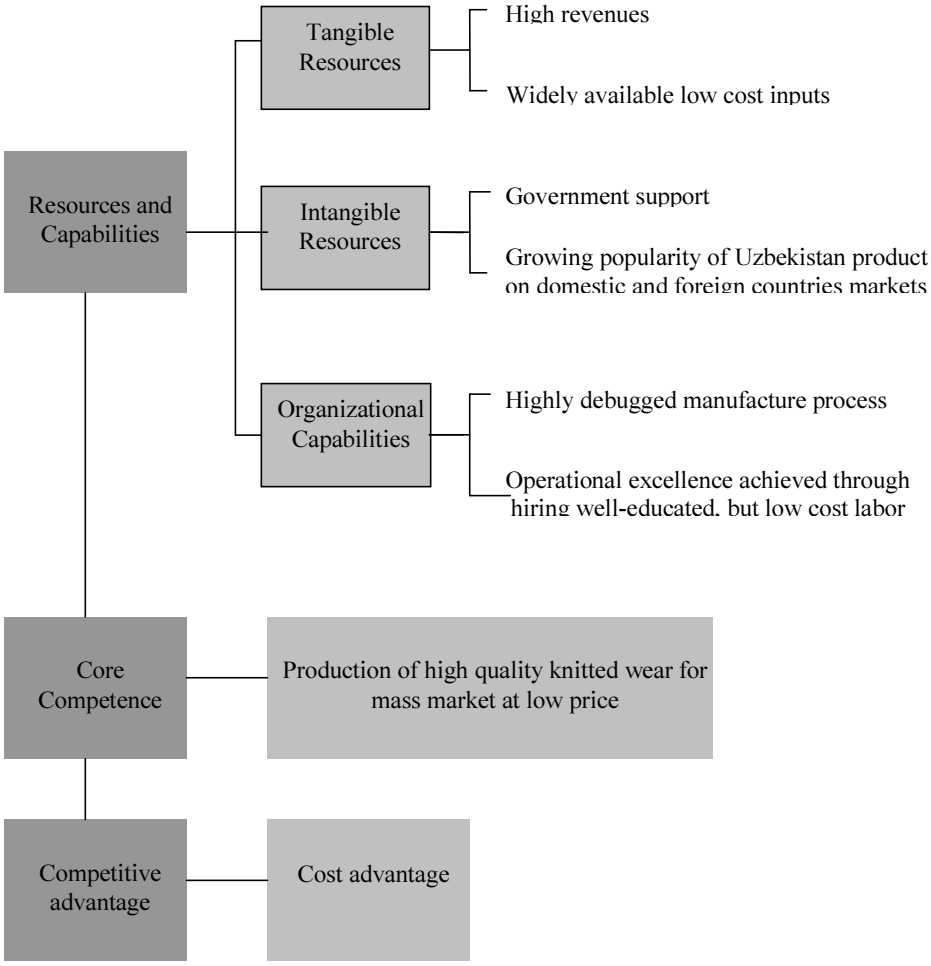
Source: SJSC "Uzbekengilsanoat"

Figure 21. Knitted wear average selling price and operating cost in Uzbekistan



All those facts allow us to state that the Uzbekistan enterprises have cost competitive advantage.

Figure 22. The foundation of competitive advantage of Uzbek clothing industry



V. Summary and Policy Recommendations

Uzbekistan, which has a population of around 26 million and largest consumer market in Central Asia, is the world's sixth largest cotton producer and second largest cotton exporter after the United States. Currently, the share of textile industry though reaching 20 % in the total volume of national industrial production constitutes merely 3.0 % of GDP. Low share of textile industry in GDP results from low share of ready-

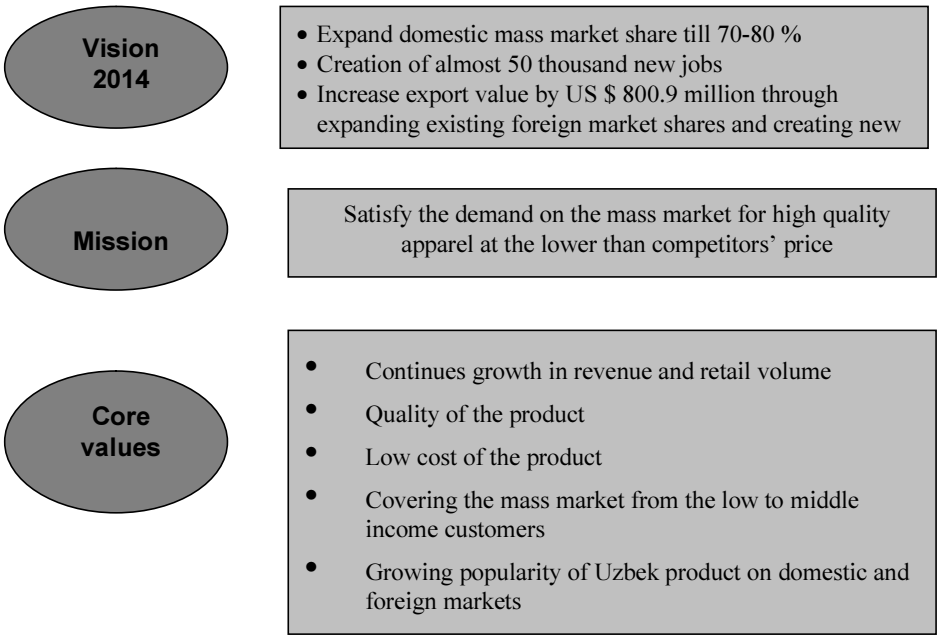
made production in the sectoral structure that generates value added. Less than a quarter volume produced in the sector is the output of clothing, knitting and hosiery industries. The main volume falls on production of cotton fiber (cotton ginning); that is 1.4-1.5 % of GDP and about 10 % of the total production volume is exported as raw cotton without extra processing. As a result, the main share of products made from raw cotton sold at low prices is typical for production with low degree of processing.

Under current conditions substantial share of cotton fiber undermines badly the development of raw material base of national textile industry, thus reducing the amount of ready-made products, impeding increase of its production volumes and employment generation. As recognition of the importance of this sector, for the first time a separate Policy Statement was made with regard to development of textile sector.

The main objective of the textile policy 2000 became cloth provision of acceptable quality at reasonable prices for the vast majority of the population of the country, to increasingly contribute to the provision of sustainable employment and the economic growth of the nation; and to compete with confidence for an increasing share of the global market.

In order to successfully achieve aforementioned objectives SJSC "Uzbekengilsanoat" has to have a clear strategy. But given the large number of possible strategies, it is hard to come up with general rules about what companies should do, or what they should have done in the past. Management gurus often emphasize that companies, in making strategic decisions, are constrained by their earlier history.

Figure 23. Mission, Vision and Core Values of apparel enterprises united by SJSC "Uzbekengilsanoat"



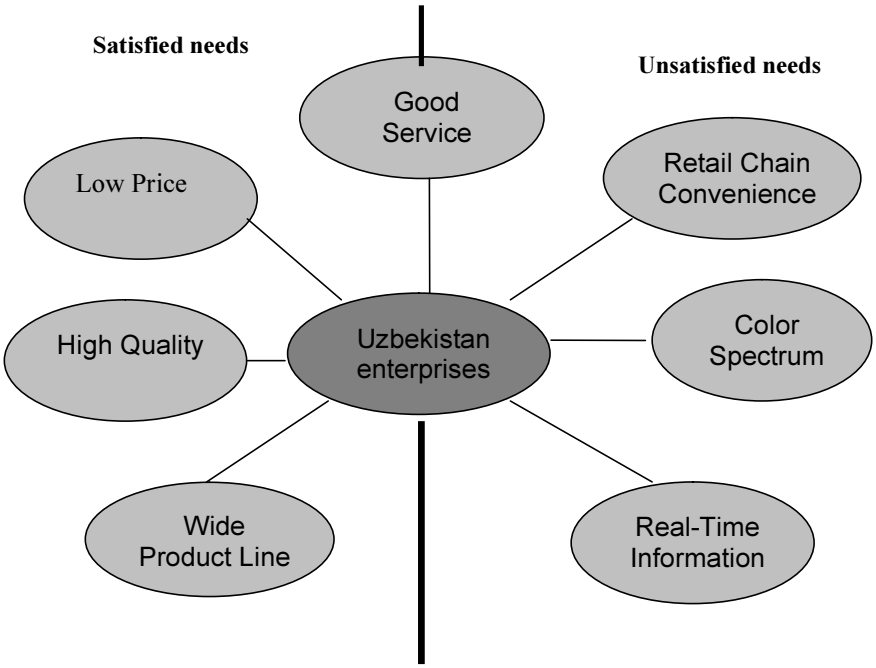
1. Expand domestic mass market share till 70-80 %

First of all Uzbekistan enterprises have to overcome the existing on the market gap between their product characteristics and consumers preferences and try to satisfy consumers need.

Retail Chain. Every enterprise has to identify its potential customers and their preferences towards the shopping places and then:

1. Open own brand/specialty shop (Low prices for Real Estate in Uzbekistan)
2. Distribute through most preferable department stores, supermarkets and so on

Figure 24. Needs of Uzbek knitted wear consumers



Apparel color spectrum can be improved through:

1. Conducting marketing research
2. Recruiting young graduates from Tashkent Textile and Light Industry Institute (design faculty), who have talent, modern views, open mind and much more lower demand for salary than foreign designers

Real time information. As conducted research showed, customers don't have enough information about products made in Uzbekistan (product line, sale places, price and so on). That's why it's necessary for enterprises to:

1. Create their own website
2. Set up cooperation among enterprises with support of SJSC "Uzbekengilsanoat" in creation common trade portal
3. Advertise sale places and product line through TV, Radio, Journals or Billboards (Advertisement costs are not expensive in Uzbekistan)

2. Increase export value by US $ 800.9 million through expanding existing foreign market shares and creating new

In order to successfully achieve this goal and sustain its longer-term competitiveness, Uzbekistan needs to complement its cluster of expertise in manufacturing by developing its expertise in the value-added service segments of the supply chain such as sourcing or retail distribution. To pursue these avenues, Government of Uzbekistan needs to place greater emphasis on investment in infrastructure, particularly transportation and logistics, and on training workers to reduce turnaround time and improve labor productivity. Further more, improving quality, developing industry expertise and linkages to global buyers, and attracting international investors will broaden it export markets, providing access to scale economies.

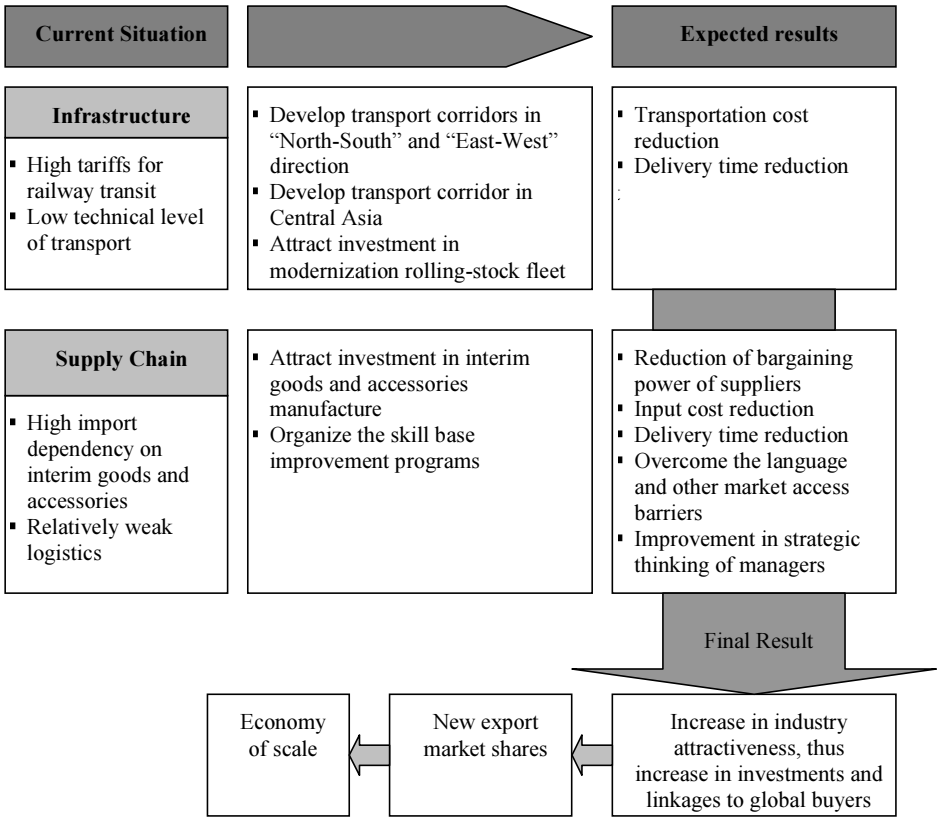
Investment in infrastructure.

Geographical location of the Republic of Uzbekistan and neighboring countries does not provide them with open access to the World Ocean, thus considerably complicating the problem of integration into the world economy. Existing transport corridors in Central Asian region due to poor technical equipping and lack of coordinated among neighboring countries mechanisms of legal regulation within single transport area complicate goods supply due to baffling complexity of mixed transportation, reloading and necessity to shift carriage wheel set, thus resulting in considerable increase of transportation and attendant costs. Therefore the most urgent issue lies in creation of alternative transport corridors.

Significant transportation costs, due to relatively high tariffs for railway transit as well as the need of transit through third countries serve as additional factor for

reduction of potential competitive advantages of domestic goods at the time of their delivery to the markets of Russia, Ukraine, Azerbaijan, and Belarus.

Figure 22. Export oriented Apparel industry strategy development



During the course of its history the region has been developing due to transit operations acting as a bridge between Europe and Asia. Hence stabilization in Afghanistan ensures new opportunities for approaching the world markets making the region more attractive for developing transport corridors in "North-South" and "East-West" direction.

In this regard CA countries should formulate (perhaps within the framework of CACO transport consortium) a long-term strategy of development of transport corridor in Central Asia. The strategy implementation may assume the following:

- concordance of normative-legal basis of CA countries on international communications and goods transportation and bringing them in line with international trade and transit agreements and conventions;
- creating conditions for common market of transport and forwarding services;
- encouraging development of multilateral regional and international investment projects of regional and international significance;
- implementation of projects in the area of developing transport corridor through Afghanistan.

Technical level of transport development is far behind the international standards by technical, economic and ecological parameters. Rolling-stock fleet structure is far beyond the requirements of national economy and population. The structure of cargo transportation means due to specific specialization cannot allow broad introduction of high performance transportation technology prevailing in foreign countries based on utilization of progressive high-speed container and contrail transportation.

China has already created a world class export infrastructure. Given the volume of projections for exports by Uzbekistan, it may be necessary to create additional export infrastructure, especially investment for modernization rolling-stock fleet.

Further development of supply chain

Logistics and supply chain would also play a crucial role as timely delivery would be an important requirement for success in international trade. The logistics

and supply chain management of Uzbekistan textile firms are relatively weak and need improvement and efficiency.

Interim goods and accessories manufacture development. Currently Uzbekistan, unlike other competing countries, does not have adequate manufacturing capacities for the production of clothing accessories. These deficiencies affect the domestic production of ready-made garments. The development of industry can be done through attracting investments in creation joint ventures on existing base (installing new technologies on existing factories) or building new plants (100 percent foreign investments).

To attract investors Government of Uzbekistan has to play a supporting role in establishing a coherent policy and regulatory framework. The objective of this framework should be to strengthen the capacity of the private sector to deal with rapid change and growing competition, and to capture the trade opportunities that are being created through improved market access. This process involves dismantling trade-distorting production measures, improving the regulatory environment on essential business services, supporting the emergence of qualified pools of expertise and the adaptability of the workforce, negotiating improved market access for textile and clothing products, and eliminating the obstacles of the establishment of retail distribution systems. Moreover, government should keep in mind that in the long run innovative capacities basically depend on the availability of suitable human resources. Therefore, a sound education and qualification system seems much more important for sustainable technical progress than public innovation programs. This applies not only to textiles and clothing, but to any other industry.

Skills Base Improvement. The strategic skills of management on many enterprises have to be improved by training existing executives or by allowing new

blood to take command. Tasks like motivation building, development of new skills in logistics, exports (international experience), human resources management, networking or partnership building have to be an integral part of modern management.

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Appendix

Table A. World Cotton Production

(Millions of 480-lb. bales)

Country	1999/ 00	% Share	2000/01	% Share	2001/02	% Share	2002/03	% Share	2003/04	% Share	2004/ 05	% Share	2005/06	% Share	2006/07 October	% Share
China	17.6	*20.1*	20.3	*22.9*	24.4	*24.7*	22.6	*25.6*	22.3	*23.4*	29.0	*24.1*	26.2	*22.9*	29.0	*25.0*
United States	17.0	*19.4*	17.2	*19.4*	20.3	*20.5*	17.2	*19.5*	18.3	*19.2*	23.3	*19.4*	23.9	*20.9*	20.7	*17.8*
India	12.2	*13.9*	10.9	*12.3*	12.3	*12.4*	10.6	*12.0*	13.8	*14.5*	19.0	*15.8*	19.2	*16.8*	21.0	*18.1*
Pakistan	8.6	*9.8*	8.2	*9.2*	8.3	*8.4*	7.8	*8.8*	7.8	*8.2*	11.1	*9.2*	9.9	*8.7*	10.1	*8.7*
Brazil	3.2	*3.7*	4.3	*4.8*	3.5	*3.5*	3.9	*4.4*	6.0	*6.3*	5.9	*4.9*	4.7	*4.1*	5.3	*4.6*
African Franc Zone	3.9	*4.5*	3.2	*3.6*	4.5	*4.6*	4.1	*4.6*	4.4	*4.6*	5.0	*4.2*	4.2	*3.7*	4.4	*3.8*
Uzbekistan	5.2	*5.9*	4.4	*5.0*	4.9	*5.0*	4.6	*5.2*	4.1	*4.3*	5.2	*4.3*	5.6	*4.9*	5.5	*4.7*
Turkey	3.6	*4.1*	3.6	*4.1*	4.0	*4.0*	4.2	*4.8*	4.1	*4.3*	4.2	*3.5*	3.6	*3.2*	4.3	*3.7*
Australia	3.5	*4.0*	3.7	*4.2*	3.3	*3.3*	1.7	*1.9*	1.7	*1.8*	3.0	*2.5*	2.8	*2.5*	2.2	*1.9*
European Union	2.6	*3.0*	2.5	*2.8*	2.6	*2.6*	2.2	*2.5*	2.0	*2.1*	2.3	*1.9*	2.5	*2.2*	2.3	*2.0*
Syria	1.5	*1.7*	1.7	*1.9*	1.7	*1.7*	1.1	*1.2*	1.3	*1.4*	1.6	*1.3*	1.5	*1.3*	1.5	*1.3*
Egypt	1.1	*1.3*	0.9	*1.0*	1.4	*1.4*	1.3	*1.5*	0.9	*0.9*	1.3	*1.1*	0.9	*0.8*	1.0	*0.9*
Turkmenistan	1.1	*1.3*	0.8	*0.9*	0.9	*0.9*	0.7	*0.8*	0.9	*0.9*	0.9	*0.7*	1.0	*0.9*	1.0	*0.9*
Tajikistan	0.5	*0.6*	0.5	*0.6*	0.7	*0.7*	0.7	*0.8*	0.8	*0.8*	0.8	*0.7*	0.6	*0.5*	0.7	*0.6*
Kazakhstan	0.3	*0.3*	0.4	*0.5*	0.6	*0.6*	0.5	*0.6*	0.6	*0.6*	0.7	*0.6*	0.7	*0.6*	0.7	*0.6*
Others	5.9	*6.7*	6.2	*7.0*	5.4	*5.5*	5.1	*5.8*	6.2	*6.5*	7.0	*5.8*	7.0	*6.1*	6.7	*5.8*
World Total	**87.6**		**88.8**		**98.8**		**88.3**		**95.1**		**120.3**		**114.2**		**116.2**	

Source : US Cotton Market Monthly Economic letter October'2006

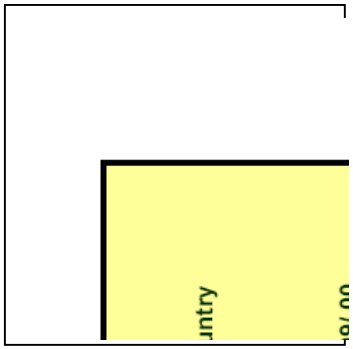

Table C. Global Trade of the Cotton Market (Thousand Tons), 1960-2002

	1960	*1970*	*1980*	*1990*	*1998*	*1999*	*2000*	*2001*	*2002*
EXPORTS									
USA	1,444	848	1,290	1,697	915	1,481	1,470	2,134	2,056
Uzbekistan[21]	381	553	616	397	900	900	820	718	717
Australia	0	4	53	329	650	710	720	650	609
Greece	33	0	13	86	320	294	293	257	249
Mali	2	19	35	114	216	201	125	126	221
Syria	97	134	71	91	210	180	245	220	171
Benin	1	14	8	58	119	151	131	132	164
Burkina Faso	0	9	22	73	117	106	107	127	154
Tajikistan[a]	na	na	na	200	90	83	110	120	147
Cote d'Ivoire	0	7	42	81	130	160	150	115	137
Zimbabwe	0	32	55	38	89	121	128	67	105
World	**3,667**	**3,875**	**4,414**	**5,081**	**5,274**	**6,054**	**5,875**	**6,167**	**6,377**
IMPORTS									
Indonesia	7	36	106	324	500	455	520	559	537
India	204	155	0	0	136	200	340	425	509
China	65	108	773	480	78	30	52	102	400
Turkey	0	1	0	46	250	459	285	385	358

[21] Uzbekistan, Tajikistan, and Russia refer to USSR prior to and including 1990

Thailand	4	46	86	354	271	302	360	387	356
Mexico	0	1	0	43	302	436	473	396	352
Russia[a]	0	238	28	37	179	284	325	341	338
Italy	218	178	193	336	330	365	310	323	315
Korea, Rep.	51	121	332	447	330	350	315	318	298
Japan	800	796	697	634	270	276	242	247	240
Pakistan	1	1	1	0	192	103	101	280	224
Taiwan	47	160	214	358	293	322	269	225	214
Brazil	0	4	2	108	296	340	131	57	200
World	**3,804**	**4,086**	**4,555**	**5,222**	**5,429**	**5,811**	**5,875**	**6,167**	**6,377**

Source: ICAC, *Cotton: Review of the World Situation*, various issues