China loses its competitive edge in clothing
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China is losing its competitive edge in textiles and clothing, according to a new report by Textiles Intelligence. Not only is it facing mounting costs on several fronts, but new sources of supply in Bangladesh, Cambodia and Vietnam mean many buyers will not return to China when safeguard quotas are removed at the end of this year.

In the first quarter of 2008 alone, US apparel imports from China declined by nearly 10% compared with the corresponding period of 2007, reaching US$4.43bn. In terms of China's currency, the renminbi, the fall was an even greater 17%.

China's drop in competitiveness stems from mounting costs on several fronts.

Apart from higher costs of energy and raw materials – which manufacturers face all over the world – Chinese textile mills face greater costs in having to comply with growing environmental legislation.

At the same time, Chinese apparel factories are having to cope with new regulations on working conditions.

Furthermore, firms wishing to invest are finding it harder to obtain finance as the Chinese authorities have tightened credit in a bid to limit inflation.

On top, Chinese exporters have been hit by lower export tax rebates.

Labour costs have become a particularly serious issue for Chinese firms. At least seven major exporting countries in Asia can now offer lower labour costs than China.

Apparel exporters in Vietnam and Pakistan are able to benefit from labour costs as low as US$0.38 and US$0.37 an hour, respectively, whereas China's labour costs can reach US$1.08 an hour in certain areas of the country's coastal provinces.

In Cambodia, labour costs are only US$0.33 an hour, and in Bangladesh they are as low as US$0.22 an hour.

Victim of its own success
In many ways, China has become a victim of its own success. Rising wages have been a direct consequence of the economic boom in the country, especially in coastal regions where it is easier to export goods to the world's major markets.

The boom has also led to upward pressure on China's currency, the renminbi.

Although the Chinese authorities have not taken the risk of allowing the currency to float freely, they have accepted that it is not possible to keep a lid on it.

On 21 July 2005, they unpegged the renminbi from the US dollar and since then its value has been allowed to increase by about one fifth. As a result, the US market has become less lucrative for Chinese suppliers.

The fall in competitiveness of Chinese apparel exporters could not have come at a worse time.

Their problems have been compounded by poor economic conditions in the US market where the sub-prime lending crisis has had a knock-on effect on the housing market, on consumer confidence and on the economy as a whole.

During the first quarter of 2008, US consumer expenditures on clothing and footwear (on an annualised basis) were 0.2% lower than in the first quarter of 2007 – after growing by 3.7% in 2007, 4.5% in 2006 and 5.1% in 2005.

Vietnam benefiting

One of the main beneficiaries of the drop in US imports from China is Vietnam.
In the first quarter of 2008, sales of Vietnamese apparel in the US market were up by over 30% compared with the corresponding period of 2007. As a result, Vietnam increased its share of the US import market significantly during that period.

Chinese exporters will probably enjoy a brief resurgence in the US market in the first quarter of 2009, after safeguard quotas have been removed by the US authorities at midnight on 31 December 2008.

Admittedly, the quotas affect only 34 product categories but many of these products sell in large volumes and China has proved in the past that it is particularly good at supplying them.

Undoubtedly, many US buyers will return to China when the quotas have been removed.
But a number have built up new sources of supply in Bangladesh, Cambodia and Vietnam while US quotas have been in place.

Having forged new relationships and partnerships, they may prefer to stay where they are – especially if the renminbi looks set to escalate further and the escalation in Chinese costs shows no signs of easing.