Box 8

POSSIBLE IMPACT OF THE REMOVAL OF TRADE QUOTAS FOR TEXTILES AND CLOTHING

In January 2005 all remaining quota restrictions on the global trade in textiles and clothing will be eliminated. This represents the last, but most significant, stage of the gradual phasing-out of these quotas carried out over the last ten years. In the euro area, the removal of trade quotas may be expected to result in lower consumer prices for textiles and clothing, and a decrease in production and employment in these sectors. Although quantifying the precise impact is difficult, on balance the gains from lower prices, higher efficiency and increased trade volumes are expected to outweigh the negative adjustment effects on production and employment in these sectors brought about by trade liberalisation. This box considers what is likely to happen when trade restrictions are removed, the factors that may determine the scale of the impact and the lessons to be learned from other countries which have already removed trade restrictions.

Over the last 50 years international trade in textiles and clothing has been restricted by a combination of quota, tariff and non-tariff barriers. A succession of agreements, ending with the Multi-Fibre Arrangement (MFA), has placed quotas or quantity restrictions on trade in textiles and clothing. The impact of quotas on trade is particularly undesirable, as it increases prices for consumers and results in the inefficient allocation and fragmentation of production across countries. However, the Uruguay Round of trade negotiations (concluded in 1994) paved the way for the elimination of quota restrictions with the adoption of the Agreement on Textiles and Clothing (ATC). Under the ATC, existing quotas were to be phased out in four stages over a ten-year period, with the last 49% of quotas due to be removed by January 2005 (see table below).

Table Removal of volume restrictions on trade in textiles and clothing

Date	Percentage share of initial quota levels to be eliminated	Accumulated percentage of initial quota levels eliminated
January 1995	16	16
January 1998	17	33
January 2002	18	51
January 2005	49	100

Source: H. Nordås. "The global textile and clothing industry post the Agreement on Textiles and Clothing", WTO Discussion Paper No 5, 2004.

Clothing plays an important role in consumer price developments, as it accounts for approximately 6% of the overall HICP. The external dimension is also important, as approximately 25% of domestic demand for clothing is met by imports from outside the euro area. As regards employment and output, although the significance of the textiles and clothing sectors has been declining over the last few decades, these sectors currently account for approximately 10% of manufacturing employment and 6% of manufacturing output.

Thus, the removal of these quotas could have a number of important consequences for the euro area. First, there should be some downward pressure on consumer prices. This is because lower-cost producers, whose access to the euro area market was previously restricted, could obtain a larger share. Total production costs should also be driven down, as production processes, which were previously fragmented, should become more efficient. Second, there may be some adverse impact on output and employment in the textiles and clothing sectors. However, as producers have had ten years to prepare for the removal of quotas, this impact should be attenuated.

However, quantifying the impact of the removal of trade quotas is difficult for a number of reasons. On the one hand, although over 50% of quotas should already have been eliminated prior to 2005, it appears that the phasing-out of quotas was effectively backloaded, with less sensitive quotas being eliminated first. This means that the impact from eliminating the remaining quotas could be proportionately larger. On the other hand, the fact that the phasing-out has been gradual should mean that it has, at least in part, already been factored into investment decisions, although the entry of China to the World Trade Organisation may increase imports from Asia. Moreover, the European Commission has recently proposed seven actions to enhance the competitiveness of the European textiles industry. These include boosting research and development and training, ensuring open markets and stepping up the fight against counterfeiting.[1] In spite of these measures, net trade (exports minus imports) is likely to continue to decline. Other factors having an impact on the likely effect of the removal of quotas include the fact that tariffs will remain in place and that, although quotas are to be removed, safeguard measures may still be applied under specific circumstances. Furthermore, it is not known a priori to what extent and how quickly retailers will pass on their lower costs to consumer prices. Data show that historically there is some correlation, with a lag, between import unit values and the subsequent impact on consumer prices. Looking ahead, import price decreases brought about by the removal of quotas should be regarded as permanent and should lead to a higher pass-through than in the case of temporary import price movements.

Evidence from other countries which have already liberalised trade in textiles and clothing indicates that, while there has generally been a significant impact on both prices and trade, the pattern and extent of the impact has been different across countries, possibly reflecting different market forces. In Norway, which reduced tariffs as well as eliminating quotas, there was a significant decline of 16% in consumer clothing prices between 1995 and 2001.[2] In Sweden, which eliminated quotas on textile and clothing imports in 1991 but had to reintroduce them prior to entry into the EU in 1995, there was a marked increase in imports from China. Although there was little visible impact on consumer prices, this might be linked to changes in the Swedish tax system and the depreciation of the krona, both of which occurred at around the same time. In Australia, which dismantled quotas in 1992-93 and reduced tariffs over the period 1992-2005, there was an increase in imports which was larger than the decrease in domestic output, although consumer prices remained fairly stable.[3]

In conclusion, the elimination of quota restrictions on textiles and clothing presents opportunities and challenges for the textiles and clothing industry, retailers and consumers. Although the precise effects are difficult to quantify, the ending of restrictions should result in significant net benefits for the euro area, mainly via downward pressure on consumer prices. Furthermore, these gains are likely to be maximised in markets characterised by a high degree of competition, underscoring the need for ongoing product market reform.

1 Commission Communication of 13 October 2004 entitled “Textiles and clothing after 2005 – Recommendations of the High Level Group for textiles and clothing”.
2 For a further discussion of this point, see the box entitled “Why have clothing prices fallen?” in Norges Bank’s Inflation Report 2/2002.
3 “Study on the implications of the 2005 trade liberalisation in the textile and clothing sector”, IFM and Partners, February 2004.