# THE ROAD TO 2025

5 market, trade and investment trends that will define the course of global textile and apparel industry

TEXTILE AND APPAREL SECTOR REPORT BY

wazir ADVISORS

# Content



**AUTHORS:**
Varun Vaid, Associate Director | varun@wazir.in
Kanika Abrol, Consultant | kanika@wazir.in

# Introduction

In 2013, we published the first version of this report which was very well received by the sector stakeholders across the globe. Three years later, we are now publishing this revised version revisiting our earlier hypotheses in light of recent developments, and the feedback that we have been receiving continuously till date. The present report is not only an update of facts and figures but also a thorough review of each of the trends. We have replaced two of the previously predicted trends with new ones which we feel will be more significant for the global textile and apparel sector by 2025.

The macroeconomic trends since last report have not changed significantly. The economical, technological, social and political landscape continue to make an irreversible impact on business operations globally. Phase out of Multi-Fiber Arrangement (MFA) in 2005 still remains the landmark event for textile and apparel sector which had far reaching impact. Asian countries like China, Bangladesh, Vietnam, India, etc. are expanding their global market shares at the expense of high cost nations like Italy, Spain, Mexico, Portugal, etc. The potential of China and India as super consumers is very well accepted as reflected from the strategies of large international manufacturers, brands and retailers to penetrate these countries.

The first and foremost prediction for 2025 is that the **global apparel consumption will become US$ 2.6 trillion from a present level of US$ 1.7 trillion**. This means a market addition of US$ 900 bn. over next 10 years which presents a huge business opportunity for sector players. Majority of this market addition is expected to happen in China and India.

In contrast, the apparel consumption in USA and Europe will rise at a much slower rate. The differential growth between today's largest markets and largest developing ones will lead to the second trend where it is projected that the **domestic market of China & India will be a big opportunity for investment and growth**.

In China, domestic demand growth will outpace exports while on the supply side, increase in manufacturing costs and a shift of focus to the value-added sectors will result in growth slowdown. This will cause China's share in global trade to reduce from the present level. This brings us to the third trend that **manufacturing competitiveness will be the key to tap trade gap created by China**.

Output of most important natural fiber viz. cotton is not expected to rise in line with the global demand. This will create a supply-demand gap which will be filled mainly by polyester that already has a larger share than cotton. Based on this the fourth trend that we visualize is that the **manmade fibres will continue to gain market share**.

Last, but not the least, we predict that **preferential market access arrangements will drive global trade and investments** in the textile and apparel sector.

The global macroeconomic and demographic changes are very clear, and so are their implications for the textile and apparel sector. For Indian manufacturers and policy makers specifically this means a great deal. Being present at the right location at the right time either to sell or to produce what the market requires is vital. On one hand, high domestic consumption is going to throw up significant business opportunities, while on the other hand slowdown in Chinese exports will provide an opportunity to exporters to fill the void. Success in exports will not only depend on capability of exporters to scale up and match buyer expectations but also on how fast India can achieve preferential market access to markets like US and EU. To compete effectively at global level, Indian industry will have to plan big and think about cross border investments while the authorities will have to focus on providing conducive, easy to do business environment and support infrastructure rather than adopting incentivizing approach.

# **TREND 1:** Global apparel consumption will become US$ 2.6 trillion

The current global apparel market consumption is estimated at US$ 1.7 trillion which forms approximately 2% of the world GDP of US$ 73.5 trillion . Apparel consumption in top 8 economies (considering EU-28 as one entity) constitutes approximately 70% of the global consumption.

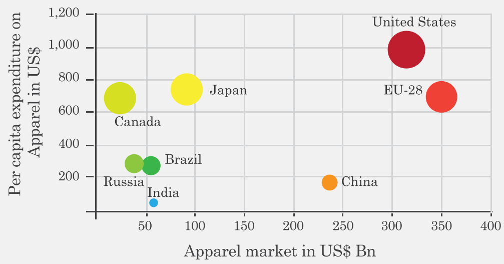
**Table 1:** Global Apparel Market Size 2015 (In US$ bn.)

| Region | Apparel Market Size |
|---|---|
| EU-28 | 350 |
| USA | 315 |
| China | 237 |
| Japan | 93 |
| **India** | **59** |
| Brazil | 56 |
| Russia | 40 |
| Canada | 25 |
| Rest of the World | 510 |
| **TOTAL** | **1,685** |

All four BRIC nations appear among the top markets having a cumulative share of approximately 23%, with China leading the pack. Rest all largest markets are developed countries.

An analysis of "Per-capita Expenditure on Apparel" (PEAP) reveals few interesting trends. US and EU are home to 11% of the world population while their combined apparel consumption share is 40% indicating extremely high PEAP in these markets. There is also a clear demarcation of PEAP between the developed and developing economies – developing countries having a much lower PEAP value than developed one.

**Figure 1:** Per-capita Expenditure on Apparel in Largest Markets (2015)




(Note: Size of bubble indicates per capita spending)

*Source: Wazir Analysis*

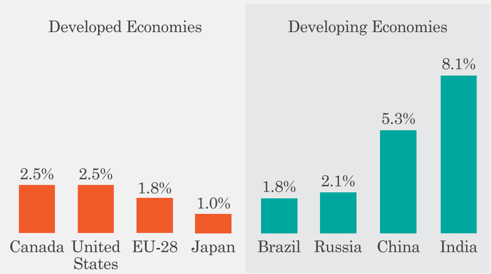
India has the lowest PEAP of US$ 45, which is less than 5% of the highest – US$ 978 in USA. Very often, comparisons are drawn between the markets of China and India; however, India's PEAP is only one-quarter of that of China.

There is a strong correlation between consumers' spending on various categories and their economic stature. With limited economic resources, a consumer's first priority is always to satisfy the basic needs of food, clothing and housing. As the consumer's disposable income increases, the share of expenditure on basic categories reduces whereas the share of new categories like entertainment, recreation, consumer durables, travel, etc. increases. The expenditure on clothing does not go down in absolute value terms but the increase is slower than the overall increase in expenditure.

This consumption behavior at a macro level would mean that for an emerging or developing market the apparel consumption growth rate would be faster than its economic growth. Similarly, for developed economies the apparel market growth rate should be lower than its economic growth.

Based on the projected GDP growth rate and its relation with apparel market growth, it is projected that the global apparel consumption will increase to US$ 2.6 trillion by 2025.

**Figure 2:** Projected GDP Growth Rate in Key Apparel Markets (2015-25)




*Source: Real GDP growth rate database published by Economic Research Service, USDA, last updated Dec. 2015*

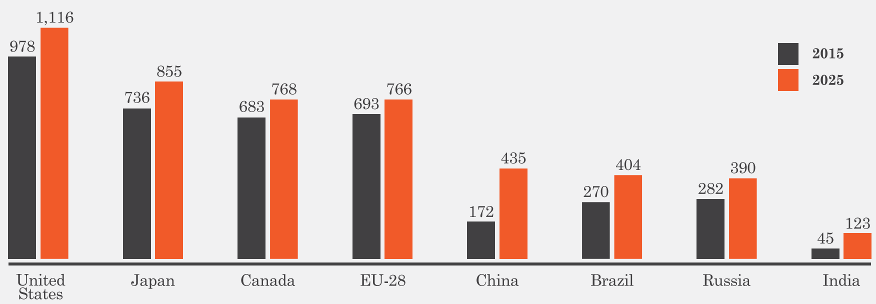
**Table 2:** Apparel Market Size Projections for 2025 (in US$ bn.)

| Region | 2015 | Projected CAGR | 2025 |
|---|---|---|---|
| EU-28 | 350 | 1% | 390 |
| USA | 315 | 2% | 385 |
| China | 237 | 10% | 615 |
| Japan | 93 | 1% | 105 |
| **India** | **59** | **12%** | **180** |
| Brazil | 56 | 5% | 90 |
| Russia | 40 | 4% | 59 |
| Canada | 25 | 2% | 30 |
| RoW | 510 | 4% | 746 |
| **Total** | **1,685** | **4%** | **2,600** |

*Source: Wazir Analysis*

Comparison of projected PEAP for 2025 with that in 2015 shows that while Indian market is expected to register highest CAGR but its PEAP will still remain lowest. China, on the other hand, will emerge as the single largest market registering double digit growth rate in PEAP as well. Still, PEAP for developed countries will remain higher than the BRIC nations.

**Figure 3:** Change in Per Capita Expenditure on Apparel from 2015 to 2025 (In US$)




*Source: Wazir Analysis*

## KEY TAKEAWAYS

- The global apparel consumption will increase from US$ 1.7 trillion in 2015 to US$ 2.6 trillion by 2025
- Developing / emerging economies will drive the apparel market growth
- Per capita expenditure on apparel in developed countries in a decade from now will still be far more than that in developing nations
- China and India will be the fastest growing apparel markets, both growing in double digits
- China will become the biggest apparel market adding more than US$ 377 bn. in market size by 2025. India will be the second most attractive apparel market adding US$ 121 bn. by 2025

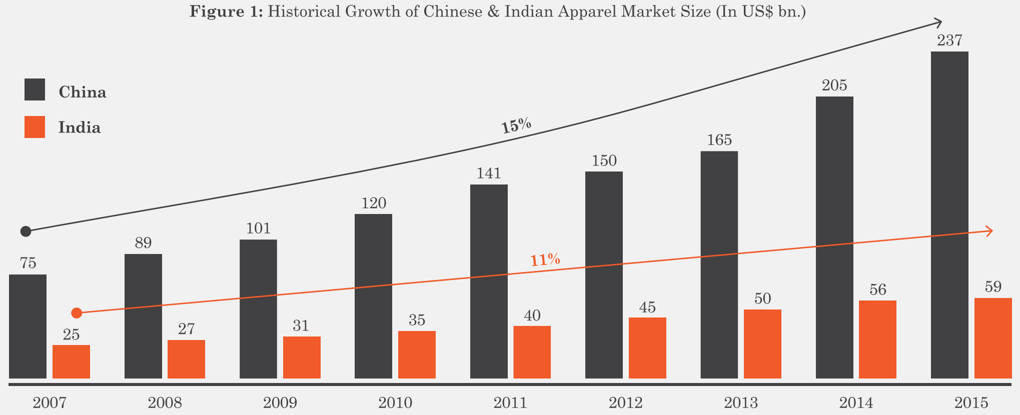
# **TREND 2:** Domestic market of China & India will be a big opportunity for investment and growth

China and India with their huge population base and growing economies have received most attention from international companies in recent times. Whilst China has been at the forefront of attracting investments across the sectors, India is also catching up fast. As a matter of fact, India replaced China as the largest FDI recipient nation in 2015. The macro-economic projections over the next few years show continuation of high growth in both countries leading to doubling of GDP by 2025.

The present apparel market size of China and India is estimated to be US$ 237 bn. and US$ 59 bn., respectively. Over next few years, the combined apparel retail economy of China and India will represent a significant proportion of the global apparel consumption surpassing several developed markets.

Both markets have shown robust growth in past despite global uncertainties and slack demand. From 2007 to 2015, the Chinese market posted an annualized growth of 15% whereas the Indian market registered a somewhat lower growth of 11%. However, both the markets have performed better than the largest consumption regions (US, EU and Japan) where change in economic conditions led to lower demand growth.

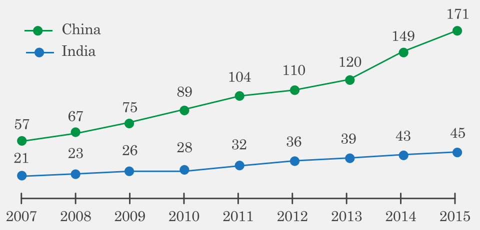
**Figure 1:** Historical Growth of Chinese & Indian Apparel Market Size (In US$ bn.)




*Source: Wazir Analysis*

The per capita expenditure on apparel (PEAP) in China is significantly higher than that in India. From 2007 onwards, PEAP in China grew at a CAGR of 15% and reached US$ 171 in 2015. During the same period, PEAP in India grew at a CAGR of 10% and reached US$ 45 by 2015. In 2007, China's PEAP was almost 2.7 times of that of India but higher growth in Chinese market has led China's PEAP to become almost 4 times that of India in 2015.

**Figure 2:** Historical Growth of Per Capita Expenditure on Apparel in China & India (in US$)




*Source: Wazir Analysis*

The key to high market growth, historical as well as projected, in China and India has a direct correlation with two parameters – a large & growing consuming class and continuous growth in their spending power.

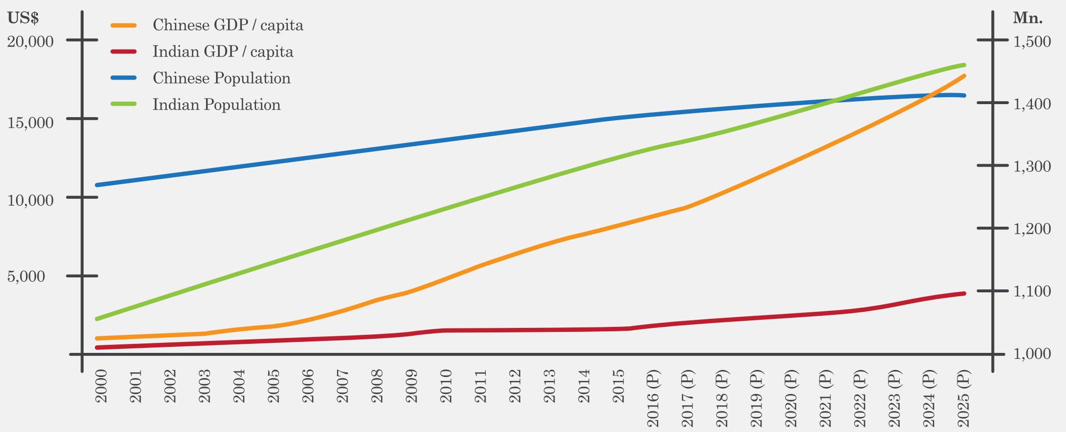
Both the Chinese and Indian economies have been the best performing large economies in the last decade. In the next decade also, they are expected to maintain high growth rates. This high economic growth will be the major driver of apparel market growth in both countries.

Studies show that countries after achieving a per capita GDP of more than $US 2,500 experience a spur of economic growth led by consumer spending. The Indian economy is expected to reach this target by 2020, whereas China is already well past this level.

## INDIA: AT VERGE OF STRUCTURAL CHANGES

Organized retailing in India currently stands at only 8% of the overall retail market of US$ 550 bn.. Within this, apparel is the single largest category with a share of ~ 35%. The vast population base and growing economy has caused global retailers and brands to actively seek Indian market participation, either on their own, or in partnership with a local player.

**Figure 3:** Historical and Projected GDP per Capita and Population of China and India




*Source: IMF's World Economic Outlook Database, Oct. 2015; UN's World Population Prospects: The 2015 Revision; and GDP projections 2016 onwards based on Real GDP growth rate database published by Economic Research Service, USDA, last updated Dec. 2015*

With Zara being a runout success since its launch in 2010 and Uniqlo expected to enter soon; apparel retail scenario is definitely heating-up in India. In 2015 itself, India saw entry of three prominent international brands – H&M, Gap and Aeropostale. H&M opened its store in October 2015 and registered sales of about US$ 275,000 on the inaugural day. Aeropostale opened its first store in November 2015 and witnessed a footfall of 35,000 people in first 10 days. Gap after opening its first store in May 2015 has opened 3 more stores in India.

Government's recent decision to provide certain relaxation in norms for FDI in retail will further support the market growth. Beyond the increasing income of Indian consumers that is making them buy more, and better; the market growth will be led by following important drivers:

1. *Demographic dividend:*

   India has the largest Gen Y population in the world. The median age in India is 27 years compared to 37.6 years in the United States. Almost half of the Indian population is under 25 years and as this population joins the workforce, gets more money in their hands, their spending power will increase. Apparel category will be the prime beneficiary of this increase in purchasing power.

2. *Aspirational buying:*

   A key factor for growing consumption is the attitude shift amongst the Indian consumers. Their buying habits are shifting from need-based purchase to aspiration-based purchase and the "guilt" related to spending which was inherent in consumers of yesteryears has suddenly vanished. Further, the consumer's product choice is becoming increasingly biased towards brands, especially in fashion segment. Indian are now shifting from traditional to modern "branded" experiences. Today consumers in even tier-II, tier-III and tier-IV cities are spending much more on apparel than they did a decade ago.

3. *Rurbanization and urbanization:*

   On one hand masses are moving from rural to urban India looking for jobs, while on the other hand rural areas are being infused with urban patterns and services (Rurbanization) and cities are engulfing villages as they expand. In 2011, 31% of India's population was urban, up from ~28% in 2001. By 2025, 36% of the population is expected to be urban . Between 2001 and 2011, 32% urban growth was due to reclassification of towns and expansion of urban areas, leading to explosive growth in farmland prices and rise of the "correlate" villagers.

   Rurbanization and Urbanization are putting more money in the hands of people and are creating new aspirations and new demand which when supported by better availability will have a major growth impact on apparel consumption.

4. *Growth in online retail sales:*

   Online retailing in India has emerged strongly over the past few years on account of the digital revolution taking place in the country. India is expected to become the world's fastest growing e-commerce market on the back of robust investment activity in the sector and the rapid increase in internet users.

   The major reasons for this growth are increasing penetration of technology in tier-II, tier-III and tier-IV cities, increased use of mobile internet, need for ease of shopping, heavy discounts offered by online portals, and better payment and return policies. In India, internet penetration currently at 19% is at the cusp of an exponential growth. 250 million people are currently connected to the internet in India and this number is expected to reach 700 million by 2025.

**Table 1:** Projected Indian Online Apparel Market

| In US$ bn. | 2015 | 2025 (P) | CAGR |
|---|---|---|---|
| Total Online Sales | 5 | 130 | 39% |
| Online Apparel Sales | 1.5 | 45 | 41% |
| Share of Online Apparel Sales | 30% | 35% | |

*Source: Census India 2011 and Indian Institute for Human Settlement 2011*

## CHINA: STRONG MEDIUM TO LONG TERM GROWTH OUTLOOK

In recent times, some domestic apparel brands in China have registered de-growth on account of premium brands, mainly the international ones, breaching their price positioning and offering products of entry to mid-price segments. Chinese retail sector overall is under a consolidation trend wherein retailers are optimizing existing stores' performance and also focusing on online presence rather than capital & resource intensive brick-and-mortar stores.

However, retail attractiveness of Chinese apparel market is not subdued even an iota, as evident from ever increasing presence and growth of international fashion brands in China. At present, China is the largest international market for Zara and Uniqlo, and the largest international market in Asia for H&M and C&A. Strong economy base which is still growing appreciably will keep the market attractiveness high in the next decade as well. Few key trends that are emerging in Chinese apparel market are:

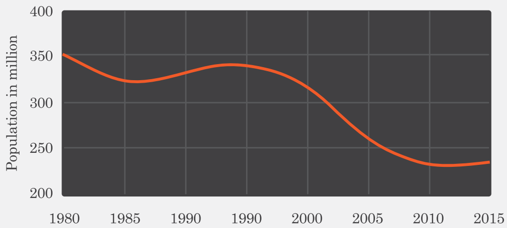
1. *Inter-segment growth realignment:*

   Growth of the largest segment viz. women's wear in China has been slowing down, though it is still growing faster than the overall consumption. On the other hand, growth of new segments of outdoor wear and fast fashion is picking up. A lot of that growth is attributed to entry and emergence of specialty brands which have found good acceptance with Chinese consumers.

2. *Demand growth in kids wear:*

   In 2015, China had a population of 237 million in the age bracket of 0-14 years, accounting for almost 17% of the total Chinese population. Since 1980s, when one-child policy was introduced, the population in this age bracket has decreased almost continuously. The de-growth rate was particularly high since the turn of this century.

**Figure 4:** 0-14 age group population in China (1980-2015)




*Source: UN Population database*

Even with a shrinking consumer base, the market demand was rising as Chinese parents drifted towards branded, fashion and lifestyle products for their kids, thanks to their rising incomes.

The one-child policy had been relaxed to certain extent in last few years and from 1st January 2016 it has been completely phased out. This change will ultimately lead to growth of population lying in 0-10 age group. Anticipating boom in kidswear segment, several international brands (like Dior, D&G, ARMANI, Gucci, etc.) as well as domestic ones (like Xtep, Anta, 361 Degree, Li Ning, Stepwolves, Baoxiniao, JNBY, GXG, etc.) have extended their product lines into kidswear.

3. *High growth of online apparel sales:*

China is witnessing a gradual shift in consumer spending from offline to online retail channel. Apparel is the most popular sub-category purchased online with an estimated sales of approx. US$ 93 bn. in 2014.

**Figure 5:** Online Apparel Sales in China (2010-2014)


*Source: Fung Business Intelligence Centre, December 2014*

In Yuan terms, the online apparel sales have grown at an astounding CAGR of 44% between 2011 and 2014.

**Table 2:** Projected Chinese Online Apparel Market

| In US$ bn | 2015 | 2025 (P) | CAGR |
|---|---|---|---|
| Total Online Sales | 630 | 1700 | 10% |
| Online Apparel Sales | 110 | 335 | 12% |
| Share of Online Apparel Sales | 17% | 20% | |

*Source: Wazir Analysis*

The growth may reduce in long term as the market evolves but it will still be in double digits, making it the single largest online apparel market in the world by 2025.

In both countries, demand for clothing is expected to outpace the overall growth of economy. As discussed earlier, it is projected that per-capita expenditure on apparel in China will rise from US$ 177 in 2015 to US$ 434 by 2025 thereby registering a CAGR of 10%. In India, the per-capita expenditure on apparel will increase from US$ 45 in 2015 to US$ 180 by 2025, growing at a CAGR of 11%.

This, in value terms, would cause the market size in China to swell from US$ 237 bn. in 2015 to US$ 615 bn., whereas India's apparel market size will reach US$ 180 bn. by 2025 from US$ 59 bn. in 2015.

On one hand, where these two economies will drive the growth of global apparel consumption; the traditional markets of USA and EU will witness slower growth rates on account of market maturity and weaker economic growth. It is expected that by 2025, the combined size of Indian and Chinese markets will overtake that of USA and EU.

The market growth in China and India will benefit national textile and apparel manufacturing firms the most. International retailers entering these countries would prefer buying locally in medium term than importing to control the lead times and cost because manufacturing set-ups are available in both the countries. Sourcing requirement clause, as enforced by Indian government, will further aid the cause. With growing demand within the country, large textile and apparel exporting firms will also find it attractive to develop a domestic supply model. By 2025, the domestic manufacturers would gain a much larger scale and become better organized than what they are presently.

**Table 3:** Projected Apparel Market Size of China/India and USA/EU in 2025 (in US$ bn.)

| | 2015 market size | Expected growth rate 2015 to 2025 | 2025 market size | Market addition by 2025 |
|---|---|---|---|---|
| India | 59 | 12% | 180 | 122 |
| China | 237 | 10% | 615 | 378 |
| **India and China** | **296** | **11%** | **795** | **500** |
| USA | 315 | 2% | 385 | 70 |
| EU 27 | 350 | 1% | 390 | 40 |
| **USA and EU 27** | **665** | **2%** | **775** | **110** |

*Source: Wazir Analysis*

## KEY TAKEAWAYS

- China and India are expected to be the major growth centers for apparel consumption by 2025
- High economic growth will be the major factor behind the increasing apparel market size in both these countries
- Other trends facilitating the growth in India are:
    1. Increasing youth population and high purchasing power
    2. Shift from need-based purchase to aspiration-based purchase
    3. Rurbanization and Urbanization increasing the market demand
    4. Increased penetration of technology and greater access to internet resulting significant growth in online retail sales
- Trends which will catalyze growth in Chinese market demand are:
    1. Boosting demand of outdoor wear and fast fashion categories
    2. End of the one-child policy fostering demand of kid's wear segment
    3. Gradual increase in spending of Chinese customer from offline to online retail channel
- It is expected that the combined apparel market size of China and India will become US$ 795 bn. by 2025 and surpass the combined market size of USA and Europe, which will be US$ 775 bn. in 2025
- Growth in retail front will lead to a trickle-down effect in the local manufacturing value chain benefitting national manufacturers the most. Huge growth will make domestic market more attractive than exports in many cases for national manufacturers

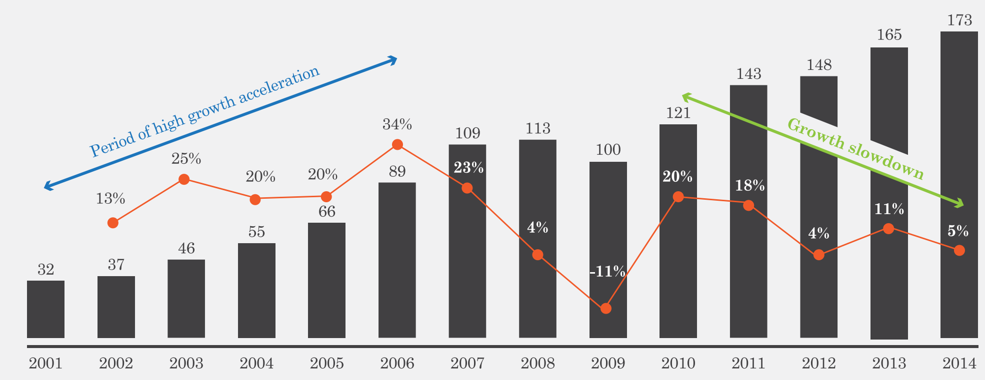
# **TREND 3:** Manufacturing competitiveness will be the key to tap trade gap created by China

China, the world's factory, has successfully leveraged its large human resource base, low manufacturing costs and large scale infrastructure to achieve pre-eminent position in the world trade. Higher productivity of workers and commendable government support are the markers of China's progress and its emergence as a developed nation. Competitive manufacturing has resulted in large investments from within the country as well as through FDI in the sector. In apparel segment specifically, China has dominated the global trade in last two decades with a share of more than 40%.

Exports have played an important role in China's economic success. But now China is at the juncture where private consumption is replacing investment as the major driver of GDP growth and will eventually constitute the largest share of GDP. High levels of investment are converting into consumption, creating structural changes in the export oriented sectors like apparel.

Between 2001 and 2014, Chinese apparel exports increased more than 5-folds from US$ 32 bn. to US$ 173 bn., growing at 14% CAGR. However, the growth has slowed down in the last few years. From the below figure, it can be seen that after 2010 the exports growth has slowed down in comparison to the period before financial crisis where annual growth was 20% on

**Figure 1:** China's Apparel Trade (US$ bn.)




*Source: UN comtrade database*

an average. The trend is expected to remain the same in future.

Following are the major reasons driving this trend:

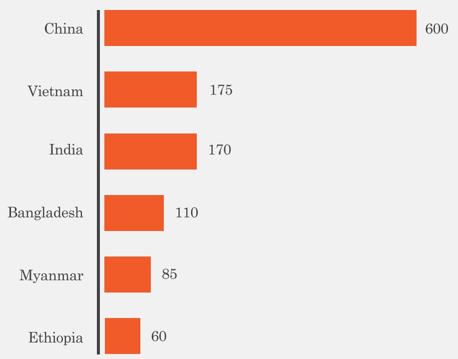
1. *Growth of domestic demand*

   As discussed previously, domestic demand of apparel in China is slated for a high growth. Per capita spend on apparel in China is expected to grow from US$ 171 in 2015 to US$ 434 by 2025; whereas the total apparel market will rise from US$ 237 bn. in 2015 to US$ 615 bn. in 2025. Addition of US$ 377 bn. in domestic market will put pressure on exports and at the same time will result in high imports.

2. *High wage growth*

   China is no longer a low cost destination as it used to be at the turn of the century. China's labor pool is shrinking due to demographic changes and reduced flow of migrant labor from rural areas, exerting upward pressure on wages. The wages across sectors and regions in China have grown in double digits over the last couple of years and will continue to grow further. For a labour intensive sector like clothing, this can put a brake on the fast growth of manufacturing output recorded historically.

**Figure 2:** Average Wages in Textile Industry (US$/Month)




*Source: Industry Sources*

3. *Movement of manufacturing towards more value added segments*

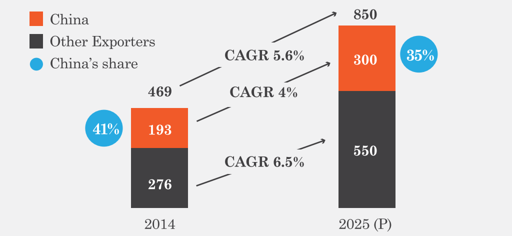
   Chinese Government is taking initiatives to reinforce higher productivity and greater incomes. As the cost of manufacturing rises and the country strives to achieve the status of a developed economy, Chinese enterprises will start concentrating more and more on innovation driven industries like Aerospace, Artificial Intelligence, Biotechnology, Technical textiles, Photonics, Nanotechnology, Robotics, etc. Conventional textiles and apparel industry will no longer be the prime focus of Government as it has been since the 1990's for enhancing exports and generating employment. This will eventually result in a slower growth of apparel output.

4. *Relocation of manufacturing to neighboring countries*

   China has established trade agreements with several Southeast and East Asian countries where manufacturing costs are lower than China. Going forward, China is expected to support investment in manufacturing set-ups as well as in overall infrastructure in these countries, to cater to China's own demand as well as exports to other markets.

Based on the emerging trends, it is projected that China's lower-than-market performance in apparel exports is expected to continue further. The apparel exports CAGR of China is expected to reduce to 4% over the next decade compared to last 10 year CAGR of 12%. As a result, the share of China in global apparel exports will reduce from 41% currently to around 35% by 2025. During this period, global exports of apparel will grow from $ 469 bn. to US$ 850 bn. at a CAGR of 5.6%.

**Figure 3:** Global Apparel Trade Projections until 2025 (in US$ bn.)




*Source: Wazir Analysis*

It is however important to state that despite of the slowdown in apparel exports, China with its vast land base, plentiful resources, manpower strength and large manufacturing setup will continue to be the single largest apparel global manufacturer in foreseeable future. Exports will only slowdown to the extent that China's domestic market will become increasingly attractive for local manufacturing.

Reduction in share of China in global exports in 2025 corresponds to a value of US$ 50 bn. for which other apparel exporting nations will compete. The beneficiary nations of this opportunity would be the ones that have competitive manufacturing cost, FTA advantage with key markets, and good export infrastructure. But, the main issue to be addressed would be development of textile capability and scale of manufacturing comparable to that of China. Beyond these productivity, service and product development will be important for filling the void created by China. FTAs with USA and EU will be an added advantage but it is important to note that China thrived without them. None of the top 5 garment suppliers to US – China, Vietnam, Bangladesh, Indonesia and India today have any preferential access to US. On the contrary, exports from countries in CAFTA, AGOA, etc. have continued to shrink in last many years.

Nations which can benefit most from Chinese growth slowdown include Vietnam, Ethiopia, Kenya, Myanmar, Bangladesh and India; but not necessarily in that order.

With recently signed FTA with EU and TPP ratification under way, Vietnam is expected to emerge as the major gainer leveraging its existing set-up and market linkages. Yarn forward rule – the important component of TPP, will make yarn a product of TPP nations as a mandate. This may prove critical in indigenizing the entire textile manufacturing value chain in Vietnam.

Ethiopia today boasts wage cost in the range of US$ 50 to 60 per month along with low power and land cost and duty free access to almost all important markets. In 2014, Ethiopia attracted US$ 1.2 bn. FDI in textile and apparel manufacturing sector. Once these projects come online in next 3 to 5 years, the apparel exports will cross US$ 4-5 bn. from a current level of approx. US$ 100 mn.. Ethiopia has already been tagged as the Bangladesh of Africa but the growth would depend on how the Government improves the ease of doing business and address the infrastructural challenges.

Kenya emerged as the largest apparel exporter to USA under AGOA surpassing Lesotho in 2014. The country is expected to remain the major beneficiary of the recent 10-year extension of AGOA. Having better infrastructure than competing African countries, comprehensive duty free access status, strong buyer linkages and workforce availability will work in favour of Kenya.

Myanmar, with removal of economic sanctions can emerge as a global manufacturing destination. Even with US sanctions in place, the apparel export from Myanmar was above US$ 1 bn., which was more than the exports of all Sub-Saharan countries put together. Its GSP status and increasing interest of investors from Japan, China, Taiwan, etc. can bring a very high growth for the apparel manufacturing industry.

Bangladesh is already a global powerhouse when it comes to apparel manufacturing and exports. To maintain the growth rate that it achieved since 2000, Bangladesh will have to address the infrastructural limitations and also placate compliance related misgivings.

India, the largest and more resourceful country of all those listed above, has not yet tapped its real potential as far as apparel exports are concerned. While for all others, apparel exports are the backbone of the economy; India's production base is much diversified. This does not imply that Government or industry is not looking to increase apparel exports but so far any spectacular growth has been elusive. India is the only nation which has the wherewithal to take-up every single dollar spill over from China because of its vast textile base, manpower availability and infrastructure. However, just like China, its own domestic market is getting increasingly attractive. There is no doubt that India is better destination than other smaller Asian and African nations but conversion of potential to reality would need tremendous structural changes in policy framework starting from refining of labor laws to exit policies to fast tracking the approval process, among several others bottlenecks. One important event that could change the fortune of Indian apparel export industry is finalization of FTA with EU.

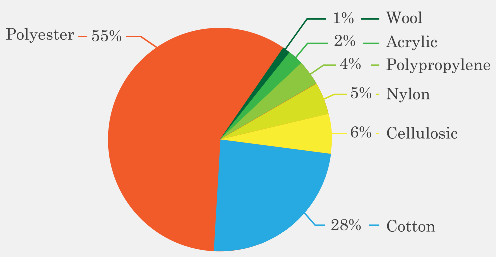
### KEY TAKEAWAYS

- China dominates the global apparel trade with a share of approximately 41%
- In the next decade, its share is expected to reduce to about 35% because of growing domestic demand, rising manufacturing costs, shift from cost driven to innovation driven manufacturing and availability of other lower cost destinations in the region with which China has established FTAs to cater to its own demand a well as exports
- The apparel exports vacuum created by Chinese exports slowdown is estimated to be US$ 50 bn. by 2025
- China's loss of share in global apparel trade will throw up opportunities for emerging exporters including Vietnam, Ethiopia, Kenya, Myanmar, Bangladesh and India

# **TREND 4:** Manmade fibres will continue to gain market share

In 2015, the global fibre consumption was around 90 mn. tons out of which polyester and cotton had a share of 55% and 28%, respectively. Rest 17% was contributed by other fibres.

**Figure 1:** World fibre consumption in 2015 (volume share)



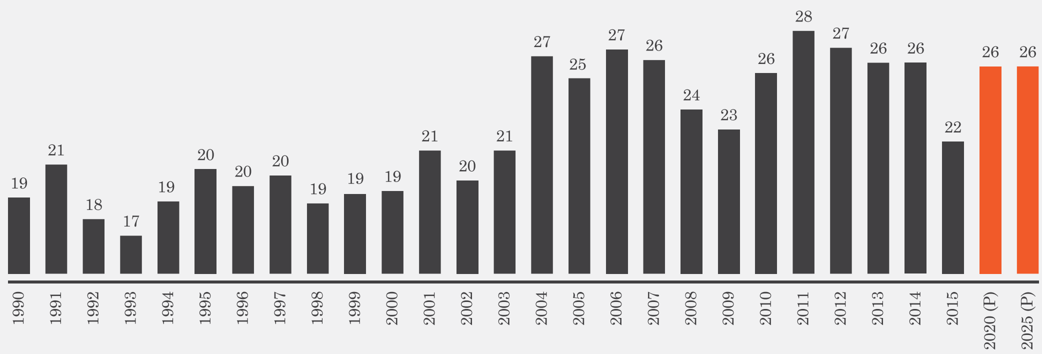

*Source: PCI Analysis*

In the total fibre consumption, China held a majority share of 53% followed by India with 11% share. In Chinese consumption, the shares of polyester and cotton were 68% and 18%, respectively. The corresponding figures for India were 38% and 54%, respectively.

Cotton has always been and will continue to be a crucial raw material to the textile industry, but due to supply side pressure it may struggle to satisfy growing demand in the future. As per ICAC estimates, the cotton production is going to stagnate around the level of 26 mn. tons for next 10 years. Reduction in land under cotton cultivation due to competing crops and loss of arable land is expected to outweigh the farm productivity improvement possible through better agriculture practices and use of GM cotton.

On the other hand, the global fibre

**Figure 2:** Historical and Projected Cotton production (million tons)

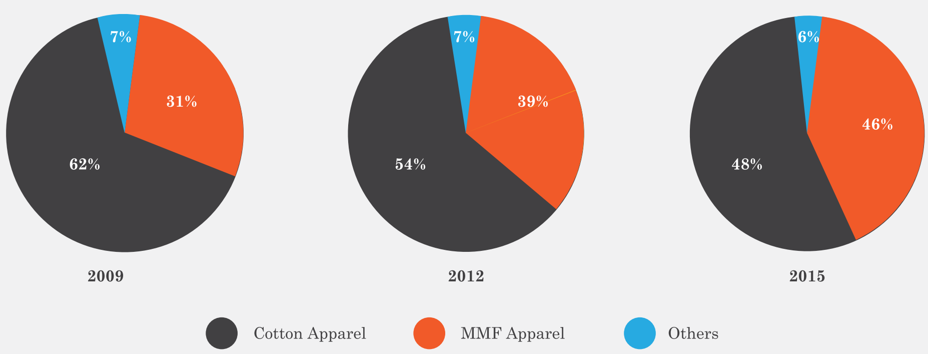



*Data Source: USDA and ICAC*

demand is continuously growing. By 2025, the projected global fibre demand is 115 mn. tons, growing at a CAGR of 2.5% from 2015 level. This supply demand mismatch will create a gap that will be mainly filled by polyester and to some extent by cotton-like fibre viz. Viscose.

Trade shift towards manmade fibre (MMF) based end products is already evident. The share of MMF apparel in US imports has increased from 31% in 2009 to 46% in 2015 while the share of cotton apparel went down from 62% to 48% during the same period.

**Figure 3:** Fibre-wise break-up of US Apparel Imports




*Data Source: OTEXA database*

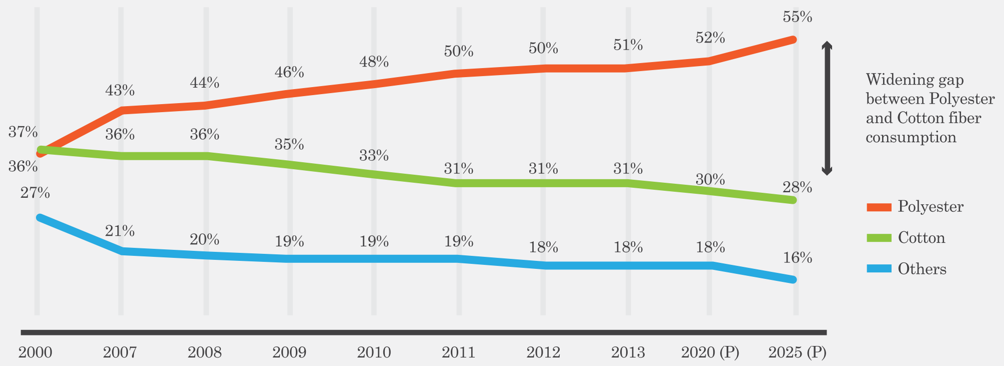
Wide acceptance of MMF in end use categories like sportswear, leisurewear, women dresses, home textiles, automotive, carpets and other industrial sectors has increased the market demand of manmade fibres. Apart from the conventional textiles, manmade fibre consumption is also catching up pace in nonwoven industry. The increasing acceptance of polyester in filter media industry including air, water and automotive filtration combined with the increasing awareness of environmental issues has significantly increased the demand of polyester fibre.

Changes in consumer lifestyle like increasing emphasis on fitness, rising brand consciousness, fast changing fashion trends, increasing women participation in workforce and hygiene consciousness are driving the trends in the end products. Impact of such trends is passed along the textile value chain which in turn has resulted in high demand of the fibres that can fulfil these requirements at affordable price. In this context polyester has proved to be the most cost effective and adaptable fibre. As a result, polyester is expected to dominate the global textiles in foreseeable future in almost all end use categories while cotton will slowly loose its share.

In recent years, polyester has shown an impressive growth gradually taking up the share of cotton as well as other manmade fibres. The share of cotton is expected to continue to decline from

31% in 2015 to 28% in 2025. During the same period, share of polyester will grow from 51% to 55% implying that by 2025 global consumption of polyester will be almost double than that of the cotton fibre.

**Figure 4:** Global Fibre Consumption Trend




*Source: PCI Analysis*

## KEY TAKEAWAYS

- Global fibre consumption will grow from 90 mn. tons in 2015 to 115 mn. tons in 2025
- Due to supply side pressures and price volatility, cotton will struggle to fulfill the growing fibre demand while manmade fibres, specifically polyester, will gain share
- Increasing use in nonwovens and technical textiles, changing consumer trends including increasing emphasis on fitness and hygiene, rising brand consciousness, fast changing fashion trends, increasing women participation in workforce will further boost the demand of manmade fibres
- By 2025, share of polyester in global fibre consumption will become 55% from current level of 51% whereas that of cotton will decline to 28% from current level of 31%

# **TREND 5:** Preferential market access arrangements will drive trade and investments in the sector

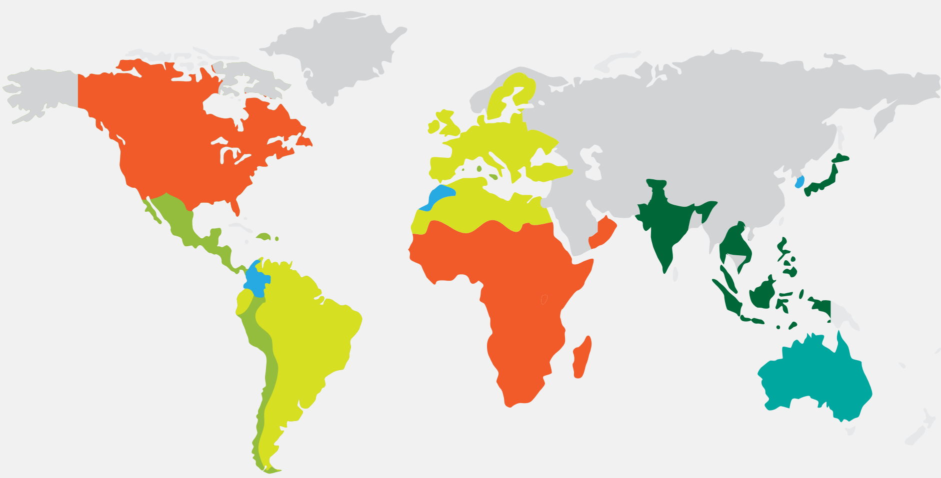
Textile and apparel articles are price sensitive commodities. In order to produce them at lower costs, the manufacturing industry has continued to shift from one part of the world to the other. Since textile and apparel manufacturing is a labor intensive industry, several nations adopt a protected regime by imposing high import duties to safeguard the interest of domestic manufacturers. Hence, FTAs have a special role to play in the development of investment and trade in this sector.

**Table 1:** Average and Peak Tariff rates on textile and apparel products in USA, EU and Japan

| | USA | | EU | | Japan | |
|---|---|---|---|---|---|---|
| | Avg. Tariff | Peak Tariff | Avg. Tariff | Peak Tariff | Avg. Tariff | Peak Tariff |
| **Textiles** | 7.9% | 34% | 6.6% | 12% | 5.4% | 25% |
| **Apparel** | 11.6% | 32% | 11.5% | 12% | 9.0% | 13% |

*Source: World Tariff Profile 2015, WTO*

**Figure 1:** Market Access Arrangement of US, EU and Japan



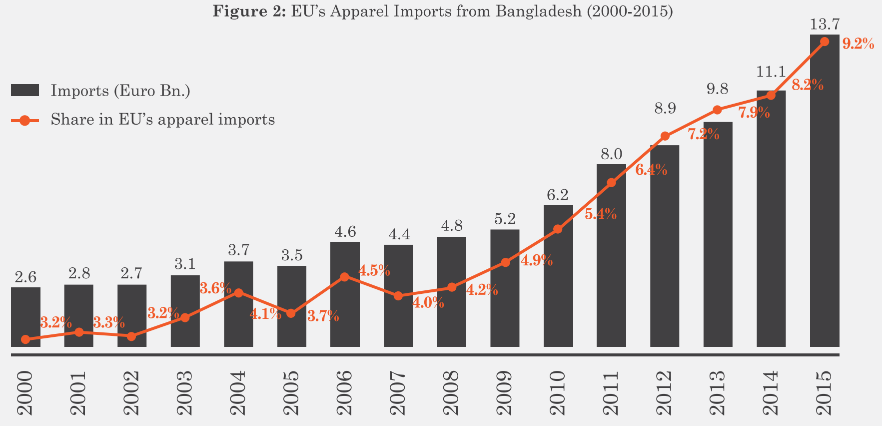
Key apparel markets - EU, US and Japan have multiple market access arrangements with several key manufacturing nations. They have either entered into different types of trade arrangements (such as Economic Partnership Agreement, Economic Cooperation Agreement, Customs Union, Economic Union, FTAs, PTAs) or provided Special Status (GSP, GSP +, EBA, etc.) to certain countries thereby lowering or eliminating tariff rates.

Nations such as Bangladesh, Turkey, Sri Lanka, Pakistan, etc. have emerged as major apparel exporters mainly because of preferential duty access they have to one or more of these markets. In fact, China is the only large manufacturer of textile and apparel which does not have any special market access to US, EU or Japan.

Bangladesh, a major success story, which managed to leverage its Everything But Arms (EBA) status to EU achieved in 2001 that grants it Duty Free, Quota Free (DFQF) access, except arms and ammunition. In 2000, Bangladesh's apparel exports to EU were € 2.6 bn. which reached € 13.7 bn. in 2015, thereby growing at a CAGR of 12%. In this period, share of Bangladesh's apparel exports in EU market grew from 3.2% to 9.2%. Today, Bangladesh has become the second largest exporter of apparel to EU after China.

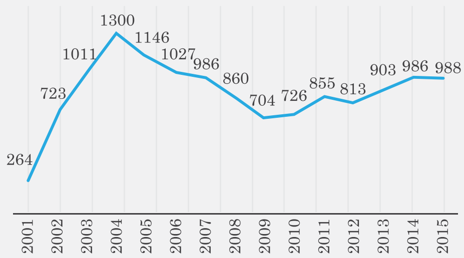
Also, there are examples where countries could not take the benefit of duty free access. For e.g. Sub-Saharan African (SSA) nations have preferential market access to US under African Growth Opportunity Act (AGOA) with relaxed Rules of Origin (ROO) for apparel under third country fabric clause. However, the data reveals that the US imports of textile and apparel under AGOA rose initially till 2004 but thereafter declined. Only three SSA nations viz. Kenya, Lesotho and Mauritius have taken advantage offered by AGOA to any appreciable extent so far. But even then, their share of textile and apparel exports to the US market is insignificant.

**Figure 2:** EU's Apparel Imports from Bangladesh (2000-2015)




*Source: Eurostat Database*

**Figure 3:** USA's Textile and Apparel imports under AGOA (US$ mn.)




*Source: Agoa.info website*

The Doha Round of trade negotiations at the WTO stalled, mainly because of lack of consensus between the developed economies and developing economies, due to which countries are seeking progress in trade policies outside the WTO, through plurilateral negotiations. The US and the EU have begun negotiations on the Transatlantic Trade and Investment Partnership (TTIP); Trans-Pacific Partnership (TPP) involving US and 11 other countries has been signed and India, China, ASEAN nations & four others have initiated negotiations to establish the Regional Comprehensive Economic Partnership (RCEP). The latter two FTAs have the potential to change the global trade and investment flow in textile sector owing to their cumulative economy size as well as population.

**Table 2:** Mega FTAs – Member nations, GDP and Population share

| | | TTIP | TPP | RCEP |
|---|---|---|---|---|
| Member Nations | | US and EU | Australia, Brunei Darussalam, Canada, Chile, Japan, Malaysia, Mexico, New Zealand, Peru, Singapore, USA, and Vietnam | Australia, Brunei, Burma, Cambodia, China, Indonesia, India, Japan, Laos, Malaysia, New Zealand, the Philippines, Singapore, Thailand, South Korea and Vietnam |
| GDP current US$ | US$ bn. | 34,574 | 27,905 | 23,138 |
| | Global Share | 46% | 37% | 31% |
| GDP PPP | US$ bn. | 37,160 | 30,782 | 41,779 |
| | Global Share | 33% | 27% | 37% |
| Population | Million | 872 | 812 | 3,490 |
| | Global Share | 12% | 11% | 47% |
| T&A Exports | US$ bn. | 84 | 84 | 449 |
| T&A Imports | US$ bn. | 248 | 216 | 171 |

*Data Source: IMF's World Economic Outlook Database, Oct. 2015; UN's World Population Prospects: The 2015 Revision; UN Comtrade. GDP and Population estimates are for 2015 and trade data for 2014*

It is interesting to note that 7 out of 16 RCEP members are negotiating under TPP as well. Also, none of the African nations are part of these mega FTAs.

Signed on 4th Feb 2016, TPP is expected to be a major game changer for textiles and apparel sector. TPP includes the single largest importer of apparel viz. US with an import level of approx. US$ 85 bn. (2015) and a low cost, fast growing apparel exporter- Vietnam. Under TPP, US will immediately remove tariff on 73% of apparel categories while 10% more will be phased out in next 5 years. For rest apparel categories, tariffs will be reduced by 35% or 50% within next few years. This indicates a significant possibility of trade diversion from US's other large suppliers - China, Indonesia, Bangladesh and India to Vietnam. Presence of other large importers including Japan and Australia will further accentuate trade diversion. The Yarn-Forward Rule of Origin will fetch investments in lower cost TPP countries in upstream manufacturing process as well. For Vietnam there is a provision of "Earned Import Allowance Program" that will allow trousers made in Vietnam from third country fabric to get duty free status into US.

RCEP clan also includes major markets as well as major supplier nations. But at this moment it is too early to judge its impact on textile and apparel sector. The shape, rules and level of market opening that will be negotiated over next few years will determine if RCEP will actually have a trade diversion or creation effect in textile and apparel sector.

Another much bigger agreement on the cards is Free Trade Area of Asia Pacific (FTAAP) which would include all 21 Asia-Pacific Economic Cooperation (APEC) countries of Australia, Brunei, Canada, Chile, China, Hong Kong, Indonesia, Japan, Malaysia, Mexico, New Zealand, Papua New Guinea, Peru, Philippines, Russia, Singapore, South Korea, Taiwan, Thailand, the United States, and Vietnam. A collective strategic study on issues related to the realization of the FTAAP is scheduled to be concluded by end of 2016. Having US and China on the same negotiating table will make things not very straight forward, to say the least. Either US led TPP or China backed RCEP could serve as the template for this super free trade zone.

Apart from these mega FTAs, there are other bilateral agreements under various stages of implementation which will impact the global trade and investment flow in textile and apparel sector. For example, Vietnam-EU Free Trade Agreement (VEFTA), which will come into effect from 2018, is expected to boost the Vietnam's apparel exports to EU at the expense of other large exporters to EU like China, Bangladesh, Turkey, India and Morocco.

Last few years have been a busy time for trade negotiators across the globe; coming few years won't be any different. By 2025, these trade agreements will be their full bloom, except AGOA which as of now is ordained to end by that time. In the next 10 years, FTAs will lead to major trade and investment adjustments causing structural changes in the textile and apparel global value chain.

## KEY TAKEAWAYS

- FTAs are gaining vital importance in global textile and apparel sector
- TPP and RCEP have the potential to change the global trade and investment flow owing to their cumulative economy size as well as population coverage
- Not all countries / regions could effectively leverage their preferential market access in past
- Vietnam is poised to grow its exports to USA and EU under TPP and VEFTA, at the expense of other large exporting nations – China, Bangladesh, Turkey, Indonesia, India and Morocco
- By 2025, FTAs will lead to major trade and investment adjustments causing structural changes in the textile and apparel global value chain

# Implications of these trends on Indian Companies

By 2025, the Indian domestic apparel consumption is expected to touch US$ 180 bn. growing by more than 3 times of its 2015 value of US$ 59 bn.. This will mean an addition of US$ 121 bn. in market size making India as one of the most attractive destinations for brands and retailers. This attractiveness will bring major changes in the manufacturing and retail landscape in India:

- *For international brands and retailers, India will become a high priority market. With slower growth in their home countries, retailers looking to expand globally will vie for share in Indian market.*
- *The market opportunity will enable emergence of strong domestic brands which will stand a chance to benefit from their indigenous supply chains and understanding of local trade dynamics.*
- *In order to increase their market share, retailers and brands will have to focus beyond Tier I Indian cities - to smaller cities and towns where larger proportion of India's population exists. The price sensitivity of this population will cause brands and retailers to develop low cost business models in which e-commerce will play a major role.*
- *On the manufacturing side, focus on domestic market over the next decade can bring unparalleled growth, provided the business model of manufacturers is geared to tap the opportunities which will appear in various market segments. The key will be to develop a supply chain which can cater to international as well as emerging Indian buyers.*
- *Manufacturers will be required to enhance their customer focus through value added services, which may include inventory management, product development and IT enabled tracking.*
- *As the brands and retailers will grow large within the country, they will look for manufacturers with economies of scale who can cater to large orders timely. Strategic tie-ups between such manufacturers and buyers will happen which will enhance stability and efficiency in the overall sector.*

The trend that China's share in global apparel exports will reduce over the next few years will provide an opportunity for Indian exporters to take up the available share. They need to be ready to undertake suitable investments for product and infrastructure expansion to meet the demand which China may no longer cater exclusively.

Indian manufacturers will have to take cognizance of increasing shift towards polyester fibre at the earliest. So far, India is known mainly for cotton products while we have a substantial fibre / filament manufacturing capacities. This image needs to be changed if we want to increase our trade share in global markets where several multibillion dollar polyester based categories exist where India has less than 0.1% share.

Mega FTAs that exclude India may pose a threat to Indian exporters. There is no alternative for India but to pursue plurilateral or multilateral trade arrangements with major markets. But in absence of any certain timeline, Indian companies should adopt a borderless manufacturing approach.

Enormous market and trade growth opportunities within India and overseas are going to unfold in the next decade. It is time for Indian companies to have confidence in India's potential and adopt a bullish approach to create world class set-ups with economies of scale and invest in productivity improvement programmes to counter a high wage growth scenario.

# **Wazir:** Your trusted advisor on the Road to 2025

Over the years Wazir has placed itself as a premier Indian consulting organization with special focus on textile and apparel value chain. Our team of textile engineers, sector experts, management graduates and economists have delivered a broad range of consulting projects working for reported Indian and international clients. With such an exclusive background, Wazir Advisors is well placed to be your trusted advisor on the road to 2025!

We assist clients in strategy formulation and implementation, forming alliances and joint ventures, investments, market understanding, sector analysis and due diligence – thereby providing end to end solutions spanning the complete business cycle in textile value chain.

Having worked with leading Indian and international companies, public sector organizations, Government departments, development agencies, trade bodies etc., Wazir has a deep understanding of global textile sector dynamics and right connect with the people who matter.

Wazir's team of textile experts possess experience across functions – projects, operations, sourcing and marketing in the sector. The team members have worked on strategy and implementation assignments in all major textile and apparel manufacturing and consumption base.

Wazir leverages its body of knowledge, contacts and combined expertise of its team to deliver value to clients.

Our services span the entire breadth of textile manufacturing value chain - from fiber to finished goods.

We cover the following segments:

- Fibers and Filaments
- Yarns
- Fabrics
- Garments
- Made-ups
- Technical Textiles
- Textile Machinery and Equipment
- Handlooms and Handicrafts

## 1. STRATEGY

Wazir delivers practical, implementable strategies for clients to meet their objectives. We assist clients to conceptualize, evaluate and select business opportunities in the textile and apparel sector.

Be it corporate strategy intending to enhance profitability or new market opportunity identification or sector growth strategy to support MSMEs, we are geared to advise our clients efficiently and effectively.

- *Corporate Strategy*
- *Market Opportunity Assessment*
- *Market Entry Strategy*
- *Location Analysis*
- *Business Performance Enhancement*
- *Product Diversification*
- *Marketing and Distribution Strategy*
- *Sector Mapping and Growth Strategy*
- *Policy Formulation Support*
- *Government Scheme Evaluation*

## 2. IMPLEMENTATION

Wazir provides implementation services to textile and apparel sector entities to convert the plans into reality. Wazir has the capability to execute every strategy that it recommends.

Whether it is to manage a Government scheme or to improve productivity in apparel factories or to identify the most suitable technology; we have in-house competence to cover all the critical elements of implementation.

- *Project Management and Monitoring*
- *Re-modelling of Manufacturing Plant*
- *Process Re-engineering*
- *Productivity Improvement*
- *Supply Chain Optimization*
- *Feasibility and Techno-Economic Viability (TEV) Study*
- *Investment Promotion*
- *Cluster and Industrial Park Development*

## 3. ALLIANCES

Partnerships and collaborations are ways to achieve accelerated growth, expand market reach and attain technical advancement. Realizing the importance and need of inter-organization alliances in textile and apparel sector, Wazir has developed broad range of services to support companies and organizations looking for inorganic growth globally.

- *Company Due-diligence*
- *Joint Venture*
- *Marketing Tie-up*
- *Technology Transfer*
- *M&A Execution*
- *Strategic and Financial Funding*

**Harminder Sahni**
harminder@wazir.in
+91 9810066246

**Prashant Agarwal**
prashant@wazir.in
+91 9871195008

**Sanjay Arora**
sanjay@wazir.in
+91 9971110566

**Varun Vaid**
varun@wazir.in
+91 9899985979

**www.wazir.in**

linkedin.com/WazirAdvisors

twitter.com/WazirAdvisors

facebook.com/WazirAdvisors

**Wazir Advisors Pvt. Ltd.**
3rd Floor., Building No. 115, Sector 44 Institutional Area,
Gurgaon - 122002, National Capital Region, India
Tel: +91 124 4590 333