7. Other factors potentially exacerbating LDC graduation impacts

Fashion brands' and retailers' efforts to improve operational efficiency could result in their consolidating their sourcing practices within these LDCs as they graduate. Nearly half of the surveyed respondents plan to reduce the number of vendors they work with over the next three to five years to focus on more efficient supply sources and strengthen their relationship with key vendors. While the most competitive vendors in a country are likely to receive more sourcing orders, this new trend also means competition among vendors in the same country could intensify. Smaller and less competitive garment factories in these LDCs will need additional help to mitigate negative impacts from this, along with any that would arise from LDC graduation.

Other developments could also affect the incentive structure for sourcing from different countries. While graduating LDCs will lose the most liberal trade preferences, FTAs could allow other countries to gain further competitiveness, making them more attractive supply sources. For instance, Viet Nam – already a top apparel exporter with strong backward linkages in the textile segment – has had an FTA with the European Union since August 2020. To put things in perspective, Viet Nam will see tariffs on its clothing exports to the European Union gradually decline from an average 9 per cent currently to around zero eventually, at the same time as Bangladesh, following its official graduation, will complete its additional three-year transition period (in 2029) with the European Union's Everything But Arms scheme. If Bangladesh is eventually subject to the European Union's safeguard measures, average tariffs on its apparel exports to the European Union will rise from zero currently to around 11 per cent. This striking change in market access conditions vis-à-vis Viet Nam could cause severe trade diversion for Bangladesh, making it much less competitive. Even when graduating LDCs can retain duty-free access under GSP+, such FTA arrangements will cause preference erosion. Pakistan, which has access to GSP+ and is a major cotton producer, and Indonesia, which is another major apparel supplying country, are currently negotiating FTAs with the European Union.[13] Competition will also emerge from garment-exporting African LDCs, such as Ethiopia, Lesotho, and Madagascar, which benefit not only from the European Union's EBA scheme, but from the African Growth and Opportunity Act (AGOA), which grants duty-free treatment for garments entering the United States.

Loss of LDC preferences, along with emerging trading arrangements involving other countries, could make it even more challenging for the T&C industries in Bangladesh, Cambodia, Lao PDR, and Nepal to attract foreign investments. Take China's foreign direct investment (FDI) strategies in the T&C sector, for example. Between 2015 and 2018, Bangladesh, Lao PDR, and Nepal were not among the top FDI destinations of China's T&C companies. Even Cambodia accounted for less than 2 per cent of China's total FDI in the T&C sector, measured by value, in this period.

Interviews with Chinese T&C companies revealed that two major strategies drove their FDI decisions. One is to develop a "China + Southeast Asia + Africa" apparel production base to improve production flexibility and agility. Duty-free market access to the leading apparel importing countries and liberal rules of origin (i.e. using Chinese yarns and fabrics) are regarded as essential for attracting the FDI. Therefore, the prospect of

losing LDC-specific market access in the world's leading apparel import market could hurt the attractivenessof Bangladesh, Cambodia, Lao PDR, and Nepal as FDI destinations for Chinese T&C companies. The other element of China's FDI strategy is to access unique resources (such as raw materials and technology) and move up the value chain. This explains why the United States and some European Union countries (e.g. France) were among China's top FDI destinations in the T&C sector.

Additionally, the growing popularity of "near-sourcing" or "reshoring" among fashion brands and retailers could further complicate the post-graduation landscape for Bangladesh, Cambodia, Nepal, and Lao PDR. Notably, United States-based apparel companies have demonstrated a strong interest in expanding their sourcing from the Western Hemisphere, including Mexico and Central American countries.[14] Meanwhile, European Union-based brands and retailers have been actively exploring increasing apparel sourcing from Eastern European Union countries and Turkey.[15] The "near-sourcing" and "reshoring" trend – exacerbated by COVID-19 supply disruptions – could add more competitive pressures on suppliers from Asian graduating LDCs.

Workplace safety, working conditions and environmental compliance are increasingly a major factor when making long-term sourcing decisions, and Asian LDCs will have to make significant improvements in these areas. Working conditions in Asian graduating LDC countries' apparel factories have been causes for widespread concern, affecting their investment and export prospects (ASEAN, 2021a, 2021b; ILO, 2017). Unfavourable working conditions and labour issues attract global attention, and international brands will avoid factories that cannot adhere to acceptable standards. International brand consortiums demand various measures to ensure compliance at source, and local factory owners must make significant investments to improve workplace safety standards and the overall working environment. On the other hand, many local firms complain about not receiving higher prices or bigger orders, despite complying with standards. Furthermore, downward price pressures persist, with big buyers seen as reluctant to accept price rises (Lopez-Acevedo and Robertson, 2016).

Along with factory working conditions and workers' safety, fashion brands and retailers are becoming more serious about introducing higher environmental and ethical standards and certifications (McKinsey Institute, 2021). The global climate change discourse has also led to proactive initiatives by many international buyers of T&C to commit to ambitious targets for reducing greenhouse emissions and their broader environmental footprint (UNCTAD, 2021). Increasing pressure from various international campaigners and advocacy groups, pushes from governments and regulators in the importing countries, and consumers' growing awareness about workers' rights and responsible sourcing imply that environmental, social and governance (ESG) factors will be critical for medium to longer-term export success, including in the textile and clothing sector.

Table 4: Top FDI destinations of China's textile and clothing companies, 2015-18

Rank	FDI destination	Value of FDI (US$ 100 million)	Rank	FDI destination	Value of FDI (US$ 100 million)
1	Viet Nam	10.71	7	Egypt	1.47
2	Singapore	7.71	8	Cayman Islands	1.32
3	British Virgin Islands	2.58	9	Cambodia	1.25
4	United States	2.14	10	Malaysia	1.02
5	Ethiopia	1.85	11	France	0.92
6	Myanmar	1.52	12	Pakistan	0.85

Source: Ministry of Commerce, China.