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INTERNATIONAL TEXTILES AND CLOTHING BUREAU

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NOTE ON  
CONSEQUENCES OF DISMANTLING THE MFA

Presented at the GATT  
Negotiating Group on Textiles and Clothing  
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Note on  
"Consequences of Dismantling the MFA"

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Note on  
"Consequences of Dismantling the MFA"

I. Background.

1. From the outset, an essential clarification is necessary. This note deals with consequences of dismantling the MFA under the assumption that such a dismantling "would permit the eventual integration of this sector into GATT on the basis of strengthened GATT rules and disciplines" (Ministerial Declaration on the Uruguay Round). The consequences of a completely different assumption, that the MFA would be replaced by another system of discriminatory restraints, or special protection, granted to the textile and clothing industries of developed countries, are not considered in this note.

2. The consequences of dismantling the MFA have to be considered in a longer-term perspective for three main reasons. (i) After 30 years of special treatment in derogation from GATT rules and principles, it cannot be expected that dismantling of the MFA can be implemented from one year to another. (ii) The extension of markets, with no internal barriers, resulting from

the North American Free Trade area and the completion of the internal market of the EEC in 1992 will have important implications for the prospects and competitiveness of the textile and clothing industries in the two leading world markets. (iii) Profound shifts in consumer demand, production and technology can be expected to continue in the next decade.

3. Apart from the economic consequences of dismantling the MFA, within the textile and clothing sectors as well as in other economic sectors, the consequences on the future of the multilateral trading system have also to be considered, given the close relationship between economic and trade policy issues. Furthermore, the consequences of dismantling the MFA have to be thought out bearing in mind the major problems facing the world economy in the longer run. Short term difficulties and concerns of particular enterprises and particular products cannot be solved through a perpetuation of special protection.

4. It is therefore useful to recall that at its last meeting, on 18- 19 May 1988, the Council of the OECD at Ministerial level, after having noted the main features of the current economic situation, concluded:

"OECD Governments will build on these developments in order to enhance job-creating, non-inflationary growth and to sustain it over the forthcoming years. There are no grounds for complacency".

Among important remaining challenges ministers retained the following:

- "to remain vigilant against any signs of a renewal of inflationary pressures;
- to make steady progress in reducing structural rigidities and distortions within economies and internationally;
- to strengthen the open, multilateral trading system;
- to combat and curb protectionism in all its manifestations;
- to cooperate with developing countries in addressing their problems and in working towards the full realization of their economic potential".<sup>1</sup>

## II. Feasibility and Necessity of a New Study.

5. It is certain that a dismantling of the MFA would have important repercussions on the consumption, production, employment, prices, profits, investment, imports from restricted

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<sup>1</sup>See OECD Press Communique, Press/A(88)28, Paris, 19th May 1988.  
Page 2.

and not restricted suppliers, etc., within the textile and clothing sectors as well as in other sectors. Many questions can obviously be raised concerning the possible effects of dismantling the MFA, such as, inter alia "What would happen in the major importing countries? Would factories close? Would prices for the consumers fall? Would everyone feel or realize that they had gained? Would the developments be orderly? Which exporting countries would stand to gain, and would there be those among them which would lose markets?" <sup>2</sup>

6. A new study on the consequences of dismantling the MFA could be either quantitative or qualitative. In the case of a quantitative study the main question concerns its feasibility. A quantitative study, implying an econometrical model, would require many detailed assumptions on factors other than imports restricted under the MFA such as macroeconomic conditions, exchange rates, consumption, consumer and producer prices, profits, investment, imports from non-restricted sources, exports, etc. of textiles and clothing. In the Scandinavian countries, for instance, imports from developing MFA suppliers represented in 1986 only 3-7 per cent of the value of consumption for textiles and 11-29 per cent

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<sup>2</sup>See Statement made by the Delegation of Finland, on behalf of the Nordic Countries, at the Meeting of the Negotiating Group on Textiles and Clothing, of the Uruguay Round, 13 June 1988, GATT doc. (MTN.GNG/NG4/W/14) page 5.

for clothing. The feasibility of a quantitative study is therefore highly questionable. Even a most complex model using the most up-to date econometric tools, computer techniques, etc. could not give reliable indications on which products, which enterprises, which countries would stand to lose or to gain from a dismantling of the MFA as regards production, employment, prices, profits, etc.

7. As for a new qualitative study, the first question to be raised concerns its necessity. Many studies and reports by international organizations, national administrations, research institutes and scholars on the cost, benefits and effects of the MFA have already been published. Practically all of them arrive at similar broad conclusions in qualitative terms, though the quantitative estimates might vary from one study to another depending on the economic assumptions made, on the time framework envisaged for dismantling the MFA etc. Although only some of these studies deal explicitly with the long-term consequences of dismantling the MFA, even those which have not explicitly examined the future provide a useful insight on the consequences of dismantling the MFA.

8. Furthermore, even if a forward looking approach cannot be based entirely on a mechanical extrapolation of past trends, an objective evaluation of past developments remains extremely valuable for examining future developments. Such an evaluation

has to consider all the main factors determining the state of the industry, taking into account the shifts likely to continue during the 1990s in consumer behavior, technology, marketing etc. In this respect sufficient background documentation has been made available to the GATT Negotiating Group on Textiles and Clothing by the GATT Secretariat, by submissions from the participants to the Sub-Group of the Textile Committee on Structural Adjustment and by the International Textiles and Clothing Bureau. Other useful documentation and analysis on recent trends and their implications for the future have been published elsewhere, as can be seen from the Bibliography at the end of this note.

9. Under these conditions, the necessity of a new study dealing with qualitative aspects or questions arising from a dismantling of the MFA is also highly questionable.

### III. Main Conclusions Emerging from Existing Studies.

#### A. Consumer Prices and Expenditure.

10. Practically all studies bring out clearly the heavy cost which consumers have to bear as a result of the MFA, even if the quantitative estimates vary. For example the World Bank Report 1987 (page 151), examining the cost of protection to consumers, states: "For textiles and clothing, all of the estimates for the United States amounted to many billions of dollars". The OECD study on "Costs and Benefits of Protection" (page 10) also

emphasizes the important impact on consumer prices of protection in textiles and clothing, making the additional point: "These changes in relative prices clearly fall most heavily in lower income households in the OECD region. To this must be added the fact that clothing accounts for a larger share of these households' consumption expenditure. Jenkins calculates that protecting the Canadian clothing industry costs lower-income households four times as much as it costs higher-income households". In the United States, the costs which protection in textiles and clothing "places on the American family and consumer are enormous, running in the range of \$200 to \$400 per year per household."<sup>3</sup>

11. Dismantling of the MFA would therefore lower markedly prices to consumers, especially to lower-income households. Silberstone in "The Multi-Fibre Arrangement and the UK Economy" (page 39) states that as a result of the abolition of the MFA: "A fall of 5 per cent in retail prices of clothing and household textiles would give an annual saving of £ 450 million and a fall of 10% a saving of £ 900 million. This would not be the whole of the benefit, however. The fall in price would increase purchases, by an amount dependent on the price elasticity of demand."

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<sup>3</sup>See "Economic Report of the President", Transmitted to the Congress February 1988, p.149.

12. The elasticity of consumer demand to relative prices of clothing and other textile articles has proved to be much higher than assumed in the past. It has been an important factor in explaining the remarkable expansion of consumer expenditure on clothing in real terms in the United States, the United Kingdom and other European countries. A dismantling of the MFA would therefore have a significant impact on consumers, not only by reducing retail prices, but also by increasing consumer expenditure in real terms on clothing and other textile products.

B. Employment.

13. This issue, of major concern to sectors of the textile and clothing industries of developed countries concerning the consequences of a dismantling of the MFA, has most frequently been invoked as an argument for special protection granted to these industries. It therefore deserves a more detailed scrutiny.

14. There is widespread recognition in the existing studies and policy statements of the following essential points:

(i) During the MFA employment in textiles and clothing has been declining, mainly due to productivity increases reflecting the substitution of machines for labour through automation, computerization and other labour-saving devices. In some countries this was also due to high wages in the textile industry. A recent study on Sweden, for example, states: "Meanwhile, wages that were

raised in low-productivity, structurally disadvantaged industries hastened their job shedding. This was particularly pronounced in the textile industry, where the solidaristic wage policy pushed "wages to the world's highest as part of a conscious effort to even out wage differentials. This accelerated the reduction of textile employment, through the closure of firms, redundancies and shift to higher-technology, more capital-intensive production."<sup>4</sup>

(ii) Even if dismantling of the MFA might accentuate the decline in employment, its effect would be only relatively small as compared with the major determinants of job shedding.<sup>5</sup> The OECD study on "Costs and Benefits of Protection", concludes (page 117) "...the net impact of protection on employment even in clothing should not be exaggerated".

(iii) The dismantling of the MFA would lead to employment gains in other industries, which would become more competitive. Silberstone, on the basis of the simulations with the growth model used, even concludes that following a dismantling of the MFA "the

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<sup>4</sup>International Labour Office, Guy Standing, Unemployment and Labour Market Flexibility: Sweden, 1988, p50

<sup>5</sup>For some quantitative estimates of the consequences on employment of dismantling the MFA, see A. Silberstone, The Multi-Fibre Arrangement and the UK Economy, p.42 and W. Cline, The Future of World Trade in Textiles and Apparel, 1987, pp.234-242.

macroeconomic effects of a fall in import prices should be good for employment generally, so that the number of new jobs created should equal, or even outweigh, the number of jobs lost."<sup>6</sup> Furthermore, the increase in consumer expenditure on clothing in real terms, resulting from a dismantling of the MFA through the decline in consumer prices, would have a beneficial effect on employment in retail trade in textile and clothing. It is noteworthy in this connection that in the United States, for example, between 1974 and 1986 employment in textiles and clothing had declined by 500,000 while employment in textiles and clothing retail shops increased by nearly 300,000.<sup>7</sup>

(iv) There is a high cost in preserving jobs through protection. Each job thus preserved ends up costing consumers more than the workers' salary.<sup>8</sup>

(v) Job maintenance through MFA protection in otherwise noncompetitive textiles and clothing enterprises does not really secure employment in the longer-term. In this connection the OECD states: "It should also be noted that whatever jobs are saved through import controls need not go to those whom the measures

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<sup>6</sup>Z.A.Silberstone, The Multifibre Arrangement and the U.K. Economy, op.cit., p.43.

<sup>7</sup>See U.S. Department of Labour, Supplement to Employment and Earnings, various issues.

<sup>8</sup>See World Bank, World Development Report 1987, op.cit. p.152.

were originally intended to protect. Thus, major changes have occurred in the regional distribution of clothing industry employment in recent years. These are most marked in the United States, where the share of New England and the Middle Atlantic region in apparel industry has declined by some 25 percentage points since 1960. This reflects the industry's search for the lowest-cost sites within its protected markets. As a result of these regional shifts, the job gains due to protection have had little positive impact on the employment pools most adversely affected by the industry's long-term decline. The United States figures imply that, even had protection been sufficient to maintain overall employment in 1976 at its 1970 level, regional shifts alone would have reduced employment in the North by 70 per cent. Whatever net job creation there was a result of protection presumably went entirely to the areas (mostly in the South and South-West) which were in any case benefiting from the regional shifts in economic activity."<sup>9</sup>

C. Prices, Profits and Investment.

15. (i) In the textile and clothing industries. Most studies on the effects of the MFA have come out with the conclusion that

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<sup>9</sup>OECD, Costs and Benefits of Protection, op.cit., pages 117 and 120.

its discriminatory restrictive measures have resulted in higher prices received by producers in developed countries, thereby improving their profit situation.<sup>10</sup> This in turn has been conducive to artificially stepping up investments, mainly in labour-saving equipment in order to increase their competitiveness, but also in expanding their capacities. The expectation that protection through the MFA will continue without any time limit has also been a powerful motivation for textile and clothing enterprises in developed countries to expand their investment plans well beyond what would have been the case in the absence of restrictions. It is therefore safe to assume that a dismantling of the MFA would have a major impact on prices received, and profits gained, by textile and clothing enterprises in developed countries. Such a dismantling would also tend to reduce investments in those textile and clothing enterprises which would lose their competitiveness.

16. (ii) In other industries and economic sectors. A dismantling of the MFA would have beneficial effects on other industries and economic sectors of the developed countries for the following reasons: (a) Following the reduction in producer prices, a number of textile and clothing enterprises would face a decline

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<sup>10</sup>See for instance, The World Bank, World Development Report, 1987 op.cit., p.152; OECD, Costs and Benefits of Protection, op.cit.p.109; Z.A.Silberston The Multi-Fibre Arrangement and the UK Economy, op.cit.p.31.

in their profits and investments and some others would have to give up production lines in which they are no more competitive. This would free scarce resources, mainly capital, for other more productive uses, which would contribute to a more efficient utilization of all factors of production. (b) It would benefit industries and other economic sectors in developed countries having important markets in the developing countries exporters of textiles and clothing, which would see their export earnings and import capacity rise as a result of the dismantling of the MFA.

D. Technological Shifts.

17. The consequences of a dismantling of the MFA have to be seen in relation to the technological "revolution" taking place in the textile and clothing industries. Most sectors of the textile industries have already become more capital intensive, with the result that the advantage enjoyed by suppliers in lower-income countries because of their lower labour costs have been increasingly offset by their higher capital and other non-labour costs. In the clothing industries the comparative advantage of developing countries can also be expected to be gradually eroded in a growing number of product lines as a result of fast technological advances in automation, computerization, etc.

E. Enlarged Domestic Markets with no Internal Barriers. Effects on Efficiency and Competitivity.

18. Textiles and clothing industries of the developed countries have increasingly benefitted from the proximity of huge domestic markets (the United States) or huge markets where they face no trade barriers (EEC and EFTA). The importance of this factor in raising the efficiency and competitiveness of these industries can be expected to grow further in the future, with the establishment of the North American Free Trade area and the completion of the internal market in the European Community.

19. It is relevant to emphasize in this connection the following conclusions drawn by the Commission of the EEC in its assessment of the potential economic effects of competing the internal market: "... The role played by external trade, as a means of market expansion that makes it possible to bring the effective size of units of production closer to the optimum and thus achieve gains in technical efficiency, has been established".<sup>11</sup>

20. A dismantling of the MFA would only permit the restricted suppliers to compensate, at least partly, for the loss in competitiveness resulting from the enlarged markets enjoyed by the

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<sup>11</sup>Commission of the European Communities, The Economics of 1992, p.117.

textiles and clothing industries in many developed countries.

F. Structural Adjustment and Efficient Allocation of Resources.

21. A dismantling of the MFA would greatly encourage the process of structural adjustment and lead to a more efficient allocation of resources both within the textile and clothing sectors, and in the economy as whole. This important aspect has to be highlighted bearing in mind the long term priorities set out at the last OECD Council meeting at Ministerial level, as well as at the Toronto Summit. On both occasions the emphasis has been increasingly lead on structural issues, less rigidities and more willingness to structural adjustment through market forces. In a recent article "Governments are looking behind the numbers" the U.S. representative to the OECD wrote: "Toronto signals a broad shift in the focus of economic policy toward greater reliance in incentives and competition... Economic performance as well as the discourse of economic policy itself will increasingly center on structural issues - in the quality of education, the quality and composition of public expenditure, businesses assimilation of new technology, the capacity for adjustment".<sup>12</sup>

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<sup>12</sup>See: International Herald Tribune, 6 July 1988, p.4.

G. Supply Constraints in Developing Countries.

22. The existing studies have also brought out the fact that when examining the consequences of dismantling the MFA the supply elasticity in developing countries should not be exaggerated. First, in all developing countries there is a vast potential of increased domestic consumption, taking into account the growth of population and the still low level of consumption of textiles and clothing per head. Secondly, several major suppliers of textiles and clothing among developing countries are increasingly faced with supply constraints reflecting faster wage increases and a gradual shift in their comparative advantage to less labour intensive products.

H. Impact on the World Trading System.

23. As regards the consequences of a dismantling of the MFA on the world trading system, the OECD study on "Structural Adjustment and Economic Performance" presented to the meeting of the OECD Council at Ministerial Level in May 1987, had the following to say in the Section entitled Strengthening the Trading System of the chapter dealing with World Trade: "Looking to the future, the scope for gains from trade will, if anything, increase.... Securing these gains requires a strengthening and extension of the open, multilateral trading system." Among the priorities standing out in this respect, "The first is to dismantle the protectionist measures which - having been put in

place to ease immediate sectoral problems - have become an enduring feature of the landscape. The regulation of agricultural trade ... is of special importance in this respect; but the Multi-Fibre Agreement and the differing trade restrictions with which it is associated stand out in the industrial context. When the current Agreement expires, fully thirty years will have passed since the first derogations of textiles trade from the ordering discipline of the GATT - derogations which were intended to be strictly temporary. While there has indeed been considerable structural change in the OECD clothing and textiles industries, there is little evidence that the MFA has contributed to the efficiency of this process or of its outcomes, while the costs the MFA engenders - not only for consumers but for the economy as a whole - are increasingly widely recognised."<sup>13</sup>

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<sup>13</sup>OECD, Structural Adjustment and Economic Performance, 1987, op.cit page 279.

IV. List of Studies, Reports and other Documentation relevant to the examination of "Consequences of Dismantling the MFA.

A. Costs and Benefits of Protection through MFA(Including Consequences of Dismantling the MFA).

1. World Bank, World Development Report, 1987.
2. OECD, Costs and Benefits of Protection, presented to the OECD Council meeting at Ministerial Level in April 1985, Paris, 1985.
3. OECD, Structural Adjustment and Economic Performance, presented to the OECD Council meeting at Ministerial Level in May 1987, Paris 1987.
4. Economic Report of the President Transmitted to the Congress, Washington, Feb.1988.
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6. Jenkins, G.P. Costs and Consequences of the New Protectionism:The Case of Canada's Clothing Sector, 1980
7. Kalantzopoulos, Orsalia, "The Cost of Voluntary ExportRestraints for Selected Industries" Industry Department, World Bank, 1986.
8. Pelzman, Joseph, Economic Costs of Tariffs and Quotas onTextile and Apparel Products Imported into the United States, Weltwirtschaftliches Archiv, Heft 3, 1983.
9. Pelzman, Joseph, The Multi-fibre Arrangement and its Effect on the Profit Performance of the U.S. Textile Industry. National Bureau of Economic Research, 1983.

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  11. Wolf, Martin, et.al. Costs of Protecting Jobs in Textiles and Clothing, Trade Policy Research Centre, 1984.
- B. Documentation Available to the GATT Negotiating Group on Textiles and Clothing.
12. GATT, Updating the 1984 GATT Secretariat Study "Textiles and Clothing in the World Economy", doc. MTN.GNG/NG4/W/8, 30 Nov. 1987
  13. GATT, "Report by Textiles Surveillance Body on its activities during the period 1 August 1986 to 30 September 1987", doc. COM.TEX/SB/1316 and Addendum 1.
  14. GATT, "Information received by the technical sub-group in response to the Textile Committee, sub committee on Adjustment, the questionnaires set out in doc. COM.TEX/W/193, Dated 16 March 1987", docs. COM.TEX/54 and Suppl.1 and Add.1
  15. GATT, "Textile and Clothing Statistics", doc. COM.TEX/W/197, 23 Nov. 1987
  16. GATT, "Recent Developments in Demand, Production and Trade in Textiles and Clothing", doc. COM.TEX/W/198, 27 Nov. 1987.
  17. ITCB, "The Evolution of the State of the Textiles and Clothing Industries in United States and European Economic Community", circulated as GATT doc. MTN.GNG/NG4/W/5, 10 July 1987.
  18. ITCB, "The Evolution of the State of the Textiles and Clothing Industries in Canada, the Nordic Countries and Austria", circulated as GATT doc. MTN.GNG/NG4/W/7, 20 Nov. 1987

19. ITCB, "The Evolution of the State of the Textiles and Clothing Industries in Japan and Switzerland", circulated as GATT doc. MTN.GNG/NG4/W/9, 7 Dec. 1987.
  - C. Other Documentation Relevant to "Consequences of Dismantling the MFA"
20. GATT, Textiles and Clothing in the World Economy, July 1984.
21. GATT, International Trade, 85-86, Chapter 1, pp. 28-31
22. ILO, Recent Events and Developments in The clothing industry, General Report, Third Tripartite Technical Meeting for the Clothing Industry Geneva, 1987.
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27. Economic Council of Canada, Adjustment Policies for Trade Sensitive Industries Ottawa, 1988

28. Economic Intelligence Unit, World Textile Trade and Production Trends, 1988.
29. Financial Times Conference, World Textiles into the 1990s  
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