

# Competitiveness of the Textile and Apparel Sector of Uzbekistan

Recommendations for Entering the Global Value Chain

August 2022



# Uzbekistan's Textile & Apparel Competitiveness Study

The aim of this competitiveness study is to define how Uzbekistan can compete with selected players/countries in the international market as it enters the global value chains, and whether and on what conditions vertical integration is possible. This study is part of Better Work's Feasibility Study and will be shared within IFC and potentially with interested parties externally who are considering Uzbekistan as a new sourcing destination.

The main objective of the study is to assess the competitiveness of Uzbekistan vis a vis selected comparator countries globally as a key driver for a medium to long-term strategy to grow Uzbekistan's textile and apparel sector and increase its market share. The study is based on a data-driven model which IFC has developed for the purpose of this study – similar to the analysis global brands/retailers undertake when deciding on a new sourcing destination for textile/apparel.

## **METHODOLOGY**

The study was carried out by Prof Heikki Mattila, IFC's global Textile & Apparel Industry Specialist between June-August 2022. Data were collected from publicly available sources and from individual apparel and textile companies in nine countries. The study compares Uzbekistan's textile and apparel sector's competitiveness with 8 other countries for the two main export markets for global brands/retailers: EU and US. IFC staff, IFC consultants and ILO (Better Work) staff collected the data.

## **COMPARATOR COUNTRIES**

China, India, Pakistan, Vietnam, Bangladesh, Turkey, Egypt, Morocco, and Ethiopia.

## **PRODUCTS FOR COMPARING PRICES AND COSTS FOR UZBEK EXPORTS: YARN, FABRIC, AND SIMPLE APPAREL PRODUCTS (T-shirt, Polo shirt, Jeans)**



T-shirt

Polo Shirt

Jeans

Cotton Yarn

Knitted Fabric

Denim Fabric

# Definitions

<b><i>CMT (Cut, Make and Trimmings)</i></b>	The supplier sells production capacity only, materials are bought and provided by the client.
<b><i>FCL (Full Container Load)</i></b>	The cargo occupies the full container.
<b><i>FOB Price (Free On Board)</i></b>	Ready to be shipped price.
<b><i>Full Package</i></b>	The supplier sources or produces raw materials for making the garment.
<b><i>Import Duty</i></b>	Import duty rate (%) on the total of FOB price and transport costs payable by client in the destination country.
<b><i>LCL (Less Than Container Load)</i></b>	A small volume cargo occupies a part of the container together with other cargos.
<b><i>Landed Price (Total cost to brands/retailers in destination country)</i></b>	FOB price + Transports Costs + Import Duty.
<b><i>LPI (Logistics Performance Ranking)</i></b>	The World Bank's LPI ranking measures trade logistics performance of a country.
<b><i>Transport Cost</i></b>	Freight, insurance, forwarding charges.
<b><i>TechPack</i></b>	Detailed product specifications supplied by the client (e.g. brand) for making the garment, often including patterns.

# Global Buyers' Perspective

Z A R A



H&M

DECATHLON



International apparel buyers (=global brands and retailers) rate and select suppliers and countries according to the following attributes:

## **Lead Times and Ease of Doing Business**

- Lead time from the factory to destination by sea/road/air transport.
- Are yarns, fabrics and accessories available in the country, or do they need to be imported?
- One-stop-shop, i.e. is the supplier vertically integrated with in-house fabric production?
- Ease of organizing transports, such as any problems with customs clearance of incoming materials and outgoing products, any concerns regarding payment transactions and currency movement, etc.

## **Price and Costs**

- Operating costs of a country, such as labor costs, cost of energy, etc.
- Trade related costs, such as import duty rates on materials and products, administrative charges, etc.
- Landed price, i.e. what is the price of a product imported and duty paid in the destination country.

## **Operations**

- On what level in the value-added curve the supplier is (CMT, Full Package, R&D capability, Integration into weaving, knitting, spinning)
- Production efficiency compared to other suppliers and supplier countries.
- Management and operator skills.
- Quality of products and operations.
- R&D capability, i.e. is the supplier able to contribute to client's design (i.e. brand/retailer's design) and product development effort?

## **Sustainability & Traceability**

- Globally recognized standards and certificates such as BCI, Better Work on environmental & labor standards
- Are there any red flags regarding sustainability?
- Can the origin of cotton be traced throughout the entire value chain: traceability from finished garment to cotton fields?
- Willingness to fulfill the requirements of client's (i.e. brand/retailer) Code of Conduct for suppliers?

# A Highly Competitive Global Industry

The most successful countries and companies control the whole textile value chain from fibers to ready-made products, while Uzbekistan has strong yarn production, but so far is weaker in fabric and garment production relative to other countries.

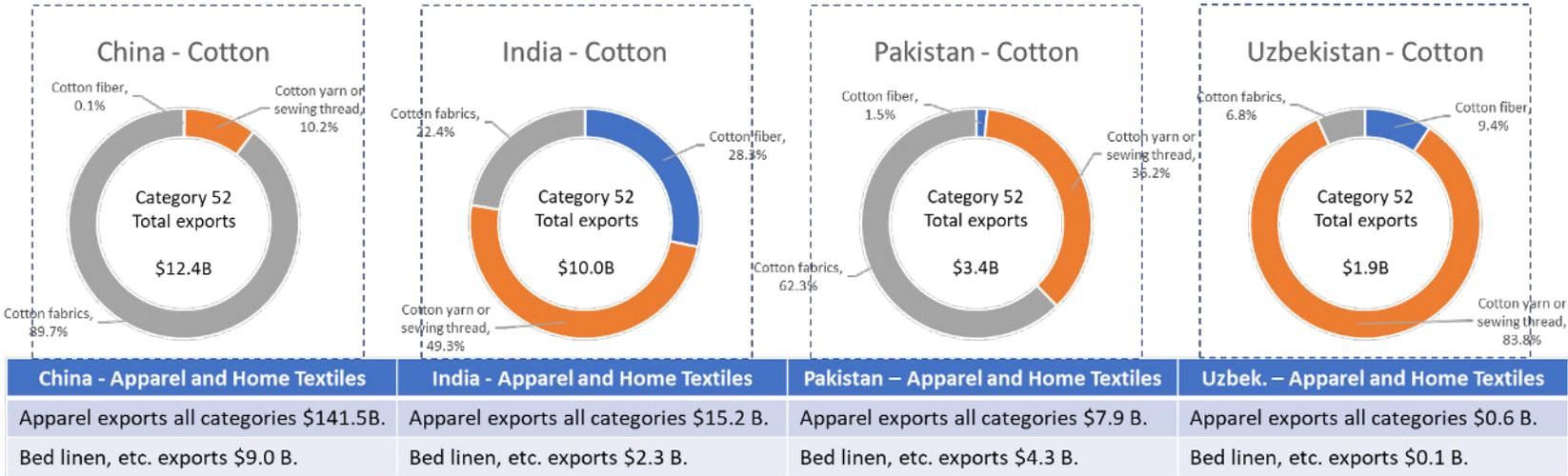
Cotton producing countries like Pakistan, China, India, Egypt, and Turkey have integrated downstream in the global value chain, towards ready-made production, while non-cotton countries, such as Bangladesh, Morocco and Vietnam are integrating upstream, from garment manufacturing to fabrics and yarns.

Exports of Category 52 (cotton fibers, yarns, and fabrics) consist mainly of fabrics in China and Pakistan, while in India and Uzbekistan the focus is on yarns (data for 2021). To become a global player, Uzbekistan needs to build up fabric production capacity to feed the local garment industry.

## GLOBAL TEXTILE AND APPAREL VALUE CHAIN



## Export Spreads of Four Cotton Countries in 2021



# Uzbekistan's Textile and Apparel Industry Today

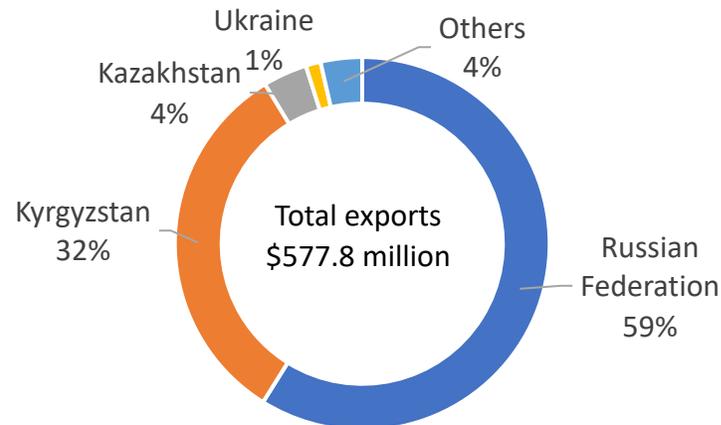
Uzbekistan's textile and apparel industry consists of 134 cotton producing clusters and over 5,600 manufacturing companies. Many of the RMG companies are, however, small and domestic/regional market oriented. The total \$0.6 billion exports of apparel products in 2021 is still low compared to, for example the near-by competitors Egypt (\$2.0 billion), Morocco (\$3.4 billion), and Turkey (18.3 billion).

The destination countries of Uzbekistan's apparel exports are Russia, Kyrgyzstan, Kazakhstan and other parts of Central Asia. Only small quantities of woven garments are exported to Europe (e.g. Germany and Poland). Leading international brands are not yet sourcing garments from Uzbekistan – but given the lifting of cotton pledge in March 2022, many are actively considering sourcing of cotton/yarn/fabrics/garments from UZ.

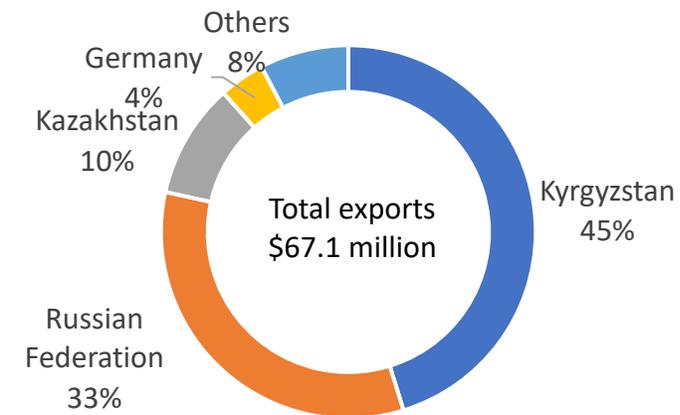
## Uzbekistan's textile industry

	No. of companies	Production in 2021
Cotton fibers	134	1.0 million ton
Spinning mills	150	862 thousand ton
Fabric manufacturers	130	717 million m2
Knitting mills	250	203 thousand ton
Hosiery manufacturers	110	458 million pairs
RMG manufacturers	5,600	2.0 billion pieces

### Knitted garment exports in 2021



### Woven garment exports in 2021



# Competitive lead times to EU – but Logistics Remain Challenging

A short lead time is highly attractive to buyers, as it improves inventory turns and speed of reacting to demand. Lead time by road to EU from Uzbekistan is very competitive, close to that of Turkey and Morocco.

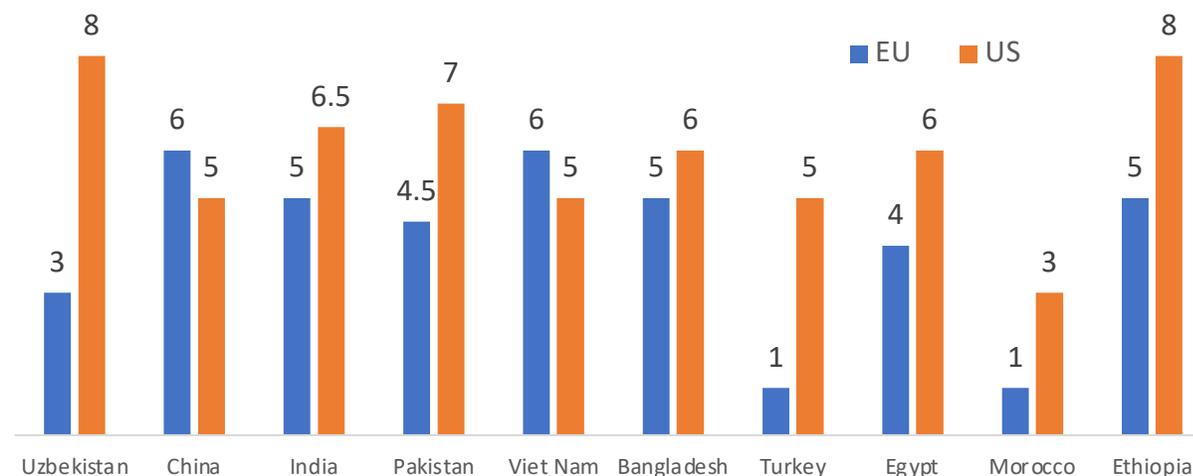
**The average Lead time from UZ to EU is 3 weeks** – at least 2 weeks faster than China, India, Pakistan, Vietnam, Bangladesh and Ethiopia. Turkey and Morocco can export to EU one week faster than UZ.

Due to being land-locked, **lead time to the USA is 8 weeks** – one to two weeks longer compared to the other countries.

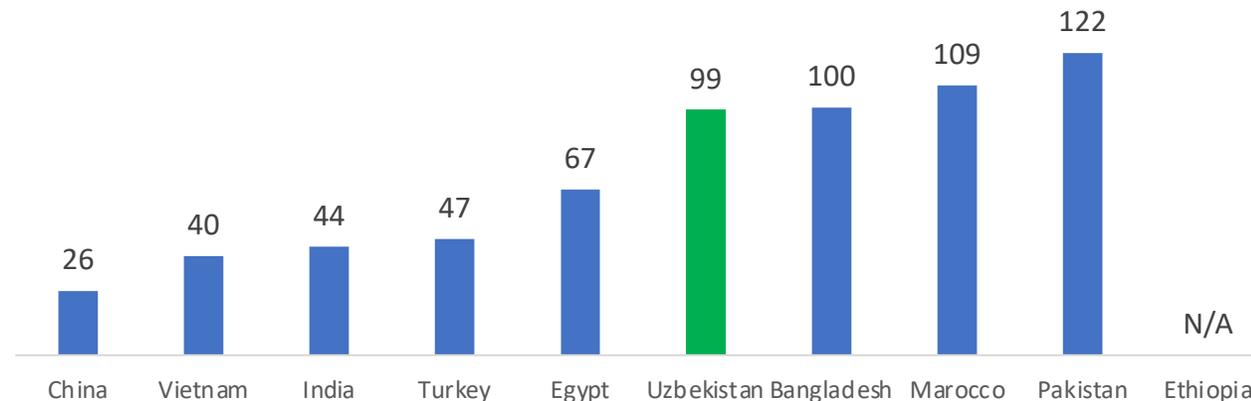
In addition to lead times, **the attractiveness of a supply country depends on skills, quality, sustainability, and the ease of doing business**. The World Bank's LPI ranking measures trade logistics performance of a country in terms of customs performance, infrastructure quality, ease of arranging shipments, logistics service quality, consignment tracking, and tracing & timeliness of shipments.

Uzbekistan's ranking is number 99: worse than China, Vietnam, India, Turkey, and Egypt, but better than Bangladesh, Morocco and Pakistan. Germany is rated the best (number 1), and Afghanistan worst (number 160).

**Lead times of sea/road transport to EU and US in weeks**



**World Bank Logistics Performance Ranking (LPI) 1 = the best**



# Uzbekistan's Exports are Duty Free to EU Only

Uzbekistan as well as Bangladesh, Pakistan, Egypt, Morocco, and Ethiopia have duty free access in the EU. From China, the tariff is 12%, from India 10% and Vietnam 6%. Without the 70% subsidy that currently exists until 01 April 2023, Uzbekistan's freight costs are not competitive in EU, but due to 0% duty the total cost is still competitive vs. Asian suppliers

In the US market, Uzbekistan is the least competitive, but with 70% transport subsidy could be equally competitive to China, Vietnam, and Turkey. Morocco and Ethiopia with 0% import duty are the most competitive countries.

Landed prices are calculated for a 40-foot container with 85% filling rate. The freight cost per product would be up to 90% higher in a 20-foot container, while in LCL (Less Than Container Load) in a 40-foot container the unit cost is almost the same as in FCL (Full Container Load). Lead time when using LCL will, however, be 4-7 days longer.

## Import duties

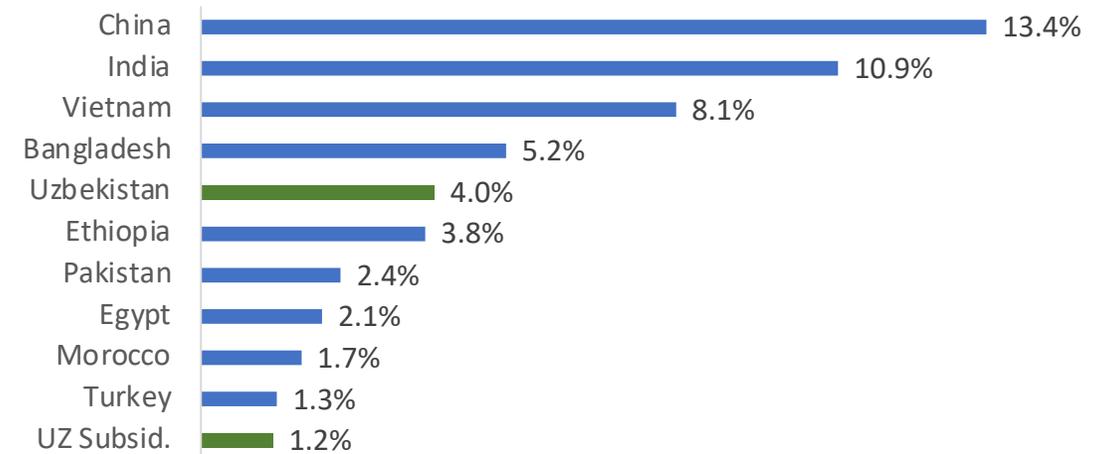
Import duty for cotton garments in the EU							
0%		6%		10%		12%	
Bangladesh	Egypt	Vietnam		India		China	
Ethiopia	Morocco						
Pakistan	Turkey						
Uzbekistan							

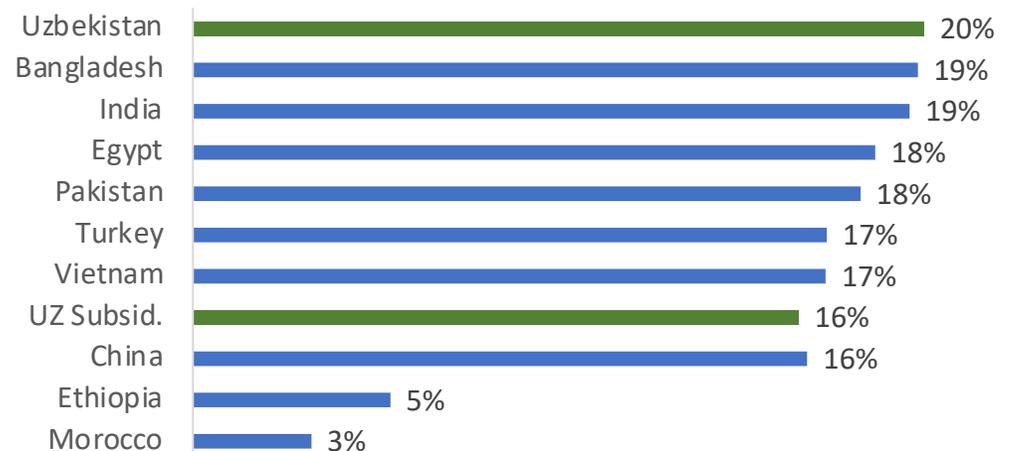
Import duty for cotton garments in the US							
0%		17%					
Morocco	Ethiopia		China	India	Pakistan	Viet Nam	
		Bangladesh	Turkey	Egypt	Uzbekistan		

## – Freight Costs to EU/US Remain High

### The share of freight + duty in Landed price of a cotton T-shirt in EU



### The share of freight + duty in Landed price of a cotton T-shirt in USA



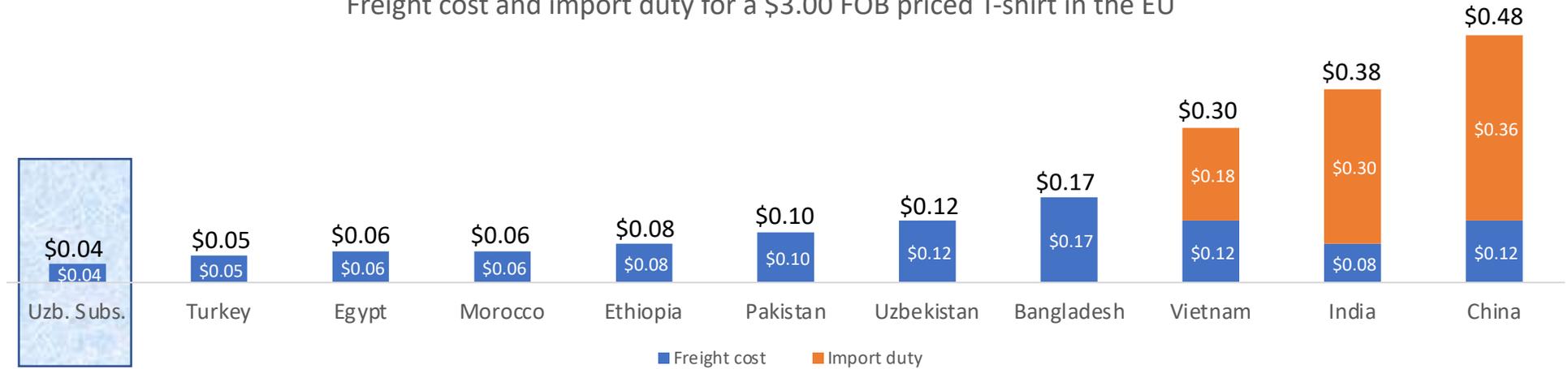
# Landed Price in EU for Uzbekistan is Most Competitive of All Countries, but the Least Competitive in the US

Landed price from UZ is the most competitive in the EU with the current 70% transport subsidy, as only \$0.04 would be added to the \$3.00 FOB price of a T-shirt.

The 70% transport subsidy would not have equally dramatic impact on exports to the US due to 17% import duty, which applies also to competing countries except for Morocco and Ethiopia.

Prices, however, are style specific depending on the cost of materials and the efficiency of the supplier. Therefore this breakdown is relative and applies to freight costs and import duties only.

Freight cost and import duty for a \$3.00 FOB priced T-shirt in the EU



Freight cost and import duty for a \$3.00 FOB priced T-shirt in the US



# The Average FOB Price from all countries for a T-shirt is \$3.00, but varies depending on style

The share of materials and direct labor cost in FOB price is between 55%-65% across all the countries of this study. In Uzbekistan, the share of material cost is in the lower end, due to own cotton production. The cost of transports and import duty are added to get the Landed Price which the client pays in the destination country.

Prices from different companies and countries cannot be directly compared as they are style sensitive depending on material construction and product details.

Due to 0% duty and subsidized transport costs, **“Landed Prices” from Uzbekistan in the EU are more competitive than from other countries of this study.**

## Breakdown of manufacturing costs for a T-shirt with \$3.00 FOB price



### FOB and Landed Price spread from different companies for this study

	FOB Price	Landed Price in EU	Landed Price in USA	Landed Price in Bangladesh
T-shirt \$/pc	1.89 – 4.50	1.97 - 4.90	2.00 – 5.42	
Polo Shirt \$/pc	2.80 – 8.76	2.88 – 8.82	2.91 – 8.87	
Jeans \$/pc	4.50 – 10.75	4.65 – 10.83	4.71 – 11.03	
Cotton Yarn \$/kg	3.63 - 4.75			4.47 – 5.51
Knit Fabric \$/kg	3.00 – 8.40			4.13 – 10.82
Denim Fabric \$/m	3.75 – 5.00			4.77 – 6.34

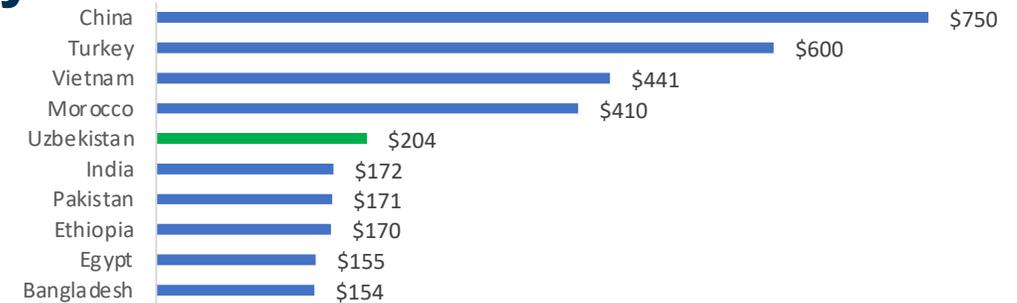
# Uzbekistan has Competitive Labor & Energy Cost, but Productivity is Lower

In terms of labor costs, Uzbekistan is very competitive, on par with India, Pakistan, Ethiopia, Egypt and Bangladesh. A part of this cost advantage is however lost due to low average production efficiency, which at 50% is lower than the comparator countries (60-70%). In apparel production, the efficiency is impacted by operator and management skills, as well as production machinery, equipment and work-flow engineering.

Production efficiency in Uzbekistan's apparel manufacturing is estimated at 50% compared to international standards. High efficiency levels in Morocco, Turkey, Vietnam and China have been achieved through latest production machinery, up-to-date production systems, managerial skills and decades of development. (Source: Industry surveys, client and stakeholder interviews)

Power and gas prices are extremely competitive in Uzbekistan, as the tariffs are heavily subsidized by GOU. The tariffs, however, are expected to increase in mid-term. The share of power and gas costs are high in yarn and fabric production, while less important in apparel manufacturing.

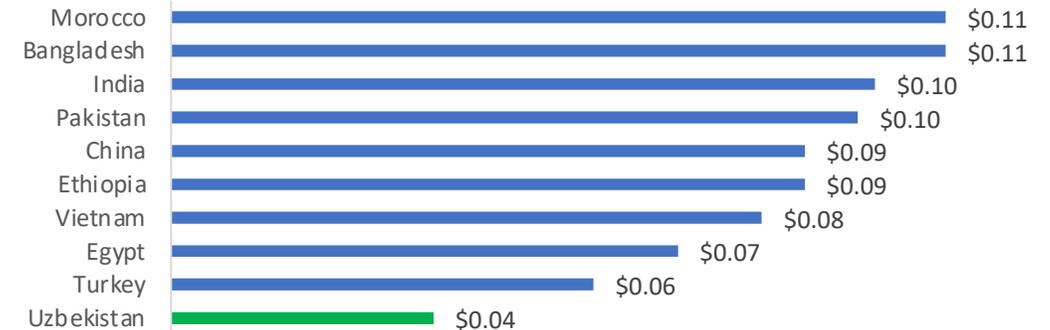
## Labor cost US\$/month



## Garment Production efficiency



## Electric power US\$/kWh



# Benefits from Vertical Integration

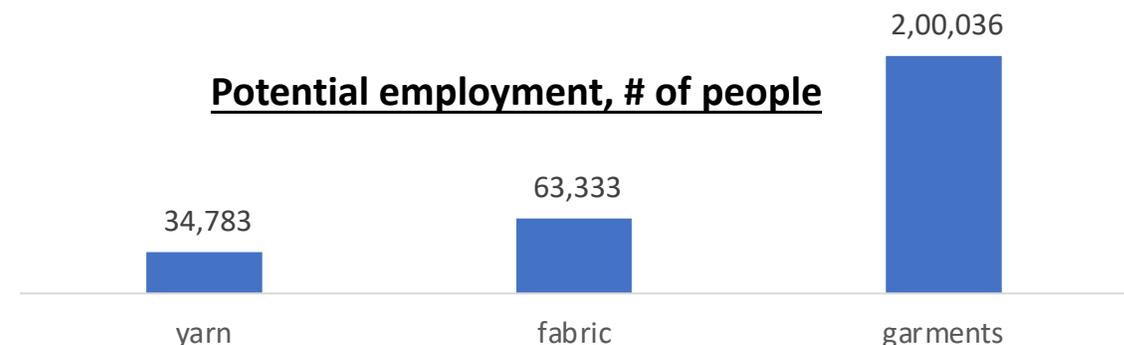
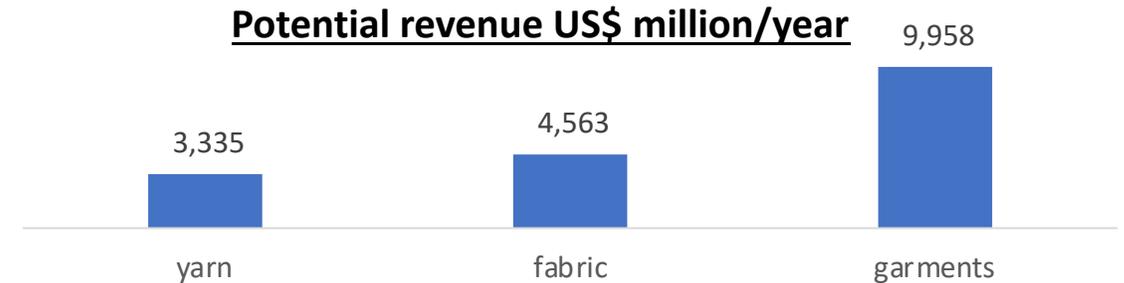
To integrate vertically would be more profitable for Uzbekistan compared to selling only fibers and yarns. Currently, goods from the value chain are sold mainly as yarn, while large quantities of fabrics are imported for garment production.

By covering the entire textile/apparel value chain from cotton to garments, Uzbekistan's cotton-based industry will produce higher revenues and EBITDA, as well as create more industrial jobs compared to selling only yarns or fabrics. The cotton output of 1.0 million tons/year has a potential to produce 0.8 million tons of yarn, 0.8 million tons of cotton fabrics and 2,153 million pieces of light weight cotton garments, such as T-shirts and Polo shirts.

From fully integrated textile/apparel industry, **the revenue from garment sales would be about US\$10 billion compared to US\$3.3 billion from yarn sales and US\$4.6 billion from fabric sales.** The overall value-added of the industry would increase, as EBITDA/kg from garment sales would be 1.61 US\$/kg compared to 0.39 US\$/kg or 0.48 US\$/kg from yarn or fabrics sales respectively. Furthermore, investments in proportion to output in yarn and fabric production are much higher than in garment manufacturing.

## Uzbekistan's Value Chain Potential with Domestic Cotton

		Cotton fiber	Cotton yarn	Cotton fabric	Cotton garments
Output	kg or pcs million	1,000	800	760	2,153
Unit price	US\$/kg ,pc		4.17	6.00	4.62
Sales	US\$ million		3,335	4,563	9,958
EBITDA	US\$ million		310	365	1,220
EBITDA/kg	US\$/kg		0.39	0.48	1.61
Output/person/year	kg, pcs		23,000	12,000	10,765
Employment	persons		34,783	63,333	200,036



# Conclusion

## Strength and Weaknesses of Uzbekistan's Textile and Apparel Industry



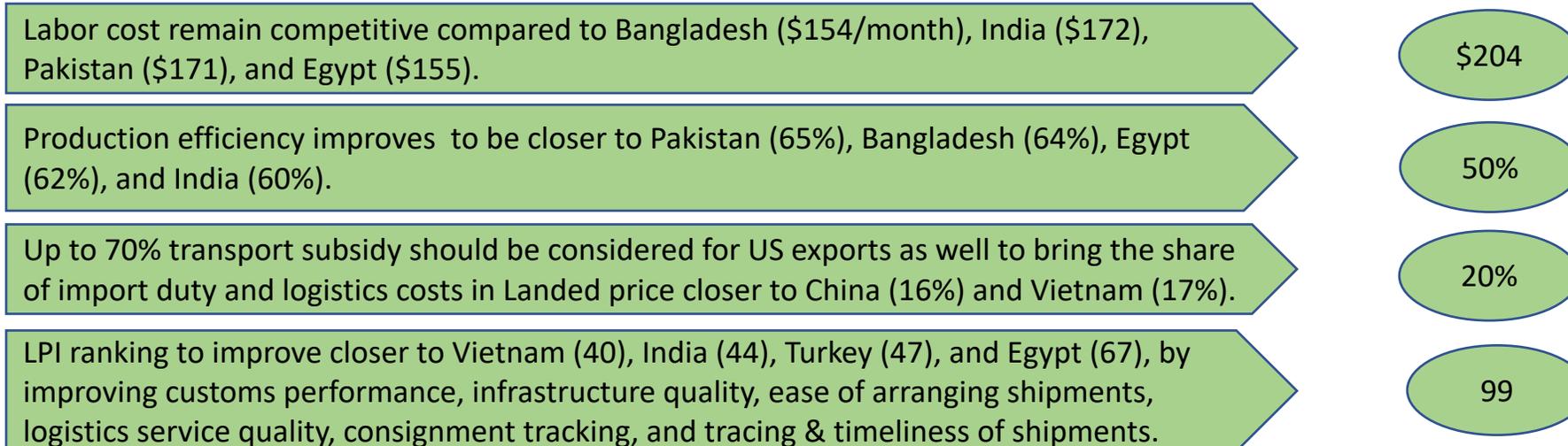
- Landed Prices from UZ are most competitive in the EU due to 0% duty and subsidized transports.
- Cotton is available domestically for mid and high-count yarns.
- Cotton yarn production is competitive due to high quality machinery and management know how brought in by FDIs
- Competitive labor cost and energy cost.



- The country is double landlocked, and fabrics and apparel export volumes are still low, mainly targeting Russia and Central Asian markets, despite of transport subsidies to EU
- Landed price in the US is higher than competitors.
- Accessories and embroideries are imported.
- Lower than peers' production efficiency level in apparel manufacturing.
- Uzbekistan's image as global apparel sourcing destination is not yet established globally.

### Uzbekistan's Garment Industry can be Globally Competitive in the Export Markets, provided that

#### Uzbekistan today



# Recommendations to Increase Uzbekistan's Market Share in Globally Competitive Industry

Uzbekistan is competitive with own source of cotton and top-of-the-class spinning mills. More than 5,000 garment manufacturers operate mostly locally or regionally. Vertical integration requires increasing of knitting and weaving capacity and improving apparel manufacturers' productivity and R&D capability, by the spinning mills integrating downstream to fabric manufacturing, or garment manufacturers integrating upstream to fabric production.

Textile and apparel industry can be very profitable and beneficial to a country. Vertical integration produces and sell higher value-added goods, increases export earnings and employment, as demonstrated by cotton producing countries in Asia (China, Pakistan, and India). The key in creating a vertically integrated textile/apparel industry is to capture the interest of the globally leading brands and retailers in the EU and the US which requires concerted efforts & time. For example, it took over 30 years for China, Bangladesh and Vietnam to become the world's leading apparel exporters.

## Buyer's Requirements

### Lead time & Ease of Doing Business

- Short lead time
- Capable management
- One-stop-shop for materials, accessories and garments
- Efficient customs clearances, low bureaucracy in travel, shipments and trade financing
- Ease of finding suitable suppliers



## Recommendations

Global buyers are interested in garment suppliers with access to materials (one-stop-shop), i.e. the apparel/home textile manufacturer drives the whole value chain and organizes yarn and fabric production according to clients' wishes. In-house material production reduces the total lead time, as planning of material production is in own hands. **Vertical integration is vital and recommended.** Local manufacturing of accessories should be started and importing of accessories not made in UZ should be made barrier-free.

Management training by international consultants is recommended for building up **international marketing capabilities and understanding of how to do business with EU and the US.** Uzbek textile and apparel manufacturers should be actively promoted through direct contacts to leading brands, match-making events, trade fairs, web-sites, etc.

On national level, **trade barriers need to be brought down.** Customs clearance, organizing shipments and trade financing need to be made less bureaucratic. The firms may need advice on how to organize speedy and cost-efficient transports.

# Recommendations continued

Buyer's Requirements
<p><u>Prices &amp; Costs</u></p> <ul style="list-style-type: none"><li>• Competitive labor cost</li><li>• Competitive Landed Price (FOB price + freight + import duty)</li><li>• Source of competitively priced materials</li><li>• Competitive terms of payment</li></ul>
<p><u>Training &amp; Skills</u></p> <ul style="list-style-type: none"><li>• Management know how</li><li>• Operator skills</li></ul>



Recommendations
<p>Labor cost (\$204) should remain competitive compared to Bangladesh (\$154/month), India (\$172), Pakistan (\$171), and Egypt (\$155).</p> <p>The Landed price in exports to the EU, impacted by import duty and transport costs, is more competitive from Uzbekistan compared to the other countries of this study. In the US market, Uzbekistan would be equally competitive as China, Vietnam and Turkey, if the same transport subsidy as in the EU is available, and if transport subsidies could be sustained overtime. The Government of Uzbekistan should actively negotiate these terms to make US market entry feasible.</p> <p><b>An integrated company</b> has more freedom in pricing materials compared to when fabrics are bought from local or international market. Vertically integrated companies are more competitive.</p>
<p>Improving garment manufacturing efficiency requires the latest machinery, advanced management skills, and operator performance. FDIs are a great way of bringing <b>management know-how</b> into the country, as has happened with the spinning industry in Uzbekistan. Using international consultants for improving material utilization and garment efficiency is recommended.</p> <p><b>In the medium to long run</b>, Uzbekistan needs <b>training facilities throughout the country with up-to-date education streams</b> for educating technical skills as well as middle and top management for the industry, including textile colleges and universities as well as competence centers. International advice should be used for setting up such facilities.</p>

# Recommendations continued

## Buyer's Requirements

### Operations

- High quality machinery and management
- Flawless product quality
- High production efficiency
- R&D capability with digitized equipment
- Access to lab testing of materials



### Sustainability & Traceability

- Compliance with E&S standards
- No red flags
- Compliance with Code of Conduct



## Recommendations

CMT and Full-Package, the so-called Tech-Pack business is a start, but Uzbekistan garment manufacturers need **to climb up the value-added complexity curve to start providing R&D services to clients and gradually becoming a strategic supply partner to them.** Such customer relationships are more loyal, value-added and give exposure to clients' long-term sourcing plans. Digital design systems together with design skills are needed for communicating with clients and for doing sampling virtually. Later, setting up of design offices in the EU and US becomes necessary.

Production efficiency should improve from 50% to similar level in Pakistan (65%), Bangladesh (64%), Egypt (62%), and India (60%). This is achievable through international advisory and consulting services.

**International consultants are recommended** for developing R&D capability, proper quality assurance systems, and testing facilities. Consultants can also advice on work-place engineering, layouts, workflows, standard time systems and production management. Focusing on home textiles is also recommended, as it is a cotton-based product category and can become a successful business as demonstrated by India and Pakistan.

**Uzbekistan should actively promote itself as one of the few garment producing countries globally with potential for full traceability** – an increasing ask of brands/retailers, and consumers. These efforts are underway and already supported by international organizations which can also assist in improving sustainability standards. Match-making events, trade fairs, webinars and direct contacts need to be organized. Leading fashion brands/retailers (e.g. Inditex) are considering sourcing from Uzbekistan: getting started with them will pull in others.