BSP2 PERFECT-LINK PROJECT

COMPETITIVENESS IN TEXTILE AND CLOTHING SECTOR IN ESTONIA

REPORT ON SURVEY

ESTONIAN CLOTHING AND TEXTILE ASSOCIATION

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CONTENT

1. Analysis of national statistics on textile and clothing sector.
2. National Questionnaires Survey results on textile and clothing sector.
   2.1. Companies profile.
   2.2 General awareness of competitiveness.
   2.3 The Chinese issue.
   2.4 The future.
3. Comparison with the other countries surveyed (presented by Cast)
   3.1 Statistics
   3.2 Questionnaires results
4. The European Framework: the European Commission support policy and programmes (presented by EURATEX)
5. Textile and Clothing industry in Estonia (presented by Ministry of Economic Affairs and Communications).
6. Conclusions
1. Analysis of national statistics on textile and clothing sector

Estonian Clothing and Textile Association have prepared, published and disseminated an overview on textile and clothing industry, incl. statistics 1996-2004 (25 pages).

Executive summary.

The clothing and textile industry is a branch of significant importance for Estonian economy. It employs ca 18% of the total industrial workforce. The share of the sale of clothing and textile products in the entire sale of the industrial production is 10%. Exports of textile and clothing articles make up 9% of Estonian exports.

The production volume of Estonian textile industry has been increasing during the last six years. The production indexes of clothing industry (compared with the year 2000) have increased from 106% (2001) up to 139% (2004). The production volume of Estonian clothing industry decreased in 2004 by 0.4%. In comparison with the year 2000 there is increasing of production +2.3%.

Investments in textile and clothing industries per turnover formed 5.5% in 2004.

Most of the production of the Estonian clothing and textile industries goes to export. Share of exports in the sales of textile/clothing products has been increasing last nine years and constituted in 2004 in clothing industry 76% and 86% in textile industry. Exports of textile and clothing products increased during the last nine years ca 2 times and were worth 425 million Euro in 2004. The foreign trade balance of textiles and clothing stayed positive.

The exported product groups of major importance were clothing, home textiles and cotton fabrics. EU markets continued to be of significant importance. The main export destinations of textiles and clothing are Finland, Sweden, Germany and United Kingdom.

Estonian imports of textiles and clothing have recorded an increase in 2004. The imported products of major importance were textile materials for clothing industry (72%) and clothing (28%). Main origin countries for textiles and clothing products were Finland, Sweden, Latvia, Germany and Italy. Market share of China has decreased in 2004 over 40% and formed only 4%.

Trends in 2005. During the first 4 months of 2005, volume index of industrial production in manufacturing of textiles was -3.6% as compared corresponding months of previous year. Industrial production of clothing decreased by 12%. Index of industrial export sales constituted -19% in manufacture of textiles and +4% in manufacture of clothing.

2. National Questionnaires Survey results on textile and clothing sector.

2.1. Companies profile.

Number of textile and clothing companies surveyed were 40, of which 31 were clothing companies.

Most of Estonian companies surveyed sold clothing items (78%), followed knitwear and home textiles. 60% of companies sold outsourced/imported products.

Majority of Estonian companies interviewed is small companies in terms of turnover (70%) and small/medium companies by number of employees (70%). Estonian companies surveyed sell mainly to European Union 15 countries (83%). Share of domestic market is only 15%.

2.2 General awareness of competitiveness

Almost 90% of surveyed companies have increased quantities sold or are stable. Similar situation on sales values. To keep the dynamic of sales most of the companies (95%) surveyed think that the current strengths need changes. More than a half companies interviewed think that in the next two years their competitive position will be similar.

Most threatening competitors for Estonian companies interviewed are from China, new member states and domestic.

2.3 The Chinese issue

More than a half companies interviewed have been directly affected by Chinese competition. Companies affected by Chinese competition have been experienced all range of possible consequences. In order of importance: decrease of own prices, reduction of sales, loss of clients, reduction of quantities and decrease of price. There were no Estonian companies with very remarkable
negative impact, but more than a half companies affected by Chinese competition have been experienced significant negative impact. Estonian companies affected by Chinese competition felt Chinese competition mostly in the EU-25 market (52%) and in domestic market (24%). Chinese products compete in middle range (48%) and lower range (43%) products.

Price is considered the winning factor of Chinese products. Estonian companies surveyed are convinced that Chinese competitors use unfair practises. But they do not have direct evidences of adopting by Chinese competitors of unfair practises. Counterfeited products and dumping practises are bigger problems in Estonia. Estonian traders and outsourcing companies are the strongest allies of the Chinese. Chinese competitors may have weaknesses in quality and delivery/services.

Chinese producers’ greatest advance is price. Also price/quality ratio seems to be a significant competitive advantage. Customisation is for Estonian companies a minor competitive advantage. The range of Chinese products is quite competitive for the Estonian companies surveyed.

2.4 The future
95% of Estonian companies interviewed point that the Chinese presence in EU markets will increase. Factors may be effective to counter Chinese competition under the current general trade conditions are (in order of importance): quality, service/delivery, productivity increase and cost reduction, fashion/design, brand/communication. Estonian companies are in opinion that to enhance the competitiveness of European manufacturers, following levers should be supported (in order of importance): innovation, lower taxes, lower social costs, human resource development, finance.

Only 20% of Estonian companies surveyed have a competitive strategy to deal with the new competition. Weights of actions of Estonian companies envisaged in a new competitive strategy (in order of importance):
- improvement of customer satisfaction through customisation,
- quality improvement
- improvement in design and fashion
- investments in image, brand and communication,
- price reduction through outsourcing of some production,
- improvement of services,
- price reduction through cost reduction and increased productivity.

3. Comparison with the other countries surveyed (presented by Cast)
3.1 Statistics
3.1.1 Textile production 2004/2000
A significant decrease both in EU-15 (-15%) and EU-25 (-14%). Estonia shows a positive trend (+41%); a position which puts Estonia in the top ranking among the New Member States (NMS).

3.1.2 Clothing production 2004/2000
Remarkable decrease both in EU-15 (-24%) and EU-25 (-23%). Estonia shows a positive trend (+7%).

3.1.3 Retail sales 2004/2000
The average trend is slightly positive in the EU-25 (+8%) and EU-15 (+7%). Estonia shows an increase of 84%; a performance well above the EU-15 and EU-25 averages and the NMS average as well.

3.1.4 Consumer price 2004/2000
Prices have been stable in the EU-25 (-0.4%) and EU-15 (- 0.4%). In Estonia prices show an increase of 9%. This result positions Estonia in the middle rank among the NMS.

Total imports of yarns and fabrics have increased +8%, and show a high concentration since two countries make up over 80%. EU-15 is the largest partner with a share of 73%, the second one being Latvia. Both increased their exports to Estonia less than the average, therefore they are classified as losers in the competition in the Estonian market. China is fast growing but it still holds a minor share; it is classified as increasing together with Lithuania and Pakistan.
Total imports of garments have increased only 2%, their concentration is high, 2 countries make up 80% of total imports. The largest supplier is still the EU-15 (78%) but it is a loser in the competition in the Estonian market due to a negative growth trend (-2%). The only winner is Latvia (second largest market share, 6%). China comes third with fast growing exports (+148%); China together with Hong Kong and Poland is increasing.

Estonian exports of yarns and fabrics decreased significantly (-21%). The second worst negative performance among the 10 countries surveyed.

In export of garments Estonia shows a slightly positive trend (+2%). However well below the average (+8%).

3.2 Questionnaires results
3.2.1 Companies profile
Total number of companies surveyed were 1007, of which 691 were textile/clothing companies. The non-homogeneity of the sample requested an analysis on normalized data and all figures of each country have been transformed into %.

The vast majority of Estonia companies interviewed are clothing companies (78%), followed by textile companies. This is different from the samples of companies interviewed in the other countries of the survey. Clothing is far more important (70%) than in the other countries surveyed (more than 30% points difference). Below the average (4.7%) is the Estonian production of technical textiles (2.5%). Far less Estonian companies than in the other countries surveyed sell the products they themselves produce. Most of them (60%) sell traded or outsourced-products. This is a unique position in the 10 countries surveyed.

The vast majority (70%) of Estonian companies interviewed is made up of small companies in terms of turnover. Far more than in the other countries. In terms of number of employees most Estonian companies are small (45%) and medium (20%) companies. This feature coupled with their average size of turnover seems to indicate that Estonian companies do not have satisfactory productivity. By far Estonian companies mainly sell to European Union 15 countries (83%). The highest percentage of all the countries surveyed. Conversely sales to domestic market is the lowest.

Conclusions. The Estonian sample of companies presents some specific characteristics that make it different from other samples:
- a majority of small companies in terms turnover and small/medium companies in terms of number of employees.
- a far lower presence of companies selling the products they themselves produce.
- an above average share of sales to European Union 15 countries.

3.2.2 General awareness of competitiveness
Almost 50% of Estonian companies – many more than the 10-country average (31%) - have increased quantities sold. The best performance! Similar situation in sales values. Together with Lithuanian and Latvian companies all values are better than the average. But still almost half Estonian companies think that major changes are needed to cope with competition. Similarly to the situation of companies in the other countries surveyed.

More than half of Estonian companies interviewed are confident to be able to maintain their current position in the next two years. Together with Lithuanian and Hungarian companies they are the most self-confident. Fear of Chinese competitors (30%) was (Dec. 2004) quite lower than in the other countries (47%). Estonian companies are more worried about domestic competitors (23%) and competitors in the new member states (26%) than companies in the other countries.

Conclusions. Estonian companies are among the most optimistic samples interviewed. Most of them are confident to be able to grow and prosper. They are aware that Chinese competition is strong but they are well aware that also local producers and producers in the other EU new member states can be very competitive.

3.2.3 The Chinese issue
Far less Estonian companies (53%) than in the 10-country average (69%) have been directly affected by Chinese competition. In those affected Estonian companies all range of possible consequences have been experienced - more or less like companies in the other countries surveyed. The Estonian sample
of companies is almost evenly split between those who felt a significant impact (57%) and those who felt a minor impact (43%). In most of the other countries companies were much more affected.

Estonian producers are highly integrated in the EU-25 market and they felt Chinese competition mostly there (52%). Much more than the 10-country average (39%). Chinese competition is evenly spread between lower and middle range products. In both cases Estonians show a large deviation with the 10-country average; more lower range products are affected (13% points higher) and less middle range products (10% points lower).

Price is widely considered the winning factor of Chinese products as in all the countries surveyed. Estonians are convinced that Chinese competitors use unfair practices. But not as many as in the other countries. And none of them has direct evidence of such unfair practices. Counterfeited products of Chinese origin seem to be a far bigger problem in Estonia (43%) than in the other countries surveyed (28%). Dumping practices are ranked similarly to the average (34%).

Estonian importers and traders are the strong allies of the Chinese, as well as local outsourcing companies. Local consumers are blamed far less than in the other countries.

Chinese producers have weaknesses in product quality (wishful thinking?) for more than half Estonian companies. Also in delivery/services. A widespread conviction in all the countries surveyed. Chinese producers’ greatest advantage is price. The competitive advantage of price is so large for Chinese products that also the price/quality ratio becomes competitive. According to Estonian companies customisation plays a minor role in providing a competitive advantage to Chinese products. Also Hungarians, Czechs and Slovenians are sure about that. The range of Chinese products is quite competitive also for the Estonian companies interviewed, although less so than for companies in the 10-country average.

Conclusions. Estonian companies have dealt successfully in maintaining sales and markets. But Chinese competition seem to have a very large advantage in terms of prices and price/quality ratio. Presence of counterfeited products of Chinese origin is a bigger problem in Estonia than in the other countries surveyed.

3.2.4 The future

Estonian companies are optimist but also realistic: they think that the Chinese presence in Europe will increase. All named in questionnaires factors (quality, service/delivery, productivity increase and cost reduction, fashion/design, brand/communication) may be effective to counter Chinese competition under the current general trade conditions as for all companies in the other countries. All levers that should be supported to enhance the competitiveness of EU manufacturers should be used, but innovation and lower taxes and social costs is preferred by a higher number of Estonian companies. More or less like in the other countries.

But only a minority of Estonian companies (19%) have already developed a strategy to deal with the new competition compared to the other countries surveyed (25%). Actions of Estonian companies envisaged in a new competitive strategy are (in order of importance):
- Improvement of customer satisfaction through customisation. More than 70% of Estonian companies interviewed think that customisation is vital for counteracting the Chinese competition, many more than in the other countries (50%).
- Quality improvement. This is an option for half Estonian companies interviewed – more or less like in the other countries.
- Improvement in design and fashion.
- Investments in image, brand and communication.
- Price reduction through outsourcing of some production. Outsourcing could be a promising option for Estonian companies.
- Improvement of services. Services too are important. Even more than in the other countries.
- Price reduction through cost reduction and increased productivity. Only 1/3 of Estonian companies think that there is room for cost reduction – as the average.

Conclusions. Estonian companies think that the Chinese presence is here to stay. Although they do not yet have a defined strategy to deal with it. They think it should be based on one hand on higher quality, innovation, and a general upgrading of the product/service range. On the other hand lower taxes and lower social costs are considered vital. The emerging strategy aims at ensuring that the
competitiveness of Estonian textile/clothing companies remains high and capable to deal with the new competitors.

4. The European Framework: the European Commission support policy and programmes (presented by EURATEX)

Estonian Clothing and Textile Association have prepared, published and disseminated an overview on textile and clothing industry, incl. special part for describing the work done by European Commission and EURATEX for sustainability of clothing and textile industries. All communications from the European Commission and Commission staff working documents, report of the High Level Group, conclusions of the competitiveness council and documents on safeguard actions against textile import from China are made available by links published.

The European Commission published on October 29th 2003 the Communication The future of the textile and clothing sector in the enlarged European Union [COM (2003) 649 final]. The Communication ends with a statement of intent on the part of the Commission to set up a High Level Group for the period 2004-2006 in order to stimulate debate and to consult with interested parties before translating ideas and suggestions into concrete action. The establishment of the High Level Group have led to the formulation of a series of major recommendations, the rationale for which is set out below:

- Complete the Euro-Med free trade area and ensure its competitiveness by
- A breakthrough in clothing technology and
- An action plan in respect of China
- Secure genuine market access to third countries (reduce tariffs, eliminate non-tariff barriers)
- Improve skills, facilitate re-conversions and protect intellectual property rights
- Ensure that the internal regulatory framework of the EU remains attractive for investment.

The European Commission published on October 13th 2004 the Communication Textiles and clothing after 2005 – Recommendations of the High Level Group on textiles and clothing [COM (2004) 668 final]. Those recommendations lists the actions to be carried out by the Commission, by the member states and by the stakeholders. Actions to be concentrated in five areas: environment, intellectual property rights, education and training, innovation and R&D, trade.

Actions at EU level are:

Environment.
Impact assessment study on the New Chemical policy – REACH. Study launched early 2005. Final results at the latest May 2005

Intellectual property.
User friendly multilingual website on IPR. On-going discussions.
Vade-Mecum on IPR. Drafting multisectorial call for tender – By April 2005.
Information & awareness seminars at national level. Drafting multisectorial call for tender – By April 2005.

Education & Training.
Common structure of courses - Network of training. Creation of Media pool – Project to be submitted by October 2005 (Leonardo).

Innovation, research, development.
Technical textiles. EC call for R&D projects for construction, medical & protective textiles, ~25Mio€
Clothing Technology Breakthrough. Leapfrog project.
Integration of SMEs in R&D programs. Euratex position paper on EU research programmes as input to FP7. Development of IT solutions for SMEs in FP6-IST Programme.

Non-technological innovation. On-going discussion linked with State-Aid. Euratex proposal for project on Innovation financing (NetFinTex).

**Euratex Projects in R&D, Innovation, Education and IPR:** LEAPFROG IP and LEAPFROG CA (clothing technology), AVALON (technical textiles), Space2Tex (environment), WebTEXpert and Tex-Weave (IT and e-business), VITA and EuroTT ((education and training), 4IPR and Transition (intellectual property rights).

**Trade.**

Market Access Task Force. Launch end January, identification of strategy expected in May 2005?

Guidelines textile specific safeguard - China. Published early April. First enquiries end April. Date of implementation?

International actions. EU—China dialogue. Coherence within DDA

Monitoring of trade. Unsatisfactory results except China licensing.

Euromed common origin rules for easier, faster trading relationship. Decision by the Council as soon as possible. Modification of the bilateral protocols by end 2005?

Concentrate GSP to smaller & LDC + adaptation rules of origin. GSP regulation under discussion including rules of origin.

**Regional level** (It is up to ACTE to work on those issues)

More flexible procedures for SMEs in Structural Funds.

Greater access to structural funds.

**Competition, Retail & Access to finance.**

Study on the EU retailing system & practices. To be launched later in 2005 (Commission)

Access to finance. On-going discussions. Guide for SMEs finalised?

Competition. On-going discussions.

Marketing. WG to be created soon.

Work to be carried-out at national level.

**Public Procurement.** Criteria art 53 Dir 2004/81/EC

Competition policy. Control, transparency, security Reverse auctions

Access to Finance. Assessment instruments access to credit for SMEs


R&D. Improve co-ordination with EC

Education. Observatories, lifelong learning strategies, increase programmes for (re-)training, (re)skilling.

In summary:

The Actions at EU level: 34

21: carried-out or in the process of completion with EURATEX involvement;

5: EURATEX could take some future initiatives;

8: EURATEX cannot act as those depend on Commission; Member States or Regions.

### 5. Textile and Clothing industry in Estonia (presented by Ministry of Economic Affairs and Communications).

Estonian public authorities support the Commission Communication [COM 668 (2004)] on future of textile and clothing industry and conclusions based on this communication. They are in favourable opinion on the analysis and proposals included in communication, excluding the part related to the re-programming of Structural Funds. Estonian statement on this case is that re-programming of Structural Funds can not be compulsory for member states. Estonian public authorities support horizontal industry policy and therefore they take carefully proposals on implementation of sectoral measures.

According to the Communication mentioned above the role of the member state is to create for the textile and clothing sector such framework conditions that enable them to compete in the new environment. The Estonian industrial policy has a horizontal character – its tools relate to all sectors of industry in the same way.

Estonia fully acknowledges the need to make a decisive shift from the cost-based competitiveness towards the knowledge-based economy. Estonian long-term economic development is oriented
towards increasing the role of the knowledge-based economy by stimulating private investment in research and development. The fact that the EU market has become a home market for local enterprises and that both enterprises and research institutions are able to participate in European cooperation networks, will definitely contribute to the realization of this goal.

The objective of the national innovation policy is to assist traditional enterprises to maintain their competitiveness, notwithstanding any erosion of the current advantages conferred by low production costs. The fields with greatest research potential in Estonia are biotechnology, information technology and material technology. The achievements of Estonian scientists in these areas are internationally acknowledged and the educational standard offered by our universities is outstanding. These factors have contributed greatly to the growth in the number of successful enterprises with high export potential in Estonia.

One of Estonia’s ambitious programmes to support the implementation of innovative ideas is the risk capital fund currently being launched by the Ministry of Economic Affairs and Communications. The aim of the fund is to provide financing to innovative and high-technology business projects in their initial phase.

Competitiveness and value added of traditional industries is one of strategic objectives of Estonian Knowledge Based Research and Development Strategy 2002-2006. To promote entrepreneurship, the Ministry of Economic Affairs and Communications has developed national business support system. All enterprises engaged in business activities in Estonia may apply for state support for the creation of infrastructure necessary for their operations, training of personnel, participation in fairs etc. However, product and technology development and co-operation between businesses, research institutions and universities are considered priority areas in considering the provision of support under this scheme.

The main support structure is Enterprise Estonia, the primary provider of support and development programmes targeted towards entrepreneurs: Consulting Programme, Training Programme, Business Incubator Programme, Export Planning Programme, Business Infrastructure Development Programme, Innovation Awareness Programme, Competence Centre Programme and R&D Financing Programme.

Future activities planned are: enhance innovation initiative, support for starting innovative companies, R&D investment stimulation, improving traditional industries innovation capabilities and R&D infrastructure development.

Ministry of Economic Affairs and Communications of Estonia will henceforth strengthen the cooperation with entrepreneurs of sector to raising the awareness of public authorities about existing problems where further action might be required.

6. Conclusions

Taking the results from analysis of national statistics and competitiveness questionnaires, Estonian textile and clothing industry is still competitive with regard to the other member states, but less so if compared to other low-wage suppliers, especially from the Far East. As has happened in European textile and clothing industry, Estonia will experience a decline in its textile and clothing industry as its economic level rises. Development in the industry over coming years will include a decrease in employment and production.

The main competitors come from low-wage textile and clothing producers around the world. To withstand this competition Estonia may take advantage of the proximity to main market (European Union) giving short delivery times and longstanding cooperation experience with trading partners. But Estonia will also have to invest in up-to-date technology to meet the quality standards of the advanced markets and should improve customer relations.

For improving the competitive position of the sector it is evident that changes necessary requires in the first place the efforts and commitment of companies, and then of public authorities at European, national and regional levels.

According to the competitiveness survey Estonian clothing and textile companies envisaged including in competitive strategy following actions (in order of importance):

- Improvement of customer satisfaction through customisation.
- Quality improvement.
- Improvement in design and fashion.
- Investments in image, brand and communication.
- Price reduction through outsourcing of some production.
- Improvement of services.
- Price reduction through cost reduction and increased productivity.

Estonian public authorities support the Commission Communication [COM 668 (2004)] on future of textile and clothing industry and conclusions based on this communication. They are in favourable opinion on the analysis and proposals included in communication, excluding the part related to the re-programming of Structural Funds. Estonian statement of this case is that re-programming of Structural Funds can not be compulsory for member states. Estonian public authorities support horizontal industry policy and therefore they take carefully proposals on implementation of sectoral measures.

According to the Communication mentioned above the role of the member state is to create for the textile and clothing sector such framework conditions that enable them to compete in the new environment. The Estonian industrial policy has a horizontal character – its tools relate to all sectors of industry in the same way. Estonian public authorities consider that developing of a special national strategy for the textile and clothing sector (and for other industrial sectors) is not necessary.

Competitiveness and value added of traditional industries is one of objectives of Estonian Knowledge Based Research and Development Strategy 2002-2006. The main support structure is Enterprise Estonia, the primary provider of support and development programmes targeted towards entrepreneurs: Consulting Programme, Training Programme, Business Incubator Programme, Export Planning Programme, Business Infrastructure Development Programme, Innovation Awareness Programme, Competence Centre Programme and R&D Financing Programme. Ministry of Economic Affairs and Communications of Estonia will henceforth strengthen the cooperation with entrepreneurs of sector to raising the awareness of public authorities about existing problems where further action might be required.

Actions at European level. In October 2003 the European Commission adopted the Communication "The future of the textiles and clothing sector in the enlarged European Union". In this Communication the Commission outlines the main challenges faced by the textiles and clothing sector in the EU, and makes a number of proposals to strengthen its competitiveness. As a result of this Communication, the Commission has set up a High Level Group for the period 2004-2006 in order to stimulate debate and to consult with interested parties before translating ideas and suggestions into concrete actions.

The Commission reported back to Member States on the follow-up to the above mentioned Communication and on the recommendations of the High Level Group in its Communication of 13 October 2004 "Textiles and clothing after 2005 - recommendations of the High Level Group for textiles and clothing". Those recommendations lists 34 actions to be carried out by the Commission, by the member states and by the stakeholders. Actions to be concentrated in five main areas: environment, intellectual property rights, education and training, innovation and R&D, trade.

High Level Group called on the EU member countries to help reconstruct their textile enterprises through such means as increasing investment to enhance competitiveness, providing enterprises with more opportunities and giving social assistance to the regions suffering the greatest losses. HLG also urged Europe's textile enterprises to fully tap their potential and take advantage of the full liberalization of the textile trade to export goods to China and other countries.