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**Why  
the Emperor's  
New Clothes  
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Made  
In  
Colombia**

**David Morawetz**

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world  
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research  
publication**

**Oxford**



# Why the Emperor's New Clothes Are Not Made in Colombia

A World Bank Research Publication

*Beauty when most unclothed is clothed best.*

PHINEAS FLETCHER

# Why the Emperor's New Clothes Are Not Made in Colombia

A Case Study in Latin American  
and East Asian Manufactured Exports

*David Morawetz*

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# Definitions

ANALDEX	The association of exporting firms (Asociación Nacional de Exportadores)
ANDI	The national association of industrialists (Asociación Nacional de Industriales)
CAT	A tax credit certificate given to exporters of goods other than coffee and petroleum (Certificado de Abono Tributario)
DANE	The national statistics office (Departamento Administrativo Nacional de Estadística)
DNP	The national department of economic planning (Departamento Nacional de Planeación)
FEDESARROLLO	A private research foundation in Bogotá specializing in development problems (Fundación para la Educación Superior y el Desarrollo)
INCOMEX	A government agency in charge of supervising foreign trade (Instituto Nacional de Comercio Exterior)
PROEXPO	The government export promotion agency (Fondo de Promoción de Exportaciones)
VALLEJO PLAN	Drawback scheme under which firms are exempt from (or receive ex post rebates on) tariffs payable on imported inputs that are used to manufacture export goods.
807	U.S. offshore-assembly scheme under which, if precut fabric and other inputs are shipped from the United States and assembled abroad, the finished garments that are returned to the United States are charged import duties only on the value that was added overseas.



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Christine Houle edited the manuscript for publication. Harry Einhorn read and corrected proof, Ralph Ward and James Silvan indexed the text, and Raphael Blow prepared the charts. The map was compiled by Julio Ruiz and drawn by Larry Bowring under the supervision of the World Bank's Cartography Division.

Despite the assistance of so many, I alone am responsible for any remaining errors and for all views expressed.





# Why the Emperor's New Clothes Are Not Made in Colombia



# *Introduction*



# Objectives and Methods

THIS STUDY attempts to answer four central questions.

1. Why did Colombia's clothing<sup>1</sup> exports, which had never exceeded \$1 million until 1970, climb suddenly to over \$50 million in 1974?<sup>2</sup>

2. Why, after 1974, did the country's exports of clothing to the United States and Europe begin steadily to decline?

3. Why is it that Colombia has been so much less successful at exporting garments to date than Hong Kong, Korea, and Taiwan?<sup>3</sup> (Hong Kong exported \$2.9 billion of apparel in 1977, Korea \$2.0 billion, and Taiwan \$1.3 billion.)<sup>4</sup>

4. More generally, what can be learned from Colombia's experience with clothing exports about the reasons Latin American nations have been less successful at exporting most types of manufactured goods than Hong Kong, Korea, and Taiwan? Do the East Asians have cheaper labor, do they work harder, do they have a transport cost advantage, do they receive massive government subsidies, are they better at selling the goods—or what?

If a key aim of this study is to learn something general about the reasons for the relatively poor performance of *Latin America* (not just Colombia) in exporting manufactures (not just clothing), why, it might be asked, is the study limited to just one industry and just one Latin American country? My reply is that it is precisely by narrowing the focus that some generally applicable and otherwise unattainable insights may be gained.<sup>5</sup> There already exist many aggregative analyses of Colombia's and Latin America's manufactured exports, some of them excellent. But I know of no study in which the performance and characteristics of a

1. The words clothing, apparel, and garments are used synonymously throughout this study. In the U.S. garment industry, the word clothing has a number of more restricted meanings: for example, it sometimes refers solely to men's suits, jackets, and dress slacks.

2. All dollar figures in this book are in U.S. dollars.

3. Korea is used throughout the study to refer to the Republic of Korea or South Korea; the term "Taiwan" refers to the economy of Taiwan.

4. \$1 billion equals \$1,000 million.

5. A Martian wondering how Earthmen differ physically from Earthwomen might learn something by looking at photographs taken with a wide-angle lens at mass rallies in male and female nudist colonies. But he, she, or it could no doubt also gain further important insights of general validity by studying narrowly focused shots of one Earthman and one Earthwoman.

Latin American exporter of manufactured goods have been compared in detail with those of the successful East Asian exporters. Further, I know of no study of an industry of interest to developing nations that has examined in as much detail as the present one the price, and especially the nonprice, determinants of export success. Of course, going into great depth and detail is a means rather than an end; whether the insights that are gained justify the effort is another question altogether. On that issue, the reader is usually better placed to judge than the writer.

In attempting to draw conclusions of general relevance from the study of a particular case, it is important to be aware of any features of that case that might make it atypical or special. Chapter 8 presents a discussion of some pertinent ways in which the clothing industry differs from other industries and Colombia differs from other Latin American countries.

During September–December 1978, I interviewed the managers or export managers of thirty Colombian firms that export or have exported clothing.<sup>6</sup> During twenty-five of the interviews, a Colombian research assistant, Martha Bermúdez, was also present. The sample of firms was stratified to include:

- Most of the largest exporters (nine of the top twelve according to value of exports)
- Some medium-size and some small exporters (size is measured here both by value of exports and by number of employees)
- Several firms that had been important exporters in 1974 but which sold little or nothing abroad in 1977
- Most of the firms that had requested quota allocations for exports to the United States for the textile year 1978–79 (fourteen of the seventeen)
- Three small firms that had been associated with a recently failed export consortium
- As many intermediaries as could be found (five)
- Firms located in six cities—Barranquilla, Bogotá, Cali, Manizales, Medellín, and Pereira—and in the Free Zone of Barranquilla.

Martha Bermúdez and I also interviewed the directors of the three full- or part-time foreign buying offices for clothing that were then located in Bogotá, as well as officials of the Colombian foreign trade

6. In four cases, two jointly owned and managed enterprises, the exports of which are registered separately, are defined as a single firm. In three cases, two separate interviews were carried out in enterprises that seemed to have particularly important histories.

institute, INCOMEX; the export promotion agency, PROEXPO; the industrialists' association, ANDI; the association of exporting firms, ANALDEX; the National Planning Department, DNP; the Board of Imports; the Chambers of Commerce; the Free Zone in Barranquilla; and the private economic consulting firm, FEDESARROLLO. Later, in March 1979, I spent a week in New York interviewing executives of fourteen U.S. corporations that import or have imported clothing from firms in the sample. These corporations included importer-wholesalers, importer-manufacturers, department store chains, independent retail houses, and a financing house. The persons interviewed were usually in charge of foreign buying in general or of importing from Latin America. While in New York, I also visited an international consulting firm that specializes in the clothing industry.

In keeping with the inductive nature of the investigation, a flexible interview guide was used in all interviews rather than a rigid questionnaire, and respondents were encouraged to relate their experience with Colombian clothing exports (or imports) in their own words and in their own sequence. The main advantage of this method is that it minimizes the likelihood that important aspects of the story will be missed. Its main disadvantage is that respondents who expatiate on areas of particular interest cannot always be asked all of the questions that are in the interview guide because of lack of time. On balance, in this study the advantages of the flexible interview guide method clearly outweighed the disadvantages.

The guide for interviews with Colombian clothing firms began with questions on the size of the firm, products sold in domestic and export markets, the value of exports, and the percentage of output exported. There followed a series of opening probes on some of the nonprice aspects of selling abroad: how did you first discover the possibility of exporting? to whom do you sell? what are your sources of information on fashion? how are product specifications set? how has this changed over time? and so forth. Next came sections on pricing and profitability in domestic and export markets, the nonmonetary benefits of exporting, the use of domestic and imported inputs, labor and productivity, capacity utilization, transport costs and problems, overseas distribution and retailing, the amount of advance notice needed and received for export orders, finance, and the organization of the export function in the firm. Finally, there were questions concerning consortia of small firms, intermediaries, quotas, the role of government, and plans for the future. In most cases, the interview was followed by a brief plant visit. The complete interview guide is reproduced in Appendix A.

The main areas that were covered in the interviews with U.S. clothing buyers in New York included the detailed history of the buyer's experience in purchasing clothing from Colombia, the effect of U.S. import quotas on the buyer's import arrangement, Colombia's main perceived strengths and weaknesses as a clothing exporter in comparison with other Latin American countries and with East Asia, and the buyer's plans, if any, for future imports of clothing from Colombia.

The interviews with the Colombian clothing exporters varied in length between one and four hours, with the majority taking between one and a half and two and a half hours. The interviews with U.S. buying firms in New York ranged from thirty minutes to two and a half hours, with the majority taking from one to one and a half hours.

Only one firm in the Colombian sample refused outright to be interviewed. Sixteen companies in the initial sample that were registered as having exported clothing during 1974 or 1977 had disappeared by the last quarter of 1978. The owner-manager of one of these firms had been kidnapped during 1978. In a second case, we were told that the secret police, DAS, was also looking for the firm, while fire had destroyed the plant of a third. In the remaining thirteen cases, there was no answer at the telephone number or address that we had, and we were unable to locate the enterprise through INCOMEX, through PROEXPO, or by other means. In an additional four cases, we could not arrange an interview in the limited time that was available, usually because the person to be interviewed was busy or was out of town while we were in a particular city. Finally, in another case the interviewee failed to appear at the appointed time and then failed twice to return calls.

The policy followed in cases of nonresponse was to try as far as possible to replace the firm in the sample with another of similar size and characteristics in the same city. This worked out quite well, and there seems to be no particular reason to expect that nonresponse has biased the findings of the study one way or another. The reason such a relatively large number of firms could not be located is substantive rather than technical, as will become clear in chapter 1.



*Part One*

*The Rise and Fall of  
Colombia's Clothing Exports?*



## Chapter 1

# Lies, Damned Lies, and Statistics

*There are three kinds of lies: lies, damned lies, and statistics.*

—DISRAELI

ACCORDING TO THE STATISTICS COMPILED BY INCOMEX, Colombia's registered clothing exports increased rapidly from \$1 million in 1970 to \$77 million in 1974, fell dramatically to \$29 million in 1975, and began to recover thereafter, without regaining the 1974 level by 1978 (see table 1).<sup>1</sup> Unfortunately, the statistics tell rather less than the whole truth.

### Registrations and Manifests

The main advantage of the INCOMEX data on export registrations, and the reason they are widely used in Colombia, is that they are published, or at least made available for public inspection, with minimal delay. Their main drawback, a serious one, is that they are based on plans rather than deeds. Any firm that receives an order for its goods from abroad is required to submit to INCOMEX a form registering its intention to export. The INCOMEX tabulations of export registrations are based directly and solely on these forms. But there's many a slip 'twixt the cup and the lip: in particular, orders are sometimes canceled. Fortunately, there exists a second set of (more tardily published) data against which the INCOMEX figures can be checked.

At the time that a bundle of export goods crosses the Colombian customs border, a second form, or manifest, has to be signed by customs officers. The signatures of these officials serve to verify that they have seen the merchandise cross the border. DANE publishes a set of export

1. Partial, preliminary figures for the first half of 1979 suggest that registered clothing exports may have surpassed \$77 million in that year (FEDESARROLLO, 1979a, p. 41). Throughout the tables in this study, sums, products, and quotients of columns and rows do not always agree with column and row totals because many figures have been rounded. For some variables (including the value of clothing exports), the fact that alternative sources give varying estimates means that the data in different tables do not always agree.

Table 1. Value of Clothing Exports: Registrations, Manifests, and Percentage of Output, 1967-78 (millions of dollars)

Year	Registrations (1)	Manifests		Clothing exports as percentage of output (4)
		Current prices (2)	Constant 1967 prices (3)	
1967	0.3	0.4	0.4	n.a.
1968	0.3	0.5	0.5	0.5
1969	0.7	0.9	0.8	0.9
1970	1.3	1.1	1.0	1.0
1971	1.8	1.9	1.7	1.5
1972	9.2	5.9	5.1	4.2
1973	31.8	19.2	16.1	10.9
1974	77.4	52.3	40.4	28.6
1975	29.3	29.1	21.8	15.2
1976	34.1	39.7	28.4	n.a.
1977	46.7	n.a.	31.7 <sup>a</sup>	n.a.
1978 <sup>b</sup>	25.8	n.a.	n.a.	n.a.

n.a. Not available.

Note: Registrations during January-July 1978 were 32.5, compared with registrations during January-June 1977 of 17.1.

a. Based on figure for registrations.

b. January-June.

Sources: Col. (1): 1967-69 Calvo and Escandón (1973, p. 12, based on INCOMEX data); 1970-77: INCOMEX, unpublished tabulations, Expo 5, 1970-77. Col. (2): ANDI, *La Economía Colombiana 1977* (fact sheet, based on DANE data). Col. (3): For index of wholesale clothing prices, see table 17. Col. (4): Value of exports: see column (2); exchange rate: see table 17; value of output: DANE, *Industria Manufacturera Nacional*, annual publication, 1968-75.

data that is based entirely on these manifests.<sup>2</sup> An additional set of registrations data is compiled by the central bank (Banco de la República) in connection with the foreign exchange aspects of exporting. These figures follow the same general trend as those of INCOMEX. For example, for 1971-77 they give clothing exports as \$1.7, \$2.1, \$28.6, \$82.7, \$32.4, \$37.3, and \$47.3 million (PROEXPO, unpublished summary of unpublished Banco de la República tabulations).

2. The DANE data presented in table 1 are taken from an ANDI publication rather than from DANE itself because the ANDI source gives the longest consistent series on total clothing exports that is available. Some data published by DANE differ slightly from those in table 1 (presumably because of differences in the way that particular items are classified), but the underlying trend is the same. For example, for 1972-76 DANE (1978, table 7) gives clothing exports as \$4.6, \$16.9, \$48.7, \$24.7, and \$34.7 million.

As can be seen from the second column of table 1, the DANE data differ to some extent from those of INCOMEX. In part, this discrepancy is no doubt caused by leads and lags: goods registered for export late one year may physically cross the customs border early the following year. But for 1973 and 1974, the INCOMEX figures exceed the DANE numbers by \$13 million and \$25 million (66 and 48 percent of DANE exports), respectively. It seems that in those two years, which marked the beginning of recession in the industrialized countries, an unusually large number of orders may have been canceled. Whatever the reason for the difference between the two sets of data, the DANE figures are clearly more useful for the present purposes than those of INCOMEX.

### Constant Prices

If U.S. producer (wholesale) prices are taken as the yardstick, world clothing prices increased by 50 percent between 1967 and 1978.<sup>3</sup> Thus, it is necessary to convert the DANE series to constant prices to reveal the trend in the *volume* of Colombia's clothing exports over the period. This is done in the third column of table 1.

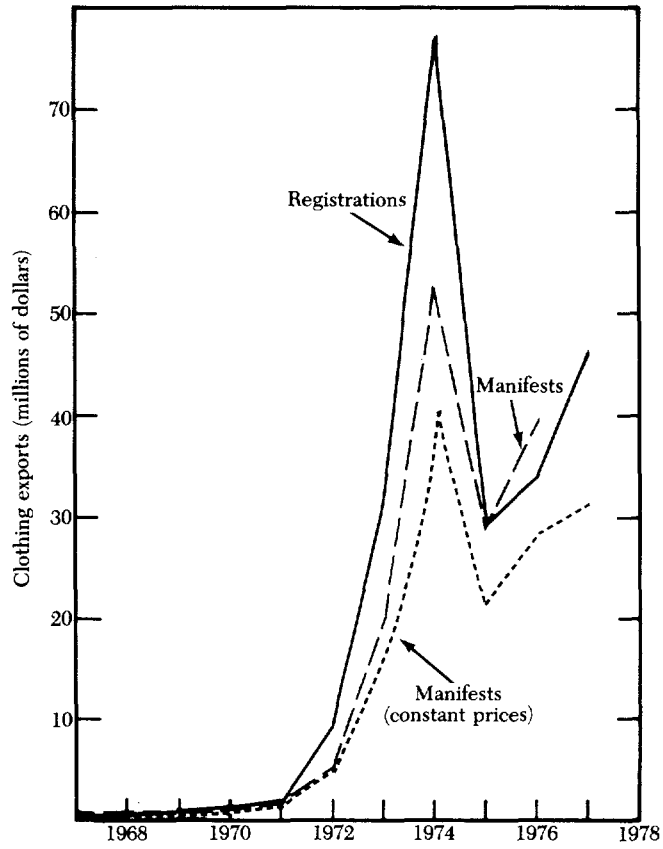
### Fictitious Exports

Nothing in the manipulations so far has either explained or removed the odd 1974 peak: as may be seen in figure 1, the constant-price manifest-based data have the same general shape as the current-price registration-based figures. The peak, nevertheless, is a mirage. The explanation, as related by a number of clothing exporters, seems to be something like the following.

In 1974 the price of Colombian coffee fell to its lowest level in real terms in more than twenty-five years. In the same year, for a variety of reasons, there was a surge in the demand for imports, with the result that the current account of Colombia's balance of payments was deeper in deficit than it had been in all but one of the previous fourteen years (table 2). Needing dollars to import foodstuffs, and aware of the existence in the country of a large pool of some tens, and maybe already hundreds, of millions of "black" dollars generated by the drug trade, the

3. The wholesale price index for clothing increased rather more slowly during 1970-78 than the unit value index for U.S. apparel imports. The latter was heavily influenced by upgrading of the quality and product composition of East Asian imports and by rising East Asian quota premiums (Keesing, 1978).

Figure 1. Value of Clothing Exports, Registrations, and Manifests, 1967-77



Source: Table 1.

Table 2. Price of Coffee, Current Account of Balance of Payments, and Premium of Black Market Exchange Rate, 1960–78

Year	Price of coffee per kilogram <sup>a</sup> (constant 1977 U.S. dollars) (1)	Current account balance (millions of current U.S. dollars) (2)	Premium of black market exchange rate over official exchange rate (percent) (3)
1960	2.59	-79	n.a.
1961	2.49	-132	n.a.
1962	2.36	-161	n.a.
1963	2.27	-127	n.a.
1964	2.76	-122	n.a.
1965	2.66	-11	n.a.
1966	2.58	-280	n.a.
1967	2.24	-67	20
1968	2.43	-160	5
1969	2.54	-175	8
1970	2.87	-302	16
1971	2.32	-453	9
1972	2.41	-191	5
1973	2.57	-56	6
1974	2.19	-351	5
1975	2.00	-176	-1
1976	3.82	187	-1
1977	5.39	n.a.	-5
1978	n.a.	n.a.	-6

n.a. Not available.

a. Colombian coffees from Manizales, Armenia, and Medellín, spot price New York. Sources: Cols. (1) and (2): World Bank, unpublished data. Col. (3): Junguito and Caballero (1978, table 9).

outgoing government of Misael Pastrana Borrero let it be known informally that persons exchanging dollars at the Banco de la República would receive the full official exchange rate and would not be asked from where the dollars were obtained. This attracted few dollars, however, since in 1974 the black market exchange rate for the dollar was still 5 percent above the official rate.<sup>4</sup> It then became known informally (whether with or without the government's knowledge is in dispute) that anyone who claimed to have exported some goods and could present an export manifest signed by a customs officer as documentation would receive the full official exchange rate for the dollars allegedly so received

4. From 1975 onward there were so many millions of black dollars in the country that the black market exchange rate was 1 to 6 percent *below* the official rate (table 2, col. 3).

plus the official export subsidy—or, more accurately, tax credit certificate (CAT)—which was then worth 15 percent of the value of exports. This arrangement proved to be attractive, since under it the number of pesos received per dollar net of all expenses was greater than the number of pesos received for a dollar exchanged on the black market. For reasons that are not altogether clear, clothing appears to have been one of the most popular items for holders of black dollars to register on their manifests. Thus, it seems that at least part of the 1974 peak in clothing exports is in fact accounted for by fake invoicing, or, as the phenomenon is known widely in Colombia, by fictitious exports. (Although some people dispute whether the government played an implicitly active role as this account suggests, I know of no one who denies that fictitious exports of clothing took place. Of course, fake invoicing by exporters is by no means restricted either to clothing or to Colombia.)

Independent pieces of evidence are consistent with this explanation of the apparent 1974 peak. First, there is no indication of any sharp increase in aggregate output or value added in the Colombian clothing industry in 1974. On the contrary, in the same year that the DANE statistics show clothing exports trebling as a percentage of clothing production and increasing as a percentage of total industrial exports, output and value added in clothing both fell significantly in real terms. They also fell as a percentage of output and value added in all industry. True, employment in clothing grew in 1974; but the increase was only 1 percent, which was less than the increment in each of the previous five years. Employment in clothing as a percentage of all manufacturing employment declined (tables 3 and 4).

Second, to return to the nonresponse question for a moment, among the firms that were included in the sample for this study but that could not be located, by far the largest single group were companies registered as having exported large quantities of clothing in 1974. The largest of these companies according to the value of registered exports was Los Alamos. This firm registered with INCOMEX its intention to export \$12 million in 1974—twice as much as any other clothing firm has registered before or since. Los Alamos would have had to have at least 1,000 employees to do business on this scale, yet no one whom I approached in the clothing industry, in ANDI, or in the government had ever heard of it. Nor is Los Alamos alone in this respect: five other firms that were registered as exporting more than \$2 million each in 1974 seem to be known to no one. (Only five of the firms interviewed for the present study have ever registered exports of more than \$2 million in a



Table 3. Value of Output, Value Added, Number of Employees, and Value of Exports in the Clothing Industry, 1969-77  
(annual percentage changes in constant prices)

Year	Value of output (1)	Value added (2)	Number of employees (3)	Value of exports (4)
1969	-2	0	8	60
1970	6	7	4	25
1971	15	18	6	70
1972	7	-1	13	200
1973	10	7	20	216
1974	-9	-7	1	151
1975	7	12	-2	-46
1976	n.a.	n.a.	n.a.	30
1977	n.a.	n.a.	n.a.	12

n.a. Not available.

Sources: Cols. (1), (2), and (3): DANE, *Industria Manufacturera Nacional*, annual publication, 1968-75; and table 17 for clothing price index. Col. (4): table 1, col. (3).

Table 4. Value of Output, Value Added, Number of Employees, and Value of Exports of Clothing as Percentage of Total Manufacturing, 1968-77

Year	Value of output (1)	Value added (2)	Number of employees (3)	Value of exports (4)
1968	3.8	3.6	8.0	0.9
1969	3.5	3.2	7.9	1.1
1970	3.4	3.3	7.7	1.2
1971	3.6	3.5	8.1	1.8
1972	3.5	3.2	8.4	3.3
1973	3.6	3.3	9.2	5.8
1974	2.8	2.6	8.8	7.7
1975	2.9	2.9	8.5	5.0
1976	n.a.	n.a.	n.a.	6.0
1977	n.a.	n.a.	n.a.	6.5

n.a. Not available.

Sources: Cols. (1)-(3): DANE, *Industria Manufacturera Nacional*, annual publication, 1968-75. Col. (4): clothing exports: table 1, col. (2); industrial exports: 1968-74: World Bank, unpublished data (based on INCOMEX, unpublished tabulations); 1975-77: FEDESARROLLO (1979, p. 71, based on INCOMEX, unpublished tabulations).

single year, and all of them are very well known.) In light of the close contact that officials of ANDI, INCOMEX, and PROEXPO maintain with the largest exporting firms, this ignorance is suggestive to say the least. It seems, in fact, that these six firms, along with an unknown number of others that were registered as exporting garments in 1974, never existed except as a device for carrying out fictitious exports.<sup>5</sup>

Interviewees who spoke about fictitious exports agreed unanimously that firms registering them were most likely to claim to be sending goods to Panama, the Caribbean, or possibly Venezuela, and were least likely, because of fear of legal complications, to nominate the United States as the intended destination. The INCOMEX statistics on registered clothing exports by destination are consistent with this reasoning. Panama, which did not receive more than \$4 million in clothing from Colombia in any one year during 1975–77, is registered as having received \$23 million in 1974, and the 1974 figures for Venezuela, Aruba, and Curaçao also seem to be somewhat inflated. By contrast, registered exports to the United States in 1974 show no noticeable bulge at all (table 5).

It is not possible to obtain a precise estimate of the value of fictitious clothing exports in 1974. Nevertheless, the \$27 million registered by Los Alamos and the other five firms that seem never to have existed may represent something of a lower bound.<sup>6</sup> If taken as such, Colombia's true clothing exports in 1977 were neither \$77 million (INCOMEX) nor \$52 million (DANE) but at most \$25 million, or \$19 million in 1967 prices. Thus, clothing exports for 1974 would appear on or below a straight line joining 1973 and 1975 in figure 1, and the peak would completely disappear.

It seems to be generally agreed that fictitious exporting on a large scale was restricted mainly to 1974. On September 26 of that year, the newly elected government of Alfonso López Michelsen announced that

5. The obverse side of this coin is that the clothing exporting firms interviewed for this study accounted for 50 to 73 percent of all registered clothing exports during 1975–78, but only 22 percent of such exports in 1974 (table 22).

6. This is consistent with Escobar's observation that "Fictitious exports of clothing were, apparently, greater than true exports" (Escobar, 1977, p. 27). If some of the fictitious exports registered with INCOMEX did not eventually "take place" (that is, if the firms did not go through with faking the manifests), the adjustment made here will be too great. But the figure quoted ignores entirely overinvoicing by legitimate firms, which seems, for obvious reasons, to have been quite common in 1974. Fictitious exports that were registered but, as a result of the new government's measures (see following paragraph), did not reach the manifest stage, may help in part to explain the unusually large gap between the INCOMEX and DANE export figures for 1974.

Table 5. Clothing Exports by Destination, Current Prices, Constant Prices, and Percentage Distribution, 1974-78

Year	United States	Europe <sup>a</sup>	Venezuela	Caribbean and Panama <sup>b</sup>	Other	Total
Millions of dollars						
1974	17.0	4.3	23.4 <sup>c</sup>	29.5 <sup>c</sup>	3.7	77.9 <sup>c</sup>
1975	16.6	4.0 <sup>d</sup>	8.1	3.0	2.0	33.7
1976	12.7	4.8 <sup>d</sup>	9.8	6.1	6.2	39.6
1977	11.6	3.5	22.6	10.5	2.9	51.1
1978 <sup>e</sup>	5.7	1.8 <sup>d</sup>	15.9	6.7	1.2	31.3
Millions of dollars in 1967 prices						
1974	13.1	3.3	18.1 <sup>c</sup>	22.8 <sup>c</sup>	2.9	60.2 <sup>c</sup>
1975	12.4	3.0 <sup>d</sup>	6.1	2.2	1.5	25.3
1976	9.1	3.4 <sup>d</sup>	7.0	4.4	4.4	28.3
1977	7.9	2.4	15.3	7.1	2.0	34.7
1978 <sup>e</sup>	3.7	1.2 <sup>d</sup>	10.4	4.4	0.8	20.5
Percent						
1974	22	6	30 <sup>c</sup>	38 <sup>c</sup>	5	100
1975	49	12 <sup>d</sup>	24	9	6	100
1976	32	12 <sup>d</sup>	25	15	16	100
1977	23	7	45	21	6	100
1978 <sup>e</sup>	18	6 <sup>d</sup>	51	21	4	100

*Note:* In 1973, according to Colombia Information Service (1979), Colombia's total garment exports of \$19.1 million went to the following destinations: United States, \$7.1 million (37 percent), Europe, \$2.0 million (10 percent), Andean Group (mostly Venezuela) \$1.8 million (9 percent), other Latin American countries, \$0.7 million (4 percent), elsewhere, \$7.5 million (39 percent) (based on DANE data).

a. Mostly Netherlands and Federal Republic of Germany.

b. Aruba, Curaçao, Puerto Rico, and Panama.

c. Probably includes some fictitious exports.

d. Estimated.

e. January-June.

*Sources:* 1974: Banco de la República, unpublished tabulations, Expo 6, 1974. 1975-78: PROEXPO, unpublished summary data based on Banco de la República, unpublished tabulations, Expo 6, 1975-78.

the CAT, or export subsidy, was being reduced from 15 to 5 percent. It also shook up the Customs Department and increased the number of signatures required on an export manifest from one or two to ten or twelve. These twin measures, particularly the latter, seem to have had the desired effect. In the words of the export manager of one clothing firm: "It would be much too expensive to do fictitious exporting now. Not only would you have to pay off many more people. Also, each one of them is more honest now than before, so you would have to pay him more."

## Destinations

In 1975, the first recent year for which reliable destination data are available, 49 percent of Colombia's clothing exports went to the United States and 12 percent went to Europe. Venezuela received 24 percent of these exports in the same year, the Caribbean took 9 percent,<sup>7</sup> and all other countries together accounted for 6 percent. Since 1975, however, there has been a dramatic change in the distribution of destinations. Exports to the United States and to Europe have fallen since 1975 both in current and constant dollars as Colombian firms have been gradually forced out of the most competitive markets.<sup>8</sup> This drop has been more than offset by an increase in exports to easier markets in Venezuela and the Caribbean. Thus, whereas the United States and Europe together received 61 percent of Colombia's clothing exports in 1975, they received only 24 percent in the first half of 1978, while the proportion taken by Venezuela and the Caribbean jumped from 33 to 72 percent during the same period (table 5 and figures 2 and 3). This change in the relative importance of the different destinations is of central significance for this study.

### *United States*

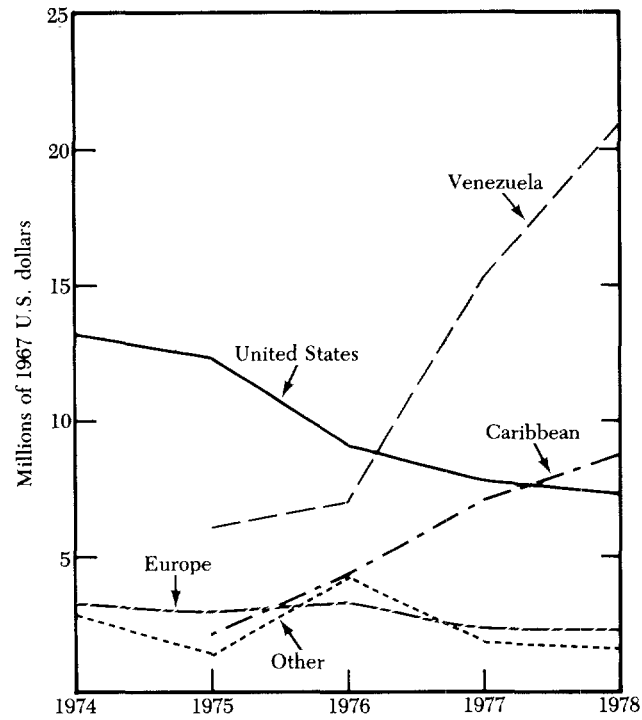
Colombian data on exports of clothing to the United States and U.S. data on imports of clothing from Colombia differ somewhat in absolute magnitude.<sup>9</sup> Fortunately, however, this difference is less important for the present study than the fact that the U.S. data show the same general pattern as the Colombian statistics during most of the period. According to U.S. figures, the value of clothing imports from Colombia in 1967 prices rose from \$1 million in 1970 to \$23–24 million in 1974–75, fell by 39 percent during the following two years, and recovered slightly in 1978 (tables 6 and 7). These data almost certainly understate the true

7. Throughout the destination section, "the Caribbean" refers to the Caribbean and Panama.

8. The causes of this decline in the ability to compete in the United States and Europe are analyzed in detail in the following two chapters and in Part Two.

9. In the world of international trade statistics, such differences are quite common. In the present case, the difference seems to be largely because U.S. imports from Colombia under the U.S. offshore assembly (807) scheme are recorded at their full value in the United States, whereas only the Colombian value added appears in Colombia's export statistics. This problem is discussed further in the following section.

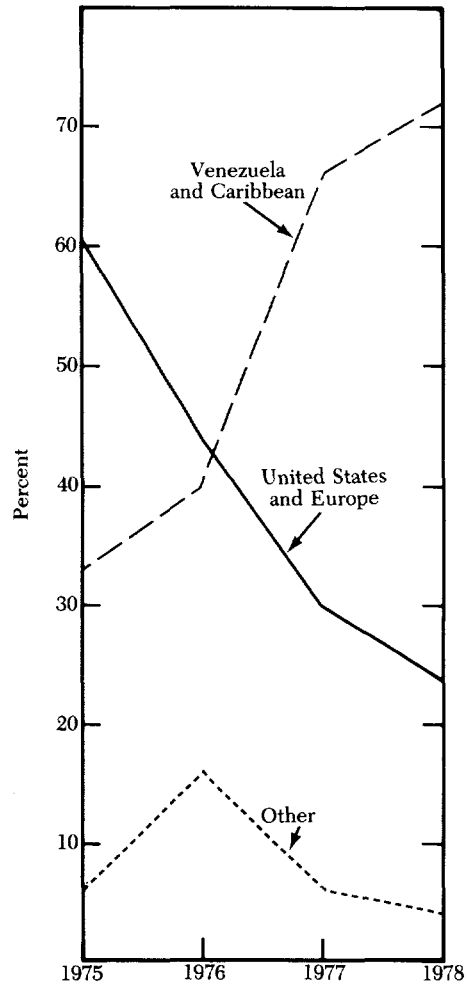
Figure 2. Value of Clothing Exports by Destination, Constant 1967 Prices, 1974-78



Note: It is assumed that total exports for 1978 are double those for January to June of that year. The figures for Venezuela and the Caribbean for 1974 are not shown because they probably include some fictitious exports.

Source: Table 5.

Figure 3. Percentage Distribution of Clothing Exports by Destination, 1975-78



Note: It is assumed that total exports for 1978 are double those for January to June of that year. The figures for Venezuela and the Caribbean for 1974 are not shown because they probably include some fictitious exports.

Source: Table 5.

Table 6. U.S. Imports of Clothing from Colombia and All Countries, Current and Constant Prices, 1960–78 (millions of dollars)

Year	U.S. imports of clothing (current prices)		U.S. imports of clothing (constant 1967 prices)		U.S. clothing imports from Colombia as percentage of U.S. clothing imports from all countries (5)
	From Colombia (1)	From all countries (2)	From Colombia (3)	From all countries (4)	
1960	—	304	—	n.a.	—
1965	—	541	—	n.a.	—
1970	1.0	1,153	0.9	1,041	0.09
1971	1.9	1,402	1.7	1,242	0.14
1972	4.3	1,718	3.7	1,497	0.25
1973	15.2	1,956	12.8	1,644	0.78
1974	29.2	2,095	22.5	1,618	1.39
1975	32.5	2,318	24.4	1,738	1.40
1976	26.3	3,257	18.8	2,328	0.81
1977	22.0	3,650	14.9	2,478	0.60
1978	27.4	4,833	17.8	3,132	0.57

— Zero or negligible.

n.a. Not available.

Sources: Col. (1): 1970–76: U.S. Department of Commerce, *Statistical Abstract of the United States 1978*, p. 884; 1977–78: U.S. Department of Commerce, *U.S. General Imports*, TQ2751. Col. (2): 1960, 1965: OECD, *Statistics of Foreign Trade, Series C: Trade by Commodities, Market Summaries: Imports Vol. II, January–December 1976*; 1970–78: U.S. Department of Commerce. Clothing prices: table 2–3. Col. (5) equals Col. (3) divided by Col. (4).

extent of the decline after 1974–75 however, largely because the U.S. apparel price index understates the true rise in U.S. clothing prices. This may be seen from U.S. data on the volume of clothing imports from Colombia in square yard equivalents (SYE) (tables 8 and 9 and figure 4).<sup>10</sup> According to these data, apparel imports from Colombia rose from 1 million SYE in 1971 to 25 million SYE in 1974, fell by 60 percent to 10 million SYE in 1977, and recovered slightly to an annual rate of 11 million SYE during the first half of 1979 (figure 4).

The decline after 1974–75 in Colombia's exports of apparel to the United States did not occur because of a fall in total U.S. imports of

10. Under the quota agreements the United States has with a number of countries, each suit exported to the United States is assumed to embody a certain number of square yards of fabric, each shirt a different number of square yards, and so forth. This makes it possible to reduce a country's heterogeneous garment exports to the United States to a single square-yard-equivalent figure.

Table 7. U.S. Imports of Clothing from Colombia by Fabric and Garment (New Classification System), 1977-78 and January-August 1978 and 1979 (millions of dollars)

<i>Fabric and garment</i>	1977	1978	<i>January-August</i>		<i>New agreement categories</i>
			1978	1979	
<b>Cotton</b>					
Pants	1.3	0.4	0.3	0.5	347-348
Coats	0.9	1.0	0.6	0.4	333-335
Other	1.1	1.4	1.0	1.0	
Total	3.3	2.8	1.9	1.9	330-359
<b>Wool</b>					
Men's suits	3.6	3.5	2.3	2.2	443
Women's suits and coats	0.6	1.0	0.7	0.6	435, 444
Other	0.9	0.6	0.3	1.1	
Total	5.1	5.1	3.3	3.9	430-459
<b>Man-made fibers</b>					
Coats	5.7	7.5	4.7	6.8	633-635
Blouses, woven	3.3	6.1	3.5	4.2	641
Skirts and blouses, knit	2.0	2.1	1.4	0.8	638-639
Other	2.5	3.8	2.0	2.8	
Total	13.5	19.5	11.6	14.6	630-659
<b>Total</b>	<b>22.0</b>	<b>27.4</b>	<b>16.8</b>	<b>20.4</b>	

*Note:* 1977 is the earliest year for which the U.S. Department of Commerce has provided value data at this level of disaggregation.

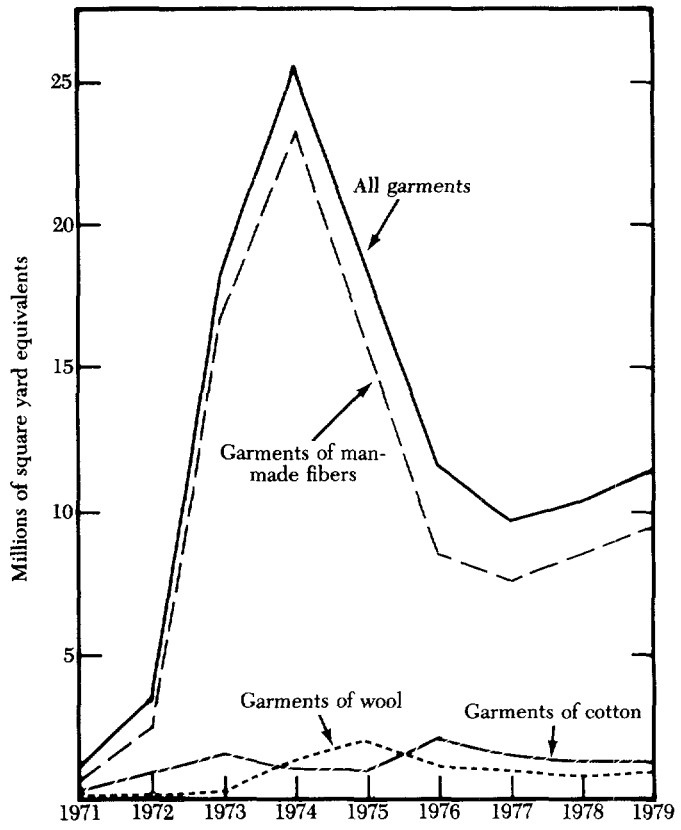
*Source:* U.S. Department of Commerce, *U.S. General Imports*, TQ2751, 1979.

clothing; on the contrary, the constant price volume of such imports almost doubled during 1974-78. Rather, it occurred because of a marked erosion of Colombia's already small share of total U.S. clothing imports. By 1978 this share had fallen to 0.6 percent, 60 percent lower than it had been three years earlier (table 6). Even among the three items that accounted together for two-thirds of the total value of Colombia's exports of apparel to the United States during 1978 (table 7), only in one (blouses of man-made fibers) did Colombia's share of total U.S. imports increase steadily over time. In the other two (men's suits of wool, and coats of man-made fibers) Colombia's share of total U.S. imports rose through 1974 or 1975 but then fell sharply, until by 1978 it was less than a third of what it had been three years earlier (table 10).

Finally, a similar erosion of Colombia's share of the U.S. import market after 1975 can be seen in the data on U.S. imports of clothing



Figure 4. Volume of U.S. Imports of Clothing from Colombia by Fabric, 1971-79



Note: For 1979 it is assumed that the percentage increase over 1978 is the same for the full year as it was for January to July.

Sources: Tables 8 and 9.

Table 8. U.S. Imports of Clothing from Colombia by Fabric and Garment  
(Old Classification System), 1971-77  
(thousand square yard equivalents)

<i>Fabric and garment</i>	1971	1972	1973	1974	1975	1976	1977	<i>Old agreement categories</i>
Cotton								
Pants	98	93	127	82	185	555	342	050-051
Coats	19	148	844	66	139	502	265	048-049
Other <sup>a</sup>	228	649	569	858	627	935	766	
Total	345	890	1,540	1,006	951	1,992	1,373	032,039-063
Wool								
Men's suits	26	13	43	428	788	579	439	120
Women's suits and coats	27	48	57	115	26	232	167	122
Other <sup>b</sup>	60	71	82	771	1,095	316	277	
Total	113	132	182	1,314	1,909	1,127	883	111-125
Man-made fibers								
Coats	43	133	1,967	4,956	3,574	2,380	1,608	229
Blouses	2	6	163	358	430	732	1,204	228
Skirts and blouses, knit	16	33	2,132	3,466	1,983	2,217	831	219
Other <sup>c</sup>	569	2,220	12,526	14,390	9,776	3,199	3,815	
Total	630	2,392	16,788	23,170	15,763	8,528	7,458	214-220
<b>Total</b>	<b>1,088</b>	<b>3,414</b>	<b>18,510</b>	<b>25,490</b>	<b>18,623</b>	<b>11,647</b>	<b>9,714</b>	

*Note:* All individually itemized garments are woven unless otherwise specified.

a. The bulk of this item is cotton clothing, not elsewhere specified.

b. The bulk of this item during 1974-75 is other knit outerwear.

c. The largest single subcategory is knit wearing apparel not elsewhere specified.

*Source:* U.S. Department of Commerce, *U.S. General Imports*, TQ2010, TQ2210, TQ2310, various years.

Table 9. U.S. Imports of Clothing from Colombia  
by Fabric and Garment (New Classification System),  
1976-78 and January-July 1978 and 1979  
(thousand square yard equivalents)

<i>Fabric and garment</i>	1976	1977	1978	<i>January-July</i>		<i>New agreement categories</i>
				1978	1979	
Cotton						
Pants	641	381	97	63	138	347-348
Coats	641	357	256	174	103	333-335
Other	716	761	851	542	545	
Total	1,998	1,499	1,204	779	786	330-359
Wool						
Men's suits	579	439	412	214	222	443
Women's suits and coats	220	178	241	131	64	435,444
Other	255	243	78	30	119	
Total	1,054	860	731	375	405	430-459
Man-made fibers						
Coats	2,707	2,041	2,092	1,136	1,536	633-635
Blouses, woven Skirts and blouses, knit	730	1,202	1,828	970	997	641
Other	1,938	739	720	413	287	638-639
Total	1,564	1,693	2,100	1,088	1,259	
Total	6,939	5,675	6,740	3,607	4,079	630-659
Total	9,991	8,034	8,675	4,761	5,270	
Total under old classification system	11,647 <sup>a</sup>	9,714 <sup>a</sup>	10,323 <sup>b</sup>	5,666 <sup>b</sup>	6,271 <sup>b</sup>	

a. From table 8.

b. These figures are calculated by multiplying the total in the previous row by 1.19.

Source: U.S. Department of Commerce, *U.S. General Imports*, TQ2010, TQ2210, TQ2310, various years.

Table 10. U.S. Imports of Clothing from Colombia and from All Countries (Three Major Items), 1971-78  
(thousands of units)

Year	<i>Men's suits, wool</i>			<i>Blouses, man-made fibers</i>			<i>Coats, man-made fibers<sup>a</sup></i>		
	<i>Imports from Colombia</i>	<i>Total imports</i>	<i>Colombia as percentage of total</i>	<i>Imports from Colombia</i>	<i>Total imports</i>	<i>Colombia as percentage of total</i>	<i>Imports from Colombia</i>	<i>Total imports</i>	<i>Colombia as percentage of total</i>
1971	6	703	0.9	2	34,799	0.0	12	25,517	0.0
1972	3	529	0.6	5	18,817	0.0	39	30,265	0.1
1973	10	694	1.4	134	18,541	0.7	572	31,845	1.8
1974	95	828	11.5	296	17,264	1.7	1,442	26,425	5.5
1975	175	999	17.5	355	19,084	1.9	1,040	22,800	4.6
1976	129	1,574	8.2	604	26,978	2.2	810	43,176	1.9
1977	98	1,503	6.5	994	36,246	2.7	624	54,696	1.1
1978	92	1,653	5.6	1,513	43,649	3.5	654	61,776	1.1

a. From 1971 to 1975, this item is no. 229 (old classification): coats, not knit. From 1976 onward, it is the sum of items 633-635 (new classification): men's and boys' suit-type coats, other men's and boys' coats, and women's, girls', and infants' coats.

Source: U.S. Department of Commerce, *U.S. General Imports*, TQ2010, TQ2210, TQ2310, various years.

Table 11. U.S. Imports of Clothing under Item 807  
by Country of Origin, 1970-76  
(millions of dollars)

<i>Country of origin</i>	1970	1972	1974	1975	1976
Colombia	0	2	19	20	14
Costa Rica	2	5	10	11	19
Dominican Republic	n.a.	n.a.	6	11	19
El Salvador	n.a.	n.a.	9	13	18
Haiti	2	4	20	19	27
Mexico	21	51	117	124	131
Philippines	1	5	13	14	13
Others	17	19	26	24	35
Total	42	85	219	236	276
Colombia as percentage of total	1	2	8	9	5

n.a. Not available.

Source: U.S. International Trade Commission (1978, p. C-67).

carried out under the offshore assembly, or item 807, scheme.<sup>11</sup> Of the seven main countries using 807 for apparel, Colombia was the only one to show a significant fall in the current dollar value of its exports after 1975; just one year later, its share of total U.S. imports under the scheme had fallen from 9 to 5 percent (table 11).

### *Europe*

If clothing exports to the United States have tended to decline since 1975, exports to the other potentially lucrative but difficult market, Europe, have fared little better. Throughout 1974-77, Colombia's total clothing exports to Europe never exceeded \$5 million. During 1977-78, about half the total was accounted for by just one firm. This company had made a heavy investment in building up not only production and marketing capabilities for export but also a long-term relation with its European buyer; hence, it had a strong vested interest in continuing to export and was holding out as long as it could. Of the rest of Colombia's European exports in 1977-78, almost one-third was purchased by a single, large European department store chain. When interviewed, the part-time buyers for this chain in Bogotá stated that almost all the garments they were ordering could be bought 10 to 30 percent less

11. Under this scheme, if precut fabric and other inputs are shipped from the United States for assembly abroad, the finished garments that are returned to the United States are charged import duties only on the value that was added overseas.

expensively in East Asia. They explained, however, that their client has a policy of spreading around half a million dollars or so in Colombia to ensure a foothold there should there be a cut in European import quotas for apparel from East Asia or should war break out again in Korea. This explanation was eminently believable; with an average degree of overpricing in Colombia of, say, 20 percent, the total cost of the insurance policy to the chain amounted to only about \$100,000 a year, which is little more than petty cash for a corporation of its size.<sup>12</sup>

#### *Venezuela and the Caribbean*

Venezuela and Colombia are both members of the Andean Group integration scheme. Like all other members of that scheme, Venezuela has placed clothing on its list of products that are exempt from tariff liberation. Thus, in practice, the only way that Colombians can export clothing to Venezuela is through the free port of the Margarita Islands (often referred to simply as the Islands). Free-port status was created for the Islands on April 1, 1975; within one year, the number of licensed buyers registered there quadrupled from 430 to 1,800.

A Colombian firm wishing to export garments to the Islands generally sends them overland to the town of Cúcuta on the Colombian side of the Colombo-Venezuelan border. There they are placed on a bonded truck, which is driven and ferried to the Islands. Travelers from Caracas fly to the Islands to pick up the merchandise in small lots at the many stores located there; provided they do not bring home more than a suitcase or two of goods, they are not charged the duties of more than 100 percent that they would otherwise have to pay.

The most important characteristic of the Margarita Islands and the Caribbean for the present discussion is that they represent relatively easy markets for Colombia with respect to price, fashion, sizing, quality control, delivery times, and marketing arrangements. In these small, isolated markets situated well away from the major trade routes, the price of apparel tends to be relatively high. Twenty-four of the thirty Colombian clothing exporters in the sample gave us detailed data on the prices received for particular garments both domestically and abroad. In only six cases was the export price (including the CAT and the value of subsidized credit) greater than or equal to the domestic price. In all six

12. To look at the same question from a micro perspective, a pair of jeans that might cost \$6 f.o.b. in Korea or Taiwan tended to cost \$7 or \$8 f.o.b. in Colombia. But since the final retail selling price was likely to be \$18 or so, provided the order was marginal (as all Colombian orders were for this chain), the extra expense was negligible.

Table 12. Relation between the Destination of Exports and the Ratio of the Export Price to the Domestic Price, Colombian Clothing Firms, 1978  
(number of firms)

<i>Destination of exports</i>	<i>Export price (including export incentives)</i>			<i>Total</i>
	<i>Lower than domestic price</i>	<i>Equal to domestic price</i>	<i>Greater than domestic price</i>	
United States and Europe	13	0	0	13
Venezuela, Caribbean, and Panama	5	5	1	11
Total	18	5	1	24 <sup>a</sup>

*Note:* The hypothesis that there is no relation between the destination of exports and the ratio of the export price to the domestic price can be rejected at better than the 1 percent level on a  $\chi^2$  test with two degrees of freedom.

a. Six firms had no domestic sales: four of these sell only to Venezuela, two sell only to the United States.

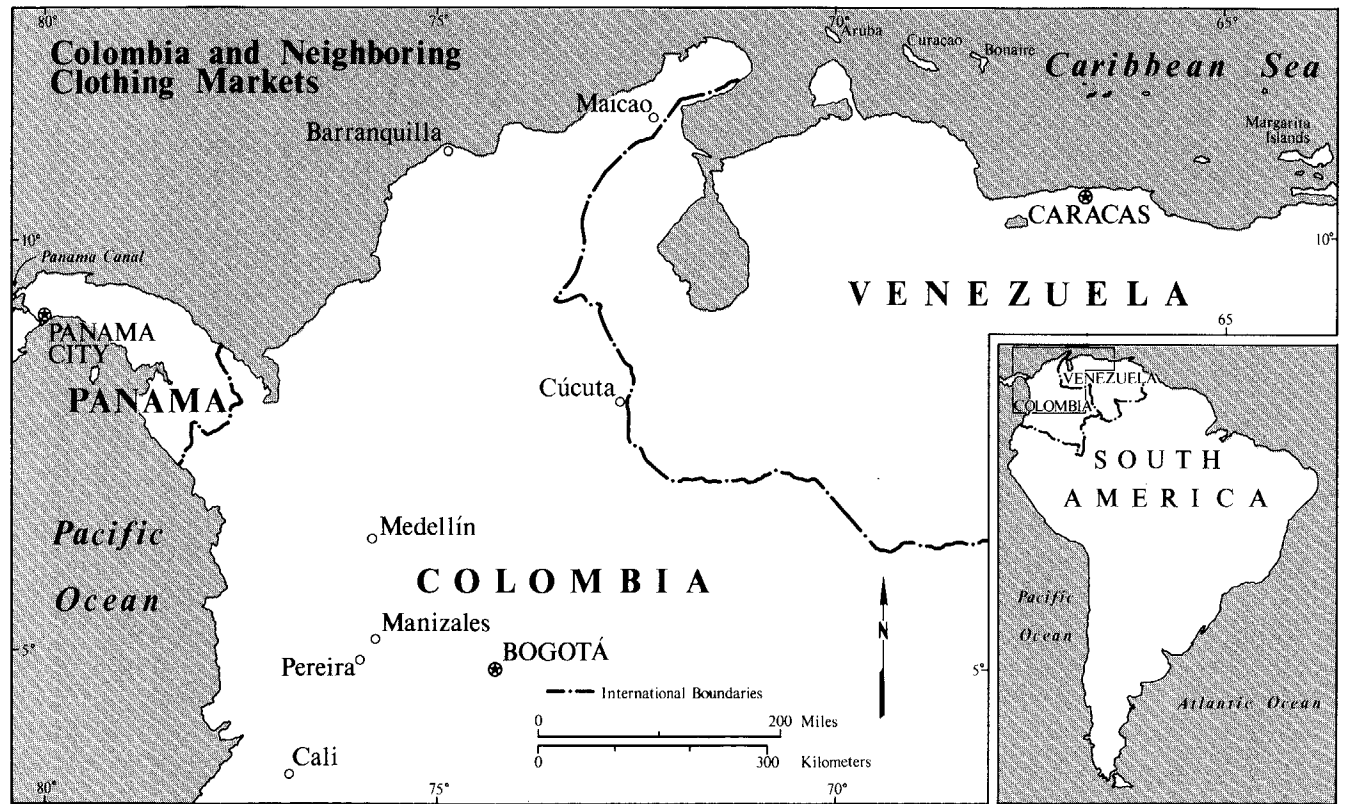
*Source:* Interviews with firms.

instances, the garments in question were being sold in the Islands or the Caribbean. By contrast, all thirteen exporters to the United States and Europe who gave us price comparisons indicated that the price received on export sales (again including the value of export incentives) was below the domestic price (table 12). In addition to having high prices for all, the Islands and the Caribbean have a second price-related attraction that is special to Colombia: because of their proximity (see map), Colombians can place garments there with significantly lower transport costs than any other nation that exports clothing.<sup>13</sup>

In fashion, Venezuela and the Caribbean, like Colombia, tend to lag a year or more behind the United States and Europe. In addition, because of their location near the equator, they experience far less seasonal variation in climate, and hence in fashion, than the rich countries of the north. Clothing purchasers in Venezuela and the Caribbean tend to be of similar size and shape to those in Colombia—but different from those in North America, Europe, and East Asia<sup>14</sup>—and their quality demands

13. Transport costs are analyzed in some detail in chapter 5.

14. Since most countries in Latin America maintain high tariff and licensing or quota barriers against clothing imports—the Islands in Venezuela and Manáos in Brazil are two





tend to be similarly less rigorous than those of consumers from the more developed countries. Partly because of the lack of pronounced seasonal variations in climate and fashion, and partly because the Islands and the Caribbean are less a buyer's market in clothing than the United States and Europe, firms generally have more lead time to produce for export there, and the consequences of late delivery are less serious.

Unlike any other major world market, the Islands and parts of the Caribbean use the same language as Colombia, which facilitates marketing for some potential exporters, especially smaller firms, and gives Colombians an obvious advantage over East Asians. For example, since Venezuelan law requires that firms exporting to the Islands use a resident representative rather than a traveling salesperson, the common language enables Colombian firms to use Colombian nationals in this capacity. Marketing is also facilitated by the fact that labeling regulations are less strict in Venezuela and the Caribbean than in the United States and Europe, and in some cases are nonexistent.

Some of these particulars may seem relatively minor in themselves. Yet together, they make such an important point in this study that it would be difficult to overemphasize it. A Colombian entrepreneur who wants to export clothing to the United States or Europe not only has to compete in price with the most efficient firms in the world, he also has to adopt an export mentality. This means that he must be willing and able, among other things, to alter his working methods to comply with clients' detailed specifications, to implement and maintain a stringent system of quality control, and to ensure that all shipments meet their tight delivery dates. By contrast, a Colombian exporting to the Islands or the Caribbean faces price competition only a little tougher than at home, can produce and sell garments to his own specifications, can use the same less-than-strict quality control apparatus he uses for domestic sales, and can be late in delivering the goods without incurring serious penalties. In other words, a Colombian firm selling to the Islands and the Caribbean can simply ship to these markets the same goods that it sells at home on much the same terms, whereas a firm exporting to the United States or Europe almost invariably has to make substantial modifications to its product, to the way it is produced, and to the way it is marketed. Further, if one notes that the three most popular Caribbean markets for Colombian clothing exporters—Aruba, Curaçao, and Pana-

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of the more important loopholes in the defense system—it is hardly worthwhile for East Asians to devote much effort to manufacturing garments to Latin American specifications of size and fit.

ma—are closer to Barranquilla than is Bogotá, while the Islands are barely farther away, the conclusion is inescapable: exporting garments to the Islands and the Caribbean has much more in common with selling domestically than it has with exporting to the United States or Europe. It is for this reason that the changing destination of Colombia's clothing exports over time—toward the Islands and the Caribbean and away from the United States and Europe—is so significant.<sup>15</sup>

### The 807 Complication

A further problem with the Colombian clothing export data stems from the country's participation in the U.S. offshore assembly (807) scheme. Under that arrangement, fabric and other inputs are made and cut in the United States, shipped to Colombia for assembly, and then shipped back to the United States as finished goods. The cut cloth and other inputs that enter Colombia under the 807 scheme are not paid for by the Colombian assembling firm, nor are they included in the value of Colombian apparel registered as having been exported to the United States. This means that a pair of pants selling for \$6 f.o.b. can appear in the INCOMEX and DANE lists of Colombian exports in three different ways:<sup>16</sup>

	<i>Value of exports listed</i>
Fabric and pants made entirely in Colombia	\$6.00
Fabric, buttons, and other inputs imported under the regular Vallejo Plan; fabric cut and garment assembled in Colombia	\$6.00
Precut fabric, buttons, and other inputs imported under the assembly provision of the Vallejo Plan; garment assembled in Colombia; assumes that fabric and inputs are 50 to 75 percent of the total cost of the pants	\$1.50–\$3.00

The only difference between the second and third cases in this table is that, in the second, the fabric was cut in Colombia, whereas in the third it was cut abroad—yet the value of exports that is listed differs by a factor

15. Of the thirty firms that we interviewed, eleven were exporting solely to the United States or Europe in 1978, fifteen were exporting solely to the Islands or the Caribbean, and only four were exporting *both* to the United States *and* to the Islands or the Caribbean. This evidence is consistent with the claim made above: these are indeed quite different markets.

16. The Vallejo Plan is a drawback scheme under which firms are exempt from or receive rebates on tariffs payable on imported inputs that are used to manufacture export goods.

of two to four. It is not clear what the ideal solution to this problem is. One possibility might be to subtract the value of imported inputs from the value of non-807 Vallejo Plan exports; the aggregate export figures would then approximately reflect Colombian direct and indirect value added. (The value of imported petrochemicals, synthetic fibers, yarns, wools, and so on, used in making Colombian fabric would, however, still be included.) A second possibility might be to add the value of inputs imported but not paid for under 807 (table 13) to the value of 807 exports; the aggregate export figures would then reflect gross value of output in the usual sense, regardless of whether inputs were produced domestically or abroad. These two adjustments are attempted in table 14. Given the crudity of the assumptions needed to generate the adjusted numbers, and since the trends they demonstrate do not differ significantly from those discussed earlier, a third option will be followed hereinafter: recognize the problem, bear it in mind throughout, but continue to use the original, unadjusted data.

### Unregistered Exports

The earlier discussion of fictitious exports was concerned with foreign sales that were registered but never took place; a mirror-image problem arises with exports that are never registered but do take place. A Colombian firm that wants to receive the export subsidy for selling

Table 13. Clothing Imports, Nonreimbursable and Reimbursable, 1973-77  
(millions of dollars)

<i>Year</i>	<i>Nonreimbursable imports<sup>a</sup></i>	<i>Reimbursable imports<sup>b</sup></i>
1973	6	1
1974	29	2
1975	12	2
1976	10	1
1977	16	2

a. These are presumably mostly cut cloth and other apparel inputs (for example, buttons, zippers, and labels) that are imported, sewn together as garments, and re-exported under the U.S. 807 scheme. The cloth and other inputs are not in fact paid for, hence the title nonreimbursable.

b. Imports of finished garments that will be sold wholesale or retail in Colombia.

Source: INCOMEX, unpublished tabulations, Impo 5, 1973-77.

Table 14. Unadjusted and Adjusted Clothing Exports: Total and to the United States, 1973–77 (millions of dollars)

Year	Total exports			Exports to the United States		
	Un-adjusted exports (1)	Minus estimated value of non-807 imported inputs (2)	Plus estimated value of inputs imported under 807 (3)	Un-adjusted exports (4)	Minus estimated value of non-807 imported inputs (5)	Plus estimated value of inputs imported under 807 (6)
1973	19.2	16.6	25.5	n.a.	n.a.	n.a.
1974	52.3 <sup>a</sup>	46.7 <sup>a</sup>	81.3 <sup>a</sup>	17.0	n.a.	46.0
1975	29.1	24.4	41.0	16.6	n.a.	28.5
1976	39.7	31.2	49.9	12.7	n.a.	22.9
1977	46.7 <sup>b</sup>	40.7 <sup>b</sup>	62.2 <sup>b</sup>	11.6	n.a.	27.1

n.a. Not available.

*Note:* The value of inputs imported under the 807 scheme is assumed to be equal to the value of nonreimbursable imports of clothing. The value of exports registered under 807 is assumed to be one-quarter of this figure. The value of non-807 imported inputs is assumed to be half the value of non-807 Vallejo Plan exports, and is estimated as half the difference between total Vallejo Plan exports and (estimated) exports registered under 807.

a. Probably includes some fictitious exports.

b. INCOMEX data.

*Sources:* Unadjusted data: tables 1 and 5. Nonreimbursable imports of clothing: INCOMEX, unpublished tabulations, Impo 5, 1973–77. Total Vallejo Plan exports: table 40.

garments to Venezuelans has to sell its goods in the Margarita Islands. If the firm is willing to forgo the CAT, however, it can take the alternative route of selling to merchants in Cúcuta and Maicao, whence the goods find their own way across the border. One reason that an exporter might be willing to forgo the CAT is that prices in Cúcuta and Maicao tend to be somewhat higher than in the Islands, because the markets in these two towns are even less competitive than the Islands' market. In addition, a firm selling to a Colombian town can avoid dealing with the export-related bureaucracy. This is likely to be a particularly important consideration for firms that specialize in a variety of shady activities, but even fully legitimate enterprises, particularly smaller ones, may place some value on the administrative and psychic costs so saved.

There are no hard data on the value of Colombian clothing that passes through Cúcuta and Maicao to Venezuela. On the basis of information collected during the interviews, however, it seems that unregistered exports following this route were probably at least as great as registered exports to the Islands in 1977 (\$23 million), and possibly considerably

greater.<sup>17</sup> The border town of Ipiales serves as a comparable focal point for unregistered exports to Ecuador, but these seem to be much less significant in volume.

If the absolute size of unregistered exports is not discernible, can anything be deduced about their likely trend over time? The volume of unregistered exports is likely to be positively related to per capita incomes in Venezuela and Ecuador, inversely related to the value of the CAT, positively related to the differential between the black market and official exchange rates, and sensitive to institutional changes. Per capita incomes in Colombia's two oil-rich neighbors have increased significantly since 1973; the CAT received by clothing exporters has been raised twice since 1975; the black market exchange rate differential has switched from positive to negative since 1975; and a number of the new traders who appeared in the Margarita Islands after the Islands were granted free-port status in 1975 previously operated in Maicao and took their trade with them. The first of these four considerations suggests that unregistered exports are likely to have increased in volume since 1974–75; the last three suggest the reverse. Unfortunately, therefore, there is no way of knowing with any degree of certainty what the net trend has been.

While an increase in the CAT makes it less likely that Colombian firms will smuggle their export goods across borders, it also increases the incentive for legal exporters to overinvoice their foreign sales. The existence of taxes on corporate profits, however, gives firms an incentive to underinvoice their exports. (Such taxes, and hence this incentive, have remained constant since 1975.) Not surprisingly, no estimates of the overall magnitude of over- or underinvoicing are available. Two interviewees suggested that, to the extent that overinvoicing does take place, it is likely to be restricted to the Venezuelan and Caribbean markets, since falsifying invoices is likely to be less risky for sales to these areas than to the United States and Europe.

17. One informant suggested off-the-cuff that they may be twice as great. One firm in our sample that had almost ceased exporting to the United States and the Islands sold goods valued at half a million dollars (half its total value of production) to Cúcuta in 1977. A second firm sent 40 percent of its output to Cúcuta, twice as much as to the Islands.

## Conclusion

The statistics are terrible.<sup>18</sup> Yet, despite their many deficiencies, and after allowing for all the unknowns, one clear and important conclusion shines through. Colombia's clothing exports to the United States, Europe, Venezuela, and the Caribbean all increased impressively from 1970 to 1974 or 1975; after that, exports to Venezuela and the Caribbean, which have more in common with domestic sales than with exports to the United States, continued to grow, while exports to the United States and Europe declined significantly through 1977 and then leveled out or recovered slightly. The task in the next two chapters is to explain the rise, the fall, and the leveling out or slight recovery in Colombia's exports to the difficult markets.

18. Needless to say, this is not the fault of the agencies that collect and publish them. Nor, to repeat, are statistical problems like those discussed in this chapter unique to the clothing industry or to Colombia.

## Chapter 2

# Exchange Rate and Export Incentive Policies

*Our business isn't really making shirts, it is making money. In the years that we could make money on exporting shirts, we were happy to do it. But now that exports are no longer profitable, we of course sell the shirts here in Colombia.*

—COLOMBIAN SHIRT MANUFACTURER

THE MOST IMPORTANT SINGLE REASON Colombia's exports of clothing to the United States and Europe began to grow rapidly after 1970 is that the government's exchange rate and export-incentive policies had begun to make them profitable. The reasons these exports subsequently declined are rather more complex, but the de facto reversal of these exchange rate policies appears to have been at least a contributing factor.

The dollar prices that Colombian clothing firms receive for exporting garments to the world markets are determined by aggregate supply and demand in those markets and are outside Colombia's control. The main variables relating to the profitability of exports that Colombian governments and producers are able to affect are the number of pesos received per dollar of exports, on the one hand, and costs of production, on the other. The analysis in this chapter focuses on the number of pesos received per dollar of exports; costs of production are examined in detail in chapter 5.

In 1967, a year of foreign exchange crisis, President Carlos Lleras Restrepo engineered the beginning of a fundamental shift in the emphasis of Colombia's foreign trade strategy away from import substitution and toward export promotion. Decree Law 444, passed in March of that year, replaced the existing fiscal export incentive of Law 81 with the more generally usable and neater CAT, revamped and simplified the Vallejo Plan drawback scheme, and set up the export promotion agency PROEXPO.<sup>1</sup> A few months later, a crawling peg exchange rate—devaluation more or less in step with inflation—was introduced. In 1973, PROEXPO began to grant credit to exporters at below market interest

1. For a more detailed description and analysis of the 1967 measures, see Díaz-Alejandro (1976).

rates. This credit is available for up to 80 percent of the value of exports, or for 80 percent of the direct domestic content of exports if the Vallejo Plan is used. The rate of interest charged on PROEXPO credit was reduced from 18 to 13 percent in 1977, while the differential between the market rate of interest and the PROEXPO rate increased from 2 percentage points in 1973 to 14 percentage points in 1978. The CAT was reduced sharply in value and was differentiated by product in 1975; it was then increased in value for certain items in 1977 and 1978. From 1974 onward, the CAT for Vallejo Plan exports has been paid only on direct domestic content. All the measures described in this paragraph and some other related data are summarized in table 15.

To estimate quantitatively the aggregate impact that the various changes in export incentives have had on the profitability of exporting over time, it is necessary first to bring these incentives to a single common denominator. This is done in table 16, which presents the value of the effective subsidies implicit in the CAT, PROEXPO credit, and the Vallejo Plan as percentages of the value of export sales during 1967-79. (The formulas used to calculate these effective values are derived and presented in Appendix B.) For a clothing exporter who did not use the Vallejo Plan, the total effective subsidy implicit in the CAT and PROEXPO credit rose gradually during 1967-74, fell sharply with the reduction of the CAT in 1975, and then increased again through 1978. For firms using the Vallejo Plan, the total effective subsidy fluctuated slightly around a constant trend during 1967-72, declined during 1973-75,<sup>2</sup> and recovered slightly during 1977-78.

Manipulation of export incentives was only one way in which the government influenced the net number of pesos received per dollar of exports after 1967; exchange rate policy was important too. The rate at which the government devalued the peso during 1967-78 can be seen from the series for the nominal exchange rate in table 17. The rate of devaluation, of course, means little in isolation from movements in relative prices. The real exchange rate, also in table 17, brings these two aspects together: it is computed by multiplying the nominal exchange rate by the ratio of U.S. to Colombian prices.<sup>3</sup> The combined effects of

2. The elimination of prior deposits was an important factor in this decline, which serves to illustrate that the "subsidy" calculated for firms using the Vallejo Plan is a rather different animal from the more conventional subsidy computed for firms not using that plan.

3. U.S. prices are used in these computations rather than prices in a basket of countries because by far the greatest part of Colombia's exports of clothing to difficult markets goes to the United States.



devaluation and export-incentive policies are reflected in the effective exchange rate. This is computed by multiplying the nominal exchange rate by  $(1 + s)$  where  $s$  is the total effective subsidy to clothing exports (table 16). Finally, all the above influences—the rate of devaluation, the rates of increase of prices in Colombia and the United States, and the effective value of export incentives—are brought together in a single summary measure, the real effective exchange rate.<sup>4</sup>

Despite its apparent complexity, the real effective exchange rate has a simple and powerful intuitive interpretation. Take a limited liability company—70 percent of the firms interviewed in this study were of this type—that does not use the Vallejo Plan. If it sells a garment abroad, the total number of pesos it receives ( $P_x$ ) will depend upon the price of the garment in dollars ( $P_\$$ ), the nominal exchange rate ( $R$ ), and the total effective subsidy ( $s$ ) it receives from the CAT and PROEXPO credit. That is,

$$P_x = P_\$ \cdot R \cdot (1 + s). \quad (2.1)$$

If it sells the same garment in the domestic Colombian market, it will receive a price in pesos ( $P_d$ ). The ratio of these two prices is

$$\frac{P_x}{P_d} = \frac{P_\$}{P_d} \cdot R \cdot (1 + s). \quad (2.2)$$

But equation (2.2) is nothing but the formula for the real effective exchange rate. Thus, changes over time in the real effective exchange rate, as it is computed here, measure changes over time in the relative profitability of exporting and selling domestically.<sup>5</sup> A rise in the real effective exchange rate means that exporting has increased in profitability relative to selling domestically; a fall indicates the reverse.

Table 17 presents two separate sets of estimates for the real effective exchange rate. One set uses wholesale clothing prices as the deflator, the other uses general consumer prices. For the present purposes, the first set is the more relevant; the second is presented mainly as a check on whether the trend of the real effective exchange rate for clothing seems to be particular to that industry.<sup>6</sup>

4. This is also known as the purchasing-power-parity-adjusted effective exchange rate.

5. It is assumed that the ratio of the cost of producing a good for export to the cost of producing the same good for domestic sale remains constant over time.

6. It would have been desirable to use general wholesale prices rather than general consumer prices in the second set of estimates. Unfortunately, however, the Colombian wholesale price index includes, and gives quite a heavy weight to, the price of coffee. The

Table 15. Nominal Incentives to Clothing Exports and Related Data, 1967–79 (percent)

<i>Item</i>	1967	1968	1969	1970
Nominal direct export subsidy (CAT) as percentage of value of exports				
Firms not using Vallejo Plan	15	15	15	15
Firms using Vallejo Plan	15	15	15	15
Discount if CAT is sold in stock market when it is received as percentage of value of CAT	19.9	11.0	9.5	7.1
Average tax rate on corporate profits				
Limited liability company	12.5	12.5	12.5	12.5
Public company	42	42	42	42
Percentage of value of exports that may be financed by PROEXPO credit				
Firms not using Vallejo Plan	0	0	0	0
Firms using Vallejo Plan	0	0	0	0
Rate of interest on PROEXPO credit	...	...	...	...
Market rate of interest <sup>c</sup>	18	18	15	14

... Not applicable.

a. Projected. Figures in parentheses are applicable to exports to the United States only.

b. From 1974 onward, exports using the Vallejo Plan have received the CAT on domestic value added only; domestic value added is assumed here to be 50 percent of the value of output.

c. The rate of interest implicit in the CAT.

Sources: CAT: Government of Colombia, Decree Laws no. 444 of 1967; 2004 of 1974; 2091 of 1976; 2227, 2990, and 2291 of 1977; and 2067 of 1978. Also Colombia–United States textile agreement, 1978.

Whichever set of real effective exchange rates is used, the pattern of variation during 1967–78 is clear. From 1967 until 1970–72, the profitability of exporting clothing in relation to selling it at home rose steadily; from about 1973 onward, the relative profitability of exporting began to decline. In the case of the real effective exchange rate deflated by general consumer prices, by 1978 the relative profitability of export-

sharp rise in the price of coffee during 1976–77 did not, directly and of itself, increase the returns to selling manufactured goods domestically in those years—yet the inclusion of coffee in the wholesale price index makes this seem to be the case. If this defect were ignored and the wholesale price index were used in computing the real effective exchange rate, the arguments that follow in the text would be further strengthened.

Another alternative real effective exchange rate might use a cost-of-inputs price index as the deflator. Such an index might include, for instance, the price of fabric, the prices of

1971	1972	1973	1974	1975	1976	1977	1978	1979 <sup>a</sup>
15	15	15	15	5	5	8	12	12(9.85)
15	15	15	7.5 <sup>b</sup>	2.5	2.5	4	6	6(4.925)
5.8	4.4	5.1	5.6	3.0	2.5	3.8	5.7	5.7
12.5	12.5	12.5	20	20	20	20	20	20
42	42	42	40	37	37	37	37	37
0	0	80	80	80	80	80	80	80
0	0	40	40	40	40	40	40	40
...	...	18	18	18	18	15.1	13	13
15	17	20	23	23	25	28	27	27

Discount on CAT: Teigeiro and Elson (1973), and Cardona (1977, table 9).

Tax rate on corporate profits: Perry (1977).

PROEXPO credit: PROEXPO, unpublished data.

Rate of interest on PROEXPO credit: Resolutions of the Junta Monetaria no. 59 of 1972 and no. 34 of 1977.

Market rate of interest: 1967-76: Carrizosa (1977); 1977-78: calculations of FEDESARROLLO.

ing had returned to what it was in the crisis year of 1967. For the index deflated by wholesale clothing prices, by 1978 the relative profitability of exporting was 15 percent below what it had been in 1967. This summary is applicable to the case of a limited liability company that does not use the Vallejo Plan; for public companies and for all companies using the Vallejo Plan, the deterioration in the relative profitability of exporting by 1978 was even greater. The relative and absolute decline in

other inputs, and the cost of employing labor. Even if time series data were available to construct this index, it would need to be compared, presumably, with similar indexes in other clothing-exporting countries rather than with a similar index for the United States. FEDESARROLLO (1979) computes a real effective exchange rate at an aggregate level for all industry using a crude cost-of-inputs price index; it shows the same general trends as the real effective exchange rates used here.

Table 16. Effective Incentives to Clothing Exports, 1967-79

<i>Effective incentive</i>	<i>Percentage of value of exports</i>			
	1967	1968	1969	1970
Effective CAT				
Limited companies				
Not using Vallejo Plan	14.2	15.5	15.7	16.1
Using Vallejo Plan	14.2	15.5	15.7	16.1
Public companies				
Not using Vallejo Plan	22.9	24.2	24.4	24.8
Using Vallejo Plan	22.9	24.2	24.4	24.8
Effective subsidy implicit in PROEXPO credit				
Firms not using Vallejo Plan	0	0	0	0
Firms using Vallejo Plan	0	0	0	0
Effective subsidy implicit in Vallejo Plan	44.0	44.0	42.2	41.6
Total effective subsidy to clothing exports (CAT + PROEXPO credit + Vallejo Plan)				
Limited companies				
Not using Vallejo Plan	14.2	15.5	15.7	16.1
Using Vallejo Plan	58.2	59.5	57.9	57.7
Public companies				
Not using Vallejo Plan	22.9	24.2	24.4	24.8
Using Vallejo Plan	66.9	68.3	66.6	66.4

*Note:* For the formulas used to calculate the effective value of the different incentives, see Appendix B.

the profitability of exporting will be examined in more detail in the discussion of costs and effective protection in chapter 5.<sup>7</sup>

The basic cause of the decline after 1972 in the real effective exchange rate was simple: the government did not devalue the peso fast enough. True, the reduction in the CAT during 1975 contributed significantly to the decline in that year—but 1975 was the only year during the 1967-78 period that the total effective subsidy to clothing exports fell.<sup>8</sup> In every

7. The fact that the U.S. wholesale clothing price index understates the true rise in U.S. clothing prices during 1970-78 means that the decline in the real effective exchange rate after 1972 weighted by wholesale clothing prices is exaggerated to some extent. As against this, however, most companies exporting garments to the United States do in fact use the Vallejo Plan; as noted above, for them, other things being equal, the decline in the real effective exchange rate was significantly greater than that described in the text. Furthermore, the general pattern of rise and decline appears also in the real effective exchange rate weighted by general consumer prices.

8. This statement refers to limited liability companies not using the Vallejo Plan (see table 16).

<i>Percentage of value of exports</i>								
1971	1972	1973	1974	1975	1976	1977	1978	1979 <sup>a</sup>
16.3	16.5	16.4	17.9	6.1	6.1	9.7	14.3	14.3(11.8)
16.3	16.5	16.4	9.0	3.1	3.1	4.9	7.2	7.2( 5.9)
25.0	25.2	25.1	24.2	7.8	7.8	10.4	14.5	14.5(11.7)
25.0	25.2	25.1	12.1	3.9	3.9	5.2	7.2	7.2( 5.8)
0	0	0.7	1.6	1.6	2.3	4.1	4.5	4.5
0	0	0.3	0.8	0.8	1.1	2.1	2.3	2.3
42.1	43.2	36.1	32.7	33.1	32.6	31.9	31.9	31.9
16.3	16.5	17.0	19.6	7.7	8.4	13.8	18.9	18.9(16.3)
58.4	59.7	52.8	42.4	37.0	36.8	38.8	41.3	41.3(40.0)
25.0	25.2	25.8	25.8	9.4	10.1	14.5	19.0	19.0(16.2)
67.1	68.4	61.6	45.6	37.8	37.6	39.1	41.4	41.4(40.0)

a. Projected. Figures in parentheses are applicable to exports to the United States only.  
*Source:* See table 15.

other year, the real effective exchange rate declined wholly and solely because the rate of devaluation was not rapid enough to compensate for the fact that prices in Colombia were rising faster than prices in the United States.

As a first step in examining the consequences of the variations in the real effective exchange rate during 1967-78, the clothing-price and consumer-price versions of this variable are plotted in figure 5, together with data on U.S. imports of clothing from Colombia.<sup>9</sup> At first glance, the graph indicates, in an apparent paradox, that the years in which the real effective exchange rate for clothing fell most rapidly, 1973-75, were also the years in which clothing exports to the United States rose most

9. Exports to the United States are used in the following analysis because they represent Colombia's main clothing exports to a difficult market and because they entail the fewest data problems. The series of U.S. clothing imports from Colombia is used rather than the series of Colombia's clothing exports to the United States because it is available for a greater number of years. Whichever series is used, the results are essentially the same.

Table 17. Nominal, Real, Effective, and Real Effective Exchange Rates for Clothing Exports, 1968–78  
(index 1967 = 100)

<i>Item</i>	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977	1978
Nominal exchange rate											
Peso per dollar	16.48	17.53	18.68	20.26	22.14	23.98	26.66	31.58	35.21	37.20	39.06 <sup>a</sup>
Index	110.8	117.8	125.5	136.2	148.8	161.2	179.2	212.2	236.6	250.0	262.5
Wholesale clothing prices											
Colombia	104.3	111.5	119.0	131.9	145.6	181.7	249.2	285.8	334.0	405.4 <sup>b</sup>	492.7
United States	103.6	107.4	110.8	112.9	114.8	119.0	129.5	133.4	139.9	147.3	152.4 <sup>a</sup>
General consumer prices											
Colombia <sup>c</sup>	105.9	116.6	124.5	135.8	153.8	185.1	229.6	281.7	338.6	448.7	530.4
United States	104.2	109.8	116.3	121.3	125.3	133.2	147.7	161.3	170.6	181.8	195.5
Real exchange rate, deflating with whole- sale clothing prices	110.0	113.5	116.9	116.5	117.3	105.6	93.1	99.1	99.1	90.8	81.2
Real exchange rate, deflating with general consumer prices	109.0	111.0	117.3	121.6	121.2	116.0	115.3	121.5	119.3	101.3	96.7
Effective exchange rate											
Limited companies											
Not using Vallejo Plan	112.0	119.4	127.7	138.7	151.8	165.2	187.6	200.3	224.7	249.3	273.3
Using Vallejo Plan	111.7	117.6	125.2	136.3	150.2	155.7	161.3	183.8	204.6	219.4	234.5
Public companies											
Not using Vallejo Plan	112.0	119.3	127.5	138.5	151.6	164.9	183.4	189.0	212.0	233.0	254.2
Using Vallejo Plan	111.7	117.6	125.2	136.3	150.1	156.0	156.3	175.2	195.1	208.4	222.4

Real effective exchange rate, deflating with wholesale clothing prices											
Limited companies											
Not using Vallejo Plan	111.3	115.0	118.8	118.7	119.7	108.1	97.5	93.4	94.1	90.5	84.5
Using Vallejo Plan	110.9	113.3	116.5	116.7	118.4	101.9	83.8	85.8	85.7	79.7	72.5
Public companies											
Not using Vallejo Plan	111.2	114.9	118.7	118.5	119.5	108.0	95.3	88.2	88.8	84.6	78.6
Using Vallejo Plan	110.9	113.3	116.5	116.7	118.4	102.2	81.2	81.8	81.7	75.7	68.8
Real effective exchange rate, deflating with general consumer prices											
Limited companies											
Not using Vallejo Plan	110.2	112.4	119.2	123.9	123.7	118.9	120.8	114.6	113.2	100.9	100.7
Using Vallejo Plan	109.8	110.7	116.9	121.8	122.4	112.1	103.8	105.2	103.1	88.9	86.4
Public companies											
Not using Vallejo Plan	110.1	112.3	119.1	123.7	123.5	118.7	118.0	108.2	106.8	94.3	93.7
Using Vallejo Plan	109.9	110.8	116.9	121.8	122.3	112.3	100.6	100.3	98.3	84.4	82.0

*Note:* For the definitions of the different exchange rates, see text. The nominal exchange rate in 1967 was 14.88 pesos per dollar.

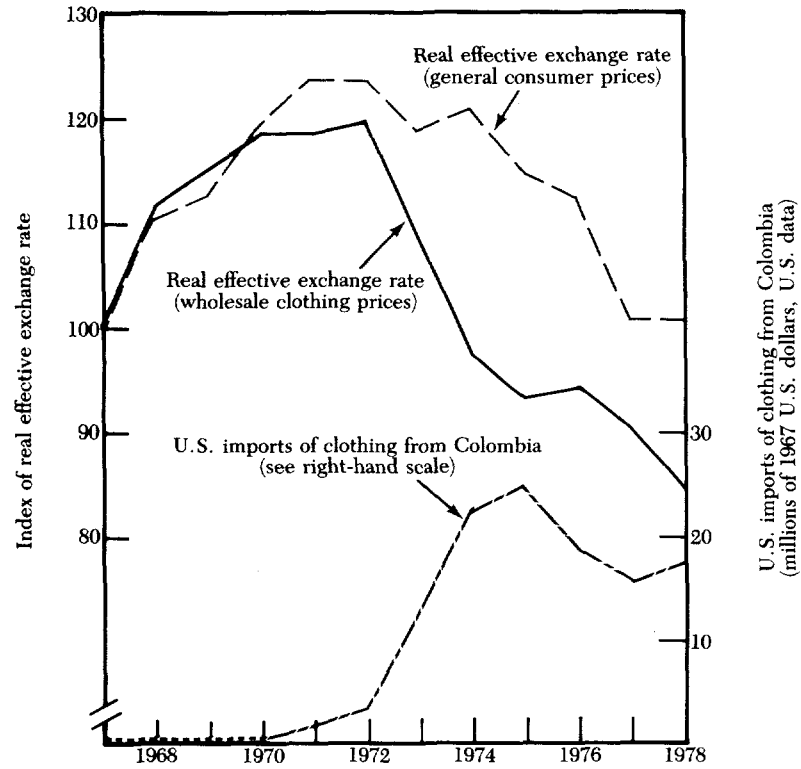
a. Projected.

b. A typographical error in the published data has been corrected.

c. Index for blue-collar workers.

*Sources:* Nominal exchange rate: averages of quarterly data presented in International Monetary Fund, *International Financial Statistics*, 1967-78. Wholesale clothing price indexes: Banco de la República, *Revista*, various issues; U.S. Department of Commerce, *Business Statistics*, 1977, p. 50; and *Survey of Current Business*, December 1978, p. S-9. Consumer price indexes: International Monetary Fund, *International Financial Statistics*, 1967-78. Export incentives: tables 15 and 16.

Figure 5. Real Effective Exchange Rates and U.S. Imports of Clothing from Colombia, 1967-78



Note: Both real effective exchange rates are for limited liability companies not using the Vallejo Plan. For public companies and for firms using the Vallejo Plan, the curves fall even more steeply after 1972.

Sources: Tables 6 and 17.



rapidly. Once allowance is made for lags, however, the data tell a rather different story.

Before 1967 Colombian governments tended to tackle balance of payments problems by carrying out a jump devaluation, waiting until inflation had eroded away its beneficial effects, and then jump devaluing again. As a consequence, between 1953 and 1967 there were never more than two consecutive years in which the real effective exchange rate moved in the same direction (table 18). The effects of such instability on potential exporters are not difficult to imagine. If an entrepreneur cannot be sure of the returns that he is likely to receive from exports

Table 18. Annual Changes in the Real Effective Exchange Rates for Clothing and Minor Exports, 1953-78 (percent)

Year	Clothing exports		Minor exports (3)
	Deflating with wholesale clothing prices (1)	Deflating with general consumer prices (2)	
1953	n.a.	n.a.	10.2
1954	n.a.	n.a.	-5.5
1955	n.a.	n.a.	8.9
1956	n.a.	n.a.	19.4
1957	n.a.	n.a.	-4.8
1958	n.a.	n.a.	-7.3
1959	n.a.	n.a.	13.5
1960	n.a.	n.a.	-11.7
1961	n.a.	n.a.	22.1
1962	n.a.	n.a.	14.7
1963	n.a.	n.a.	-13.2
1964	n.a.	n.a.	-11.5
1965	n.a.	n.a.	29.6
1966	n.a.	n.a.	-17.2
1967	n.a.	n.a.	3.4
1968	11.3	10.2	9.4
1969	3.3	2.0	3.6
1970	3.3	6.0	2.8
1971	-0.1	3.9	2.3
1972	0.8	-0.2	2.7
1973	-9.7	-3.9	n.a.
1974	-9.8	1.6	n.a.
1975	-4.2	-5.1	n.a.
1976	0.7	-1.2	n.a.
1977	-3.8	-10.9	n.a.
1978	-6.6	-0.2	n.a.

n.a. Not available.

Sources: Cols. (1) and (2): table 17. Col. (3): Díaz-Alejandro (1976, p. 56).

even a year or two in advance, he is hardly likely to make long-range export plans, to invest large sums in new plant and equipment, or to risk hiring difficult-to-fire workers.

As is clear from table 18, the situation changed dramatically in 1967. From this date on, for the first time in more than a quarter of a century, the relative profitability of exporting rose continuously, or at least did not fall, for six consecutive years. Not surprisingly, it seems to have taken some time before the export pessimism that was as common in Colombia as in most of Latin America could be overcome. It took time for entrepreneurs to believe that exporting goods other than coffee and petroleum might be feasible and profitable—Colombia's total exports of all manufactured goods were only \$44 million in 1967, less than exports of clothing alone a decade later—and that this profitability might be maintained for more than just a year or two. It took further time to adapt plant and equipment and retrain workers to fulfill the stringent requirements of export markets. And it took time for buyers to be found, orders placed, goods produced, and an export momentum built up.

Clearly, the sum of these lags will have been different for each firm. Nevertheless, of the twenty firms in the sample that were established before 1967, only one began exporting before the policy reforms took place, whereas thirteen (two-thirds) made their first small foreign sales during 1968–71 (table 19). At the aggregate level, although clothing exports began to increase from 1968 onward, it was not until 1970 that they first exceeded \$1 million.

The lags seem also to have been operating for changes in the reverse direction. When, after six consecutive years of improvement, the real

Table 19. Date of Establishment of Firms in the Sample and Date of Their First Exports, 1900–78

Year	Number of firms	
	Established	First exported
1900–44	5	1
1945–59	12	0
1960–64	2	0
1965–69	3	7 <sup>a</sup>
1970–74	3	15 <sup>b</sup>
1975–78	5	7
Total	30	30

a. Six of the seven began exporting in 1968 or 1969; one began in 1967.

b. Seven of the fifteen began exporting in 1970 or 1971.

Source: Interviews with firms.

effective exchange rate began to decline in 1973, it appears to have taken some time until entrepreneurs who were exporting or gearing up for export began to believe that the decreased profitability of selling abroad was likely to be a long-term, rather than a temporary, phenomenon. Many of them had begun to think of exports as the wave of the future—government pronouncements, as opposed to policies, continue to this day to encourage them to believe this—and were planning output, investment, and hiring policies accordingly. Several firms had set up export departments at considerable expense. Some businessmen had had a taste of the unit costs that could be cut and the profits that could be made by specializing and doing long production runs for the U.S. market. (The eyes of one former exporter of jeans to the United States lit up during our interview as he recalled how low his unit costs had been in the old days when exporting was profitable.) A few firms had painstakingly built up relations with U.S. and European buyers and were reluctant to lose them to competitors in other countries. It is not surprising, then, that as the relative and absolute profitability of exporting began to decline, the first reaction of many firms was to cut costs, attempt to increase efficiency, and continue to expand exports as before, rather than to abandon the new, exciting export optimism overnight. In what was probably a coincidence, two or three years again passed before the break in the trend of the real effective exchange rate (1973) caused a change in the trend of clothing exports (1975–76).<sup>10</sup>

The existence of this three-year lag can be tested for statistically. In the regressions in table 20, U.S. imports of clothing from Colombia in constant prices (XCON) or in square yard equivalents (XSYE) are estimated as a function of the real effective exchange rate of three years earlier (REER<sub>-3</sub>) and of total U.S. imports of clothing in constant prices (M). This last variable is included because the sharp increase in U.S. demand for clothing imports after the mid-1960s no doubt played a role in the expansion of Colombia's clothing exports to that country.<sup>11</sup> In equations (2.3) and (2.5) the real effective exchange rate is deflated by wholesale clothing prices; in equations (2.4) and (2.6) it is deflated by general consumer prices (table 20).

10. The constant price data show this decline beginning in 1976; the square-yard-equivalent data show it beginning in 1975. After being pushed out of the U.S. market some firms gave up exporting altogether; others switched to the easier markets of the Margarita Islands and the Caribbean where they were still able to compete.

11. U.S. imports of clothing rose in constant prices by 15 percent a year between 1970 and 1978 (table 20).

Table 20. Estimates of the Relation  
between Colombia's Exports of Clothing to the United States  
and the Real Effective Exchange Rate, 1970-78

Equation number	Dependent variable	Independent variables							Period
		Constant	REER <sub>-3</sub> (WPI)	REER <sub>-3</sub> (CPI)	M	R <sup>2</sup>	DW	F	
2.3	XCON	-62.75 (5.28)	8.03 (3.96)		3.65 (6.65)	0.88	1.53	22.81	1970-78
2.4	XCON	-69.13 (7.62)		13.03 (5.90)	1.25 <sup>a</sup> (2.88)	0.94	2.08	45.49	1970-78
2.5	XSYE	-102.05 (4.31)	15.22 (4.33)		5.25 (4.82)	0.83	2.30	11.87 <sup>a</sup>	1971-78
2.6	XSYE	-93.57 (4.74)		20.26 (4.77)	0.80 <sup>b</sup> (1.33)	0.85	1.81	14.33	1971-78

*Definitions:*

XCON = Value of U.S. imports of clothing from Colombia in constant 1967 prices.  
 XSYE = Volume of U.S. imports of clothing from Colombia in square yard equivalents.  
 REER<sub>-3</sub>(WPI) = Real effective exchange rate deflated by wholesale clothing prices and lagged three years.  
 REER<sub>-3</sub>(CPI) = Real effective exchange rate deflated by general consumer prices and lagged three years.  
 M = Value of U.S. imports of clothing from all countries in constant 1967 prices.

*Notes:* All variables are in logarithmic form. Figures in parentheses are *t* statistics.

a. The coefficient is significant at the 5 but not at the 1 percent level.

b. The coefficient is not significant at the 5 percent level.

The regression results are consistent with the hypothesis that the rise and fall of the real effective exchange rate has played an important role in the rise and decline of Colombia's exports of clothing to the United States.<sup>12</sup> Taken at face value, the coefficient estimates suggest that an increase of 1 percent in the real effective exchange rate led to an increase, three years later, of between 8 and 20 percent in the volume of these exports. Nevertheless, I would place no reliance at all on the precise magnitudes estimated here. To begin with, the data are problematical, and only nine years of figures are available. In addition, it may

12. Others who have found that the real effective exchange rate has an important effect on minor exports in Colombia—those other than coffee and petroleum—include Sheahan and Clark (1967), Urdinola and Mallon (1967), Musalem (1970), Nelson, Schultz, and Slighton (1971), Eaton (1972), Teigeiro and Elson (1973), Díaz-Alejandro (1976), and Cardona (1977).

well be largely coincidence that the two lags—the one between the 1967 policy changes and the surge in exports, and the one between the downturn in the real effective exchange rate and the decline in exports—were each about three years in length.<sup>13</sup> Finally, the decline in the real effective exchange rate was by no means the only cause of the fall in Colombia's clothing exports after 1974–75. As a result of the boom in the domestic demand for apparel, which was caused by high coffee prices and increased exports of drugs<sup>14</sup> and exacerbated by high protection against imports of garments, selling domestically became increasingly more profitable than exporting to the United States. Indeed, some firms that would still have been able to export to the United States at a profit switched to selling almost all their output in the home market.<sup>15</sup> The high and rising cost of fabric, made possible by stiff protection against textile imports, accentuated the squeeze on the returns to exporting—and several nonprice factors were also important causes of the decline. (These nonprice factors, effective protection, and several other omitted factors, will be analyzed in detail in Part Two.) The omission of these important variables no doubt causes the coefficient of the real effective exchange rate estimated in table 20 to be biased, probably upward.<sup>16</sup>

Why is it that the rate of devaluation of the peso was not rapid enough after the early 1970s to maintain constancy of the real effective exchange rate? At least since 1976, Colombia has been confronted with a dilemma similar to that faced by many other nations that depend heavily on natural-resource-based exports as sources of foreign exchange. When the price of the major export product rises sharply, should the national

13. To quote Robert Solow in this regard: "Show me the man who will go to the stake for the lag distribution he has estimated and I will show you a fool." (Personal communication to the author.)

14. According to conservative estimates, Colombia's exports of marijuana and cocaine earned about \$650 million in 1978 (Junguito and Caballero, 1978). Less cautious observers suggest that the two drugs may have surpassed coffee (exports of which earned \$2 billion in 1978) as the country's foremost source of foreign exchange.

15. One such firm, which specializes in fashion clothing for middle-aged women, is owned by one of the few Colombians who is said to be up-to-the-minute with the latest in world clothing trends. During the mid-1970s, this firm was exporting 80 percent of its output to the United States, and it counted Bloomingdale's and several other high-class establishments among its clients. By 1977 the lure of the domestic market had become too great; the owner completely revised his plans in that year, and the company now sells 90 percent of its output at home.

16. The fact that the constant term is strongly and significantly negative in all four equations is consistent with this hypothesis.

currency be allowed to rise in value to maintain balance of payments equilibrium and neutralize the inflationary pressures that would otherwise be generated, in which case exporters of manufactures are likely to be priced out of their markets? Or should the rate of devaluation continue to compensate for the inflation differential, in which case a balance of payments surplus is likely to accumulate and inflationary pressures are likely to rise? When stated in this form, the dilemma seems serious indeed—yet these two possibilities do not exhaust the field. Although the Colombians chose the former option, a third possible response to the 1976 increase in coffee prices was also available: continue to devalue at the inflation-differential rate, at the same time pushing ahead with the progressive liberalization of imports. Such a policy would have yielded benefits on several fronts: balance of payments surpluses would have been avoided; the differential between the incentive to produce for the home market and the incentive to export would have been narrowed;<sup>17</sup> firms would have been forced to become more efficient generally; the absolute level of competitiveness of manufactured exports in foreign markets would have been maintained; and inflationary pressures in the economy because of the rise in the price of coffee would have been moderated. Thus, although there were strong macroeconomic reasons why Colombian governments began to devalue the peso more slowly, this course was certainly not the only one available.

Finally, what explanation can be given for the leveling off or slight recovery of Colombia's clothing exports to the United States during 1978–79? First, it ought to be noted that such recovery as did occur was extremely modest; in real terms, the after-the-fall annual rate of 1976 had not yet been regained by the first half of 1979 (figure 4). Second, the leveling off or recovery seems to have rested on the shoulders of a very small group of companies. In particular, three of the firms in the sample accounted for fully half Colombia's total exports of apparel to the United States in 1977–78; these were also among the relatively few companies we visited that planned to expand their sales to the United States in 1979–80. Apart from being among the four or five best-managed firms that we saw, each of these three is in a way rather special. One is the only firm in the sample that is foreign-owned (by its U.S. buyer). A second has close ties with a French designer and, together with this designer, owns equity in its U.S. buyer and distributor. The third is the only firm

17. U.S. pressure on countervailing duties makes it difficult to achieve this goal by raising export subsidies.

that we visited in which the U.S. buyer maintains (and covers the cost of) a full-time production engineer at the plant. Thus, while the outstanding quality of management has no doubt been important in explaining the continued *ability* of these three firms to export to the United States, the unusually close relations between the firms and their buyers is important in understanding their continued *willingness* to export to the United States at a time when other markets, domestic and neighboring, appear to be considerably more profitable. Third, most of the firms still exporting to the United States seem to realize that, if they want to succeed in exporting to difficult markets in the long term:

[They] have to sell when prices are unfavorable as well as when they are favorable. It is impossible to try to participate in one of these markets [the United States or Europe] only when the conditions are advantageous . . . Any interruption means no less than that all the efforts that have been expended will be lost (Escobar, 1977, p. 22).

Fourth, most of the firms still selling to the United States export a relatively small fraction of their total output. Thus, among the thirteen firms in the sample for which the United States is the main export market (these thirteen accounted for 75 percent of Colombia's total exports of garments to the United States in 1977-78), nine exported 20 percent or less of their total production in 1977-78, and only two exported more than 50 percent. This means that most are able to continue to supply their U.S. buyers, at least for the time being, without making too much of a dent in their total profits.

In summary, the rise in Colombia's clothing exports from 1970 to 1974-75 seems to be largely attributable to the unprecedented six-year rise in the real effective exchange rate (that is, in the relative and absolute profitability of exporting) that began when a series of policy reforms was introduced in 1967. The fall in Colombia's clothing exports to the United States, which began in 1975 or 1976, seems to have been due partly to the subsequent decline in the real effective exchange rate, and partly to other price and nonprice factors that have yet to be discussed in detail. The leveling off or slight recovery in garment exports to the United States during 1978-79 appears to be attributable mainly to the fact that a small number of firms, several of them having quite special links with their U.S. buyers, were clinging to their foothold in the U.S. market for as long as possible in the hope that the profitability of selling in the United States would increase in the future.

## Chapter 3

# Some Nonprice Factors

ALTHOUGH THE EXCHANGE RATE and export incentive policies pursued by successive Colombian governments seem to have been an important cause of the rise and decline of Colombia's exports of clothing to the United States and Europe, nonprice factors played some part as well. This chapter examines the role of U.S. buyers, foreign brand-name agreements, and small firms in getting exports off the ground after 1970. The analysis of the role played by nonprice factors in halting and reversing this rise is presented in chapter 6.

### U.S. Buyers

In the richer, industrialized countries, especially with respect to imports, the role of the buyer in the clothing industry is great. When Colombian firms export clothing to the United States and Europe, it is almost always the foreign buyer who sets the detailed specifications for the product, who physically imports the good, and who arranges for its wholesale or retail distribution. In some cases, the buyer also helps the Colombian manager in purchasing fabric and other inputs—this is true, of course, for all exports made under the 807 offshore assembly scheme—and in the day-to-day running of the factory.

A few years before Colombia began to reorient its trade policies toward export promotion, several other developing nations, especially in East Asia, took similar steps with a great deal of success. As a result, by the late 1960s and early 1970s, U.S. and European clothing manufacturers, wholesalers, and retailers realized that they would have to increase their imports of clothing from developing countries if they were to stay in business and began to rove the world in search of new sources. Most of the scouting was then concentrated in Hong Kong, Korea, and Taiwan, but some seekers found their way to Colombia as well. The arrival of these buyers helped greatly to break the stiff marketing barriers that face any potential new entrant into garment exporting.

### Foreign Brand Names

At about the same time as foreign buyers were beginning to appear in Colombia, a second, related phenomenon was taking place: Colombian



firms increasingly began to purchase licenses to use foreign brand names and trademarks. By 1978 Levi's, Blue Bell (Wrangler), Lee, and Landlubber all had licensees in Colombia, as did Manhattan, Arrow, Van Heusen, Bobby Brooks, BVD, Jockey, Pierre Cardin, and Yves St. Laurent.<sup>1</sup>

One of the attractions to Colombian firms of buying the license to use a foreign trademark is, of course, that products branded with an internationally known name can be sold at a higher price than similar garments bearing a label that is less well known. The manager of one Colombian firm was good enough to let me have some hard information on this subject. This firm produces two versions of one style of pants that are identical in every respect, except that one bears the firm's domestic label whereas the other carries an internationally famous name. The firm sells both these versions rather than concentrating only on the higher-priced one because, the manager explained, in this way it is possible to tap both the upper- and the middle-income markets. Both versions are sold in the Margarita Islands; because this market is marginal in world terms, the licensor has been willing to turn a blind eye to the use of its label for exporting in this case. (To protect the parent company and parallel licensees in other countries from identically branded competition, licensing agreements usually restrict the use of foreign brand names to the domestic market.) The prestige-branded version of these pants sold for \$22.38 in the Islands in late 1978, or 21 percent more than the domestic-labeled version. The profit rate (after payment of royalties) for the prestige-labeled version was 39 percent of total costs, which is 40 percent greater than for the Colombian version (table 21, cols. 2 and 3).<sup>2</sup>

Except in the few cases in which Colombian firms have been permitted to export garments using a foreign brand name, the above-illustrated benefit from licensing agreements clearly accrues only to the private producer. If there were no other benefits to be obtained from such agreements, the considerable royalty payments involved—from 2 to 15 percent of sales, depending on the name—would make them a poor investment for the country. But two benefits from the purchase of foreign trademarks are of social as well as private value; these, too, may have played some part in helping Colombia's clothing exports get off the ground in the early and mid-1970s.<sup>3</sup>

1. Some of these licenses had been acquired many years earlier.

2. The profit differential for sales of items bearing foreign brand names would be rather less than this for firms whose licensors are less prestigious.

3. Both of these benefits are almost totally ignored in the symposium on "Trademarks in Developing Countries" that occupies the entire July 1979 issue of *World Development*.

(Note continues on the following page.)

Clothing producers who wish to export garments to world markets have little chance of breaking into the market if they are not reasonably up-to-date with world fashion trends. One way of keeping up-to-date might be to travel abroad extensively and often; but most Colombian clothing enterprises are family firms—three-quarters of the sample enterprises fall into that category—in which the owner is needed to run the business at home. Alternatively, the producer might try to study fashion trends in imports—but imports of finished garments were prohibited in Colombia until 1973, and because of stiff tariffs and prior licensing, never exceeded \$2 million a year (1 percent of total consumption) through 1977 (table 13).

A third option, the only real one open to a large number of small and medium-size Colombian firms, is to sign a licensing agreement. As part of most licensing agreements in the apparel business, the licensor agrees to supply the licensee with fashion information relevant to its line of business. The precise form in which the information is supplied varies widely from in-house fashion magazines to ready-to-use patterns and molds; but the value of this information in raising the fashion awareness of local firms, and hence their ability to export when exporting is profitable, is indisputable.<sup>4</sup>

In addition to supplying fashion information, licensing agreements have further helped Colombian clothing firms to begin exporting by providing technical assistance. Again, the precise form this assistance takes has varied widely. Some foreign firms have carried out time and motion studies in their licensees' plants and have recommended ways to reorganize the flow of production. Others have made suggestions concerning techniques of cutting fabric, machine maintenance schedules, methods of sewing, and the use of better materials (such as collar stays and linings) or better methods of joining materials (fusion instead of sewing). Several of the firms interviewed indicated that this production help was by far the most significant benefit of the foreign licensing arrangement. In one case, the time needed to sew a jacket fell from 146

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They are also implicitly ignored in Decision 24 of the Andean Group integration scheme and in most of the Andean Group literature.

4. The increase in fashion consciousness and quality consciousness among Colombian clothing firms has had incidental spillover effects for at least a certain segment of Colombian consumers. The elegant Parisian aspect of much of the locally made clothing that was displayed in shop windows in the upper-income areas of Bogotá during 1978 contrasted sharply with the relatively uninspired merchandise that could be seen in the same districts in 1970. Only part of this change is due to licensing agreements; part is no doubt due simply to learning-by-doing in exporting.

Table 21. Comparison of Costs and Profits on Pants  
 Made in Colombia for Export to Venezuela  
 Using Domestic and Imported Fabrics  
 and Domestic and Foreign Brand Names, 1978  
 (pesos)

Item	Costs in common for all three pants (1)	Costs and profits on otherwise identical pants		
		Domestic fabric		Imported fabric
		Domestic brand name (2)	Domestic brand name (3)	Foreign brand name (4)
Fabric <sup>a</sup>		208	128	128
Labor	275			
Pocket lining	25			
Waistband	18			
Packaging	11			
Zipper	5			
Polyester label	4			
Waist band lining	2			
Button	1			
Thread	1			
Price tag	1			
Total	343	343	343	343
Commission (10 percent of sales price)		59	74	90
Royalties (5 percent of sales price) <sup>b</sup>		...	...	45
Total variable costs		610	545	606
Sales price		590	739 <sup>c</sup>	895 <sup>d</sup>
Profit		-20	194	289
Profit as percentage of total cost <sup>e</sup>		-3	28	39

... Not applicable.

Note: The exchange rate in late 1978 was Col\$40 = US\$1.

a. Fabric is gabardine, 100 percent polyester.

b. Estimated royalties paid for the use of the foreign brand name.

c. The sales price is greater than Col\$590 because the imported fabric, even though less expensive, is of better quality than the domestic fabric. If the imported and domestic fabrics had been of identical quality, and the sales price had therefore remained at Col\$590, profit would be Col\$45 or 8 percent of total costs.

d. The sales price is greater than Col\$739 because of the use of the foreign brand name.

e. It is assumed that fixed costs are 20 percent of total costs (25 percent of total variable costs) in col. (3).

Source: Interview with a pants manufacturer.

minutes to 90 minutes as a result of assistance from a full-time production engineer provided as part of the agreement. This 38 percent reduction in labor costs was instrumental in enabling the firm to reduce its prices sufficiently to begin exporting to the United States; its cumulative exports to that market totaled more than \$5 million by 1978, and it was planning a 50 percent increase in production capacity and exports for 1979–80. In a second instance, the Colombian licensee of an internationally famous brand of jeans explained that his labor costs had been halved since he received technical help from the U.S. parent company; he now produces twice as many pairs of jeans with the same number of workers. The U.S. parent company's jeans used to be smuggled into Colombia but now this has ceased; instead, jeans, made in Colombia with the U.S. company's label are smuggled out of Colombia and into neighboring markets.

Some observers have suggested that developing countries ought to permit local firms to buy fashion information and technical assistance but not the use of foreign brand names; or all local firms should have an equal right to pirate foreign trademarks without paying royalties;<sup>5</sup> or all licensing agreements and foreign brand names should be banned altogether. The problem with banning licensing agreements altogether is that the baby (fashion information and technical assistance) is thrown out with the bathwater. The problem with not allowing foreign trademarks to be used in the country at all, or with allowing anyone and everyone to pirate them, is that it would amount to an open invitation to illegal imports of "the real thing." In Colombia, there already exists some smuggling of internationally branded garments, which the local licensor either does not produce or produces poorly: Pierre Cardin underwear is a best-selling item on the black market in Bogotá. Although such smuggling is currently relatively limited, its potential for growth if circumstances were to change can hardly be doubted.<sup>6</sup>

5. I was partial to this view myself before undertaking this study.

6. The Marlboro affair is a case in point. Several years ago, the Colombian government issued a permit to the Philip Morris Company to start producing Marlboro cigarettes in Colombia using locally grown tobacco. The firm began by mounting a massive advertising campaign and soon captured a substantial share of the market. But more than half (some say 90 percent) of the Marlboro cigarettes that have been sold in Colombia in recent years were not made in Colombia; rather, they were made in the United States and smuggled into the country. The reason, apparently, is that Colombian smokers of Marlboro prefer Virginia tobacco to the darker locally grown variety. In late 1978, one rarely had to walk more than a few blocks in the downtown area of any of the main cities in Colombia before coming upon someone crying, "Marlboro, Marlboro!" This person invariably carried only

## Small Firms

In 1970–71, I interviewed the managers of several clothing firms in Colombia for another project. It appeared then that much of the apparel produced by these companies was competitive in world terms in both price and quality,<sup>7</sup> yet the firms were not able to export because they were too small either to seek out the markets<sup>8</sup> or, if buyers visited them—as happened in several cases—to accept the large orders buyers wanted to place. How, if at all, were these problems overcome after 1970–71? What role did small firms play in the rise of Colombia's clothing exports?

To the best of my knowledge, no published or unpublished data are available on clothing exports by size of firm in Colombia. Nevertheless, an indirect but fairly clear idea of the relative importance of small firms in these exports can be gained by examining the sample of clothing firms interviewed for the present project. These thirty firms alone accounted for between half and three-quarters of total Colombian clothing exports during 1975–78 (the data for 1974 must be discounted because of the presence of fictitious exports) and for fully 69 to 90 percent of exports carried out using the Vallejo Plan. Further, the top ten exporters in the sample alone accounted for from 38 to 65 percent of total exports and for from 58 to 74 percent of Vallejo Plan exports during the same period (table 22). If a small enterprise is defined liberally as one with fewer than

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the smuggled cigarettes, in their original packets, with "Made in U.S.A." printed clearly on the label.

7. See Morawetz (1971). Others who believed that Colombian clothing firms were internationally competitive in price and quality at that time included Colombian economists who then worked for the National Planning Department (DNP, 1971), participants in a World Bank mission (Avramovic, 1972), and fellow members of the Harvard Advisory Group attached to DNP.

8. In a study of perceived barriers to exports, Martinez (1973) found that in the clothing industry the proportion of small firms reporting marketing problems (58 percent) was significantly higher than that of large firms (38 percent). Small clothing firms also reported shortages of working capital and difficulties with domestic raw materials significantly more frequently than large ones. Small firms interested in exporting often suffer from additional handicaps, including inadequate management skills, inadequate cost accounting data on which to base price quotations, unevenness of product quality, and difficulty in obtaining credit; on these and related issues, see de la Torre (1972), UNIDO (1972), Van Ruth (1976), and Alexandrides and Moschis (1977).

Table 22. Registered Exports of Clothing, Vallejo Plan and Total, the Sample and All Firms, 1974-78 (millions of dollars)

Type of exports	Sample of 30 firms	All firms	Sample of 30 firms as percentage of total	Largest 25 firms in sample as percentage of total <sup>a</sup>	Top 10 exporters in sample as percentage of total
Exports using Vallejo Plan					
1974	6.5	16.9	39	39	35
1975	10.0	11.1 <sup>b</sup>	90	90	74
1976	13.8	17.2	80	80	66
1977	12.8	15.8	81	81	59
1978 <sup>c</sup>	6.8	10.0	69	69	58
Total exports					
1974	16.3	75.5	22	21	19
1975	21.4	29.3	73	72	65
1976	20.2	34.0	59	58	48
1977	23.4	46.7	50	46	38
1978 <sup>c</sup>	12.8	25.8	50	47	42

a. All firms with 100 employees or more.

b. Estimated.

c. January-June.

Source: INCOMEX, unpublished tabulations of registered exports, Expos 5, 10, and 11, 1974-78.

100 employees, five small firms were included in the sample (table 23). None of these five used the Vallejo Plan in the years covered here (because of its complexity, the plan is used mainly by large companies), and their combined clothing exports never exceeded \$1.8 million, or 4 percent of the nation's total, during 1974-78. Clearly, then, even if all clothing exporters not included in the sample were small, which is not the case, small exporters have played a limited role in Colombia's clothing export history.

Small firms that wish to export have four possible solutions to the problems, especially in marketing, that their lack of size creates: they can join together with other small firms in a consortium; they can export through an intermediary or trading company; they can manufacture goods as subcontractors for a larger exporter; or they can grow and themselves become large enterprises. Small firms in Colombia have tried all four methods.

Table 23. Size of Firms in the Sample: Value of Exports, Value of Total Sales, and Number of Employees, 1977-78

<i>Size of firm</i>	<i>Number of firms in the sample</i>
Value of registered exports, 1977 (millions of dollars)	
More than 1	5
0.5-0.9	10
0.1-0.4	10
Less than 0.1	5
Total	30
Value of total sales, 1978 <sup>a</sup> (millions of dollars)	
More than 10	4
5-9.9	4
1-4.9	13
Less than 1	9
Total	30
Number of employees, 1978	
More than 1,000	8
500-999	3
100-499	14
Fewer than 100	5
Total	30

a. Estimate of the sum of domestic and export sales.

Sources: Value of registered exports: INCOMEX, unpublished tabulations of registered exports, Expo 11, 1977. Value of total sales and number of employees: interviews with firms.

### *Consortia*

Between 1970 and 1973 meetings were held to establish export-oriented consortia of small and medium-size clothing firms in Bucaramanga (Consexport), Pereira (Conevica), Medellín (Confexcol), Cali (Exporcali), and Barranquilla.<sup>9</sup> By 1978 the last of these consortia had failed. The Bucaramanga and Pereira groups enjoyed some success for five to seven years but then collapsed;<sup>10</sup> the central body set up in

9. This section draws on interviews with the managers of two firms that participated in one of the last consortia to fail and on reports on consortia by International Trade Center (1973), Carrillo and Gonzalez (1976), Hjelm (1976, 1977), and Perry (1978).

10. Consexport was created in 1970 with 18 members, 1,600 sewing machines, and 2,800 workers. In its first year it received an order of \$250,000 to export bikinis to the United States; in 1972 it exported \$1 million worth of jeans to Denmark; and in 1973 it sent \$600,000 worth of shirts to Italy. Conevica was created in 1972 with 26 members, specialized in men's clothing (especially shirts), and exported a total of about \$2.5 million during 1974-77, almost all to the United States.

Medellín never had much more than advisory functions; and the Cali and Barranquilla consortia never got off the ground. How can these failures be explained?

Any attempt to set up a consortium of small firms for export necessarily has to overcome several problems. Enterprises, especially family enterprises that have competed with each other for years and perhaps generations, are likely to be reluctant to share hitherto secret financial and technical information. (After all, if the consortium should break up, they will once again be rivals.) Once export orders are received, which firms should have priority if, as is likely at least in the beginning, there are not enough orders to go round? Since no two clothing firms ever produce exactly the same quality garments, and since strict product standardization will have to be established, some firms (but which?) will have to change the way they have traditionally organized their production and sewn their garments. Most difficult of all, once export orders have been received, there is always an incentive for the buyer to approach the firm or firms producing his particular order with the proposal that they work directly for him, thus saving the 5 percent or so commission (more profits for everyone) and saving the time and paperwork needed to deal through the consortium as well.

The consortium attempts to overcome these very real problems by holding out to its members the prospect of finding them new markets. Almost all the prospective benefits from grouping together small firms—lowering of unit production costs, rationalization of production, utilization of excess capacity—stem from the potential for increased sales. But finding new foreign markets requires a considerable initial investment and a particular kind of expertise, both of which tend to be in short supply in small firms even if they are grouped together. This leads to a vicious circle. A consortium is usually financed by a surcharge on exports; hence, before exports get started, little finance is available. But if little finance is available, the consortium is unlikely to be able to hire the kind of person or persons who would be good at finding new markets. But if new markets are not found, little finance is available—and so forth.<sup>11</sup>

These fundamental realities seem to have been at the heart of the collapse of those Colombian consortia that did get off the ground. The central organizing bodies were apparently not able to do well enough at finding new markets to persuade their members to resist the built-in centrifugal forces that any consortium contains.

11. PROEXPO provided some initial financing for several consortia but it was understandably unwilling to act as chief financier on a long-term basis.



### *Intermediaries*

If small clothing enterprises have not had a great deal of success in exporting through consortia, they have not had much better luck with intermediaries. (An intermediary is defined here as a firm whose primary business is to arrange for the export of articles produced by other firms or people.)

Thirteen firms listed as intermediaries were registered as exporting more than \$100,000 worth of apparel during 1977,<sup>12</sup> but six of these had disappeared by late 1978.<sup>13</sup> This illustrates the extent to which intermediaries tend to come and go on the Colombian scene: apparently it is not a very stable business to be in. In the event, we were able to interview five of the thirteen.<sup>14</sup>

A solidly based intermediary might be expected to have a well-organized market-search system, well-staffed branch offices overseas, and well-established relations with clients and suppliers. None of the firms we interviewed fits this image. The most successful operation, according to volume of exports, employs two people in its market-searching department and is owned and managed by a lawyer who plans to retire in three or four years to devote himself to writing law books. One agency is run single-handedly by a man who sells anything from blouses to fertilizer and who uses the business partly as a means of visiting his former wife and children in the United States. Another is run from a single dark room in a seedy section of town by a Colombian who has been expelled from Mexico and from the United States (apparently for shady dealings) and who likes to travel. A fourth firm was just being set up by two men with impressive plans but little to show for them thus far. The fifth is a putting-out operation that is run with very little help by a remarkable mother of seven children.<sup>15</sup>

12. Firms that are listed as intermediaries but which simply market a single firm's (or family group's) output are excluded. Also excluded is the intermediary who acts in the clothing business as the exclusive purchasing agent for a single European chain of stores.

13. These six firms are presumed not to have been fictitious since, as noted in chapter 1, most fictitious exporting of clothing seems to have been confined to 1974.

14. One could not be interviewed in the time available, and the thirteenth failed to appear at the appointed time.

15. This woman, working with a total office staff of fifteen persons, gathers and copies designs from abroad (European designs for the United States, U.S. designs for Venezuela and the domestic market), organizes the purchase of fabric and embroidery materials and their distribution to 650 housewives who work at home, has the embroidered material made up into charming clothes for children in a small factory, and then sells these clothes

In addition to sharing the characteristic of being rather special cases, the five intermediaries interviewed had other features in common. All buy their merchandise primarily from small producers who would not be able to export independently and all export primarily to the Margarita Islands and the Caribbean. The first four complained that their suppliers' goods had sometimes been of poor quality and that they had not always been delivered on time; at one stage or another, all four had made an attempt to set up their own production facilities to overcome this problem. Finally, all but the putting-out woman relied heavily on personal travel, usually by the principal or principals, to seek markets; the only foreign publication which any of them saw regularly was *The Economist*.<sup>16</sup>

### *Subcontracting*

At least eight of the medium and large firms interviewed have subcontracted work out to smaller firms at one time or another, and two of the smaller firms have themselves worked as subcontractors for others.<sup>17</sup> Subcontracting was usually done for 807-type assembly work, with the parent firm cutting the fabric and supplying all inputs. Subcontracting tended to be most common when the parent intended to introduce new product lines but had not yet had a chance to set up its own production facilities. It also occurred, however, when demand was irregular and the parent wished to reduce its risks by avoiding the need to hire workers who would later be difficult to fire. (The difficulty and

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domestically and abroad, mostly in small lots. Her operation is so cramped that she does not have a separate office for herself; our interview was conducted in her small retail sales outlet. The buzzer that used to open the door to this shop does not work, so the secretary who sits in the far corner of the room opens the door to visitors by pulling a string which runs up the wall, along the ceiling, and down to the door latch. That ingenious and quite serviceable arrangement illustrates accurately the brilliance of the management of the entire operation.

16. Bernhart (1973) interviewed seven intermediaries who were attempting to export a wide variety of goods in 1972 and found their sources of information on foreign market opportunities to be similarly limited. They had between them two subscriptions to *Nuevo Mercado*, one subscription to *Business World*, one subscription to the PROEXPO weekly bulletin, and one copy of the *International Yellow Pages*.

17. Unfortunately, because of lack of time during the interviews, not all firms could be asked about their experience with subcontracting; this section is therefore based on partial data only. In East Asia, subcontracting of work from large firms to small ones seems to be one of the more important ways in which small firms are able to participate in exports. See, for example, Watanabe (1971, 1972), Geiger and Geiger (1973), and Wortzel and Wortzel (1979a).

expense involved in firing workers seems to be extremely important in restricting the extent to which firms are willing to specialize in the risky and relatively unstable business of exporting.) Generally, no more than 25 percent or so of the parent's value of output was subcontracted out at any one time. None of the firms that stated they were participating in subcontracting arrangements offered any criticism about how they had worked out.

### *Growth*

If consortia, intermediaries, and subcontracting arrangements have played only modest roles in Colombia's experience with clothing exports, the growth of small firms into large ones seems to have been more important.<sup>18</sup> Though the available data are sketchy, it seems that not one of the twenty-five large firms in the sample started out with as many as a hundred employees, and most of them appear to have commenced operations with forty or fewer. In most cases, growth seems to have taken place gradually over at least fifteen or twenty years and to have been financed both from reinvested profits and by borrowing. There were, nevertheless, a few cases of extremely rapid growth. For instance, one firm that had seemed to be too small to accept large export orders in 1970 increased the number of its employees sevenfold—from 150 in 1970 to more than 1,000 in 1978—and its clothing exports averaged more than \$1 million a year during 1974–78.

### Spectacular Failures

Interestingly, only one firm interviewed reported having received an order that was too large for it to handle; that case ended in disaster. The episode began when this relatively large company landed a plum contract to supply 120,000 suits a year to the U.S. licensee of a top European fashion house. For reasons that are disputed, the firm shipped only about 60,000 suits to the buyer in the first year. What is more, many of the suits that did arrive were judged to be of such poor quality that they had to be sold in discount houses, which allegedly damaged the buyer's reputation. Problems continued during the next two and a half years, at which time the buyer unilaterally abrogated the five-year contract.

18. For theoretical arguments and evidence from Denmark, Holland, and Israel that large firms are likely to export a larger share of their output than are small firms, see Hirsch and Adar (1974).

Apparently, largely as a result of this one failure, the buyer lost its preeminent position in the U.S. market to a European rival and has not regained it since.

Because of the glamour attached to the buyer's name, the story of this failure was written up in *Business Week*, and the news spread rapidly among the clothing traders of New York. (Three years later it was still referred to by several of the New York buyers whom I interviewed.) As a consequence, at least one other Colombian suit maker and its U.S. importer-manufacturer had to fight a two- to three-year battle to persuade U.S. retailers to accept their top-quality suits. According to the importer-manufacturer, the first reaction of the retailers was usually: "You're offering Colombian-made suits? No thanks—they're probably the same ——— that the Colombians made for ———." With commitment and dedication the battle was eventually won, but the moral of the story remains: a spectacular failure by one firm can have important spillover effects for other firms from the same country that wish to export.<sup>19</sup>

19. This was by no means the only instance in which such an externality occurred; several buyers with whom I spoke related bad experiences with one or two Colombian firms and vowed that they would not go back to Colombia.

*Part Two*

*Comparison of  
Colombian and East Asian  
Clothing Exports*



## Chapter 4

# Exports and Prices

WHY IS IT THAT when a person walks into a store in the United States and buys an imported garment, the chances are eight out of ten that it was made in Hong Kong, Korea, or Taiwan but only one in a hundred that it was made in Colombia—this despite the fact that Hong Kong, Seoul, and Taipei are three times farther from New York than is Bogotá? The solution to this riddle is the subject of Part Two.

To obtain some perspective on the relative export performance of the three East Asian economies, on the one hand, and Colombia and Latin America, on the other, consider the following facts, which are drawn mainly from tables 24 and 25 and refer to 1976, except as otherwise indicated. (See also figure 6.)

- Hong Kong, Korea, and Taiwan have a combined population less than one-quarter that of Latin America, yet the value of the manufactured goods exported by *each* of them is almost as great as the total value of manufactured goods exported by *all* of Latin America (including Brazil).<sup>1</sup>
- The three East Asian economies' combined exports of *clothing alone* are almost equal in value to Latin America's total exports of *all manufactured goods*.
- The clothing exports of Hong Kong, Korea, and Taiwan are more than twelve times greater in value than Latin America's clothing exports.
- All of the Latin American countries together have not yet exported as much clothing in any one year as Hong Kong alone exported in 1967. But in the case of the other two East Asian economies, the disproportion did not always exist. No more than fifteen years ago, *Korea and Taiwan together* exported less clothing than *Colombia alone* does today. In 1961 Korea's exports of *all* commodities amounted to \$41 million, of which \$6 million were manufactured goods and a considerable proportion was duck feathers and seaweed; by 1978, its total commodity exports had surpassed \$10 billion.<sup>2</sup>

1. Table 24 includes only six Latin American nations, but these account for more than 75 percent of Latin America's manufactured exports. By 1978, it seemed that the word "almost" could be omitted from this and the following sentence in the text.

2. The 1961 data for Korea are from Cole and Lyman (1971).

Table 24. Population, GNP per Capita, and Exports of Clothing and All Manufactured Goods: Selected East Asian and Latin American Economies, 1976

Area	Population (millions) (1)	GNP per capita (dollars) (2)	Millions of dollars	
			Exports of all manufactured goods (3)	Exports of clothing (4)
East Asia				
Hong Kong	4	2,230	6,480	2,907
Korea	36	700	6,675	1,846
Taiwan	16	1,050	6,921	1,322
Total	56	909 <sup>a</sup>	20,076	6,075
Latin America				
Argentina	26	1,580	972	38
Brazil	110	1,300	2,332	99
Chile	10	1,050	109 <sup>e</sup>	—
Colombia	24	650	659 <sup>d</sup>	40
Mexico	62	1,060	2,327 <sup>b</sup>	174 <sup>bc</sup>
Venezuela	12	2,540	115 <sup>c</sup>	—
Total	244	1,256 <sup>a</sup>	6,161	351

— Negligible.

a. Weighted average.

b. Estimated, including border zone, with help of U.S. as well as Mexican data.

c. 1975.

d. Plesch (1979, table B.10) gives this figure as 384.

e. 1974.

Sources: Cols. (1) and (2): World Bank, *Atlas*, 1978. Col. (3): Chenery and Keesing (1978, table 8). Col. (4): United Nations, *Yearbook of International Trade Statistics*, 1977; and Keesing (1978, table 10).

- Latin America is not the only area that has had difficulty competing with the three East Asian economies; even if Greece, Portugal, Spain, Yugoslavia, and other South European nations were classified as developing countries, in 1977 the East Asian three accounted for half of all manufactured exports and 75 percent of all clothing exports from the developing world.<sup>3</sup>

When I asked Colombian clothing manufacturers how they explain the fact that Hong Kong, Korea, and Taiwan have been so much more successful than them at exporting garments, their first response was

3. These percentages have remained relatively constant at least during 1972–77 (Plesch, 1979).



Table 25. Exports of Clothing Not of Fur: Selected East Asian and Latin American Economies, 1964-77  
(millions of dollars)

Area	1964	1967	1970	1973	1976	1977
East Asia						
Hong Kong	287	407	698	1,418	2,871	2,936
Korea	7	59	213	744	1,845	2,024
Taiwan	17	47	213	708	1,320	1,323
Total	311	513	1,124	2,870	6,038	6,283
Latin America						
Argentina	—	—	4	11	19	n.a.
Brazil	—	—	3	83	89	85
Colombia	—	—	1	19	40	47
Mexico	—	—	9	67 <sup>a</sup>	33 <sup>a</sup>	n.a.
Total	—	—	17	180	181	n.a.

n.a. Not available.

— Negligible.

a. Excludes border zone. The figure for 1976 is estimated at \$174 million if the border zone exports are included.

Sources: United Nations, *Yearbook of International Trade Statistics*, various years; International Monetary Fund, *International Financial Statistics*, May 1976 and July 1979; United Nations, *Supplement to the World Trade Annual*, various years; Keesing (1978, table 10); and World Bank, unpublished data.

invariably, "We cannot compete with their prices." An illustration of the size of the price differential that exists is given in a report prepared by PROEXPO (1977a). In early 1977, this report states, the price that Colombian exporters were offering for both jeans and men's shirts was 44 percent above the Korean price quote, 25 percent above that of Hong Kong, and 11 percent greater than that of Taiwan. (The Taiwan figure is for shirts only.) At about the same time, Escobar (1977) stated that Colombian prices offered for a wide range of clothing items were systematically 20 to 30 percent above those of the East Asian nations. The impression I gained from the interviews for the present study is that the price gap has not narrowed since 1977; on the contrary, it may have increased somewhat.<sup>4</sup>

4. An indirect indication that Colombian price quotes are still systematically higher than those of East Asian garment exporters may be seen from the fact that of all the Colombian garment makers that have bought the license to use a foreign brand name, only one is currently able to export items using that brand name to the parent company for distribution in the United States. The vast majority of parent companies buy their brand name imports in East Asia.

Figure 6. Clothing Exports and Population:  
Hong Kong, Korea, Taiwan, and Colombia, 1976

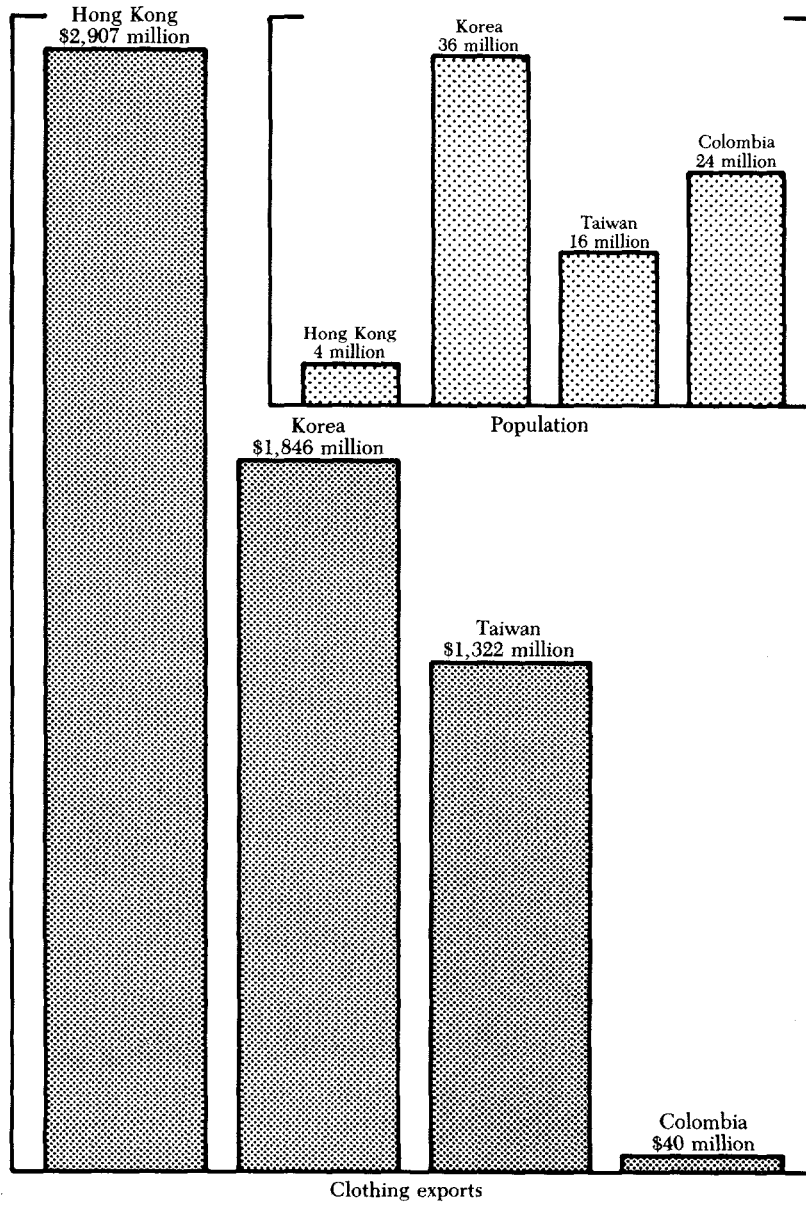


Table 26. U.S. Imports of Men's and Boys' Clothing  
by Area of Origin: Selected Items, 1965, 1970, 1975, and 1978

<i>Item and area of origin</i>	<i>Percentage of value of U.S. imports</i>			
	<i>1965</i>	<i>1970</i>	<i>1975</i>	<i>1978</i>
Pants, cotton				
Hong Kong	51	51	74	43
Japan	29	27	1	0
Korea	2	0	2	2
Taiwan	8	7	10	6
Others	10	15	13	49 <sup>a</sup>
Total	100	100	100	100
Shirts, man-made fibers <sup>b</sup>				
Hong Kong	21	28	8	11
Japan	30	13	0	0
Korea	32	37	60	54
Taiwan	12	20	19	27
Others	5	2	13	8
Total	100	100	100	100
Suits, wool				
Colombia	0	5	18	6
France	0	2	24	21
Hong Kong	21	15	1	6
Japan	72	32	1	0
Korea	0	19	36	19
Others	7	27	20	48 <sup>c</sup>
Total	100	100	100	100

a. Includes Singapore (11 percent), People's Republic of China (8 percent), and many smaller entries.

b. In woven blouses of man-made fibers, Korea had 25 percent in 1978, Hong Kong and Taiwan had 17 percent each, and there were many small entries, including Colombia (3 percent).

c. Includes Poland (8 percent), Chile and Italy (6 percent), Romania (5 percent), and a number of smaller entries.

Sources: 1965, 1970, 1975: Allison (1977, pp. 7-8); 1978: U.S. Department of Commerce, *U.S. General Imports*, TQ2010, TQ2210, TQ2310, July 1979.

The competitiveness of the prices that the three East Asian economies are able to quote and their share of total U.S. imports vary somewhat by type of garment, composition of fabric, and typical size of order (table 26).<sup>5</sup> Hong Kong is dominant in pants and other cotton

5. The share of U.S. imports in particular categories tends to be based on historical performance as frozen by the U.S. quota system as much as on current comparative advantage.

garments and tends to specialize these days in more fashionable, higher-priced articles. Korea is preeminent in men's shirts, and specializes mainly in inexpensive basic garments that require long production runs. Taiwan falls somewhere between the two. Both Korea and Taiwan concentrate particularly on articles of man-made fibers. Colombia tends to be like Taiwan in specializing in goods that are neither high fashion nor bargain basement. The main items exported by firms in our Colombian sample were pants and jeans (thirteen firms), blouses and shirts (eleven firms), and men's suits, sports coats, and jackets (five firms) (table 27).

The one clothing category in which Colombia has accounted for a non-negligible share of total U.S. imports is men's woolen suits (tables 10 and 26), the class of men's apparel in which U.S. imports have grown most rapidly in the 1970s (table 28). Eighteen percent of all U.S. imports of men's woolen suits came from Colombia in 1975, more than from any other country except Korea and France. Two qualifications need to be added to this apparent success story, however. First, since 1975 Colombia's position has been eroded sharply; by 1978 Colombia provided only 6 percent of the suits imported to the United States, and the number of countries that surpassed or equaled it in market share had risen from two to six—France, Korea, Poland, Chile, Hong Kong, and Italy. Second, suits are sold on styling and image as much as on price; if they were not, France, which has labor costs far higher than those of East Asia, could never have become the number one source of U.S. imports. More than 90 percent of Colombia's exports of suits come from

Table 27. Main Items Exported by Firms in the Sample, 1978

<i>Item of clothing exported</i>	<i>Number of firms</i>
<i>Men's and boys'</i>	
Pants (including jeans)	13
Shirts	5
Suits, sports coats, and jackets	5
Other	2
<i>Women's and girls'</i>	
Blouses	6
Slacks and skirts	2
Suits and coats	1
Other	4
Total	38 <sup>a</sup>

a. Total is greater than thirty because some firms have more than one main export item.  
Source: Interviews with firms.

Table 28. U.S. Imports of Clothing: Selected Items, 1967-77

Year	Apparel, not knit, man- made fibers (MMF) (millions of pounds of MMF equivalent) (1)	Men's and boys' clothing (million units)		
		Pants and trousers (2)	Shirts, woven (3)	Suits (4)
1967	30	30	84	0.3
1968	41	34	100	0.5
1969	67	36	125	0.9
1970	91	39	144	1.5
1971	106	39	154	1.2
1972	93	55	135	2.0
1973	82	51	92	2.0
1974	77	39	97	2.1
1975	94	55	100	3.1
1976	133	74	158	3.6
1977	147	77	145	3.3

Sources: Col. (1): U.S. Department of Commerce, *Business Statistics 1977*, p. 175, and *Survey of Current Business*, 1978, p. S-39. Cols. (2)-(4): Allison (1977, pp. 11-14); and U.S. Department of Commerce, *U.S. Production, Imports and Import-Production Ratios for Cotton, Wool, and Man-Made Fiber Textiles and Apparel*, January 1979.

one company which, in addition to being extremely well managed, has close financial links with a French suit designer-manufacturer; both the French and the Colombian firms, in turn, have close financial ties to their U.S. buyer. Thus, although men's woolen suits do provide an example of the success that Colombian garment-exporting firms might be enjoying if they could overcome some of their other problems, they do not represent an instance in which Colombia has been able to compete successfully with East Asia purely on price.

## Chapter 5

# Costs and Subsidies

THE C.I.F. DOLLAR PRICE a manufacturer is able to quote to a potential foreign customer for a garment depends upon the cost of producing the good (costs of labor, fabric, other inputs, and overhead), the cost of transporting it to the foreign country, any subsidies or other assistance that the manufacturer receives from the government for exporting, and the exchange rate. To try to understand why Colombian price quotes are so much higher than those of Korea, Hong Kong, and Taiwan, each of these elements will be examined separately.

### Transport and Communications

Because they have to travel a relatively short distance, and because of problems with shipping services, 99.9 percent of Colombia's clothing exports are transported to the United States by air. By contrast, more than 80 percent of East Asia's clothing exports to the United States are sent by sea (table 29).<sup>1</sup> The cost of airfreighting garments from Bogotá to New York is \$0.66 a kilogram; the cost of flying them from East Asia is more than four times as great (table 30). Ocean freight rates are quoted in dollars per cubic meter and hence are difficult to compare with airfreight costs, which are quoted in dollars per kilogram. Nevertheless, since it costs only a little less to ship garments from Colombia to the United States by sea than by air,<sup>2</sup> it follows from the data in tables 30 and 31 that the cost of shipping garments to the United States by *sea* from East Asia is roughly the same as the cost of transporting them by *air* from Colombia. (These transport costs are converted to a per garment rate in table 32 and range from about 5 percent of the f.o.b. price or less for lightweight items such as women's blouses of synthetic fabric to 10 percent or more for heavyweight, relatively inexpensive merchandise such as classic denim jeans.)

For the 80 percent of East Asia's clothing exports that arrive by sea, therefore, the big disadvantage compared with Colombia is not in

1. As might be expected, the fraction that is sent by air tends to be of higher than average unit value. This may be seen from the fact that the proportion of the value of East Asia's clothing exports that are flown to the United States is significantly greater than the proportion of their volume that arrives by air (table 29).

2. Information from interviews with Colombian firms.

Table 29. Percentage of Clothing Exports to the United States Transported by Air: Selected Exporters, 1977

<i>Exporter</i>	<i>Volume of exports</i>	<i>Value of exports</i>
Korea	11	17
Taiwan	13	18
Hong Kong	17	28
All countries	21	35
Colombia	99.9	99.9

*Note:* The balance was shipped by sea.

*Source:* U.S. Department of Commerce, *U.S. General Imports, World Area by Commodity Grouping*, 1978.

freight costs but in the time spent in transit: Colombian goods can be flown to the United States in a matter of hours; from East Asia the voyage by sea takes about four weeks (table 33). This gives Colombia a tremendous potential advantage over the East Asian countries. For one thing, it makes the use of the U.S. 807 offshore assembly scheme feasible. (It is not by chance that the first six nations in the list of those which export apparel to the United States using the 807 scheme [table 11] are within five hours flying time from the United States.) At least as important, in an industry in which every week is crucial, the time difference allows buyers who import from Colombia the chance to wait one month longer than those who import from East Asia before having to

Table 30. Airfreight Costs for Clothing Flown from Colombia and East Asia to the United States, Europe, and Venezuela, September 1979 (dollars per kilogram)

<i>Exporter</i>	<i>To New York</i>	<i>To Amsterdam and Frankfurt</i>	<i>To London</i>	<i>To Margarita Islands and Venezuela</i>
Colombia	0.66	2.79	3.08	0.56 <sup>a</sup>
Korea	2.68	3.35	3.35	n.a.
Hong Kong	2.84	2.83	2.91	n.a.
Taiwan	2.92	2.72	2.72	n.a.

n.a. Not available.

*Note:* The rates quoted are for a shipment of more than 500 kilograms from the capital city.

a. The rate quoted is for shipment by road and ferry; because air services were not available, this was the most common means of transport used in late 1978.

*Sources:* Avianca, Japan Air Lines, Korean Air Lines, Pan American, and interviews with Colombian firms.

Table 31. Ocean Freight Costs for Clothing Shipped from Colombia and East Asia to the United States and Europe, September 1979 (dollars per cubic meter)

Exporter	To		
	To New York	Amsterdam and Hamburg	To London
Colombia (Barranquilla)	77 <sup>a</sup>	120 <sup>b</sup>	100 <sup>c</sup>
Hong Kong	93 <sup>d</sup>	94 <sup>e</sup>	97 <sup>e f</sup>
Taiwan	93 <sup>d</sup>	97 <sup>e</sup>	99 <sup>e f</sup>
Korea	116 <sup>g</sup>	99 <sup>e</sup>	101 <sup>e f</sup>

a. The rate is \$59.56 if the merchandise is valued at less than \$500 per 40 cubic feet. The quoted rate includes Colombian port taxes and surcharges of \$6.32 per 40 cubic feet and a fuel surcharge of \$5.75, but does not include additional Colombian port charges of \$1.30 per 2,000 pounds.

b. The rate is for garments of cotton; for garments of wool it is \$95.74 and for shirts, \$66.96. All three rates include a fuel surcharge of \$7.

c. The rate is for garments of cotton; for garments of wool it is \$79.87 and for shirts, \$56.24. All three rates include a fuel surcharge of \$7.

d. Includes a loading charge of \$2.50, a fuel surcharge of \$9, and a destination charge of \$6.

e. Includes a fuel surcharge of 35 percent and a currency surcharge of 27 percent (Hong Kong), 31 percent (Taiwan), and 33 percent (Korea). For garments of synthetic fabric the rate is about 10 percent more than that quoted. Users of an entire 40-foot container (55-58 cubic meters) pay about 10 percent less than the quoted rate.

f. Includes a destination charge of £1.225.

g. Includes a loading charge of \$3.50, a fuel surcharge of \$10, and a destination charge of \$4.50.

Sources: Flota Mercante Grancolombiana, Evergreen Lines, and Boston Overseas Corporation.

Table 32. Airfreight Costs per Garment for Clothing Flown from Medellín to Miami and New York: Selected Women's Garments, 1978 (dollars)

Garment	To	
	Miami	New York
Blouse	0.04-0.50	0.7-0.60
Skirt	0.09-0.53	0.18-0.63
Short suit	0.11-0.65	0.21-0.78
Long suit or dressing gown	0.14-0.89	0.27-1.07

Note: The precise airfreight cost depends upon the weight of the garment and the total weight of the shipment in which it is sent. The lighter the garment and the heavier the total shipment, the lower the airfreight cost per garment.

Source: Interview with a Colombian firm.



Table 33. Approximate Number of Days at Sea for Clothing Shipped from Colombia and East Asia to the United States and Europe, September 1979

<i>Exporter</i>	<i>To U.S. east coast</i>	<i>To Europe</i>
Colombia	13-21 <sup>a</sup>	18-30
East Asia	26-30	25-35

a. Almost all clothing that moves on this route is in fact shipped by air since it takes only a few hours.

Sources: Flota Mercante Grancolombiana, Commerce Handling Company, and Evergreen Lines.

commit themselves to the make-or-break decision on what they think will be "in" next season.

For sales to Europe, Colombian and East Asian transport costs and times are more evenly matched. Airfreight charges from all four countries to Europe are similar to (or, for Korea, greater than) airfreight costs from East Asia to the United States, and hence are prohibitive for most goods (table 30). Ocean freight rates from Barranquilla to London are about the same as those from East Asia, while ocean rates from Barranquilla to Amsterdam and Hamburg exceed those from East Asia by 20 to 25 percent (table 31). Offsetting this cost difference, the journey from East Asia to Europe takes about a week longer than that from Barranquilla (table 33)—though sailings from East Asia are available much more frequently.

In an industry requiring frequent close contact between buyer and manufacturer, the cost and ease of availability of international communications services is also important. The cost of communicating between Colombia and the United States is in general less than, or equal to, the cost of communicating between the United States and East Asia (table 34). A U.S. buyer who wishes to visit his supplier need pay only about \$567 for a round-trip ticket to Bogotá, compared with three times this amount for a trip to Hong Kong, Taipei, or Seoul. A three-minute phone call from the United States to Seoul costs 50 percent more than one to Bogotá; a call to Hong Kong or Taipei costs 33 percent more. Telex and cables from the United States' east coast cost roughly the same to all four destinations, but the unavailability of a special night-letter rate for telegrams to Colombia makes this the one form of communication in which that country is at a disadvantage.

At least partially offsetting these cost disadvantages, the availability and reliability of communications to East Asia tend to be superior.

Flights to that part of the world operate much more frequently than to Latin America,<sup>3</sup> and a special bargain fare increases the attractiveness of the East Asian trip: a businessman can stop off in Tokyo, Seoul, Taipei, and Hong Kong for the same price as for a regular round-trip visit to Hong Kong alone. The phones tend to work more reliably in East Asia, and garment firms there are more likely to own a telex machine.

In summary, whereas Colombia and East Asia face relatively similar transport costs and conditions for exports of clothing to Europe, Colombia has a distinct advantage for exports to the United States: at no extra cost, Colombians can land goods at their destination four weeks faster than East Asians. This serves to illustrate why the United States is the logical market for Colombia's clothing exports—but it is of no help at all in explaining why Colombians have been unable to compete in price with East Asians in that market.

### Wages

*You want to know why we can't compete with Korea and Taiwan?  
Because they pay their workers miserable wages, that's why.*

—COLOMBIAN BLOUSEMAKER

Comparisons of wage levels between countries are made difficult by the need to include fringe benefits. These often vary considerably from firm to firm within one country, and it is not always possible to find reliable data describing them. For Colombia, a recent detailed examination of the clothing industry in the Aburrá Valley (Medellín) area by Peláez (1978) found that fringe benefits add 45 percent on average to the cash wage. Peláez's figure is probably more reliable than the estimates obtained in interviews for the present study because the latter were usually given off the top of the head without books being consulted. They varied so widely, even among apparently similar enterprises, that I suspect some firms were including items, such as provisions for eventual retirement payments, that others were omitting. The highest estimate, obtained from a few firms in interviews, was that fringe benefits can reach 100 percent of the cash wage. Table 35 presents two sets of wage data for Colombia: one assumes that fringe benefits are 45 percent of the cash wage; the other assumes, as an upper bound, that they are 100 percent.<sup>4</sup>

3. Thirty-five international airlines have offices in Hong Kong compared with only half a dozen or so in Bogotá.

4. In Colombia it is more difficult and costly to fire workers than it is in East Asia. This "fringe benefit" is not taken into account here, but see chapter 7.

Table 34. Travel and Communications Costs  
from the United States to Colombia and East Asia, September 1979  
(dollars)

Destination	Means of communication from Boston				
	Round trip flight from New York <sup>a</sup> (for three minutes)	Telephone <sup>b</sup>	Telex (for one minute)	Cable (per word)	Night letter telegram <sup>c</sup> (per word)
Bogotá	567	7.65	2.88	0.31	0.31 <sup>d</sup>
Hong Kong	1,708	10.20	2.78	0.28	0.14
Taipei	1,592	10.20	2.78	0.34	0.17
Seoul	1,604	11.42	2.78	0.34	0.17

a. Regular economy-class fare. The regular first-class round-trip fares are \$793, \$2,832, \$2,552, and \$2,392, respectively. The 7–28 day excursion fare to Bogotá is \$493; 14–21 day excursion fares to Hong Kong, Taipei, and Seoul are \$1,618, \$1,550 and \$1,437, respectively.

b. Person-to-person call.

c. Minimum twenty-two words.

d. Colombia does not have a separate rate for night-letter telegrams.

Sources: Braniff International, Japan Air Lines, Pan American, New England Telephone Company, and Western Union.

To the best of my knowledge, Hong Kong is the only country of the four under study here that publishes wage data both excluding and including fringe benefits. For Korea, a description was available of the fringe benefits that are typically paid, but not of their cost. For Taiwan, since I could find no data on fringe benefits at all, the conservative assumption is made that they are considerably less than in Colombia.

Data on the hourly wage *excluding* fringe benefits in the clothing industry are available for all four countries. In 1973 this wage in Colombia was about half that in Hong Kong, about the same as that in Taiwan, and almost 50 percent greater than that in Korea. By 1977, however, the situation had changed radically: Colombia was now the lowest-paying country of the four. The before-tax, take-home wage of a Colombian garment worker in that year was \$0.30 an hour, compared with \$0.40 in Korea, \$0.51 in Taiwan, and \$0.75 in Hong Kong.

If the Peláez estimate of 45 percent for Colombian fringe benefits is used, the wage *including* fringe benefits follows essentially the same pattern. In 1973 Colombian wages including fringe benefits were well below those in Hong Kong, probably greater than those in Taiwan, and significantly greater than those in Korea. By 1977 the Colombian wage including fringe benefits was barely more than half that in Hong Kong, was 14 percent lower than the wage *excluding* fringe benefits in Taiwan,

Table 35. Wages in the Clothing Industry in Colombia, East Asia, and the United States, 1973–77  
(dollars per hour)

Area	1973	1974	1975	1976	1977
Wage excluding fringe benefits					
Colombia <sup>a</sup>	0.23	n.a.	n.a.	0.26	0.30
Korea <sup>b</sup>	0.16	0.18	0.22	0.32	0.40
Taiwan	0.24	0.35	0.37	0.46	0.51
Hong Kong	0.48 <sup>c</sup>	0.53	0.53	0.68	0.75
United States	2.78	2.99	3.19	3.40	3.62
Wage including fringe benefits					
Colombia <sup>a</sup>	0.33(0.46)	n.a.	n.a.	0.38(0.52)	0.44(0.60)
Hong Kong	0.52 <sup>c</sup>	0.57	0.58	0.73	0.81

n.a. Not available.

a. The 1973 figures are extrapolated from Morawetz (1971); in 1967 and 1971, Colombian wages without fringe benefits were \$0.22 an hour. The figures for 1976 and 1977 refer to the Aburrá Valley (Medellín) area, and are from Peláez (1978). Peláez found that fringe benefits add 45 percent to wage costs. By contrast, in the interviews for the present study some entrepreneurs claimed that, once provision for severance payments and other often-omitted items are taken into account, fringe benefits can reach 100 percent. Hence, two figures are given here for the Colombian wage including fringe benefits: for the first, it is assumed that fringe benefits are 45 percent, and for the second (in parentheses), it is assumed, as an upper bound, that they are 100 percent. The interviewees indicated that wages in 1978 were about \$0.33–\$0.47 an hour, or about \$0.66–\$0.94 an hour, assuming fringe benefits of 100 percent. This probably overstates the average for the clothing industry as a whole because large firms, which generally pay higher than average wages, are overrepresented in our sample.

b. Fringe benefits that are often provided gratis by industrial firms in Korea include meals, work uniforms, transport, accident insurance, and medical and sports facilities. Subsidized low-cost housing is also sometimes provided (Pursell and Rhee, 1979).

c. This figure is approximate.

Sources: Colombia: Morawetz (1971), Peláez (1978), and interviews with firms. Korea: Bank of Korea, *Monthly Economic Statistics*, 1978 and International Labor Office, *Yearbook of Labor Statistics*, 1976. Taiwan: Republic of China, *Monthly Bulletin of Labor Statistics*, June 1978. Hong Kong: Hong Kong government, *Monthly Digest of Statistics*, March 1978 and Yung (1977). United States: U.S. Department of Commerce, *Business Statistics*, March 1978, and *Survey of Current Business*, December 1978. Exchange rates: International Monetary Fund, *International Financial Statistics*, May 1976 and July 1979.

and was almost certainly below that in Korea—the modest assumption here is that the cost of providing meals, work uniforms, transport, accident insurance, medical and sports facilities, and (sometimes) subsidized housing in Korea must surely amount to more than 10 percent of the cash wage.<sup>5</sup>

5. An editorial reader familiar with Korea estimates the figure at 20 to 30 percent.

Even if the upper bound estimate of 100 percent is used for Colombian fringe benefits, the picture changes only slightly. On this assumption, in 1973 Colombian wages including fringe benefits were less than those in Hong Kong but more than those in Taiwan and Korea; whereas by 1977 they were 25 percent lower than those in Hong Kong,<sup>6</sup> equal to those in Taiwan (provided that fringe benefits in that country amount to at least 18 percent), and probably no higher than those in Korea.

In summary, on the best available estimates (those of Peláez), whether fringe benefits are included or not, hourly wages in the clothing industry in Colombia are lower than in Korea, Taiwan, and Hong Kong. Even if an upper-bound estimate is used for the cost of fringe benefits in Colombia, Colombian wages are still significantly lower than wages in Hong Kong and are no higher—or, in the extreme case, not significantly higher—than those in Korea and Taiwan. It seems, then, that it is not because the East Asians “pay their workers miserable wages” that Colombian clothing firms cannot compete with them in price.<sup>7</sup>

### Labor Productivity

Wages give information on the cost of labor per hour worked; but a businessman needs to know the cost of labor *for each garment produced*. The missing link is the number of garments produced per hour worked, or labor productivity.

Labor productivity in the clothing industry tends to rise over time, not as a result of quantum jumps in the type of machinery used, but rather through the implementation of many small improvements in particular operations or in the organization of the production process. Examples of such improvements were mentioned in the discussion of

6. Wages in Hong Kong were not always more than those in Colombia; in 1959–60 and 1963–64, Hong Kong clothing industry wages were only \$0.8 and \$0.14 an hour, respectively (ILO, 1965). The reason for the rapid increase in wages that occurred in Hong Kong, Korea, and Taiwan during the 1960s and 1970s is, of course, that the swiftly rising demand for workers who could produce manufactured goods for export (including garments) first mopped up all available surplus labor in the three countries and then exerted upward pressure on wages and standards of living. On the success the three East Asian countries have had in raising their standards of living relative to those of other developing nations, see Morawetz (1977).

7. Nor do relative wage levels explain the rise and fall of Colombia's clothing exports to the United States and Europe, for the ratio of Colombian to East Asian wages was higher during the rise than it was during the decline.

the technical assistance provided to Colombian firms under brand-name licensing agreements—reorganizing production flows, introducing new methods of cutting, sewing, or joining materials, minimizing the downtime of machinery, and so forth. Some productivity increases do arise as a result of improvements in the machinery itself, but such innovations are usually less than revolutionary: built-in thread clippers and needle-positioners; automatic buttonholers, pocket-setters, and polybaggers; machine speeds of 4,500 stitches a minute instead of 2,500. Because most measures to increase productivity in garment making involve changing ways of doing and organizing things rather than introducing new machinery, the efficiency of management, especially at the middle level, tends to be crucial. An illustration of the way in which productivity improvement has taken place over time in the production of a particular garment (men's trousers) in the United States is presented in table 36.

In the interviews with Colombian firms, I was fortunate to come across several managers who were aware that a U.S. company (usually an importer-manufacturer or a brand-name licensor) was producing a garment identical to one they themselves were fabricating and who were able and willing to provide data on the precise number of minutes required to cut, make, and trim that garment both in Colombia and in the United States. (Interestingly enough, no Colombian manager claimed to have comparable data for East Asia, although in several cases parallel licensors in Korea or Taiwan were known to be producing identical garments.) I was fortunate, also, to be able to obtain estimates of average labor productivity in the manufacturing of specific garments in Colombia, East Asia, and the United States from a firm of international consultants that has specialized in the apparel business for several decades and knows all three areas well. The average figures for Colombia and the United States provided by the consulting firm are roughly consistent with the data provided by Colombian managers; if anything, the consultant's estimates of labor productivity in Colombia are a little higher than those derived from the interviews.

The full set of information available on labor productivity in Colombia, East Asia, and the United States from both the consulting firm and the interviews is summarized in table 37. On average, labor productivity appears to be 30 to 50 percent higher in East Asia than in Colombia, while productivity in the United States may be up to 50 percent higher again.<sup>8</sup>

8. Though the sample is small, there may be a systematic relation between type of garment and productivity difference. Among the articles surveyed here, Colombia's

Although eleven of the Colombian sample firms in table 37 appear to be operating below, and often well below, the East Asian level, for two companies this is not the case. One is the jeans producer which, as mentioned in chapter 3, has doubled its labor productivity as a result of receiving technical assistance from a foreign licensor: this enterprise is now producing at approximately the East Asian level. The other is the maker of suit coats which increased its labor productivity by two-thirds as the result of receiving assistance from a U. S. importer-manufacturer.<sup>9</sup> Interestingly, a second Colombian producer of the identical suit coat, which has been the recipient of the same technical assistance from the same source, has thus far not been able to improve its labor productivity at all. The problem, apparently, is that even though the wages paid by this firm depend on output, some workers have been unwilling to change the way they have traditionally done things. Also, the management of this large and well-known company apparently does not have sufficient shop-floor control to persuade them to do so. The example of the two suit coat firms serves to illustrate how important management, especially middle-level management, is to garment making and how the lack of it is largely to blame for Colombia's productivity problem.<sup>10</sup> By contrast, the examples of the jeans manufacturer and the more successful suit coat maker illustrate that Colombian firms that are exceptionally well managed (as these two enterprises are), and that have access to foreign technical help, can indeed produce up to, and even above, average East Asian productivity levels.

In sum, depending on what one believes about the size of fringe benefits in the different countries, labor costs measured in dollars per garment produced may well be lower in Korea and Taiwan (and possibly Hong Kong) than in Colombia; but if so, it is not because wages are lower in East Asia, but because labor productivity is higher there.

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disadvantage appears to be greatest in men's shirts. The production of men's shirts in the United States and East Asia is more mechanized than that of almost any other garment—on some operations, the investment required to equip a plant with state-of-the-art, shirt-production technology is now as much as \$35,000 per operator (Armfield, 1977)—but few Colombian firms possess the latest equipment. Data from Hasan (1976) are approximately consistent with these figures. He states that, in the mid-1970s, Korean labor productivity in garment production was about 75 percent of European levels. For example, the time required to produce a long-sleeved shirt was 27 minutes in Korea compared with 20 minutes in Germany; for short-sleeved shirts it was 18 minutes compared with 14 minutes.

9. On the implications of such sharp increases in labor productivity for the relation between growth in exports and growth in employment, see Morawetz (1980).

10. Some further reasons for the difference in labor productivity between Colombia and East Asia are examined in chapter 7.

Table 36. Increases, and Their Sources, in Labor Productivity in the Production of Men's Trousers in the United States, 1940s-1970s and Projections for the 1980s (percent)

<i>Item</i>	<i>1940s</i>	<i>1950s</i>	<i>1960s</i>	<i>1970s</i>	<i>1980s (projected)</i>
Dress trousers <sup>a</sup>					
Standard allowed minutes (average direct labor standard time per pair—stitching and finishing)		43	37	27	23
Productivity (pairs per operator per hour)	1.1	1.4	1.6	2.2	2.6
Cumulative gain (percent)	—	27	45	100	136
Casual trousers (slacks) <sup>b</sup>					
Standard allowed minutes (average direct labor standard time per pair—stitching and finishing)	37	21	18	16	13
Productivity (pairs per operator per hour)	1.6	2.8	3.3	3.8	4.6
Cumulative gain (percent)	—	75	106	138	188

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END



Contributions	Conversion of line shafts to individual work stations	Improved workplace engineering	Premade waistbands	Auto sew down left fly machine
	Workplace engineering	Mobile bundle production systems	Cam-operated sewing (back darts, side pockets)	Combined seams and press machine
	Progressive bundle production systems	Combining of operations	Automatic stacker and disposal devices	Contour seaming equipment
	Bundle clamps (better pick-up and disposal)	Zippers attached from chain	Clipper thread disposal for serging	Automatic and tandem serging machine
	Tandem equipment set-ups	Tandem (automatic) hook and eye	Back pocket welt (PW) machines	Automatic belt loop tacking machine
	Chain-cutting presser feet	Needle positioner and thread trimmer (1st generation)	Automatic-feed button sew machine	Other special purpose machinery
		Guillotine type cutting devices	Needle positioner and thread trimmer (2nd generation)	
			Elimination of final thread trimming	

a. Tailored dress trousers feature these construction details: stitched, turned, and restitched side and back pockets; fully booked side and back pockets; double besom back pockets; outseams, inseams, seatseams all pressed open (including side seam at pocket); both flies pressed with right fly seam pressed open; folded crotch liner stitched in at the serge fronts operation; belt loops tacked on and down at the end of the assembly line with French tacks; hand-felled waistband and outlet.

b. Casual Trousers or Slacks feature these construction details: stitched, turned, and restitched side pockets; fakestitched and Reece-type back pockets; pressed open side, seat, and inseams; no other underpressing; no crotch lining, premade waistband.

*Source:* Salmon Associates (1976, p. 2).

Table 37. Labor Productivity in the Clothing Industry in Colombia, East Asia, and the United States, 1978

<i>Garment and location of producer</i>	<i>Number of garments produced per machine operator in an 8-hour day</i>	<i>Index (U.S. = 100)<sup>a</sup></i>
<i>Classic jeans (five pockets)</i>		
Colombian average	19-24	43-55
East Asian average	28-30	64-68
U.S. good average firm	44	100
U.S. theoretically best possible	53	120
Colombian firm no. 1		
Actual output	9	24
Best possible output if no raw material or other holdups	16	43
U.S. firm producing identical garment	37	100
Colombian firm no. 2		
Output in 1975 before help from U.S. firm	10	31
Actual output	21	66
U.S. firm producing identical garment	32	100
Colombian firm no. 3		
Output that "would be good"	16-19	36-43
Colombian firm no. 4		
	12	27
Colombian firm no. 5		
	14	32
<i>Men's casual slacks</i>		
Colombian average	12	52
East Asian average	17	74
U.S. good average firm	23	100
U.S. theoretically best possible	28	122
Colombian firm no. 1		
U.S. firm producing identical garment	7-11	23-35
Colombian firm no. 2		
U.S. firm producing identical garment	28-34	100
Colombian firm no. 2		
U.S. firm producing identical garment	10	63
Colombian firm no. 3		
Actual output	16	100
Maximum possible output if no breakdowns, absenteeism, or other holdups	5	22
U.S. firm producing identical garment	8	35
Colombian firm no. 4		
	3	13

(Table continues on the following page.)

Table 37 (continued)

<i>Garment and location of producer</i>	<i>Number of garments produced per machine operator in an 8-hour day</i>	<i>Index (U.S. = 100)<sup>a</sup></i>
<i>Men's dress shirts (single pocket, banded collar, about \$9 at Sears or \$11 at department store, branded)</i>		
Colombian average	16 <sup>b</sup>	57 <sup>b</sup>
East Asian average	23	82
U.S. good average firm	28	100
U.S. theoretically best possible	37	132
Colombian average	<24	<67
Breakeven point with U.S. wages	24	67
U.S. and East Asian average	36 <sup>b</sup>	100
Colombian firm no. 1	6-7	21-25
Colombian firm no. 2	5-6	18-21
<i>Men's tailored suit coats (grade X)</i>		
Colombian average	3	38
East Asian average	5	63
U.S. good average firm	8	100
Colombian firm no. 1		
Output before help from U.S. firm	3	43
Actual output	5	71
Colombian firm no. 2 producing identical garment	3	43
U.S. firm producing identical garment	7	100
<i>Men's suits</i>		
Colombian firm no. 1	n.a.	67
French firm making identical garment	n.a.	100

n.a. Not available.

a. Where U.S. (or, in the case of suits, French) figures for identical garments are available, they are used as the base for this index. In all other cases, the base is the output of a good average U.S. firm as indicated in the table.

b. Approximate.

Sources: The first sets of figures under jeans, slacks, shirts, and suit coats are from an international apparel consultant in New York (15 to 20 percent should be subtracted from these figures if style changes, downtime of machines, and the like are to be taken into account). The second set of figures under shirts is from a U.S. shirt manufacturer. All other data are from interviews with Colombian firms.

## Fabric Prices

*I was at a textile fair in Denmark last month, and I came across some corduroy that was made by Coltejer. Even if you include the transport costs in both directions, it would have cost me less to buy that fabric in Copenhagen and ship it back here [\$3 a meter c.i.f.] than it costs me to buy it in Colombia [\$4.27 a meter from the factory]. Of course, I would have to pay tariffs, and there would be a long time lost in transit . . . Still if, for some reason, I particularly wanted to use precisely that Coltejer fabric for exporting, and no other, it would certainly be cheaper to import it from the United States or Europe using the Vallejo Plan than to buy it direct from the factory in Medellín.*

—COLOMBIAN JEANS MANUFACTURER

Apparel manufacturing is the most labor-intensive of all industries, but it is even more fabric-intensive than it is labor-intensive. In Colombia and East Asia, depending on the type of garment and the nature of the cloth, the share of fabric costs in the total costs of producing a garment (35 to 60 percent) is often double the share of labor costs (15 to 25 percent).<sup>11</sup> Consequently, as Escobar points out, “one can almost establish as an axiom that when the fabric is not exportable as fabric, nor is it exportable as a garment.”<sup>12</sup>

In Hong Kong, Korea, and Taiwan, a wide range of cotton and synthetic<sup>13</sup> fabrics is available to garment exporters at world prices either from domestic sources or as easily accessible, duty-free imports from a fellow East Asian economy (especially Japan) or elsewhere. In Colombia the situation is quite different.

Some synthetic fibers, and the petrochemicals on which they are based, are produced in Colombia; but the plants are small by world standards, cannot take advantage of economies of scale, and have high unit production costs.<sup>14</sup> As a result, Colombian synthetic textiles are priced well above world levels and are rarely exported either as fabric or

11. The share of labor is higher, and the share of fabric is correspondingly lower, in high-wage countries such as the United States. On these proportions, see for example, Allison (1977), Escobar (1977), Peláez (1978), and Scott (1979).

12. Escobar (1977, p. 9).

13. Except as otherwise indicated, “synthetic” is used throughout this study to include all man-made fibers.

14. These plants are able to survive only because they receive substantial protection against foreign competition from the government’s tariff and licensing system. Four of the five synthetic fiber plants so protected are more than 50 percent foreign owned; see Morawetz (1975).

Table 38. Fiber Content of U.S. Apparel, 1972 and 1976 and Forecasts for 1985 and 2000 (percentage of total weight)

<i>Fiber content of apparel</i>	1972	1976	1985 <sup>a</sup>	2000 <sup>a</sup>
Cotton	37	35	32	29
Wool	3	2	2	2
Noncellulose synthetics (polyester, nylon, acrylic)	48	57	60	63
Cellulose synthetics (rayon, acetate)	12	6	5	4
Other	0	0	1	2
Total	100	100	100	100

a. The forecasts are the consensus predictions of eighty-nine apparel, textile, and allied manufacturers in the United States and of fourteen expert observers who participated in a Delphi survey during 1978.

Source: Salmon Associates (1978, p. 25).

in made-up garments. For many synthetic fabrics, the ratio between the Colombian price and the world price was 3:1 until a few years ago; more recently, smuggled imports have kept the rate of increase of prices of synthetic fabrics below that of cotton cloths, and the ratio has now fallen to 2:1.<sup>15</sup> The cost of the overpricing of synthetic fabrics to the Colombian economy in terms of forgone clothing exports seems unlikely to diminish in the future; on the contrary, according to the recent forecast of a group of U.S. apparel specialists, noncellulosic synthetics are likely to continue to increase their share of the total weight of apparel through the year 2000 (table 38).

By contrast with the situation in synthetics, the basic constituent of cotton textiles—raw cotton—is available domestically in Colombia at world prices. Since textile manufacturing is one of the oldest, largest, and most efficient industries in the country, and since exports of cotton textiles amounted to about \$75 million to \$100 million a year during 1974–78,<sup>16</sup> it might be expected that domestically produced cotton

15. For obvious reasons, we did not ask clothing exporters whether they used smuggled fabric in their business, but three firms felt safe enough to volunteer that they do. This suggests that, at least among smaller firms in the coastal regions, the use of smuggled synthetic fabric may not be uncommon.

16. INCOMEX, unpublished tabulations, Expo 5, 1974–77, and Colombia Information Service (1979). It is said that the textile firms have been forced to continue exporting by the terms on which they received large-scale, emergency loans from the government in 1975—but they began exporting long before that date. It is interesting, incidentally, that

Table 39. Comparison of Domestic and Export Prices of Selected Pants Fabrics of 100 percent Cotton: Two Large Colombian Producers, February 1979

<i>Fabric</i>	<i>Domestic price</i>		<i>Export price c.i.f. New York (dollars)</i>	<i>Excess of domestic price (percent)</i>	
	<i>Pesos<sup>a</sup></i>	<i>Dollars<sup>b</sup></i>		<i>Over export price c.i.f. New York</i>	<i>Over export price from factory<sup>c</sup></i>
Corduroy	152.01	3.80	2.45	55	71
Indigo denim (firm 1)	132.59	3.31	2.20	51	66
Indigo denim <sup>d</sup> (firm 2)	196.88 <sup>e</sup>	4.92	3.12 <sup>f</sup>	57 <sup>e</sup>	73
Drill	81.69	2.04	1.50	36	50
Pocket	49.90	1.25	0.66	89	108

a. List price July 1978, plus the 20 percent increase expected for fabrics of 100 percent cotton in January 1979, less the discount of 13 percent granted to large domestic customers.

b. The exchange rate used is Col\$40 = US\$1.

c. It is assumed that transport costs from the factory to the port of New York are 10 percent of the price from the factory.

d. The width of this fabric is 150 centimeters, compared with 115 centimeters for the first indigo denim fabric.

e. Quote from one of the textile firm's domestic sales agents for delivery in February 1979.

f. The export price for this fabric was quoted as \$2.84 f.o.b.

*Sources:* Domestic prices: price lists of the two producers; see also notes a and e above. Export prices: quotes from the export departments of the two producers for delivery of 50,000 meters of the fabric to New York in February 1979. Transport costs: DNP (1978).

fabrics would be available to local clothing producers at world prices. Yet the most common and most vehement complaint expressed by apparel producers during the interviews was that they have to pay far more than world prices, often even double, for their cotton fabrics—even for precisely the same fabrics as their textile suppliers export!

To check whether these claims had any foundation, I first requested the managers of one of the smallest of the big four textile producers for detailed data on the firm's domestic and foreign selling prices for certain key fabrics. Unfortunately, the little information they were willing to provide was neither enlightening nor credible, so I decided to change tactics. Speaking as the director of a fictitious New York apparel firm, in December 1978 I telephoned the export departments of each of the two largest textile producers and asked them for price quotes for delivery in New York in two months' time of 50,000 meters of each of five pants fabrics. Pants fabrics were selected because two of these, indigo denim and corduroy, make up the bulk of Colombia's exports of fully finished fabrics and because, in keeping with Escobar's above-quoted axiom, the bulk of Colombia's exports of clothing that use domestic fabric are pants or jeans of indigo denim or corduroy. Having earlier obtained list and discount prices from local agencies of the two textile firms, I was then able to compare the export price quotes for these five fabrics with the price charged to large domestic clothing manufacturers.

The results of this exercise are summarized in table 39. The five fabrics, all 100 percent cotton, ranged in degree of overpricing from 50 to 108 percent, with an average of 74 percent; the all-important corduroy and indigo denim were overpriced by 71 and 70 percent (average of two quotes), respectively. Since the cost of the fabric usually represents at least 40 percent of the value of a finished garment, with such overpricing it is remarkable that Colombian firms have been able to export any apparel using domestic fabric. And indeed, the proportion of clothing exports to the United States using fabric imported under the Vallejo Plan rose from 56 percent in 1974–75 to 76 percent in 1976–77 (table 40) as profits from exporting began to be squeezed by the fall in the real effective exchange rate. Of the thirteen sample firms still exporting to the United States in 1978, only one was predominantly using domestic fabric, and the U.S. exports of that firm amounted to less than half a million dollars.<sup>17</sup>

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although Coltejer's earnings as reported in its financial reports fell in 1975, its profits were nevertheless still positive in that so-called crisis year.

17. More than half of total clothing exports to all destinations still apparently used

Table 40. Clothing Exports to the United States  
and to All Destinations, Vallejo Plan and Total, 1971-77  
(millions of dollars)

Year	Exports to the United States			Exports to all destinations		
	Vallejo Plan (1)	Total (2)	Vallejo Plan as percentage of total (3)	Vallejo Plan (4)	Total (5)	Vallejo Plan as percentage of total (6)
1971	n.a.	n.a.	n.a.	0.5	1.7	28
1972	n.a.	n.a.	n.a.	2.3	9.2	25
1973	n.a.	n.a.	n.a.	6.7	28.6	23
1974	9.6	17.1	56	18.4	82.7	22
1975	8.9	16.0	56	12.4	32.4	38
1976	9.8	12.8	77	19.4	37.3	52
1977	8.5	11.3	75	15.8	47.3	33

n.a. Not available.

Sources: Cols. (1) and (2): INCOMEX, unpublished tabulations, Expo 6, 1974-77. Col. (4): 1971-76: Sarmiento and Burgos (1977) based on Banco de la República, unpublished tabulations; 1977: Banco de la República, unpublished tabulations, Expo 10. Col. (5): 1971, 1973-77: PROEXPO, unpublished summary data, based on Banco de la República, unpublished tabulations; 1972: INCOMEX, unpublished tabulations.

The effects of fabric overpricing on export of apparel to the United States can be seen clearly in the breakdown of these exports by fabric and garment (figure 4 and tables 7 to 10). During 1972-78, although more than 80 percent of all textile exports were cotton, exports of cotton garments never exceeded \$3 million, or 20 percent by volume of total garment exports to the United States. Equally striking, exports of pants (including jeans) of denim and corduroy to the United States had fallen to less than half a million dollars in 1978, and seem never to have exceeded \$3 million in any year between 1971 and 1978—despite the fact that corduroy and denim are Colombia's two main exportable fabrics, and that pants and jeans seem to be the single most popular clothing export in the country (table 27). From a slightly different perspective, during 1972-77, 46 percent of the value of primarily cot-

domestic fabric in 1977 (table 40). This is explained in part by underreporting in the INCOMEX registrations of the extent to which the Vallejo Plan is used, and in part by the fact that the prices of apparel in the Margarita Islands and the Caribbean are so high that some exporters can still compete using either local fabrics or imported fabrics on which duty has been paid.



ton-containing exports consisted of raw cotton, 45 percent was cotton textiles, and only 9 percent was cotton garments.<sup>18</sup>

The effects of fabric overpricing on the decisionmaking and profitability of an individual garment-exporting company may be illustrated with data from the firm, introduced in chapter 3, that exports two sets of pants identical in all respects except that one is domestically and the other is internationally branded. The manager of that firm provided me with a comparison, for the domestically branded pants, of the costs of production that he would incur and the profits that he would receive if domestic fabric were substituted for imported fabric but everything else remained the same (table 21, cols. 2 and 3): the domestic fabric would have been 63 percent more expensive than the imported one. In addition, the imported cloth was of better quality, which enabled the manufacturer to increase the sales price of the pants by 25 percent. The net result was that the use of domestic fabric would have yielded a loss amounting to 3 percent of total outlays, whereas the use of imported fabric yielded a profit of 28 percent. Needless to say, the manufacturer used the imported fabric.

As this instance suggests, although the overpricing of locally produced fabrics necessarily causes the domestic content of garment exports to fall, provided that imported cloth is available duty-free, the aggregate value of such exports need not be affected too seriously. In Colombian practice, however, peculiarities of the Vallejo Plan, the Customs Department, and the ports combine in many cases to make the importing option less real than it would seem to be. These problems are considered in the following chapter.

In addition to having been traditionally high by world standards, the prices of many Colombian fabrics have risen particularly fast in recent years. In the case of the two most important fabrics, the peso prices paid by local garment makers for Colombian indigo denim and corduroy increased by 130 and 150 percent, respectively, between January 1976 and January 1979, at the same time as the official exchange rate increased by less than 25 percent (tables 41 and 42). To place these increases in perspective, it would be necessary to compare them with price rises for identical fabrics elsewhere in the world. Although the data needed for this comparison are not easily available, it nevertheless seems reasonable to assume that the steep rises in key fabric prices since

18. PROEXPO, unpublished summary data, based on Banco de la República, unpublished tabulations.

Table 41. Annual Increases in Colombian Fabric Prices:  
A Large Textile Producer, 1971-78

Year	Annual increase in price of fabric (percent)				Number of items included			
	Corduroy	Indigo denim	Other pants	Shirts	Corduroy	Indigo denim	Other pants	Shirts
1971	14	n.a.	16	19	3	0	9	4
1972	29	n.a.	32	18	4	0	15	3
1973	54	n.a.	43	61	4	0	20	7
1974	13	n.a.	11	6	4	0	29	12
1975	29	6	24	17	5	1	25	11
1976	n.a.	12	30	12	0	1	19	33
1977	n.a.	37	14	16	0	1	19	22
1978 <sup>a</sup>	39 <sup>b</sup>	50	33	23	12	1	8	11
<i>Average</i>								
1971-78	28 <sup>c</sup>	25 <sup>d</sup>	25	21				
1977-78	30 <sup>c e</sup>	43	23	19				

n.a. Not available.

a. Estimated on the assumption that price increases in early January 1979 were 20, 20, 18, and 14 percent for the four columns, respectively.

b. May 1978-January 1979.

c. Calculated on the basis that the average price of five corduroy items in July 1978 was 81 percent greater than it had been in January 1976.

d. 1975-78.

e. 1976-78.

Sources: Computed from the price lists of the textile producer for various dates. Approximate indigo denim prices kindly supplied by a large customer of the textile firm.

early 1976 have contributed, at least to some extent, to the decline after 1975 of Colombia's clothing exports to the United States.

How is it that the producers of textiles in Colombia—including the firm that employs Escobar, whose axiom was quoted in the first paragraph of this section—are able to charge domestic garment manufacturers 50 to 100 percent more than they charge foreigners for the same fabrics, seriously damaging the nation's clothing exports in the process? The immediate reason is that they are well protected against competition from imports. Although Colombia has exported large volumes of cotton textiles for more than a decade, anyone wishing to import cotton fabric still must pay duties of 55 to 75 percent of the value of the cloth. Imports of synthetic fabrics are liable for duties of 40 to 55 percent and are subject to licensing, and imports of woolen fabrics are taxed 75 percent. Behind this protection, the more fundamental reason lies in economic and political power. The textile industry employs more people than does any other industry in Colombia. It is heavily concentrated

Table 42. Increases in Colombian Textile, Clothing, and Consumer Price Indexes, 1968-78

Year	Percentage increase in index		
	Wholesale prices of fabric and yarn	Wholesale prices of clothing	Consumer prices <sup>a</sup>
1968	5	4	6
1969	7	7	10
1970	7	7	7
1971	11	11	9
1972	15	10	13
1973	28	25	20
1974	48	37	24
1975	10	15	23
1976	26	17	20
1977	23	21	33
1978	24	22	18
<i>Average</i>			
1971-78	23	19	20
1977-78	24	21	25

a. Index for blue-collar workers.

Sources: Wholesale price indexes: Banco de la República, *Revista*, various issues. Consumer price index (1967 = 100): table 17.

in Medellín, the nation's industrial capital; it is said in Colombia that without Medellín, no president is elected. The industry is run as a tight oligopoly—Coltejer has about 50 percent of the market, Fabricato has about 30 percent, and the top four firms together control more than 90 percent.<sup>19</sup> There is a clear pattern of price leadership: Coltejer raises its prices, the others follow within a week or two. Coltejer's sheer size may be appreciated from the fact that, if the heterogeneous food-processing sector is excluded, it alone employs more persons than does any manufacturing industry in Colombia. The one serious challenge to the power of the textile firms that has been thrown out in recent years was the attempt of the reformist administration of President Alfonso López Michelsen in 1976 to transfer synthetic fabrics from the list of imports requiring a prior license to the free list. Within six months, the transferal was reversed.<sup>20</sup>

19. Both Coltejer and Fabricato are based in Medellín, and the Coltejer building happens to be the tallest building in the city.

20. See, for example, Urrutia (1980).

### Prices of Other Inputs

Whereas East Asian garment manufacturers can obtain most other nonfabric inputs at world prices either domestically or from easily accessible imports, Colombians are less fortunate. In 1978 Colombian apparel firms had to pay three times the duty-free c.i.f. price of competing imports for locally made zippers, and double the duty-free c.i.f. price for thread. As is the case with fabric, the reason for this overpricing lies partly in the high degree of industrial concentration—only one large firm in Colombia makes zippers, and only one or two large enterprises manufacture thread, linings, and cardboard cartons—and partly in the protection against competing imports granted by the tariff and licensing system, on the one hand, and the bureaucratic and administrative problems in importing, on the other.

### Capital Utilization

Although fixed capital costs account for a small proportion of total outlays in garment manufacturing (usually less than 10 percent), the degree to which buildings and machinery are utilized nevertheless has some influence on total costs, and hence on price. Of the thirty firms in the Colombian sample, only two of the best-managed enterprises normally operate more than one shift. Of the other twenty-eight firms, many of the managers did not seem to have considered seriously the possibility of running the plant for more than one shift; others cited difficulty in finding reliable night managers and supervisors, and problems in apportioning responsibility for care of sewing machines among night and day operators, as their reasons for running one shift only. In Taiwan single shifting seems to be the rule in garment making;<sup>21</sup> on Korea I have no hard data; but in Hong Kong, where floor space is scarce, and hence expensive, multiple shifting is, I believe, not uncommon.

### Export Subsidies and Effective Protection

Several Colombian apparel manufacturers asserted during interviews that East Asian clothing exporters can charge such low prices for their

21. Riedel (1975, table 2).

products because they receive massive government assistance. In fact, this seems not to be the case. In laissez-faire Hong Kong there are no government subsidies to exports. In Korea the effective value of all export-incentive measures—including reductions in direct and indirect taxes, wastage allowances, preferential access to credit, and preferential electricity and railroad rates—amounted to only 12 percent on average in 1968 and seems to have changed little since then.<sup>22</sup> For Taiwan I have not been able to find a calculation of the effective value of export incentives; but given the nature of the incentives that have been available—exemption from some indirect taxes, deduction of 2 percent of annual export earnings from taxable income, availability of low-interest loans to finance imports of raw materials and machinery used in exporting, and availability of government-provided export insurance—it seems unlikely that they add up to more than 10 or 15 percent of the value of exports.<sup>23</sup> Contrary to the Colombian manufacturers' beliefs, then, the effective value of the export incentives they themselves have received—14 to 20 percent during 1967–74 and 1977–79, and 8 percent in 1975–76 (table 16)—seems to have been generally greater than or equal to that of incentives granted to apparel exporters in East Asia.

In analyzing the price-related influence of government on exports, although the absolute value of export incentives is of some interest, at least as important is the effect of the entire system of export subsidies and import restrictions on the relative profitability of selling goods abroad or at home. Hong Kong grants its firms no protection against imports at all, hence the incentives to export and to sell domestically are equal. In both Korea and Taiwan, although there has been considerable variation among products and over time, the net effect of the incentive system, on average, has been to make selling abroad about as profitable as selling at home.<sup>24</sup> In Colombia, by contrast, the trade-incentive system has caused selling at home to be much more profitable, on average, than exporting.

Until 1973 the Colombian import duty on finished garments was more than 200 percent, and almost all imports were prohibited in any case. Since then, imports of clothing have been subject to prior licensing and to tariffs that are still greater than 90 percent and have never amounted to more than \$2 million, or 1 percent of total domestic sales, in any one year (table 13). The low volume of legal imports has been supplemented to some extent by smuggling, but illegal imports seem to have been

22. Westphal and Kim (1977), Balassa (1978), and Westphal (1978).

23. Balassa (1971), Little (1979), and Scott (1979); Balassa and associates forthcoming.

24. See the references cited in the previous two footnotes.

Table 43. Effective Protection for Import Substitutes and Exports of Clothing, 1967-79 (percent)

<i>Item</i>	1967	1968	1969	1970
Average tariff on clothing <sup>b</sup>	207.45	207.45	207.45	207.45
Average tariff on fabric <sup>c</sup>	69.11	69.11	69.11	69.11
Value of fabric as percentage of value of clothing (estimated)	50	50	50	50
Prior deposit for imports of clothing	132.19	130.00	130.00	130.00
Prior deposit for imports of fabric	126.10	126.43	122.96	121.82
Effective protection for import substitutes	346	346	346	346
Effective protection for exports				
Limited company not using Vallejo Plan	-40.80	-38.14	-37.68	-36.96
Public company not using Vallejo Plan	-23.36	-20.70	-20.24	-19.52
Limited company using Vallejo Plan	28.32	30.98	31.44	32.16
Public company using Vallejo Plan	45.76	48.42	48.88	49.60

a. Projected. Figures in parentheses are applicable for exports to the United States only.

b. Most clothing items were on the list of prohibited imports during 1967-73 and were on the prior licensing list thereafter.

c. Most items of fabric were on the prior licensing list until 1973 and on the free list in

restricted mainly to the coastal markets and, some Pierre Cardin underwear notwithstanding, to goods in the lower price ranges.

Although garment making is one of the more competitive industries in Colombia, the domestic market is to some extent segmented by product and by geographical location. Thus, for example, the manager of the firm that produces fashion clothing for middle-aged women claimed to have no local competitors at all; three or four large companies dominate the market for men's underwear; and there is only one major producer of jeans in the Bucaramanga area. This market segmentation further raises the profitability of domestic sales.

A rough quantitative estimate of the extent to which the Colombian trade-incentive system has favored domestic sales over exports can be obtained by comparing the effective rates of protection that have been granted to import substitutes with those granted to exports (table 43).<sup>25</sup> Effective protection received by clothing exporters who did not use the Vallejo Plan was negative throughout 1967-78, varying from a high of

25. On the calculation of effective rates of protection, see, for example, Corden (1969). Although the data cited in this paragraph refer to limited liability firms, the conclusions are similar for public companies.

1971	1972	1973	1974	1975	1976	1977	1978 <sup>a</sup>	1979 <sup>a</sup>
207.45	207.45	182.90	94.89	94.89	92.30	91.17	91.17	91.17
69.11	69.11	69.12	65.31	66.18	65.18	63.75	63.75	63.75
50	50	50	50	50	50	50	50	50
130.00	130.00	23.92	0	0	0	0	0	0
121.82	121.82	22.50	0	0	0	0	0	0
346	346	297	124	124	119	119	119	119
-36.58	-36.16	-35.04	-26.22	-50.70	-48.40	-36.10	-26.04	-26.04(-31.16)
-19.14	-18.72	-17.60	-17.52	-47.32	-45.02	-34.76	-25.78	-25.78(-31.36)
32.54	32.96	33.41	19.56	7.74	8.38	13.84	18.86	18.86(16.30)
49.98	50.40	50.86	25.80	9.42	10.08	14.50	19.00	19.00(16.20)

1974. From 1975 onward, some were free and others, especially synthetic fabrics, have been subject to licensing.

Sources: Tariffs: Banco de la República, *Revista*, various issues. Prior deposits: Resolutions of the Junta Monetaria no. 2 of 1965, nos. 6 and 9 of 1967, no. 61 of 1969 (January and October), no. 40 of 1971, and no. 9 of 1973; and Decree no. 1121 of 1973.

-26 percent in 1974 to a low of -51 percent when the tax credit (CAT) was reduced sharply in 1975. By contrast, effective protection for domestic sales was always positive, ranging from 119 to 346 percent. This latter set of figures is misleading, since it assumes that there was no water at all in the apparel tariff. Nevertheless, the price data available from the interviews on two categories of clothing (jeans, and blouses and shirts) yield the same qualitative conclusions: effective protection for domestic sales was strongly positive, whereas that for foreign sales was heavily negative (table 44).<sup>26</sup>

The only exporters who received positive effective protection for foreign sales during 1967-78 were those using the Vallejo Plan. Effective protection for a limited liability company using this plan varied from a high of 33 percent in 1973 to a low of 8 percent in 1975 and stood at 19 percent in 1978 (table 43). An exporter of blouses and shirts using the plan still would have received greater effective protection in 1978 if he

26. Jeans, and shirts and blouses were the only two relatively homogeneous categories of clothing in which the number of observations in the interviews was sufficient to enable reliable comparisons to be made. Fabric costs are assumed to be 50 percent of total costs in both cases, but the qualitative results are the same whatever plausible percentage is used.

Table 44. Price Differentials and Effective Protection  
for Domestic Sale and for Export:  
Jeans, and Blouses and Shirts, 1978  
(percent)

<i>Item</i>	<i>Jeans</i>	<i>Blouses and shirts</i>
Excess of domestic price over export price <sup>a</sup>		
Finished garment	50	100
Fabric	70	100
Fabric costs as percentage of total costs	50	50
Effective protection		
For domestic sale	30	100
For export not using Vallejo Plan	-32	-62
For export using Vallejo Plan	38	38

a. The export price excludes the value of the CAT and PROEXPO credit because these are taken into account directly in the calculation of effective protection for export sales.

Source: Interviews with firms.

had concentrated on the domestic market; but a jeans manufacturer using the plan received slightly higher effective protection for exports than for sales at home (table 44). These findings serve to reemphasize the importance of the high price of domestic fabric in biasing producers against exporting, and the importance of the yet-to-be-discussed non-price barriers to importing fabric in restricting Vallejo Plan exports.

At the end of chapter 2, it was asked why Colombia's exports of garments to the United States leveled off or recovered slightly in 1978-79. In the light of the analysis in this section, this question might now be broadened: if selling at home is in general more profitable than exporting, why are any Colombian garment makers still exporting at all? It was also mentioned in chapter 2 that a few important firms have close financial ties with their foreign buyers, and that some firms appear to be holding onto their overseas markets during a difficult period in the hope of better times to come; these reasons are no doubt relevant to the broader question as well. In addition, at least three further factors may help to explain the continuance (and, to the neighboring markets, the growth) of Colombia's apparel exports. First, for some firms that export to the Margarita Islands and the Caribbean where prices are high, exporting is indeed as profitable, or almost as profitable, as selling domestically. It is presumably no coincidence that of the seven sample firms that exported 90 percent or more of their output in 1978 (table 45), five sold predominantly to the Margarita Islands and the Caribbean, and



Table 45. Percentage of Output Exported:  
Firms in the Sample, 1978

<i>Percentage of output exported</i>	<i>Number of firms</i>
0-9	7
10-29	9
30-49	4
50-69	2
70-89	1
90-100	7
Total	30

*Source:* Interviews with firms.

the other two did 807 assembly work for one U.S. client each. (One of the latter two is the only firm in the sample that is owned by its foreign buyer.) Second, some companies still exporting face a limited domestic market for their products; exports may yield lower per-unit profits for these companies than domestic sales, but they still add to total profits. Third, several enterprises seem to be exporting mainly for reasons other than direct profitability. Some want to maintain an export image in the domestic market: advertisements that state “export quality” or “we sell to Saks” are thought to help domestic sales. Others are eager to obtain the credit directed preferentially to exporters and sometimes difficult for others to obtain in sufficient quantities. Still others are interested in government goodwill; an exporter interviewed by Bernhart several years ago said that although he was only breaking even on exports to the United States, “when I go to INCOMEX they give me the abrazo, congratulations for my patriotic effort, and an import license for anything I want” (Bernhart, 1973, p. 2-22).<sup>27</sup> The relatively large number of firms that export a small fraction of their total output—even the sample, which is biased toward large-volume exporters, includes seven firms that exported 9 percent of their output or less in 1978, and sixteen that exported 29 percent or less—presumably includes quite a few for whom the indirect benefits are among the main attractions of selling abroad.

27. One manager I interviewed, who has a larger-than-usual need to import machinery for the textile side of his business, keeps a running estimate of precisely the value of garment exports that he needs to sell each year to keep the government’s favor. According to the apparently reliable figures he showed me, these exports are mostly sold at a loss.

### Costs and the Exchange Rate

All costs converted to U.S. dollars in this chapter to enable comparison with other countries—costs of transport, labor, fabric, other inputs, and so forth—were converted from pesos using the official Colombian exchange rate.<sup>28</sup> Clearly, had the exchange rate been higher—that is, if the peso had been devalued more rapidly—then, other things being equal, these costs expressed in dollars would have been lower. Thus, although the exchange rate was rarely mentioned explicitly in this chapter, in quite a fundamental sense it underlies much of the analysis.

28. Although the Kravis-type purchasing-power-parity-adjusted exchange rate is appropriately used to compare standards of living among countries, the official exchange rate is the correct one to use for comparing costs.

## Chapter 6

# Marketing, Input Problems, Bureaucracy, and Quota

BEING ABLE TO SUPPLY GOODS at a competitive price is a necessary condition for successful garment exporting—but it is by no means sufficient. The potential exporter must also be able, at a minimum, to locate a potential foreign buyer, to produce a garment of acceptable quality, and to guarantee delivery on time.

### Locating Buyers

A firm that wants to export and is seeking its first foreign client might approach its government export-promotion agency, commission a market research study, participate in trade fairs in foreign countries, subscribe to trade journals, send its own representative abroad, or, if it is able to do so, it might contact foreign buyers directly.<sup>1</sup> In East Asia this last option—direct contact with foreign buyers or their agents—tends to be the predominant way in which garment makers discover export possibilities. In a study conducted in Taiwan, for instance, 83 percent of the managers of apparel firms interviewed mentioned foreign customers as a source of information on export sales possibilities, whereas no more than one-third of them mentioned any other single source (table 46). In Hong Kong:

Almost the entire clothing export [has been] run by western trading companies; they supplied designs and models and often raw materials, too, checked product quality, attended to sales and shipping and sometimes also partly to financing. At first, these duties were fulfilled mainly by British colonial trading companies, later they were joined by the buyers of American and European department stores, chain stores, mail-order companies, and import firms. An estimated 70 percent of clothing exports passes via subcontracting through the hands of these traders.<sup>2</sup>

1. *Multinational corporations tend to play a relatively small role in the international apparel business, and intrafirm exports are much less common than, say, in the electronics industry.*

2. Evers and others (1977, p. 4); see also Geiger and Geiger (1973).

Table 46. Sources of Export Market Information:  
Apparel Firms and All Industrial Firms, Taiwan, circa 1976  
(percent)

<i>Source of export-market information</i>	<i>Apparel firms<sup>a</sup></i>	<i>All industrial firms<sup>a</sup></i>
Foreign customers <sup>b</sup>	83	76
Own representative in foreign country	33	33
Foreign partners	32	28
Chamber of commerce market studies	15	15
Trade fairs in foreign countries	11	13
Market research commissioned on firm's behalf	7	9
Government export-promotion organizations	7	7
Other		

a. The sample included a total of 415 firms and was distributed across the manufacturing sector to be representative of manufactured exports. It is biased toward large firms that export a large proportion of their output. The principal question on marketing was: How do you obtain information on sales possibilities for your products in foreign markets? The total number of responses adds to more than 100 percent because many firms gave more than one response.

b. This is the most important single source for each of the sixteen industries for which results were tabulated.

Source: Riedel (1977, table 1).

In Korea, too, buyers, especially from Japan and the United States, have played a predominant role in stimulating garment exports.<sup>3</sup>

In Colombia, by contrast, only about one-third of the managers interviewed for this study mentioned foreign buyers as a source of information about export possibilities, whereas over half mentioned trips abroad by the firm's principals. The reason for the difference between Colombia and East Asia in this regard is both simple and important: there are many more resident and visiting foreign buyers in East Asia for a prospective garment exporter to contact than there are in Colombia. In part, this is because success breeds success. Because Seoul, Taipei, and Hong Kong are the garment-exporting centers of the developing world, tens of foreign buyers and thousands of national and foreign trading companies maintain full-time purchasing offices there. In less-successful Colombia, by contrast, only one full-time foreign buying office specializing in garments was in operation in late 1978, and even it has since reverted to part-time commissionaire status because of lack of business (the office operated full-time for only two or three

3. Hone (1974); see also Pursell and Rhee (1979a).

years). In part, also, the difference in the number of buyers that can be found in East Asia and Colombia reflects externalities of geographical location. A businessman who intends to travel to Hong Kong to place some orders can stop off in Japan to select fabrics and in Korea and Taiwan to look for potential new suppliers, all for the same price. Bogotá, by contrast, is not on an established buying route, nor are Medellín, Cali, Barranquilla, and Pereira, Colombia's other centers of garment production for export.

The ease with which East Asian apparel firms have access to resident and visiting foreign buyers and their agents makes garment exporting a much less risky business in East Asia than in Colombia. If a Colombian entrepreneur loses a foreign customer, he may have to spend more than \$1,000 and several days of his time on a trip abroad to find another. In Hong Kong the proprietor of a firm whose buyer decides to go elsewhere has to do little more to find a replacement than pick up the telephone.<sup>4</sup>

In both East Asia and Colombia the overseas offices of government export-promotion agencies have been of little assistance in helping firms locate new buyers. That this should be so is not surprising; two or three officials are unlikely to know as much about the full range of a country's industries as is needed for success in finding new markets. In Taiwan, among the seven sources of export-market information about which garment exporters were asked in the survey mentioned earlier in this section, government export-promotion agencies were rated least useful (table 46). In Colombia not one of the thirty firms interviewed credited an overseas office of PROEXPO with having found it a buyer. The Bogotá office of PROEXPO does perform a useful marketing function, however, in directing foreign buyers who need assistance to appropriate potential supplying firms. PROEXPO is also invaluable in providing almost unlimited export credit to firms that need it—though a few firms in smaller cities complained that this credit was not always available to them.<sup>5</sup>

4. The perceived risk in exporting is particularly great for small firms in Colombia, as exemplified by the case of a woman from a small town who runs a second embroidery-based, putting-out operation (not to be confused with the one mentioned in chapter 3). In 1976 this woman displayed her wares at the Bogotá International Fair and received a highly remunerative offer from the agent of a major European chain of stores. But she was afraid of getting involved with what was, to her, an unknown purchaser in a far-away country; so, after some consideration, she rejected the offer. The European concern now buys its embroidered blouses outside Colombia.

5. For information on PROEXPO's credit activities, see PROEXPO (1977 and 1978).

## Fashion Awareness

*If you are not in fashion, you are nobody.*

—LORD CHESTERFIELD, *LETTERS*, 1750.

*What is a fashion? From the artistic point of view, it is usually a form of ugliness so intolerable that we have to alter it every six months.*

—OSCAR WILDE, *SUITABLE DRESS FOR WOMEN WORKERS*.

Once the prospective exporter has located a potential foreign buyer, or vice versa, the buyer is likely to want evidence that the garment maker is reasonably aware of world fashion trends. It is not necessary that the producer should be up-to-the-minute in fashion—that is the buyer's job. But he should be aware enough of what is selling, and of what is and is not acceptable in world markets, to enable him to respond flexibly and quickly to the buyer's requests without these having to be spelled out in inordinate detail. Although some Colombian garment executives have no trouble at all in passing this test, the buyers with whom I spoke in New York rated East Asian managers, many of whose firms live almost entirely from exports, ahead of Colombians on average. As the chief purchaser of women's apparel for one New York department store explained: "If I visit Korean and Taiwanese firms, their lines are up to date with U.S. and European fashions. If I visit a Colombian firm, I often have to start by telling them what sold well in the United States last year. Then I have to suggest changes in the products that they are offering and supervise the alteration process . . . it all takes much more time."<sup>6</sup>

6. A few of the fashions that came and went in the relatively stable men's tailored clothing business (suits, trousers, and jackets) in the United States during the 1970s were: 1970—knits, safari suits, wide lapels, flared bottoms; 1971—double knits, vested suits, bold plaids; 1972—warp knits, the coordinate concept, bell bottoms; 1973—vested suits, fitted-waist jackets; 1974—leisure suits, safari suits; 1975—ethnic looks, survival looks; 1976—the British look, the military look; 1977—the composed look, pegged pants; 1978—disco fashion, narrow lapels; and 1979—the classic look, broad shoulders, wide lapels. (*Daily News Record*, November 16, 1979, section 2, pp. 1-16.)

## Quality Control

*They complain about labels. They complain about shrinkage. They complain about zips. Doing business with the Americans is a pain in the neck. We get no complaints about these things at home or in the Islands. We can sell here and in the Islands at a good price—why get caught up in all these extra requirements?*<sup>2</sup>

—COLOMBIAN PANTS MANUFACTURER, IN AN ASIDE THAT WAS OVERHEARD BY A VISITING U.S. BUYER.

*We have thirty people in our quality control department and we haven't had a complaint yet. We know that if just one order arrives defective in New York, we've lost the client.*

—COLOMBIAN JACKET MAKER.

If a garment is to be of acceptable quality in the U.S. market, it must be styled, cut, and sized according to specifications; it must be strongly sewn and neatly finished; and the fabric, buttons, linings, and other materials of which it is made must be good enough to pass shrinkage, colorfastness, and other quality control tests. The best-managed garment-making firms in Colombia consistently meet these standards—but a number of less well-managed companies do not.

The results of tests carried out by a large U.S. retail chain on apparel purchased in Colombia give some idea of the degree of variance in quality that can be found among some of the less reliable Colombian suppliers.<sup>7</sup> Of twenty-two Colombian garments (mostly children's wear) tested by this chain during 1976–77, thirteen were judged to be unsatisfactory; on three, follow-up information was required; three were satisfactory with qualifications; and only three were clearly satisfactory. That is, of the twenty-two items examined, 59 percent were rejected outright, and only 14 percent were clearly acceptable. By comparison, apparel from East Asia tested by the same quality control department during 1976–78 generally had a rejection rate of 10, or at worst 20, percent.

The quality problems that this and other U.S. buyers have encountered with Colombian garments cover a broad spectrum.

- A maker of children's jeans did not have any small zippers in stock, so he cut off the ends of some larger ones and used these instead. The zippers broke, and the entire \$25,000 shipment was worthless.

7. This chain operates at the low- to medium-price end of the apparel market.

- When some children's pants were washed in washing machines, they shrank more than was tolerable, and U.S. customers began returning them to the stores. The manufacturer's response was "tell them to wash the pants by hand." (Household-owned washing machines are less common in Colombia than in the United States; many upper-income Colombian families employ live-in maids who wash clothes by hand.)
- The stripe on the shoulder of a boy's cotton sports shirt lost its color in the wash. The manufacturer suggested that the shirt be labeled "dry clean only."
- The lining within the collar of some corduroy shirts was poorly constructed, with the result that the garments lost their attractiveness after two or three washes. The manufacturer was not willing to change his production process for just one customer.
- In several shipments of women's blouses the sizing was not accurate, so the buyer scoured Colombia for a free-lance pattern maker familiar with U.S. sizes.<sup>8</sup> Eventually he found one, but even this person did not possess the necessary mannequins and tools. (In Korea and Taiwan many pattern makers specialize solely in work for the U.S. market.)

As can be inferred from these instances, some Colombian garment exporters simply do not understand the requirements of the U.S. market—zippers that break, pants that shrink excessively, colors that run, collar linings that wrinkle, sizes that are incorrect are not acceptable. True, hand-washing or dry-cleaning could solve some of these problems, but American consumers are not interested in children's pants that have to be washed by hand or boys' shirts that have to be dry-cleaned. As one buyer complained, "They were trying to sell us what they've always sold in Colombia instead of adjusting to U.S. requirements." This buyer canceled a Colombian apparel-purchasing program of a million dollars a year as a result of quality control problems with two or three firms; her department store now buys the items in East Asia.

At least some officials in Colombia seem to be aware of the quality control problem. In a speech in Bogotá in late 1978, the minister of development made the same point as the New York buyer: "Even though it is painful to admit it, we are inexpert at international market-

8. Colombian firms that have licensing agreements with foreign companies receive sizing information and assistance from their licensors, but the small firm in question had no such agreement.



ing . . . we have thought, wrongly, that we could simply export what was left over."<sup>9</sup> Nor are Colombians alone in sometimes misjudging the markets to which they sell. According to a trade newspaper of the New York garment industry, in late 1979 West German retailers believed that the U.S.-made outerwear being offered by hopeful U.S. garment exporters featured colors and styling not in tune with German taste; it was of poor quality, was made to last only a very short time, and was not adapted in sizing and fit to the German figure.<sup>10</sup>

Before I leave the subject of quality control, a tangentially related example of lack of attention to detail in finishing export-related products is worth mentioning. PROEXPO (1978a) publishes an attractively designed, glossy *Directory of Exporters* each year, the main function of which, presumably, is to serve as the central source of information on export-supply availabilities for prospective foreign buyers. But on close inspection, the directory's long lists of firms that export garments fail to include fully one-third of the firms in my sample, including two of the top four exporters and six companies that have been exporting continuously at least since 1974. Further, the English translation of the introductory information in the 1978 directory is pure Spanglish in parts and contains three typographical errors, one covering two lines, on the first page.<sup>11</sup>

### Punctual Delivery

Delivery dates are much more important in the U.S. market than in Colombia, Venezuela, and the Caribbean because seasonal variations in fashion and climate, and hence in the clothing that is salable, are more marked in the United States. A department store buyer in the United States who orders shirts for delivery in March is quite likely to cancel the order if they have not arrived by April 1, because after that date they can

9. Gilberto Echeverri Mejía, in *El Tiempo*, Bogotá, October 28, 1978, p. 7-C.

10. *Daily News Record*, August 8, 1979, p. 6.

11. Bernhart (1973) used the lists of exporting firms in an earlier edition of the same directory as the population from which he drew his initial sample of exporters, but he found many of the selected firms had to be discarded because they were not currently exporting. In a second example of inadequate quality of information about exporters and export products, Bernhart reports that when he visited the Ninth Bogotá International Trade Fair posing as a buyer for a Boston import house, only four of the sixteen apparel and leather products firms whose stalls he approached were able to provide him with dollar prices; and the two sets of samples that he ordered were never delivered.

be sold only at a discount of 40 or 50 percent. Since replacement merchandise is not always immediately available, the floor space set aside for the canceled order might be underutilized, and the money that was spent on newspaper advertising might be wasted. It takes only two or three episodes like this for a department store buyer to lose his job,<sup>12</sup> which helps explain why buyers attach so much importance to delivery dates.

Some of the U.S. buyers I interviewed expressed total satisfaction with the punctuality of their Colombian suppliers; but many were less than satisfied on this score, and several indicated that the failure of some Colombian suppliers to deliver goods on time was the last straw that caused them to cease purchasing garments in Colombia. A few specific instances illustrate the nature of the problem. A U.S. manufacturer of custom-tailored slacks said that it costs him \$5 more to have his trousers made in the United States than in Colombia, but that the increased reliability of delivery is worth \$10 more to his customers. A U.S. importer-wholesaler who tried to specialize in Colombian apparel eventually lost most of his U.S. customers because of the unpunctuality of some of his suppliers. A department store chain ordered 100,000 jackets from a large Colombian firm, trimmed the order to 50,000 when the supplier ran into difficulties, then cut it to 5,000—"and in the end they did not even deliver five samples. I would never go back to them," my informant stated, "and that experience turned me off Colombia." A second department store chain sent a buying mission to Colombia, but the few orders that they placed were never delivered. The buyers would be wary of going to Colombia again: "It was a sheer waste of our time."

As is the case with quality control, at least some officials in Colombia seem to be aware of the punctuality problem. Referring to the punctuality with which both samples and finished garments are delivered (as well as to the degree to which both of these conform to the initial specifications), PROEXPO (1978*b*, p. 30) states: "The Colombian image that has been created with respect to attention to the client is quite discredited."

The most important single determinant of the degree to which a garment-exporting firm is able to maintain quality control standards and to deliver goods on time is the quality of its management. Thus, it is no coincidence that several of the Colombian companies that have often

12. The reverse seems to occur as well; one of our informants claimed that his U.S. buyer was promoted to merchandising manager as a reward for building up a long-term, reliable supply relation with his (the informant's) firm.

delivered unacceptable garments have also often delivered late—whereas the firms that almost always maintain high quality standards are those that almost always deliver on time. But a firm does not exist in isolation from its environment; some problems that are external to the individual enterprise can tax, and occasionally defeat, even the best managers.

### Problems with Domestic Inputs

The protection Colombian textile producers receive against competition from imports enables them not only to charge high prices for their products, but also to take considerable liberties with the nature and quality of the fabrics they supply to garment makers and with the punctuality with which they deliver. The complaint of a manager of a medium-size, relatively new pants-making firm illustrates the problem:

We asked for three different shades of brown corduroy—but in the first month they sent us only black. Then they sent us all black and a bit of bright red. They sent us colors that are not even in their catalog. We asked for A grade [export quality]; they sent us B grade—look, it's written on the label. We ordered 6,000 meters a month—they sometimes send us only 2,500 meters. They just send us whatever they like, whenever they like. How can we possibly export like that?

The manager of a second pants-making firm reported similar experiences:

If we could rely on local suppliers of fabric we would much prefer to use it instead of exporting under 807 as we do now—but we've had terrible problems with the textile firms. We ordered 100,000 meters of indigo denim in December for delivery in June. By July only 1,000 meters had come. Now it's December and we've still only received a third of it. We ordered 20,000 meters of corduroy—none of it arrived. We had to run around looking for substitute fabrics—you can't export like that.

These were the two worst cases we came across, but they were far from being the only ones. Fully half the domestic-fabric-using garment makers interviewed complained that the quantities, qualities, or colors of fabric they received were sometimes different from what they had ordered, and that the fabrics that did arrive were often weeks or months late. As might be expected, newer and smaller firms tended to have more complaints on this score than large, long-established companies.

## Barriers to Importing Inputs

The garment makers' solution to problems like these, and to fabric overpricing as well, would seem to be to import fabric from abroad. In Hong Kong, Korea, and Taiwan garment exporters have guaranteed access to imported fabrics on virtually free-trade terms. In Colombia the Vallejo Plan drawback scheme appears to offer similar access—but in practice, several steep barriers must be overcome.

### *Vallejo Plan*

According to officials of INCOMEX, a company wishing to use the Vallejo Plan has to wait a minimum of two weeks, and an average of three or four, until its application is approved. The average delay is composed of a week for prestudy, a week until the committee meets, a week for signatures, stamps, and so on, and a week until the approval is registered and received by the firm. The delay can extend beyond a month if a relevant INCOMEX official is abroad, if the petitioning company has to make a last-minute change in the specifications of the fabric it wishes to import, or if an official decides to return the form to the petitioner because it contains a spelling or punctuation error (several garment exporters reported in annoyance that this had happened to them).

These preapproval delays are not the only problems inherent in the operation of the Vallejo Plan as it stands. Equally serious, anyone wishing to import a fabric also made by a Colombian textile company (particularly denim or corduroy) has to produce a letter from that company stating that it is unable to supply the fabric in the required quantity and quality by the required date. But, as several interviewees pointed out, any garment maker who asks the textile companies for such a letter risks having his name placed on their blacklist and thus risks jeopardizing all future local supplies.<sup>13</sup> Better, in the view of many, to put up with unreliable supplies than to be cut off altogether.

All things considered, the operation of the Vallejo Plan could certainly be worse: it seems that little or no bribery is involved, for instance, and many garment makers interviewed went out of their way

13. PROEXPO has recognized this problem, too. "Although imports of textiles are permitted, few garment makers have taken advantage of this possibility. This is because they fear the reaction of the textile firms on whom they depend for their regular supplies" (PROEXPO, 1978b, p. 12).

to praise INCOMEX for doing a relatively good job. But when the competition is able to import fabric under free-trade conditions, the delays inherent in the Vallejo Plan as it currently operates undoubtedly handicap Colombian suppliers.

#### *Ports and Customs*

Once approval to import inputs has been granted and the goods reach the Colombian ports, they routinely encounter delays caused by congestion, labor disputes, and the slow clearing of storehouses. After that, a final hurdle still has to be surmounted: customs. In the Dominican Republic, where most garment exports take place under the U.S. 807 scheme, clearing imported merchandise takes twenty-four hours. In Taiwan it takes two or three days. In Colombia, according to numerous accounts, it takes two to four *weeks* and often involves bribery,<sup>14</sup> theft, and rain damage to the goods to boot. Indeed, the problems involved in clearing imported goods through customs probably provide almost as much protection to the Colombian textile manufacturers as the rest of the tariff and licensing system put together. This is because the customs problems affect Vallejo Plan and 807 imports as well as ordinary imports and introduce an important element of risk into the business of importing. Once again, perhaps the simplest way to give an idea of what is involved is to let some of the persons concerned speak for themselves.

Among the interviewees in Colombia and New York who have had dealings with Colombian customs, those who did *not* recount incidents or offer comments like the following were in the minority. A Colombian jacket maker:

I imported some linings in March last year. The customs officer called me up daily after they arrived. He wanted me to pay a bribe of \$3,500 to expedite their release. When I went to his office, there he sat, my papers in one hand behind his back, his other hand stretched out for the money. "Here, I've got your papers," he said, "do you want them?" I refused to pay. I finally got the goods after three months, but most of them had been ruined by the rain. Of course, I lost that order and the client. Now, even though it costs me more, I buy all my inputs locally.

14. The bribery occasionally surfaces publicly. During November 1978 the Colombian newspapers reported in great detail on some tape recordings that had been made undercover in the Customs Department in Bogotá. A lawyer and three customs officers could allegedly be heard agonizing on the tapes over whether it was preferable to pay \$7,500 to burn or otherwise cause to disappear all incriminating evidence concerning earlier bribes or to pay \$3,750 and settle for the current investigation's being shelved indefinitely.

## A Colombian jacket assembler:

We refused to bribe the customs officers, so it took us one and a half months to get the goods [imported under 807] out of customs. When we finally got them, 274 jackets were useless because the box containing their collars had been stolen. We lost the contract and the client.

## A U.S. importer-wholesaler:

I had ten tons of piece-goods on the tarmac. All the licenses were in order, but some customs guy wanted to open it all to examine the buttons. I had a license for polyester buttons; he wanted to make sure that they were polyester and not acrylic. I ask you, who cares? It took him a week to find the right package, then he took off for a long weekend. While he was away a lot of work piled up, so it was another week until he finally got round to doing the chemical analysis.

## A U.S. importer-manufacturer:

Our supplier is one of the biggest apparel firms in Colombia, but they still routinely wait three to six weeks to get goods out of customs. Six weeks is half of our season!

## A Colombian government official:

If you are importing goods from abroad, you have to expect that up to 50 percent of them will be stolen; but usually it's more like 10 percent. The gangs of thieves seem to have worked out that 10 percent is enough to make stealing worthwhile, but not so much that people will complain.

*Free Zones*

One way in which garment makers who wish to import fabric and other inputs can avoid the delays inherent both in the Vallejo Plan and in clearing goods through customs is by setting up operations in an export processing zone or, as they are known in Colombia, a free zone (*Zona Franca*). Hong Kong, of course, is one giant free zone. In Taiwan more than \$300 million worth of garment exports a year, and a sixth of all garment-industry employment, stem from the country's free zones.<sup>15</sup> Yet in Colombia, where one might expect them to be so useful in overcoming the problems associated with importing, free zones seem to have been a failure.

15. Scott (1979); table 24 above; and *Monthly Bulletin of Labor Statistics* (Taiwan, June 1978), table 1-3.

Table 47. Exports from, and Employment in, the Barranquilla Free Zone by Industry, 1973-78

Industry	1973	1974	1975	1976	1977	1978
						(January-June)
<i>Net value of exports<sup>a</sup> (millions of dollars)</i>						
Clothing and textiles	0.8	1.2	0.9	0.9	1.2	0.5
Metal manufactures	0.0	0.2	0.1	1.3	4.6	0.9
Leather products	0.3	0.7	0.9	1.9	2.4	0.8
All industries	1.1	2.1	2.5	4.2	8.2	2.3
<i>Employment (thousand persons)</i>						
Clothing and textiles	1.7	1.2	1.6	1.7	1.8	1.6
Metal manufactures	0.1	0.3	0.3	0.8	1.2	0.9
Leather products	0.2	0.2	0.2	0.6	0.3	0.3
All industries	2.2	1.9	2.2	3.4	3.5	3.1

a. Gross value of exports less value of imported inputs.

Source: Ministerio de Desarrollo Económico (1978, pp. 51 and 55).

From the viewpoint of industrial production and export, the two most important free zones in Colombia are at the seaport in Barranquilla and at the Palmaseca airport outside Cali.<sup>16</sup> In the Barranquilla zone, total garment exports never exceeded \$4 million gross (or \$1.2 million net of imported inputs) in any year through 1978 (table 47); total garment-industry employment never exceeded 1,800 persons; and only five garment firms were producing for export in 1978.<sup>17</sup> At the Palmaseca airport, the situation is even bleaker; with the closing of a large foreign-owned company about 1977, there are now apparently no important garment exporters left in the zone.

Why have the Colombian free zones not attracted and retained more garment-exporting firms? First, both the Barranquilla and Cali zones are some distance from the areas in which their workers live, which means that companies locating in them incur extra costs for transport

16. The Barranquilla zone accounted for 80 to 90 percent of total Colombian free-zone production, employment, exports, and value added in exports of all industries in 1977; the Palmaseca zone accounted for between 10 and 20 percent; the Buenaventura zone accounted for less than 1 percent; and the zones at Cartagena and Cúcuta were confined almost entirely to commercial activities (Echavarría, 1979, table II-3).

17. Seven separately registered firms were exporting, but in two cases two firms were jointly owned and managed. Another twelve firms were producing garments in the free zone and had at one time exported, but in 1978 they used mostly domestic inputs and sold their output only in the domestic market (Ministerio de Desarrollo Económico, 1978a).

and food. Since it probably costs considerably less to transport goods once each way than to transport the entire labor force back and forth each day, it may make sense to follow the example of the Taiwanese who, learning from the experience of their first zone, located the next two near their labor forces instead of immediately at the ports.<sup>18</sup> Second, since almost all Colombia's garment exports to the United States are transported by air, the rationale for a free zone at the seaport of Barranquilla is not clear, at least as far as garments are concerned. (True, this argument does not apply to Palmaseca—but the distance of that zone from almost everything else in Cali may be its main drawback.) It would be interesting to see whether a free zone near the airport (and near employee housing) in Medellín or Bogotá might not have better success. Third, although I have no information on the Palmaseca zone in this regard, in Barranquilla inadequate management may have had something to do with the zone's lack of success. Fourth, the role of customs and regulation problems and theft may be worth examining. These explanations should be regarded as hypotheses for further study rather than well-researched conclusions. But given the importance of the role that free zones could play in sidestepping Vallejo Plan and customs problems, it may be worth devoting considerable effort and resources to studying free zones that have been successful elsewhere (Korea, Mexico, and Taiwan) to understand more fully why the existing Colombian zones have done so poorly, and then to set up new zones that do not suffer from the same defects.

### Lead and Cycle Times

The lead time facing a buyer is the time that elapses between placing an order and receiving the finished garments; the cycle time, for a buyer who uses the assembly system, is the time between dispatching the precut fabric and receiving the fully assembled apparel. Fashions change so abruptly and so frequently in the garment business that the shorter the lead and cycle times a country is able to offer, the more likely it is to succeed in exporting.

U.S. buyers who use U.S. apparel firms to assemble their garments can generally count on cycle times of two to three weeks. (This means that a U.S. manufacturer who sends one set of precut inputs to a U.S. assembler and flies a second identical set to a Colombian rival is likely to have the locally assembled finished garments in his warehouses, ready

18. Scott (1979).



for sale, before the Colombian firm has got its inputs out of customs.) For imports, the acceptable cycle time is generally about six to eight weeks. For imports from Colombia, however, the cycle time is usually ten weeks or more. This delay is composed of at least two weeks until the import is approved by INCOMEX, at least two weeks to get the imported materials out of customs and into the factory, five weeks in the factory, and one week to get the finished garments back to the United States. Further, it is not uncommon for another week or two to be added because of longer-than-minimum delays in approval of the import, or in customs, or because the finished goods have to wait to get on a flight. Thus, as a result of the delays in the administration of the Vallejo Plan and in customs clearance, the one important potential advantage that Colombian garment exporters have over their East Asian rivals is lost. Instead of being several weeks shorter, the lead and cycle times that Colombians can offer U.S. buyers are either the same as those offered by East Asians or, in many cases, one or two weeks *longer*. Of course, for the 20 percent of East Asian garment exports that travel to the United States by air, the time differential is considerably greater again.

### Export Formalities

As a result of the Customs Department reforms of 1974, up to twelve signatures now have to appear on each export manifest. These signatures attest that the goods exist; they have entered the storehouse; they are made of the materials stated on the manifest (two signatures are needed for this, including that of an auditor); the transporter has seen the goods; they have left the storehouse; they have been placed on the plane; and the export has been authorized. The purpose of so many signatures is, of course, to reduce fictitious exports to a minimum.<sup>19</sup> The effect, unfortunately, is to add a little more to Colombian lead and cycle times and to the cost of exporting; most large exporters maintain from one to three full-time employees whose sole function is dealing with these formalities.<sup>20</sup>

19. Despite this elaborate system of checks, some fictitious exports still seem to slip through. For example, the exports of cheese registered in Santa Marta in late 1978 were apparently considerably greater in value than total local cheese production.

20. Of course, it is largely because the export-incentive system is so complex—involving the CAT, the Vallejo Plan drawback scheme, subsidized export credit, and so forth—that export formalities have to be so rigorous (to check very carefully that registered exports do in fact take place). If a more realistic exchange rate were used to replace the export-incentive system, such stringent export regulations would no longer be needed.

### Range of Fabrics and Garments

A U.S. buyer of pants or shirts wants to buy all the merchandise he needs in one country, or at least on one business trip; he is likely to try to avoid importing corduroy pants from one continent and polyester-cotton trousers from another. In East Asia, as many buyers stated, they can get any garment they want, made of any material: cotton, synthetics, wool, leather, fur. In Colombia, by contrast, the range of available fabrics, and hence garments, is extremely limited. Colombian denim and corduroy are of good quality if high price, but almost any other fabric has to be imported. Thus, Colombia is a possible source for some pants, skirts, and jackets made of domestic denim or corduroy; but it is immediately ruled out, for example, for shirts, which are predominantly of polyester-cotton blends and alone make up about half the total value of U.S. imports of men's garments (table 48). Furthermore, the delays inherent in the Vallejo Plan and customs clearance mean that Colombia is effectively denied duty-free access to Japanese fabric which, in the mid-1970s, was one of the world's premier sources. (Japan is six weeks by sea from Colombia but only two weeks or less from Korea, Taiwan, and Hong Kong; the addition of administrative delays makes importing fabric from Japan impractical for Colombians in many cases.)<sup>21</sup> The resulting narrowness in the range of exportable fabrics and garments available reinforces some of the country's other marketing problems: because Colombia is a relatively unattractive source of apparel, buyers visit infrequently and refrain from establishing permanent offices, Colombian clothing firms find exporting risky and concentrate on selling domestically, and thus buyers find Colombia unattractive—and so forth.

### U.S. Import Quotas

Some government officials to whom we talked guessed that Colombia's clothing exports to the United States might have done relative-

21. True, Japanese fabrics can be imported into the United States, cut, and flown to Colombia for assembly under 807—but in such cases, which do sometimes occur, duty has to be paid on the fabric when it first enters the United States. U.S. duties on imported fabrics of wool, man-made fibers, and cotton are 50, 35, and 8 to 18 percent, respectively.

Table 48. U.S. Imports of Selected Clothing Items as Percentage of Total U.S. Imports of Men's Clothing and as Percentage of U.S. Production of Item, 1965, 1970, and 1975

<i>Imports</i>	1965	1970	1975
As percentage of total value of U.S. imports of men's clothing			
Pants	32	24	27
Shirts	62	59	50
Suits	6	17	22
Total	100	100	100
As percentage of U.S. production of item (in units)			
Pants	0	8	12
Shirts	10	44	31
Suits	0	24	37

Source: Allison (1977, pp. 7-8 and 11-14).

ly poorly because U.S. import quotas held them back. In fact, this does not seem to have been the case.

In each of the two most recent U.S.-Colombia bilateral textile agreements, the apparel section contains more than sixty separate categories. During 1975-76 and 1976-77, in fully 70 percent of these categories, less than 10 percent of the allotted quota was used. Of the twenty-four cotton categories in the agreement, not one had its quota even one-third filled. Overall, only four categories in 1975-76 and two in 1976-77 had their quota allotments at least two-thirds filled (table 49). By comparison, Korea used at least 85 percent of its quota allotments in twenty-three categories in 1975-76, as did the Philippines in fifteen, Taiwan in fifteen, and Hong Kong in eleven (including several broadly bracketed categories)—all coming much closer to utilizing their quotas than Colombia (table 50).

Nevertheless, in two categories, the U.S. quota does seem to have become a binding constraint. One is men's and boys' suits of wool; the other is women's blouses, not knit, of man-made fibers.<sup>22</sup> In the first category, as noted earlier, one large firm accounts for more than 90 percent of all Colombian shipments to the United States; in the second, two firms, both using the 807 scheme, share a similarly large proportion

22. For data on exports of these two items, see tables 7 to 10.

Table 49. Colombian Utilization of Quotas for Exports of Clothing to the United States by Type of Raw Material, 1975-76 and 1976-77

<i>Exports as percentage of quota allotments</i>	<i>Number of agreement categories</i>			
	<i>Cotton</i>	<i>Wool</i>	<i>Man-made fibers</i>	<i>Total</i>
1975-76				
Less than 10	20	10	16	46
10-33	4	2	6	12
34-67	0	1	3	4
68 and over	0	2	2	4
Total	24	15	27	66
1976-77				
Less than 10	19	11	18	48
10-33	5	3	7	15
34-67	0	0	1	1
68 and over	0	1	1	2
Total	24	15	27	66

Source: Unpublished data.

of U.S.-bound exports.<sup>23</sup> The managers of these three firms all indicated (and their U.S. buyers confirmed) that they would have been able to export more to the United States in 1978 but for the limitations imposed by the quota.<sup>24</sup> None of these firms showed any signs of diversifying into product areas in which quota restrictions are not yet binding.

In parts of East Asia, exporting to the United States is so profitable that quota is traded among firms and commands a premium that can reach 50 percent of the value of sales. In Colombia, by comparison, quota is allocated gratis by INCOMEX, carries no premium—apparently no bribery is involved either—and may not be bought or sold. After interviewing the managers of a number of Korean clothing-exporting firms, Wortzel and Wortzel (1979a, p. 13) reported: “Although our interviewees were reasonably open with us on most subjects, [they] refused to discuss quota allocations in any depth. The litany that was repeated to us whenever we asked about quota was: ‘The allocation of

23. Two of these three firms are the companies mentioned in chapter 2 that own equity in, or are owned by, their U.S. buyers.

24. This illustrates the general thrust of U.S. quota policy in dealing with clothing-exporting countries other than the big three East Asian suppliers: prevent them from concentrating heavily on the particular, narrow product lines in which they do best (Wortzel and Wortzel, 1979a).

Table 50. Utilization of Quotas for Exports of Clothing to the United States: Selected Exporters, 1975-76 and 1978-79

<i>Exporter</i>	<i>Number of agreement categories in which clothing exports reached 85 percent of quota levels<sup>a</sup></i>	
	<i>1975-76</i>	<i>1978-79</i>
Korea	23	8
Philippines	15	8
Taiwan	15	9
Hong Kong	11	12
Mexico	6	0
Haiti	5	1
Poland	4	5
Pakistan	3	2
Romania	3	5
<i>Colombia</i>	2	2
India	1	5
Macao	1	2
Malaysia	1	4
Singapore	1	6
Thailand	1	1

a. Not all figures are strictly comparable, because different agreements break up the universe of clothing items into different total numbers of categories, and because the numbers of categories have changed significantly over time. Other countries with which the United States has bilateral agreements on exports of textiles and apparel are Brazil, Dominican Republic, Japan, Romania, and Yugoslavia. Countries with which the United States maintains open-ended consultative agreements that can trigger import restraints if needed are Czechoslovakia, Egypt, Greece, Hungary, Jamaica, Malta, Nicaragua, Peru, Portugal, and Spain.

Sources: U.S. International Trade Commission (1978, p. C-70); U.S. Department of Commerce, unpublished data; and *Daily News Record*, November 12, 1979, p. 5.

quota is the allocation of wealth.'” In Colombia, by contrast, no interviewee refused to discuss quota with us; what is more, even after being invited to do so, no one—not even producers of men’s suits and women’s blouses—expressed dissatisfaction with the quota allocation that his or her firm had received. This is further evidence that quota was generally not a binding constraint in Colombia during 1975-78, and that, even where it was, exporting to the United States was not such a profitable business as to make quota worth fighting about.

Even though U.S. quotas are not currently binding, they could still be a disincentive to exports if their existence discourages potential exporters from trying to break into the U.S. market. We found no entrepreneurs who claimed this to be the case. One U.S. buyer did

mention that, because Colombia has relatively small quotas, this militates against his investing much time and energy in searching there; but other U.S. buyers claimed that, because they are running out of quota in East Asia, and because quota is raising prices there, they are interested in seeking new sources of supply, including those in Colombia.

Not content to rely on quotas, in late 1978 the United States threatened to impose countervailing duties of 2.15 percentage points on Colombia's clothing exports, allegedly to offset unfair subsidy elements in the CAT. An alternative solution proposed that the Colombian government should reduce the nominal CAT received by exporters of clothing to the United States by 2.15 percentage points. Either way, the end result was likely to be to reduce still further the profitability of exporting to the United States.

Up to the time of writing, the European Economic Community had not yet imposed quotas on imports of clothing from Colombia because those imports had not yet reached significant levels.

Although quotas have not yet severely hampered Colombia's clothing exports to the United States and Europe except in two subsectors, this does not mean, of course, that quota could not become a problem in the future. On the contrary, if exporting to world markets were to become profitable, the low levels of quotas for exports to the United States, and the relatively low import levels at which consultations are triggered in the Colombia-EEC textile agreements, could become real restrictions.<sup>25</sup>

### Marketing Profits

For most goods these days, from a loaf of bread to an ounce of marijuana, only a small proportion of the price the final consumer pays finds its way to the original producer.<sup>26</sup> For garments exported from Colombia to the United States, the situation is no different. Assuming, as is common, that transport costs are about 5 percent of the Colombian f.o.b. price, that the U.S. importer's markup is 33 percent, and that the U.S. retailer's markup is 100 percent,<sup>27</sup> a Colombian garment-exporting

25. There is, of course, room for Colombia's clothing exports to the United States to increase at least three- or fourfold within the existing quotas if—and this is a big if—these quotas could be more fully utilized.

26. For marijuana, it has been estimated that a mere 3 percent of the U.S. retail price is received by Colombians (Junguito and Caballero, 1978; Niedergang, 1979).

27. In the U.S. garment industry, the importer's markup is generally stated as 25 percent (of the price to the retailer), while the retailer's markup is generally stated as 50

Table 51. Comparison of U.S. Retail Price with Colombian F.o.b. Price for Hypothetical Garment Exported from Colombia, 1978

Price or price component	U.S. import duty		
	Zero	25 percent	50 percent
F.o.b. price of garment in Colombia	100	100	100
Plus transport cost (5 percent)	5	5	5
C.i.f. price	105	105	105
Plus import duty	0	26	53
Plus importer-agent's margin (33 percent) <sup>a</sup>	35	43	52
Price to retailer	140	174	210
Plus retailer's margin (100 percent) <sup>b</sup>	140	174	210
U.S. retail price	280	348	420
Colombian f.o.b. price as percentage of U.S. retail price	36	29	24

a. This margin is generally stated as 25 percent (that is, 25 percent of the price to the retailer) in the U.S. garment industry.

b. This margin is generally stated as 50 percent (that is, 50 percent of the price to the consumer) in the U.S. garment industry.

Sources: Adapted from Little (1972), and interviews with firms.

firm using domestic fabric generally receives between one-quarter and one-third the price paid by the U.S. consumer (table 51).<sup>28</sup>

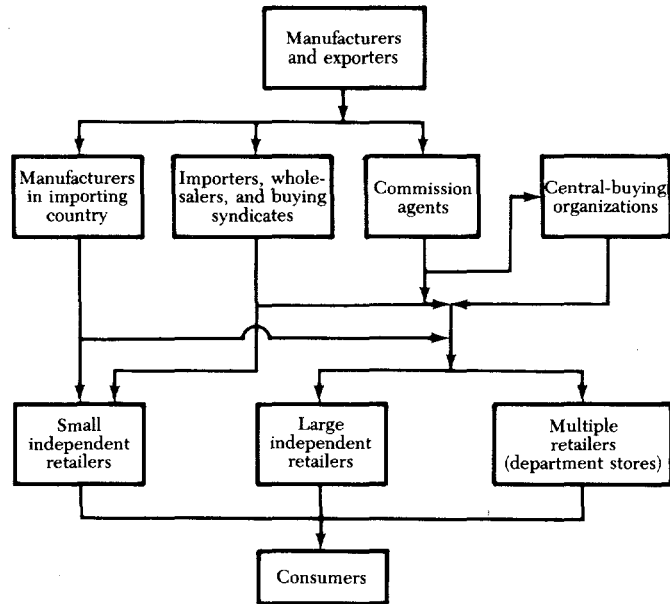
If the 807 scheme is used, the proportion of the consumer price received by the Colombian garment exporter is still lower. For example, one company receives \$3.65 for a jacket that retails in the United States for \$60; a second receives \$5 on a coat retailing for \$45 to \$65. One reason for these apparently extremely low returns to 807 sales is that the exporting firm receives payment only for the labor that it provides (but of course it does not have to pay for the fabric that it uses). A second reason is that, because U.S. retailers usually prefer not to get involved in 807, firms that choose or are forced to export under 807 have to go through an extra middleman (the importer-wholesaler or importer-manufacturer who conducts the 807 operation) instead of being able to

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percent (of the price to the consumer). The difference, of course, is only a matter of perspective.

28. The price that is paid by the consumer is not always unambiguous. The manager of one Colombian clothing firm showed us some computer-compatible price tags he had just received from his buyer in the United States, and which he was about to attach to his finished jackets. The typed price of \$120 had been crossed out on these tags and a "special price" of \$89.99 had been inserted in red ink.

Figure 7. Typical Distribution Pattern for Garments Imported to the United States under the 807 Scheme



Source: Adapted from International Trade Center (circa 1977).

sell directly to the department stores that eventually sell most of their goods (figure 7).<sup>29</sup>

Before examining how Colombian garment exporters might increase the share of the U.S. consumer price they receive, it is useful to look at a marketing schema developed by Wortzel and Wortzel (1979). Generalizing from a study of East and Southeast Asian exports, they argue that exporting firms in developing countries tend to pass through five distinct stages of marketing capability. In stage 1, the firm is discovered by

29. In men's shirts, for instance, department stores are responsible for 58 percent of total U.S. retail sales volume. Men's specialty stores (35 percent) and discount shops (5 percent) account for most of the remainder (International Trade Center, circa 1977).



an importer who is searching for new sources of supply. The importer makes all decisions with respect to product specifications; the exporter simply sells production capacity. In stage 2, the firm starts to search for importers to whom it can sell. It also begins to develop some internal design capability and to establish a rudimentary sales and marketing organization. By stage 3, the search for potential importers has broadened and become more systematic. The firm's principals make frequent trips abroad and may open overseas liaison and information-transmitting offices. The firm begins to participate in the determination of product specifications, and is able to show at least a rudimentary product line of its own (for example, men's shirts in a variety of styles and colors). In the big leap to stage 4, the firm makes the transition from marketer of production capacity to producer and marketer of its own products to its own specifications. It takes responsibility for shipping the product to the country of destination and for distribution to wholesalers or retailers within that country; it begins to use its own brand names rather than those of its buyers and starts to advertise and promote its products abroad; and it may set up its own overseas warehousing system. By stage 5, the firm has become undistinguishable from competing companies in the country to which it sells. Its strategy is to differentiate its products by branding, distinctive styling, and so forth.

According to this schema, a Colombian firm that wishes to increase its share of the price paid by the consumer has to make the transition from stage 3, in which it sells to an importer of some kind, to stage 4, in which it takes responsibility for shipping the product to the country of destination and for distribution within that country. Although the prospect of making such a transition is clearly an attractive one, as Wortzel and Wortzel point out, it also involves considerable risk. Whereas the stage 3 firm receives designs from its clients, produces only to customers' orders, and is paid through irrevocable letter of credit at the time of shipment, the stage 4 enterprise stands or falls on the basis of its own design capability, produces for inventory, and sells on open account. Even in East Asia, only a handful of the largest garment firms have made the transition to stage 4 for exports to the United States; in Colombia, none of the firms in the sample has yet done so. True, two Colombian firms have occasionally exported goods of their own specifications to the United States and have sometimes sold items bearing their own names as well as those of their clients (this has mostly occurred in lines such as women's dresses in which brand names are less important), but only two or three of the garment makers interviewed have advertised their products in the United States, and none has established a U.S. warehousing or distribution system.

The fate of the one Colombian firm in the sample that has made a serious attempt to break into stage 4 for exports to the United States and Europe illustrates just how difficult this transition can be. The main business of the company in question is making not garments but yarn. To promote the use of their yarns, the firm's managers hit on the idea of trying to revive the fashion among women of wearing hand-embroidered garments. Their idea was not only to sell such garments themselves, but also to encourage women in the United States and Europe to buy the company's yarns and to do their own embroidering. They therefore created a subsidiary company, employed more than 1,000 embroiderers, set up stands at several trade fairs, and produced an attractive, glossy brochure containing color photographs of some of their products. By late 1978, after two years of trying, they had had a great deal of success in the domestic market, but their total exports of embroidery-related goods amounted to less than \$20,000. They found that it is not easy for one Colombian firm, no matter how large, to create or revive a fashion abroad; that duties of 35 percent and more on imports of embroidered garments cause their products to be high-priced in the United States; that it is difficult to find a way of selling directly to boutiques (the natural outlet) because this type of store does not generally import goods directly itself; and that once their products finally get into a store, they tend to be displayed next to machine-embroidered garments from India, which are apparently identical in the eyes of most customers, but which sell for a fraction of the price.

By contrast with the situation for exports to the United States, in domestic sales and in exports to the Margarita Islands and the Caribbean, many Colombian clothing firms have attained, or are approaching, stage 4 or even stage 5. In these markets, most firms use their own original or copied designs, and sell under their own (or licensed) brand names rather than under those of their buyers. Some firms advertise their products and some have their own warehousing or distribution systems. For domestic sales, many of the largest firms own their own chains of retail stores, and a large proportion of the others bypass the wholesale stage and sell directly to retailers.<sup>30</sup> Although only

30. In a recent study of the Colombian clothing market conducted by the *Corporación Financiera Popular* (1977), 24 percent of the garment firms surveyed mainly sold directly through their own stores, and another 48 percent sold directly to retailers. For the Medellín area, Peláez (1978) put these two percentages at 13 and 37 percent, respectively. Retail markups in Colombia tend to be considerably lower than in the United States—33 to 50 percent or so instead of 100 percent.

a handful of firms have their own stores for sales in the Islands and the Caribbean, by selling through agents and commissionnaires, many are able to retain for themselves all but 10 to 30 percent of the retail price. This ability to capture a large fraction of the marketing profits is thus another attraction of exporting to the Islands and the Caribbean; when added to the high retail prices that rule in these markets, it helps to explain why some Colombian garment exporters routinely earn profits of 30 percent and more there (see, for example, table 21)—far more than they could hope to earn on exports to the United States.

### Nonprice Problems, Protection, and the Exchange Rate

Many of the nonprice problems discussed in this chapter, especially the inadequate performance of many Colombian firms on quality control and punctuality of delivery, are relevant not only to the question asked in Part Two of this study—Why has Colombia been unable to compete with East Asia in the difficult markets?—but also to a question posed in Part One—Why did Colombia's exports of clothing to the United States and Europe begin to decline after 1974–75? Some of the detailed reasons these nonprice problems have not yet been solved will be discussed in the next chapter. But one general, overriding point is that the combination of a relatively slow rate of devaluation and continued high protection against imports of apparel from abroad has caused selling domestically to be significantly more profitable for most Colombian clothing firms than selling to the United States (tables 43 and 44). If this profitability gap could be narrowed (by making exporting to the difficult markets more profitable or by reducing protection against imports), more local companies might be induced or forced to improve their performance in these crucial nonprice areas, and hence become more competitive in exporting to the difficult markets.

## Chapter 7

# Cultural Differences

*Hoist sail, my dear boy, and steer clear of culture.*

—EPICURUS

ONLY TWO OR THREE DECADES AGO, development economists routinely discussed the social and cultural determinants of development in some detail.<sup>1</sup> More recently, the tendency has been to state in a sentence that cultural factors are no doubt of some importance—and then to ignore them. The latter attitude has grown out of the realization that it is difficult to say anything either quantifiable or generalizable about the relation between culture and development, and that it is equally difficult, once cultural barriers to development are exposed, to do anything to change them. Better, it is felt, to concentrate on things that are quantifiable, and on changes of policy that are possible and can have some effect, than to ruminate on what might have been had things been different. To have heeded the warning of Epicurus would certainly have been the path of least resistance in the present study. Yet the possibility cannot be rejected that cultural factors have been at least partly responsible for the fact that Hong Kong, Taiwan, and Korea have had so much more success than Colombia in exporting clothing.

To investigate the role, if any, that cultural factors play in garment exporting, three simple models have been constructed. The first sets out the determinants of labor productivity in garment manufacturing; the other two analyze the determinants of reliable quality control and punctual delivery. Labor productivity, quality control, and punctuality of delivery have been chosen as the focus for these models because they are the three most important areas in which East Asian garment exporters have outperformed Colombians. I cannot stress too much that this is a first, highly inadequate attempt, and that the findings that emerge, no matter how baldly stated, should be regarded as hypotheses for further research rather than as firm conclusions. The analysis presents what is average or typical in the society—obviously, within all societies, there is a great deal of variation around the mean. Further, *no judgment is being made anywhere in this discussion about which cultural traits are desirable and which are not*. The questions being asked are: first, if a country

1. See, for example, Higgins (1959) and Hagen (1962).

wants to succeed in exporting garments, what are some of the ways in which cultural factors influence its ability to do so? Second, to what extent do cultural factors seem to have been responsible for the difference in export performance between Colombia and East Asia? In the following discussion, variables that are mainly culturally determined are italicized the first time they appear.<sup>2</sup> For readers who prefer equations, the three models are summarized in Appendix C.

### Labor Productivity

The productivity of labor (the number of garments produced per worker per hour) in a typical clothing firm in a given country depends on the skill of the workers; the intensity of the workers' work effort; the efficiency with which production is organized (this in turn depends on the skill and intensity of the managers' work effort, *and the degree to which the labor force is susceptible to organization and discipline*); and the quality of the machinery and its maintenance (for simplicity, this is taken to be the same in all countries, although machinery, especially for shirts, tends to be somewhat more modern in East Asia).

The skill of the workers in a garment firm depends on their manual dexterity, on the training they have received that is specific to the job, and on the number of years' experience they have had on the job. Manual dexterity, in turn, depends on *the physical characteristics of the workers* (in particular, the size and thickness of their fingers) and on *the generalized societal training in manual dexterity they have received*.

The intensity of the workers' effort depends on the average level of wages they receive and on the degree to which the wage is dependent on the number of pieces produced; their other assets (broadly defined to include, in addition to financial and other tangible assets, *the degree to which family or government support systems provide a form of insurance, the protection that workers have against being fired, and so on*); the physical environment in which work takes place (such as lighting and ventilation); the psychological environment in which work takes place (workers' morale and *the degree to which they identify with the goals of*

2. The expression "culturally determined" is used rather loosely throughout this chapter. In theory, "'culture' puts the focus on the customs of a people; 'society' puts it on the people who are practicing the customs" (Keesing, 1958, p. 30). In practice, I have not always managed to keep to this distinction. Some factors labeled cultural below might better be called genetic (for example, size of fingers); others, such as the ease with which workers can be fired, might rather be regarded as economic policy variables.

*the firm*); and *the place that money income has in the workers' scale of values in relation to the place of a relaxed and sociable work experience, an easy life, the approval of other people, and so forth.*

The skill of the managers depends on *their innate or culturally conditioned ability to organize*; their job-related training; the number of years' experience they have had on the job; and the degree of exposure they have had to modern organizational methods and techniques.

The intensity of the managers' work effort depends on the average level of wages or profits they receive and the degree to which their earnings depend on the number of pieces produced or on other performance criteria; their other tangible and intangible assets; and *the place of income or profits on their scale of values in relation to the place of a sociable work experience, an easy life, the approval of other people, and so forth.*

A full-fledged study of productivity would examine *all* cultural and other factors and would probably concentrate especially on how and why management differs from firm to firm and from country to country. But the purpose here is to focus solely on the eight culturally influenced factors and their differences across the countries being studied. The reason for focusing only on these variables is quite simply that, until now, they have usually been ignored in studies by economists.

#### *Cultural Variables in Labor Productivity*

Because of a long Confucian tradition of respect for authority, the degree to which the work force is susceptible to organization and discipline tends to be high in Korea. For similar reasons, it is also quite high in Taiwan and Hong Kong—but it is considerably lower in Colombia. Several interviewees in Colombia and New York described instances in which Colombian workers successfully resisted attempts to change production flows, seating arrangements, or the way in which items were sewn. The experience of a U.S. garment industry production engineer is representative. This man spent two years working as an importer-wholesaler with several Colombian firms trying, mostly in vain, to help them increase productivity, and thus export. In one shirt-making company, he said, “there were five women making cuffs, each using a different method. One of them was the most efficient, so I tried to get them all to do it that way—but they didn't stick to it. The five were not sitting next to each other, so you could not easily see if there was a backlog or buildup of cuffs—but they didn't want to move.” As the engineer pointed out, “This could not have happened in the United

States or East Asia. There you just say 'this is how it will be done,' and it is done."

Evidence from physical anthropology suggests that East Asians may indeed have smaller hands and more slender fingers than Europeans and, probably, than South Americans.<sup>3</sup>

All East Asians receive considerably more generalized societal training in manual dexterity than do Colombians. The use of chopsticks rather than fork and spoon as food conveyors, the widespread use of the abacus, and the precision required in calligraphy all condition East Asian workers' fingers to be particularly nimble.

It is considerably less difficult and less costly to fire an employee in East Asia than it is in Colombia. Several Colombian managers interviewed claimed that it is partly because they have no effective means of dismissing a worker who does not obey orders or who does not work hard that productivity is low.

From scattered verbal evidence, it seems that many East Asians, especially Koreans, identify quite closely with the company for which they work; the company, in turn, takes care of many of their needs. In Colombia, by contrast, the relation between employer and employee is more distant. One Taiwanese-owned, garment-making enterprise that was planning to set up operations in Barranquilla began by organizing the construction of employee housing on the premises but was soon forced to give up the idea because of worker opposition.

It is difficult, indeed, to measure empirically the innate or culturally conditioned ability of managers to organize their operations—yet the fact that for several thousand years China has been one of the most highly and effectively organized societies in the world might give managers raised in Chinese or Chinese-influenced cultures at least some advantage in this regard.

Finally, workers and managers in different cultures may differ considerably in the value they place on money income or profits compared with that placed on a relaxed and sociable work experience, an easy life, the approval of other people, and so on.<sup>4</sup> In several instances in which Colombian workers resisted changes in their work arrangements, they did so even though under the new method they were likely to earn a higher income. Some workers apparently valued their comfort and familiarity with the old ways more than the extra money; others feared

3. Coon (1970, p. 149).

4. In East Asia the desire to be respected (as a person who works hard) or the desire to do one's duty may be as important as money income in influencing how hard people work.

that under the new system they would have to work much harder; while still others did not want to leave the friendly and sociable work groups of which they were a part. Presumably, some managers might have had more success in overcoming such opposition had they involved their workers more in the process of implementing the proposed changes; but the possibility remains that, at least for some, the extra income to be earned would not have been considered sufficient to compensate for the dislocation caused by the change.

For managers, too, the place of money in the scale of values may be of some importance. A manager who values the approbation of his workers may sometimes retreat from proposed changes to improve productivity in the face of worker opposition, whereas a manager for whom profits are more important may not.<sup>5</sup> Immigrants who arrive in a country with little material wealth are noted for the relatively high value they tend to place on its accumulation; so it may not be coincidental that Hong Kong is largely populated by immigrants, for many of whom economic gain was a consideration in their decision to leave China, and that 40 percent of the top twenty-four exporting firms in the Colombian sample are owned or managed by Jewish or Lebanese immigrants or their descendants. (Such persons almost certainly constitute less than 1 percent of the total Colombian population.)

The nature of a people's system of values is relevant not only to the level of productivity likely to be attained, but also to the broader issue of the likelihood of successful participation in the rough, competitive, world capitalist market. Value systems can probably be placed on a continuum in this regard. At one end, Chinese and Chinese-influenced civilizations, though different from the archetypically capitalist U.S. and European civilizations in many important respects, have value systems which, at least after the fact, appear to some observers to be fundamentally compatible with capitalist aims. Thus, Geiger and Geiger (1973, p. 35) argue:

The great civilizations of India and of the other South and Southeast Asian countries influenced by it, or of the Moslem states of West Asia and North Africa, or of the many indigenous tribal societies of tropical Africa were all more profoundly divergent—although, of course, in widely different ways—from Western civilization than was that of China. In contrast to all

5. Though the evidence is of course highly subjective, my impression when visiting different Colombian plants was that a positive correlation existed between the degree to which the manager was respected or feared by the workers (as opposed to being liked or ignored) and the efficiency with which the plant was run.



of them, Western and Chinese societies—each in its own way—were more practical and rationalistic, more oriented toward achievement in this world, more disposed to physical and mental work as the preeminent—and not perforce simply the predominant—human activity, more inclined to save and invest, and more conducive to social mobility. The values, motivations and institutional constraints responsible for these similarities were different . . . But, they were not incompatible. A Chinese—or Japanese or Korean—given the opportunity to engage in Western-type economic activities did not find it psychologically too difficult to do so because—unlike many other Asians or Africans—he was already accustomed to think and act in ways that were substantially consistent with the motivational and conceptual requirements for successfully adopting Western techniques.

At the other extreme, some societies value spiritual matters more than material wealth, or at least regard material wealth and its attainment rather differently than do Western capitalist societies. For example, in parts of the Northern Province of Papua New Guinea, persons who die are now buried not only with their traditional forms of wealth, as in the past, but also with their transistor radios, portable record players, and bank savings books.<sup>6</sup> Such value systems are presumably not likely to be conducive to success in exporting manufactured goods in competition with the most efficient countries in the world.

Where does Colombia's value system lie on this continuum? It ought to be possible to adapt or devise some attitudinal tests to find out. In the meantime, three slender pieces of evidence suggest that it may lie at least a little distance from the U.S.-European-Chinese end of the continuum. First, although per capita incomes are now higher in Hong Kong, Taiwan, and Korea than in Colombia (table 24), the number of hours garment industry employees work a week in the East Asian countries (fifty to sixty or more) still tends to be higher than in Colombia (forty-eight). Second, the number of annual paid vacation days is greater in Colombia than in East Asia. In Hong Kong, there are six public holidays, and six days' annual vacation are now granted as well. In Colombia, by contrast, there are thirty-two paid vacation days—eleven for religious holidays, six for national holidays, and fifteen working days for annual vacation.<sup>7</sup> Third, there is evidence from the interviews that

6. Newton (1978). On other aspects of the attitudes of Northern Province people to material wealth, see also Morawetz (1967) and Newton (1979).

7. In part, the number of hours worked and the number of public holidays and vacation days is determined by legislation copied from the International Labour Office or from developed countries.

some Colombians believe it is partly because they place material wealth lower on their scale of values that they have a hard time competing in world markets. As the manager of one large clothing firm said, "The problem in Colombia is that this is a country of *mañana*, a country of fiestas. We never had to reconstruct this country like the Asians did after the War. We don't have a serious attitude to work and productivity. We like to have a good time while we work. There's not much that can be done about it. . . ." I repeat—to state that this is a problem *if* one wants to export clothing is not by any means to say that the values *ought* to be changed. Indeed, this manager went on to say, "I don't think we *should* do anything about it either. Our workers might be undisciplined like our traffic—you know, drivers stop their cars in the middle of the road to talk to each other—but it's better that way when everyone can do what he likes. I wouldn't like to live under the sort of discipline and policing that the Americans have even if it would make us richer."

In regard to the narrower issue of the role of cultural factors in explaining productivity differences among countries, one piece of hard evidence is shortly to become available. Elisabeth Allison of Harvard University is currently conducting a study of the tailored-clothing segment of the U.S. apparel industry, and has kindly consented to allow me to mention some of her preliminary findings. Among many other things, Professor Allison has collected data on the wages earned by workers. Piece-rates in this section of the industry are usually such that employees who finish a standard fourteen-week training program earn about \$4.40 to \$4.50 an hour. Yet one group of workers consistently earns about 30 percent more than this. The key distinguishing characteristic of this group appears to be neither age, nor sex, nor marital status—rather, it is that they are Koreans.<sup>8</sup>

### Quality Control

The percentage of a firm's exported garments deemed by buyers to be of unacceptable quality depends on the ability of the firm's managers and workers to maintain strict quality control and on the degree to which they perceive the need to maintain such control. The ability of managers and workers to maintain quality control depends, as does productivity, on the skill and intensity of work effort of workers and managers and on

8. The Allison study includes Colombian and other Latin American workers among its sample, and also includes the results of manual dexterity tests by nationality of worker. It is hoped that a fuller report of its findings will be available soon.

the quality and maintenance of machinery; hence, most cultural factors influencing productivity are also relevant to quality control. The ability to maintain quality control also depends on the quality of the inputs the firm is able to obtain.

The difference between current Colombian and East Asian quality control is probably explained in part by the lack of ability of some Colombian managers to maintain strict standards; this, in turn, may be in part due to the cultural factors enumerated above. But perceptions of the need for quality control may also differ. The degree to which managers and workers perceive quality control to be important depends on the extent to which exporting is profitable; the more profitable it is, the greater the incentive for owners or managers to discover that strict maintenance of quality control is a requirement of success. Also important are *the place of precision and neatness of finish in the artistic values of the society*, and the degree of exposure of managers to the quality norms of the countries to which they export. A comparison of traditional arts and crafts indicates, for instance, that micro-level precision and neatness of finish are emphasized more in Chinese and Chinese-influenced cultures than in Latin America.<sup>9</sup> It is probably not coincidental that almost all Colombian managers in the sample who have consistently maintained high quality-of-finish standards have lived in the United States or Europe for at least a year or two and hence have been exposed to norms different from the traditional local ones.

### Punctual Delivery

Consistent with quality control, the frequency with which garment exporters meet their delivery dates depends on their ability to do so, and on the degree to which they perceive that it is important to do so. But even more than in quality control, where the manual dexterity of workers plays a part, the ability to guarantee punctual delivery depends on the organizational skills of management: planning, implementation of plans, crisis intervention, and so forth. The degree to which workers are susceptible to organization and discipline is also significant, as is the extent to which workers identify themselves with the company and hence are willing to work long overtime hours if necessary to get out an order on time. The degree of punctuality with which domestic and

9. Of course, nothing is being said here about beauty; an approach to art that relies on broad brush strokes is often imprecisely finished in the sense meant here, yet may be exquisitely beautiful.

imported inputs are received, and the reliability of freight transport services, may also be significant.

The extent to which punctuality of delivery is perceived to be important depends on the extent to which exports are profitable (again, the more profitable exporting is, the more likely managers are to learn the requisites of success), *the degree of importance the society places on punctuality*, and the degree to which managers have been exposed to punctuality norms in the countries to which they export.

The difference in the punctuality of East Asian and Colombian clothing exporters is no doubt due in part to differences in the ability to guarantee delivery on time. The organizational ability of the average manager and the degree to which workers identify with the enterprise may also be important. In Korea it is not uncommon for selected employees to work around the clock for several days in succession if a report or job has to be finished urgently; in Colombia this is less common. The extent to which inputs are late in arriving probably differs also between the two societies; in Colombia the unreliability of domestic supplies, the customs clearance delays incurred when inputs are imported, and the lesser degree of reliability of freight transport services handicap even efficiently managed firms.

But partly, too, as a result of differing cultural norms of punctuality, perceptions of how important it is to deliver on time may well differ between Colombia and East Asia. In Colombia, for instance, a person who is invited for dinner at 7:00 p.m. and is on the doorstep at 7:30 p.m. has certainly arrived too early; unless "U.S. time" was specified, 8:00 p.m. or 9:00 p.m. would have been regarded as punctual. In much of East Asia, by contrast, 7:30 p.m. would be considered either late or on the borderline of lateness; while by 9:00 p.m. the guest is likely to have missed the meal. Nor, of course, is the difference in the concept of punctuality restricted to dinner invitations—the general Colombian relaxedness and East Asian precision with respect to time pervade most areas of life. As with quality control, almost all the managers in our sample who have consistently delivered on time are either immigrants or their descendants, or they are Colombians who have lived for at least a year or two in the United States or Europe and have thus been exposed to the attitudes to time of those cultures.

### Changes over Time

By nature, culturally influenced variables such as attitudes to quality control and punctuality of delivery might be expected to change only

slowly, if at all, over time. Yet outstanding counterexamples exist. As recently as the 1950s, "Made in Japan" was synonymous with shoddy workmanship—so much so that a presumably apocryphal story made the rounds that a Japanese city had been renamed Usa so that merchandise originating there could be stamped MADE IN USA. Compare the image of quality that is conjured up today by names such as Honda, Nikon, Seiko, and Sony.<sup>10</sup> During the last decade, the reputation of products made in Hong Kong and Singapore has similarly begun to improve.<sup>11</sup>

With respect to punctuality, it is only three decades since the Korean concept of time was more akin to that of Latin America than to that of the United States.

Finally, not fifteen years have passed since numerous, well-qualified social scientists expatiated on the cultural barriers to economic development in Korea—and on the reasons Koreans do not work hard. The following passages are representative:<sup>12</sup>

Confucianism influenced Korea together with Buddhism for over 2,000 years . . . it is evident that the Confucian ideal still overwhelmingly sways Korean social usages . . . The traditional idea of Korean Confucianism did not have much respect for technical and physical or manual labour but rather despised this. Laboring for material production could not have the qualities of being the gentleman. Labour was the job only for a workman. Therefore, industrial techniques could never be developed . . . Trade and commerce, without being esteemed, even nominally, had been regarded as the meanest sort of work . . . Such ideas of the Korean traditional Confucianism should be thoroughly eliminated to make way for the ideological bases for democratic and liberalistic modernization.<sup>13</sup> One of the principal virtues necessary for increased production seems to be *diligence*. Work should be liked, and labor should be respected . . . The traditional values of Korea, however, do not always encourage the virtue of diligence or the will to work . . . Confucians and Korean ancestors . . . advised diligence mainly in connection with mental work.<sup>14</sup>

10. It might be argued, however, that even in the 1950s the Japanese were capable of producing top-quality articles, but that they were simply producing the cheap, five-and-ten-cent merchandise their foreign buyers then wanted from them.

11. See, for example, "Store Execs Look to Hong Kong for Quality [in garments]," *Daily News Record*, September 17, 1979, p. 4.

12. For a fascinating recent account of the role of cultural factors in entrepreneurship development in Korea, see Jones and Sakong (1979).

13. Choi (1966, pp. 81–82).

14. Kim (1966, p. 119; emphasis in original).

Not only does there seem to have been a remarkable change in the Korean attitude in just over a decade,<sup>15</sup> but there also seems to be a discrepancy between the evaluations of the compatibility of Confucianism with development that were current in the mid-1960s and that of Geiger and Geiger of 1973. Maybe I should have heeded Epicurus after all.

15. One possible explanation of this apparently abrupt change is that Korean culture was always potentially compatible with rapid capitalist development, but that it was necessary to enter a period of political and economic stability and to "get the policies right" before this potential could be realized. If this hypothesis is credible, it is interesting to speculate on whether it might not have some applicability in Colombia and other parts of Latin America as well.

One critic suggests that the rapid changes in Korean punctuality and work attitudes may be a consequence of the rise in the level of formal education in the country during 1960-80. There may be something in this hypothesis. Yet it is interesting that several Latin American countries have education levels as high as Korea's—Argentina and Chile to name two (World Bank, 1979)—without having that country's punctuality and work habits.

*Summary, Conclusions,  
and Generalizations*





## Why the Emperor Buys in East Asia

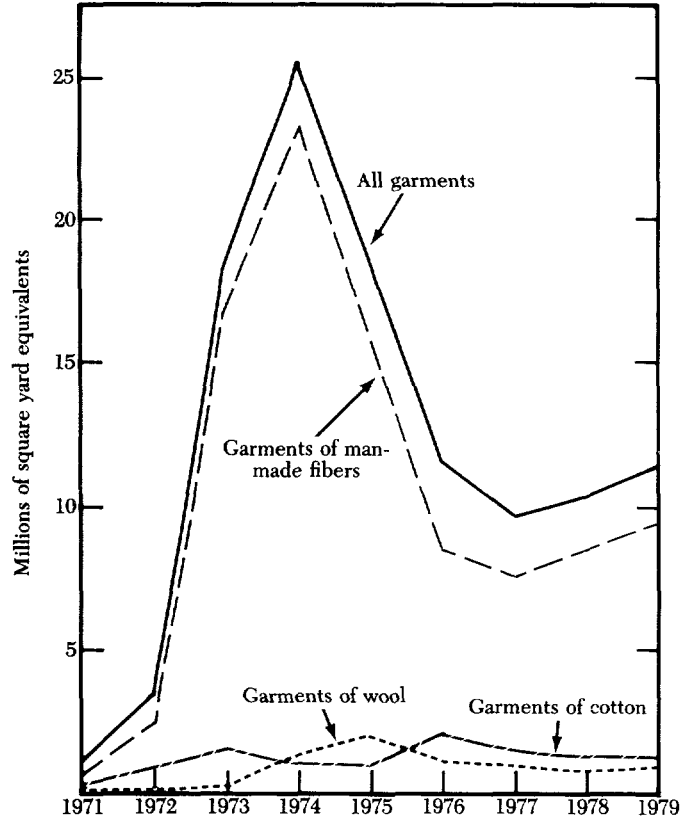
SINCE A DISTINGUISHING feature of this study is the amount of detail into which it has been possible to go, any summary necessarily omits at least part of what is interesting. Thus, in the interests of brevity, it is not possible to summarize here, among other things, the discussion of Colombia's fictitious and smuggled clothing exports, the reasons for the failure of intermediaries and consortia of small exporters, the distribution among U.S. buyers and Colombian sellers of the marketing profits from exporting, or the changes over time that have occurred in Korean attitudes to punctuality and physical work. Nevertheless, it is possible, and it may perhaps be useful, to bring together some of the more general conclusions.

Although the statistics on Colombia's clothing exports are highly problematical, the overall trend is clear. Before 1970 exports were negligible. Between 1970 and 1974-75 exports to all markets grew rapidly. After 1974-75 exports to Venezuela and the Caribbean continued to rise, but sales to the United States and Europe declined sharply. This decline leveled off, and there was a slight recovery, between 1977 and 1979; but the volume of exports during the first half of 1979 (converted to an annual rate) was still no greater than the after-the-fall volume of exports of 1976. The all-important pattern of Colombia's exports of clothing to the United States is illustrated in figure 8.<sup>1</sup>

By concentrating in this study on the rise and decline of Colombia's clothing exports to the United States and Europe, I do not mean to imply that exports to Venezuela and the Caribbean are unimportant. A dollar is a dollar, and neighbors' dollars are as good as anyone's. But exporting apparel to Venezuela and the Caribbean is little different from selling domestically: the same garments can be shipped on essentially the same terms. For exports to the United States and Europe, by contrast, competition is keener and prices are lower; quality control is tighter; lead times are shorter; punctuality demands are stricter; seasonal and fashion changes are more frequent and up-to-dateness in

1. The same figure appeared earlier as figure 4; it is reproduced here for convenience of reference.

Figure 8. Volume of U.S. Imports of Clothing from Colombia by Fabric, 1971-79



Note: For 1979 it is assumed that the percentage increase over 1978 is the same for the full year as it was for January to July.

Sources: Tables 8 and 9.

fashion is more important; and the sizes and shapes of customers differ from those in Colombia. In addition, since the Venezuelan and Caribbean markets are minuscule by comparison with those of the United States and Europe, and since Colombian firms have important transport cost and institutional advantages in their own region, it is clearly Colombia's sales to the United States and Europe rather than those to Venezuela and the Caribbean that determine the long-term health and future prospects of the country's garment-exporting industry. If present trends continue, Colombia may have to resign itself to being just another of the many also-rans in the international garment-exporting business; at worst, its exports of apparel to the United States and Europe might disappear altogether.<sup>2</sup> Eventually, if the roots of the problem are not tackled, Colombia may also begin to lose ground to its competitors in Venezuela and the Caribbean.

### Causes of the Rise and Fall

The most important single reason Colombia's exports of clothing to the United States and Europe began to grow rapidly after 1970 is that the government's exchange rate and export-incentive policies had begun to make them profitable. Before 1967 Colombian governments tended to tackle balance of payments problems by carrying out a jump devaluation, waiting until inflation had eroded its benefits, and then jump devaluing again. As a result, between 1953 and 1967 there were never more than two consecutive years in which the real effective exchange rate moved in the same direction.<sup>3</sup> This made exporting a risky business indeed, since a businessman could never be sure what his real returns would be from one year to the next.

From 1967 onward there was a dramatic and well-publicized change. As a result of the introduction of a crawling-peg exchange rate and other export-incentive measures, for the first time in more than a quarter of a century, the real effective exchange rate rose continuously, or at least

2. Colombia would not be the first country whose clothing exports to world markets first increased and then disappeared; Japan's exports of apparel to the United States rose from insignificance to dominance and returned to insignificance within fifteen years (Allison [1977]; and table 26). But in Japan's case, it was the rapid rise in domestic living standards, and hence labor costs, that forced it out of the U.S. market.

3. The real effective exchange rate is the nominal or official exchange rate adjusted for export incentives and for domestic and foreign price increases. In this study, it measures the relative profitability of exporting as opposed to selling domestically.

did not fall significantly, for six consecutive years. Not surprisingly, it took two or three years for this new policy to bear fruit. It took time for entrepreneurs to believe that exporting goods other than coffee and petroleum might be feasible and profitable and that this profitability might be maintained; time to adapt plant and equipment and retrain workers to meet the stringent requirements of export markets; and time for buyers to be found, orders received, goods produced, and an export momentum built up.

Then, in 1973, this time without any official pronouncement—on the contrary, government statements continued and continue to stress the importance of exports for the country's future—the post-1967 policy was reversed. For the next six years the real effective exchange rate underwent an almost continuous decline. Once again, it was two or three years until entrepreneurs perceived what was happening, believed that it was likely to continue, adjusted their plans, and either cut back their exports or switched them to easier neighboring markets. By late 1978, depending on the particular index chosen, the real effective exchange rate was either equal to, or 15 percent *below*, the level at which it had stood in the balance of payments crisis year of 1967. The 1967–73 improvement in the profitability of exporting in relation to selling domestically was totally reversed. The fall in the profitability of exporting is reflected clearly in the figures for effective protection for 1978. In that year, a firm manufacturing jeans, blouses, or shirts from domestic fabric received effective protection from the tariff and export subsidy system of 30 to 100 percent if it sold the garments in Colombia, compared with –32 to –62 percent if it sold them abroad.

Nonprice factors played some role in the *rise* of Colombia's clothing exports after 1970. Visits of U.S. buyers to Colombia in the early 1970s helped new exporters overcome some of their initial market-entry problems; the purchase by some Colombian companies of licenses to use foreign brand names helped these firms raise both fashion awareness and labor productivity, and hence increased their ability to offer up-to-date garments on world markets at competitive prices. But it was in the *fall* of Colombia's clothing exports to the difficult markets that nonprice factors played a crucial part. This role is discussed in the following section.

The leveling off or slight recovery of garment exports to the United States after 1977 has rested heavily on a handful of firms that appear to have been holding onto their hard-won U.S. markets for as long as possible in the hope that the profitability of exporting might improve in the future. Three of these firms, which accounted for half Colombia's

total garment exports to the United States in 1978, have special long-term arrangements with their U.S. buyers.

### Causes of East Asian Predominance

Whereas Hong Kong, Korea, and Taiwan have a combined population less than 2.5 times that of Colombia, the total value of the three nations' garment exports is 150 times that of Colombia. Colombian clothing exporters interviewed for this study generally blamed cheap labor, heavy government subsidization, or cheap transport costs for the difference. On all three counts they were wrong.

Because of rapidly rising East Asian standards of living, garment industry wages in Hong Kong are now 50 to 100 percent more than those in Colombia, while wages in Korea and Taiwan are at least not significantly lower than Colombia's. Government export subsidies are nonexistent in Hong Kong; in Korea and Taiwan they seem to be no greater than in Colombia. If, as is common, Colombians use air transport whereas East Asians ship by sea, Colombians have a significant advantage: they can land goods in New York for the same transport costs as East Asians but at a saving of four weeks in transit time. Since transport and communication services tend to operate more frequently and more reliably in East Asia, this advantage is offset, but only in part. Nor do U.S. import quotas explain East Asia's predominance; only in two narrowly defined product lines has lack of quota hampered the growth of Colombia's clothing exports, and then only since 1977.

The main price-related factors that do help explain the difference in clothing-export performance between Colombia and East Asia are labor productivity and fabric prices. On average, output per worker in the garment industry appears to be 30 to 50 percent higher in East Asia than in Colombia; as a result, Colombia's labor costs (wages paid per garment produced) are significantly higher than those in Korea, Taiwan, and possibly Hong Kong. Differences in the abilities of management, both top- and middle-level, seem to be of primary importance in explaining this productivity difference, but cultural and social factors may also play some role. The latter might include the degree to which workers identify with the goals of the firm, the degree to which they are susceptible to organization and discipline, the protection they have against being fired, the generalized societal training they receive in manual dexterity, and the place that money income or being seen to be doing one's duty holds on workers' and managers' scales of values in relation to the place of a relaxed and sociable work experience or an easy life.

In East Asia garment exporters are assured of duty-free access to top-quality fabrics at world prices. In Colombia, despite the fact that local textile firms export fabric and have done so for more than a decade, the prices clothing exporters must pay for domestically produced fabric are 50 to 100 percent above world levels. For cotton cloth, this is because the four large textile firms use their oligopoly power behind high protective walls to raise prices. For synthetics, the problem begins further back in the production chain with the too-small plants for petrochemicals and synthetic fibers, which also enjoy high protection and produce at high unit costs. The effects of the overpricing of domestic fabrics can be seen clearly in the breakdown of Colombia's clothing exports to the United States by type of material. Whereas more than 80 percent of the country's *textile* exports are of cotton, less than 20 percent of its exports of *garments* are of cotton.

The garment exporters' logical solution to this overpricing problem would seem to be to import fabric under the Vallejo Plan drawback arrangement, and almost all firms that export to the difficult markets do so; but administrative problems and delays reduce the scheme's value. At least two weeks' delay is incurred before an import request is approved by INCOMEX, and at least two to four weeks more are needed to clear the goods, once landed, through customs. Since the season in the clothing business is only twelve weeks, these delays are crucial. Together, they effectively nullify, and often reverse, the one clear advantage that Colombia has over East Asia in garment exporting: the ability to offer shorter lead and turnaround times. Since they are of unpredictable length, the delays also increase the risk involved in exporting. Garment exporters who wish to import fabrics that are also produced locally must submit a letter of approval from the relevant local textile firm; but garment makers are understandably reluctant to request such a letter for fear of retaliation. The export-processing zones (free zones), which ought to provide a solution to these problems, do not do so.

Among the nonprice reasons for Colombia's inability to compete with East Asia, differences in the degree to which quality control and punctuality of delivery are maintained seem to be the most important. The best Colombian firms meet these two criteria as well as any other firms; but the less than satisfactory performance of some Colombian companies has given the country a bad name and has contributed to the fall of the country's exports to the difficult markets. Some managers apparently do not perceive how important quality control and punctuality are for sales to world markets. This may partly reflect the fact that

quality control and punctuality norms in Colombia are rather different from those in the United States and Europe; which, in turn, may be partly because Colombian garment producers have been sheltered from import competition in the domestic market. The unreliability of domestic textile suppliers (both in quality and in the timing of deliveries), delays in importing inputs, and robberies in the ports all aggravate the quality control and punctuality problems.

U.S. garment buyers commonly point out that they can get anything they want in Hong Kong, Korea, or Taiwan—any garment, in any material (cotton, wool, synthetics, fur, or leather), at competitive prices, of acceptable quality, and delivered on time. In Colombia, by contrast, the range of garments and fabrics is limited, prices are in general higher, and quality and delivery times are less dependable. As a result, whereas many buyers maintain full-time purchasing offices in East Asia, there is not a single permanent foreign buying office in Colombia that specializes in clothing. This, in turn, makes garment exporting a riskier business for Colombian clothing firms than it is for East Asians; thus, few Colombian firms specialize in exporting, few foreign buyers come to the country—and the East Asia–Colombia gap continues to widen. Success breeds success, failure breeds failure.

Despite the apparent bleakness of the picture, it is important not to lose perspective. Only ten years ago, Colombia exported hardly any clothing, and few Colombians believed that exporting to world markets on today's scale would be feasible. If the apparently impossible could be achieved once, perhaps it can be achieved again.

### Policy Options for Colombia

If the Colombian government is interested in helping the country's garment exporters compete with East Asia, what measures might it take? First, it might try to ensure that exporting garments is made (and remains) at least as profitable as selling the same goods at home. To achieve this, the real effective exchange rate for clothing exports would need to be raised—this would at the same time help narrow the cost differential between Colombia and East Asia—and the government would have to commit itself and its successors to maintaining this real effective rate for at least five or ten years. Such long-term policy commitments are of course more difficult to make under the Colombian political system, which seems to require a biparty agreement, than under the systems that prevail in Hong Kong, Korea (at least until 1980),

and Taiwan. Protection against imported garments might also be lowered.

Second, clothing exporters would need to be assured of duty-free, minimally delayed access to a wide range of top-quality fabrics at world prices. Tariffs on imported textiles might be lowered, and the full range of fabric imports could be transferred from the licensing list to the free list. The Vallejo Plan might be streamlined so that approvals could be granted in twenty-four hours instead of two weeks; perhaps the requirement that fabric imported under this scheme be re-exported could be converted to a ton-for-ton basis. The ports and customs authorities would need to be overhauled to ensure that, once goods arrive, they are cleared in a day or two instead of weeks. The existing free zones might be studied to discover the reasons for their failure; new, improved zones could then be established. An indirect export subsidy might be introduced; domestic textile firms that sell fabric to garment makers, who in turn use this cloth in their exports, would then be entitled to receive the CAT for such sales, and perhaps PROEXPO credit as well. Indirect export subsidies of this type have been used successfully for important domestically produced inputs in Korea, Taiwan, and Israel.<sup>4</sup>

Third, since management ability seems to be crucial in both price (labor productivity) and nonprice (quality control and punctuality) areas, the government might try various strategies to improve the country's management. Large numbers of top- and middle-level managers and graduate students in business might be sent abroad for study and work experience and for exposure to U.S. and European standards of quality control and punctuality of delivery. Foreign buyers could be invited to Colombia to give short courses for managers and would-be managers, which would again emphasize the important, but often-neglected, nonprice aspects of exporting.<sup>5</sup>

It is difficult to rank these policy options in order of importance. As New York buyers repeatedly stressed, price, quality, and punctuality are all necessary conditions of export success in the clothing industry; the absence of any one of these disqualifies the would-be exporter from

4. On Korea, see Frank, Kim, and Westphal (1975); on Taiwan, Little (1979). Of course, granting export subsidies to local suppliers of exporting firms is a third best solution to the problem, and might cause controls and export formalities to become even more complicated.

5. A critic suggests that, since government-sponsored quality control institutes have had some success in East Asia, such an institute might be set up in Colombia. It is not clear, however, whether the benefits would outweigh the costs (additional red tape and administrative delays, increased incentives for corruption, and so forth).



serious consideration. If one set of implications had to be chosen as the most important, however, it would probably be that relating to price; for, if exporting were made more profitable, entrepreneurs and foreign buyers would have a strong incentive to overcome the quality control and punctuality problems on their own.

It has been argued in Colombia that the nation's governments have been right to allow the real effective exchange rate to decline since 1973. Inflationary pressures began increasing about that year, making a slowdown in the rate of devaluation apparently desirable, while the coffee bonanza of 1975 and later years has lessened the need for dollars to be earned by clothing and other manufactured exports. If and when coffee prices fall, this line of reasoning concludes, then the pace of devaluation can be resumed, and clothing exports will pick up again. Although this argument has some appeal, it contains two important flaws. First, clothing manufacturers learn from experience. They were drawn into exporting once and have now painfully begun to withdraw; they are likely to be less willing to invest the time, effort, and money needed to break into foreign markets again. Second, foreign buyers learn from experience too, with the result that it is sometimes more difficult for an exporter to regain a lost market (particularly if the market was lost for quality control or punctuality reasons) than it is to enter the same market for the first time. True, in itself, the lowering of the real effective exchange rate after 1973 influenced the prices offered by clothing exporters rather than their quality control or punctuality; but a price problem is often translated into one of punctuality since, in a squeeze, producers tend to deliver first to the markets they find most profitable. Buyers have the whole world to choose from; if they have been let down by Colombian suppliers once, they are likely to try many other possibilities before they return. If clothing and other manufactured exports are to be put on a long-run footing, therefore, a more appropriate response to inflationary pressures and balance of payments surpluses arising from high coffee prices might be to push ahead with the liberalization of imports (which helps on both fronts and aids manufactured exports as well), rather than to cut back on the rate of devaluation.

### Generalizing to Other Industries

The preceding policy implications were drawn up on the assumption that the Colombian government is interested in stimulating exports of clothing to world markets; but, of course, there is no particular reason to want to export *clothing* as opposed to any other commodity. It may be

useful, therefore, to examine the extent to which the conclusions and policy implications derived from this study are generalizable to other Colombian manufacturing industries. In the absence of similarly detailed studies of other industries, the following discussion is necessarily somewhat tentative.

Colombia's exports of other manufactured goods appear to have followed a pattern similar to that of exports of clothing to all destinations: a rapid rise through 1974-75 followed by a more modest rate of increase since those years.<sup>6</sup> The increasing importance of Venezuela as a destination also seems to be paralleled: by 1977-78 Venezuela had overtaken the United States as the most important single market for Colombia's total registered noncoffee exports.<sup>7</sup> The difference in order of magnitude between Colombia's exports of other manufactured goods and those of Hong Kong, Korea, and Taiwan is almost as great as for clothing.<sup>8</sup> Furthermore, Colombia's share of total U.S. imports under the U.S. 807 offshore assembly scheme is significantly *lower* for all manufactured goods (it never reached half of 1 percent during 1973-77) than for apparel (5 to 9 percent during 1974-76).<sup>9</sup>

Clothing is similar to other industries in which developing countries have achieved export success in that average wages are low, the share of wages in value added is high, and economies of scale are unimportant.<sup>10</sup> Garments tend to be differentiated from each other more than some other developing-country manufactured exports, but the marketing problems that arise from this differentiation are generally taken care of by the developed-country buyers. This all-important role of the buyers is by no means limited to the clothing industry; rather, it is common in many types of developing-country manufactured exports.<sup>11</sup>

The most important problems that have restricted Colombia's clothing exports seem likely to have affected other Colombian industrial export and potential export industries as well: a combination of high protection for domestic sale of final goods and declining real effective exchange rates that has caused the relative and absolute profitability of exporting, as opposed to selling domestically, to decline;<sup>12</sup> lack of access

6. Computed from table 4, col. 4.

7. FEDESARROLLO (1979, table 6); also Berry and Thoumi (1977).

8. Table 24.

9. Korea's share of total U.S. imports of all goods under 807 fluctuated from 30 to 37 percent during 1973-77 (Echavarría [1979]; and table 11).

10. Helleiner (1976).

11. Hone (1974); and table 46.

12. The real effective exchange rate deflated by general consumer prices shows a similar trend over time to that deflated by wholesale clothing prices (figure 5).

to inputs at world prices because of high protection granted to domestic input producers and because of problems with the Vallejo Plan, ports, and customs; and low labor productivity, inadequate quality control, and unpunctuality of deliveries resulting from management deficiencies and cultural factors. Clothing is also typical of other Colombian industries in the disproportionate importance of a small number of firms in total foreign sales;<sup>13</sup> the apparent inability of most small firms to export, whether alone, through intermediaries, or through consortia;<sup>14</sup> the failure of the free zones to stimulate exports (with the partial exception of manufactured metal products);<sup>15</sup> and the inability of local exporters to capture a significant share of total marketing profits.<sup>16</sup>

One difference between clothing and other industries is that since seasons are more important and fashions change more frequently in the case of garments, short lead times and punctuality in delivering are more important than in most industries. Nevertheless, no exporter of manufactured goods is likely to keep his clients for long if his deliveries are continually late or if his lead times are weeks longer than those of his competitors. For example, one U.S. manufacturer closed down an electronics assembly plant it had established in Haiti in favor of one in Mexico because, even though Mexican wages were more than double those in Haiti, the cycle time was two weeks shorter in Mexico.<sup>17</sup>

It might be thought that quality control is more important in apparel than in other industries—yet for many manufactured products quality control is extremely important. The damage that results if trousers shrink, colors run, or zippers break can hardly be compared with the consequences that would ensue if a lathe's cutting edge or an automobile's wheel nuts were defective. Indeed, there must be few manufactured goods in which quality control is not of primary importance. It might seem, too, that it is more important for exporters of garments to have access to a wide range of imported inputs than it is for producers of other goods—yet again this is not the case. Some 90 percent of all manufactured exports from developing nations originate in countries that guarantee their producers this kind of access.

Perhaps the most important difference between apparel and other sectors for the present discussion is that clothing is currently one of the few industries in which developing-country exports are subject to quota

13. Díaz-Alejandro (1976).

14. Bernhart (1973), Hjelm (1976, 1977), and Perry (1978).

15. Ministerio de Desarrollo Económico (1978, 1978a).

16. Wortzel and Wortzel (1979, 1979a).

17. Keesing (1978a).

restrictions. The distribution of quotas among exporting nations tends to be based on historical performance; thus, Colombia's garment quotas are only a fraction the size of those of Hong Kong, Korea, and Taiwan. This means that even if all obstacles to increased exports were removed tomorrow, Colombia could still look forward to only modest rates of increase in its exports of apparel to the United States and Europe.<sup>18</sup> This difference will not necessarily continue in the future; it seems at least possible that the increasingly protectionist developed countries will impose quantitative restrictions sooner or later on imports of other manufactured goods as well. These quotas, too, are likely to be distributed on the basis of past export performance—which underlines the urgency of the need for policy reform in Colombia if exporting manufactured goods is to continue to be a central focus of the national development strategy.

In sum, clothing shares several important characteristics with other industries in which developing countries have achieved export success to date; and the principal problems that have impeded Colombia's clothing exports in the past seem likely to have retarded the exports of other Colombian manufactured exports too. Thus, the findings of this study may well be relevant not only to clothing but also to other Colombian export and potential export industries.

### Generalizing to Other Latin American Countries

To what extent are the conclusions and policy implications of this study likely to be relevant to Latin American countries other than Colombia? In most relevant respects, Colombia is about as close to an "average" Latin American country as can be found. It ranks fourth after Brazil, Mexico, and Argentina in size of population, and fifth after these three and Venezuela in size of gross national product (GNP). It is neither among the most nor the least industrialized Latin American nations; in GNP per capita, it is poorer than many countries but by no means the poorest; the growth rate of its GNP per capita has been close to, if slightly below, the Latin American average for two and a half decades; and its distribution of wealth and income is typically skewed.<sup>19</sup>

18. The possible increases would be modest, but they would by no means be zero. To begin with, clothing exports could increase severalfold before all existing quota is utilized. After that, the successful East Asian strategy of upgrading items within quota categories (and hence increasing the value of exports while the volume is held constant) could be followed.

19. World Bank *Atlas*, 1977; and Morawetz (1977).

In total value of clothing exports, Colombia ranks equal third with Argentina behind Mexico and Brazil; in total value of exports of all manufactured goods, it ranks fourth behind Brazil, Mexico, and Argentina. In clothing exports per head of population, Colombia (\$2) is surpassed only by Mexico (\$3); while in per capita exports of all manufactured goods, Colombia (\$27) is surpassed by Mexico (\$38) and Argentina (\$37), but ranks ahead of Brazil (\$21), Chile (\$11), Venezuela (\$10), and most, if not all, other Latin American countries. By Latin American standards, therefore, Colombia has been at least moderately successful as an exporter of clothing and other manufactured goods; certainly, its inability to compete with Hong Kong, Taiwan, and Korea has not been unusual (tables 24 and 52).<sup>20</sup>

Colombia has been typical in the timing and nature of its policy changes: several other Latin American countries shifted from import substitution to export-promotion strategies during the mid- to late 1960s. It has also been about average for Latin America in its degree of political and policy continuity: some less democratic countries have had more stable economic policies, but others (Chile, Peru, Argentina, and Bolivia) have been much more unstable.

Many of the problems that have hampered Colombia's exports of clothing and other manufactured goods seem likely to have been similarly important in other Latin American countries. In the face of sharply fluctuating world prices for natural-resource-based exports and moderate to runaway domestic rates of inflation, few Latin American countries have managed to maintain constant real effective exchange rates (and hence constant real returns to exporting) for any length of time. In most countries, export subsidies were simply grafted onto the existing import substitution structure; since protection against imports remains high, the incentive to sell domestically is still greater than to export.<sup>21</sup> Many countries still hamper their firms' access to imported inputs when domestically produced substitutes are available;<sup>22</sup> and the port, customs, transport, and communications problems of Colombia are by no means unique.<sup>23</sup> Colombia's low level of labor productivity in garment production is typical for Latin America—if anything, Colombian pro-

20. One U.S. department store chain that sent a buying mission to Colombia did so because it deemed Colombia to be the best prospective source of garments in Latin America. A second U.S. chain that did a study of the desirability of setting up permanent buying offices in Latin America had Colombia high on its list of prospective locations.

21. Balassa (1978).

22. *Ibid.*

23. In Haiti it can take from one day to two months for imported goods to clear customs, depending on who the importer is (Thoumi, 1979).

Table 52. Per Capita Exports of Clothing and All Manufactured Goods: Selected East Asian and Latin American Economies, 1976 (dollars)

Area	Per capita exports	
	All manufactured goods	Clothing
East Asia		
Hong Kong	1,620	727
Taiwan	433	83
Korea	185	51
Weighted average	359	108
Latin America		
Mexico	38 <sup>a</sup>	3 <sup>a,b</sup>
Argentina	37	2
Colombia	27	2
Brazil	21	1
Chile	11 <sup>c</sup>	—
Venezuela	10 <sup>b</sup>	—
Weighted average	25	1

— Negligible.

a. Estimated including border zone, with the help of U.S. as well as Mexican data.

b. 1975.

c. 1974.

Source: Table 24.

ductivity is 5 percent above the Latin American average.<sup>24</sup> Some of the cultural characteristics that may cause Colombia's relatively inadequate productivity, quality control, and punctuality (for instance, the relatively relaxed attitude to time) are shared with much of Latin America.<sup>25</sup>

Colombia differs from much of Latin America in being ideally located to sell to the U.S. east coast market; but Central America<sup>26</sup> and the

24. Data supplied by a New York consulting firm specializing in the garment industry worldwide.

25. In Bolivia difficulties in standardizing quality control, among other things, have hampered exports of handicraft garments (Inter-American Development Bank, 1979).

26. Several Korean garment-exporting firms have attempted to sidestep the quotas that restrict their home-based exports by setting up operations in Central America, but they have been unsuccessful so far, apparently because of problems in obtaining inputs, whether domestically or by importing (Wortzel and Wortzel, 1979a).

Caribbean islands share this locational advantage, while Mexico has still easier access to the United States. The Colombian drug trade has distorted the nation's economy somewhat; but its main effect has been a domestic boom which exacerbates rather than causes the differential in profitability between selling goods domestically and exporting them. It seems unlikely that growers, processors, and smugglers of drugs would themselves be producing and exporting manufactured goods if the drug trade were shut off. Illegal sectors of economic activity are hardly unknown elsewhere in Latin America.

In sum, Colombia is in many respects an average Latin American country; its manufactured export performance has been quite good by Latin American standards; and many of the problems that have impeded its exports of clothing and other manufactured products seem likely to have retarded the manufactured exports of other Latin American countries too. Thus, the findings of this study may be relevant not only to Colombia but also to some other Latin American nations.<sup>27</sup>

27. Although it is beyond the scope of this study to go into the issue in detail, many of the findings may also be relevant to some developing countries outside Latin America. In the Philippines, where most domestically produced fabrics are not of export quality, garment exporters routinely have to import fabric, and imported goods can take three to six months to clear the ports and customs. In Thailand, a Taiwanese clothing entrepreneur who opened a factory complained that productivity is lower than in Taiwan and that absenteeism is high after payday. According to a U.S. buying office in Thailand, quality control (use of the wrong zippers, threads, and so on) is a problem there (Wortzel and Wortzel, 1979a).





## Appendix A

# Guide for Interviews with Colombian Clothing Exporters

1. *Basic data*
  - Name of firm
  - Name and title of interviewee
  - Date of interview
  - When was the firm started?
  - Any foreign affiliations? (Ownership, licenses, trademarks?)
  - Background of owners/managers? Any employment with MNCs [multinational corporations], overseas education, travel, etc.?
2. *Size of firm*
  - Size of firm when started? (Number of employees, value of sales).
  - Size now? (Same data including numbers in sewing, cutting, administration, export, etc.)
3. *Products sold in domestic and export markets*
  - What products did you start with in the domestic market? High fashion or not?
  - When did you first export?
  - What products did you first export? Were they earlier produced for the domestic market? High fashion or not?
  - Changes over time in products exported? Any clear trend in terms of price, quality, value added, product specialization, etc.?
4. *Value of exports and percent of output reported*
  - Value of exports 1968–78? (including Cúcuta, Maicao, Ipiales, etc.)
  - Destination of exports over time by products?
  - Percentage of production exported at first? (Including Cúcuta, etc.) Evolution over time?
5. *How did you first discover the possibility of exporting and to whom do you sell?*
  - How did you first discover the possibility of exporting? Did you seek out buyers or vice versa? If you sought them, how did you find them? What about for more recent exports?
  - To whom was the first export sale made: to a foreign parent company, manufacturer, retailer, importer-wholesaler, or inter-

- mediary; to a Colombian intermediary; through PROEXPO; or in some other way? (Specify.) What about subsequent sales?  
 —Names, addresses and phone numbers of buyers (to interview them).
6. *Buyer relationship*  
 —How stable is the buyer relationship? How many years has it existed?  
 —Have there been many changes over time? Why? Are you satisfied with the buyer relationship and with the price received? Suggestions for improvement?  
 —Degree of dependence on one or two buyers? (Percentage of exports? Percentage of total production?) What if they shift to someone else? Have you tried to diversify markets? How? How do you maintain contact with buyers? Visits, agents, telephone, telex, mail? Changes over time? Problems?
7. *Sources of information on fashion*  
 —What are your main sources of information on overseas fashion trends and export possibilities? Trips overseas, visits of foreign buyers, market research, trade and fashion magazines?
8. *Product specifications and design*  
 —Who set the product specifications for the first export? How were they tested, by whom, where? Any problems initially? (Fabric, cut, sizes, collar stays, lapel inners, colors, labeling, packaging, etc.)  
 —What about for more recent exports?  
 —Did the customer help with specs initially? How?  
 —Did he help with export formalities, etc.? What about for more recent exports?  
 —Who did the designs and cutting initially? What about now?  
 —Have you used any of your own designs in exported products?  
 —Do you have or have you had contracts with foreign designers? Have any other firms in Colombia had any? Has this been important? In which products?
9. *Size of orders*  
 —What was the size of your first export order? Percentage of production capacity?  
 —What about later orders?  
 —Have you received any orders that were too large for you to fill alone? What happened?  
 —Which came first—the export orders or the production capacity?

10. *Prices and profitability in domestic and export markets*
- How do you settle on the price with a customer? What is the process?
  - What was the price for the first export? Did you make money on it?
  - Percent? Changes over time?
  - Is there anything you can do to influence the export price? (advertising, brand name, etc.)
  - What are the domestic and export prices (ex factory and f.o.b.) for the items that you export? (for effective protection calculation). Which is more profitable—selling domestically or exporting? What about after you include CAT, Plan Vallejo, PROEXPO credit, etc.? By what percentage do these increase the export price received in pesos? If domestic sales are more profitable, why do you export at all?
  - Have there been any changes in the relative profitability of domestic and export sales over time? What caused them?
  - Have there been changes in the proportion of your output sold domestically and exported over time? What are the reasons for these changes?
  - How severe is competition in the domestic market in your line? Where does it mainly come from: locals, imports, contraband imports?
  - How would it affect you if the government liberated clothing imports and reduced tariffs? Would you have to export more?
11. *Nonmonetary benefits to exporting*
- Are there nonmonetary benefits to exporting? Government help in receiving import licenses or in other ways? Prestige and image for domestic sales? Overseas travel?
  - How important are these nonmonetary benefits of exporting relative to monetary benefits?
12. *Inputs—domestic and imported. Vallejo Plan*
- Do you have any problems in buying inputs locally—fabrics, buttons, collar stays, etc. Quality and design? Price? Availability?
  - How does the domestic price of fabric compare with the import price?
  - Changes over time?
  - If you want to import inputs, can you do so easily? Delays? Changes over time?
  - Do you use the Vallejo Plan? If so, which version? If not, why not? Changes over time? Comments?

- Have you had any problems with INCOMEX, customs? What?
  - Have there been any significant changes in the extent to which you have used imported inputs over time? Which? Why?
  - Have you had any problems in obtaining packaging and printing materials locally? Quality? Price? Availability? Have you imported any of these?
  - Changes over time?
  - When producing for export, do you have higher input or other costs?
  - Do these increased expenses pay for themselves in increased profits?
  - What percentage of your total costs are value added?
  - What percentage of total costs are labor costs?
13. *Labor and productivity*
- Do you have any problems in finding skilled labor? Export personnel?
  - Labor troubles, strikes?
  - Do you have any problems with labor productivity? Have you done anything to increase it? When? What? Is there anything more that could be done?
  - What is the number of shirts, jeans, etc., produced per person per day?
14. *Capacity utilization*
- What is the average number of hours worked per day in your firm?
  - Number of days per week?
  - What percentage of full capacity is utilized now? In previous years? Is there much variation from season to season?
  - What is the number of paid holidays per year? Did your firm work on Friday after Independence Day (12 October) this year? (the puente).
  - How common are puentes?
15. *Production process changes*
- What changes have you made in the production process, since you began exporting?
  - Degree of mechanization?
  - Type of materials used?
  - Organization of production flows?
  - Did these changes happen because you now export?
  - Who initiated or suggested them—you or your clients? When? Why?

16. *Transport—internal and international*

- What means of transport do you use for your exports? Air, sea, road, rail, combination? Problems with parts delays, pilferage? Satisfied?
- Do you have detailed data on transport costs to particular overseas markets by air, land, or sea?

17. *Role of government*

- Do you receive help from the government in exporting? CAT, Vallejo Plan, PROEXPO credit, PROEXPO marketing help, Free Zone (Zona Franca)? Satisfied?
- What do you think of the government's devaluation policy?
- Does the government pressure you to export?
- Does it make exporting difficult in any way? Red tape, etc.?
- What could the government do better than it does now? What else could it do?

18. *Quotas*

- Has the existence of the quota affected your decisions about exporting at all? How?
- Has it affected the number of pieces of each product that you export?
- Would you sell more if there were no quota? To whom? Have you had to turn down any orders because of quota? For what? To whom?
- Has the quota changed your product line or mix at all? If so, how?
- Fewer or more products? More expensive products? Diversification into nonquota businesses? Transfer manufacturing to non-quota countries?
- How is quota distributed among firms?
- Can it be bought and sold? If so, how does the market work? Is quota for sale only when someone does not have a lot of orders? Are there quota brokers?
- How well or poorly is quota administered? Changes over time? On U.S. end? At home end? What are the administrative problems if any?

19. *Consortia (members and former members only)*

- Have you ever been a member of an export consortium?
- Did you benefit in any way? (Found new markets, accepted orders which would otherwise have been too big?)
- Were you satisfied with the consortium?
- Why did the consortium collapse?

- Did buyers choose to place orders with particular members? Why?
- Was there a problem that some members were not exporting at any given time and did not want to bear overhead costs?
- Was there a problem with distribution of production quotas?
- PROEXPO's role?
- What happened to other consortium members?
- Do you think that consortia are feasible? Suggestions?

20. *Intermediaries*

- Have you ever exported through an intermediary?
- Did you benefit in any way? (Found new markets, accepted orders which would otherwise have been too large?)
- Were or are you satisfied with the intermediary? If not, why not? Problem of profit margins? If not satisfied, why do you continue (if you do)?
- Suggestions?

21. *Trend and volume of exports*

- Why did (you and) most Colombian clothing exporters not begin exporting until the early 1970s?
- Why has the growth of such exports slowed down so much in recent years whereas exports from Asia have continued to grow rapidly?
- Why do you think that Colombia has never managed to export more than US\$80 million of clothing in one year whereas Hong Kong exports US\$3,000 million p.a.?

22. *Plans for the future*

- How do you see the future prospects for your exports?
- What are the main constraints?
- What new products or lines would the firm like to get into? Why? For local markets, exports or both?
- Where did the idea for getting into this business come from? What analysis had been done?
- What are the marketing plans for any new products?
- What are the difficulties foreseen in developing these new products?
- How might they be overcome?

23. *Financing exports*

- How are your export sales financed? Letter of Credit, buyers, PROEXPO, banks? Changes over time? Comments on this?
- How is working capital financed? Problems with this? Suggestions?

24. *Financing growth*  
 —How has the firm's growth been financed? Profits, loans, new equity capital? Comments on this?
25. *Overseas distribution and retailing*  
 —How is your product distributed and retailed overseas?  
 —Under what name is it sold?  
 —What stores sell it? If selling to importer-wholesaler, who decides at which store it will be sold?  
 —What is the retail price overseas? (Percentage above ex factory or f.o.b. price?)  
 —How is the product promoted, if at all? (Agents, own efforts?)  
 —How satisfied are you with these efforts?  
 —Who are the main competitors in your line? From which countries?
26. *Overseas regulations*  
 —What are the U.S. or other overseas regulations concerning your product: labeling (composition of fabric, "Made in Colombia," care instructions), sizes, washability, flammability, etc.? Any problems with these? Any customer help?
27. *Advance notice for orders*  
 —How much advance notice does the buyer usually give you for an order?  
 —Is this enough time?  
 —Have you had any problems with providing goods on time?  
 —What is the length of your order book on average? At present?
28. *Wages*  
 —What is the average wage per hour/day/month for a seamstress?  
 —For how many months is this wage paid?  
 —What is the percentage of prestaciones sociales (social security, etc.) paid?
29. *Organization of the export function in the firm*  
 —Who is in charge of exports?  
 —Number and type of people involved?  
 —Changes over time?  
 —Do any of the people in the export section have overseas experience? What type?
30. *General comments*  
 —Do you have any general comments on the history of and prospects for Colombia's clothing exports?

## Appendix B

# Formulas for Effective Export Incentives

The formulas used to calculate the effective rates of subsidy implicit in the CAT, in subsidized PROEXPO credit, and in the Vallejo Plan draw-back scheme are derived below. In each case the effective subsidy is expressed as a percentage of the value of exports.

### 1. CAT

*Question:* What is the pretax taxable income ( $X^*$ ) that produces the same net income after taxes as that received by a firm exporting goods valued at 100 pesos which receives an export subsidy (CAT) and sells it at a discount ( $d$ ) in the market?<sup>1</sup>

*Definitions:*

$X$ = income from exports	(assumed to be 100 pesos)
$CAT$ = export subsidy	(assumed to be 10 percent)
$d$ = market discount on sale of CAT	(assumed to be 20 percent)
$t$ = rate of company tax	(assumed to be 40 percent)

<i>Before the 1974 tax reform</i>		<i>Pesos</i>
Income from exports	$X$	100.00
<i>Plus net income</i>		
from CAT	$+ CAT(1 - d)$	8.00
= Total pretax income		$= X + CAT(1 - d)$ 108.00
<i>Less exemption of CAT</i>		
from taxable income	$- CAT$	- 10.00
= Taxable income		$= X - dCAT$ 98.00
Taxes payable	$t(X - dCAT)$	39.20
Net income after taxes		
( = 108.00 - 39.20 )	$= X + CAT(1 - d) - t(X - dCAT)$	68.80
	$= X(1 - t) + CAT(1 - d + td)$	

Now derive the desired pretax taxable income ( $X^*$ ) and the implicit effective CAT ( $CAT^*$ ):

1. To simplify the analysis, it is assumed that the firm's costs of production are zero. The results are unchanged if this assumption is relaxed.



		<i>Pesos</i>
$X^*(1-t)$	$= X(1-t) + CAT(1-d+td)$	68.80
$\therefore$	$X^* = X + \frac{CAT(1-d+td)}{(1-t)}$	114.67
$\therefore$	$CAT^* = \frac{CAT(1-d+td)}{(1-t)}$	14.67

*After the 1974 tax reform*

		<i>Pesos</i>
Income from exports	$X$	100.00
<i>Plus</i> net income		
from CAT	$+ CAT(1-d)$	8.00
= Total pretax income	$= X + CAT(1-d)$	108.00
<i>Less</i> taxes payable	$- t[R + CAT(1-d)]$	- 43.20
<i>Plus</i> tax discount of $t$		
times nominal CAT	$+ tCAT$	4.00
= Net income		
after taxes	$= X(1-t) + CAT(1-d+td)$	68.80

Thus, the real subsidy implicit in the CAT is the same as before the 1974 tax reform despite the change after 1974 in the way the CAT is treated for tax purposes.<sup>2</sup>

*Timing:* The above derivations ignored the fact that the CAT is not valid for paying taxes immediately it is received. The period before it becomes valid for such use varied from three to twelve months during 1967-78. The derivations also ignored the fact that the CAT is sometimes sold in the market only after a delay of from one to several months, and not, as is assumed above, immediately it is received. Defining  $n$  as the average number of years' delay before the CAT is sold ( $0.08 < n < 1.00$ ), and defining  $r$  as the market rate of interest, the above formula would need to be altered as follows if such delays are to be taken into account:

$$CAT^* = \frac{CAT[1 - d/(1+r)^n + td/(1+r)^n]}{1 - t/(1+r)^n}$$

The net effect of taking these delays into account would be to diminish the value of CAT\* to some extent. The delays are not taken into account in the present study because the necessary data are not available.

2. This is true for business enterprises but not for "personas naturales" and others who face different tax rates on their personal and business incomes.

## 2. PROEXPO credit

*Question:* What is the effective value ( $P^*$ ) of the subsidy that is implicit in the cheap credit that is provided by PROEXPO to exporters for six months?

*Definitions:*

$C/X$  = the percentage of the value of exports for which PROEXPO credit can be received (80 percent from 1973 onward, or 40 percent for users of the Vallejo Plan. For the latter, it is assumed that imported inputs account for 50 percent of the value of output).

$r$  = the market rate of interest (varied between 14 percent and 28 percent during 1967–78).

$r_p$  = the rate of interest on PROEXPO credit (18 percent from 1973 to mid-1977, 13 percent thereafter).

The effective subsidy implicit in PROEXPO credit ( $P^*$ ) is equal to the present value of what is received less the present value of what has to be repaid six months later. That is:

$$P^* = \frac{C}{X} \left[ 1 - \frac{(1 + r_p)^{1/2}}{(1 + r)^{1/2}} \right].$$

## 3. Vallejo Plan

*Question:* What is the effective subsidy ( $V^*$ ) that is implicit in the Vallejo Plan? An enterprise using this plan is exempt from paying tariffs and prior deposits on imports of raw materials or semifinished goods that are to be used in producing commodities for export.

*Definitions:*

$M/X$  = the percentage of the value of exports that is represented by imported inputs (assumed to be 50 percent on average for Vallejo Plan users).

$t_i$  = the average tariff on imported inputs (for fabric the rate declined from 69 percent in 1967 to 64 percent in 1978).

$dep$  = the average effective rate of prior deposits on imports (130 percent until early 1973, zero thereafter).

$m$  = the average number of months during which prior deposits were maintained at the Banco de la República (ten until 1972, five during early 1973, zero thereafter).

$r$  = the market rate of interest.

Then, following Teigeiro and Elson (1973),

$$V^* = (M/X) [t_i + dep. (mr/12)].$$

As for  $CAT^*$  and  $P^*$ , the absolute figures derived for the value of  $V^*$  are valid only for a comparison between an exporting firm that uses the incentive scheme and one that does not. The figures give an exaggerated idea of the absolute value of the subsidy to a firm that would not have been able to export in the absence of the scheme, since in this case part of the subsidy goes toward enabling the firm to lower the offering price of its exports. Nevertheless, since this study is mainly concerned with the changes that have taken place over time in the effective value of the different incentives, this problem is not too serious.

## Appendix C

# Models of the Determinants of Labor Productivity, Quality Control, and Punctual Delivery in the Garment Industry

Labor productivity

$$P_w = P_w(S_w, I_w, OR, (S_m, I_m, \overline{D_w}), QM) \quad (1)$$

$$S_w = S_w(M_w(\overline{C_w}, \overline{G_w}), T_w, E_w) \quad (2)$$

$$I_w = I_w(W_w, \overline{A_w}, PE, \overline{SE}, \overline{V_w}) \quad (3)$$

$$S_m = S_m(\overline{B_m}, T_m, E_m, N_m) \quad (4)$$

$$I_m = I_m(W_m, A_m, \overline{V_m}) \quad (5)$$

The variables are defined as follows. The subscripts  $w$  and  $m$  denote workers and managers respectively. "Managers" include both top- and middle-level managers. All variables relate to the average for the society. A variable with a bar above it is considered largely culturally determined.

$P_w$  = productivity of labor (number of garments produced per worker per hour)

$S_w, S_m$  = job-related skill of workers or managers

$I_w, I_m$  = intensity of effort applied to the job by workers or managers

$OR$  = Efficiency with which production is organized

$\overline{D_w}$  = susceptibility of the work force to organization and discipline

$QM$  = quality of machinery and its maintenance (assumed for simplicity to be the same for all countries)

$M_w$  = manual dexterity of workers

$\overline{C_w}$  = physical characteristics of workers (for example, size and thickness of fingers)

$\overline{G_w}$  = generalized societal training in manual dexterity that workers receive

- $T_w, T_m$  = specific training received by workers or managers in skills relevant to the job
- $E_w, E_m$  = years of experience on the job of workers or managers
- $W_w, W_m$  = reward (wage or profits) received by workers or managers (average level, and degree to which it is dependent on the number of pieces produced or other performance criteria)
- $\bar{A}_w, A_m$  = other assets of workers or managers (including tangible assets, insurance provided by family or government support systems, degree of job security, etc.)
- $PE$  = physical environment in which work takes place (lighting, ventilation, etc.)
- $\bar{SE}$  = psychological environment in which work takes place (workers' morale, the degree to which they identify with the goals of the company, etc.)
- $\bar{V}_w, \bar{V}_m$  = place of income or profits on the scale of values of workers or managers (in relation to the place of a sociable work experience, an easy life, being liked by people, etc.)
- $\bar{B}_m$  = innate or culturally conditioned ability of managers to organize
- $N_m$  = exposure of managers to new or modern organizational methods

Quality control

$$QC = QC(AQ, PQ) \tag{6}$$

$$AQ = AQ(S_w, I_w, OR(S_m, I_m, \bar{D}_w), QM, QI) \tag{7}$$

$$PQ = PQ(PR, \bar{SQ}, X_m) \tag{8}$$

Variables not previously defined are:

$QC$  = quality control (percentage of exported garments rated unacceptable by buyers)

$AQ$  = ability of managers and workers to maintain quality control

$PQ$  = degree to which managers and workers perceive the need to maintain quality control

$QI$  = quality of the inputs the firm is able to obtain

$PR$  = profitability of exporting

$\overline{SQ}$  = place of precision and neatness of finish in the artistic scale of values of the society

$X_m$  = degree of exposure of managers to quality control norms in the countries to which exports are sent

Punctual delivery

$$PD = PD(AP, PP) \quad (9)$$

$$AP = AP(S_w, I_w, OR(S_m, I_m, \overline{D_w}), PI, RT) \quad (10)$$

$$PP = PP(PR, \overline{SP}, Y_m) \quad (11)$$

Variables not previously defined are:

$PD$  = punctuality of delivery

$AP$  = ability of managers to guarantee punctual delivery

$PP$  = degree to which managers perceive the need to deliver punctually

$PI$  = degree of punctuality with which domestic and imported inputs are received

$RT$  = reliability of freight transport services

$\overline{SP}$  = degree of importance that the society places on punctuality

$Y_m$  = degree of exposure of managers to punctuality norms in the countries to which exports are sent

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