



Republic of Bulgaria  
ECONOMIC  
AND SOCIAL COUNCIL

## **OPINION**

**on**

### **PROBLEMS OF TEXTILE AND APPAREL IN BULGARIA**

(on its own initiative)

Sofia, 29 January 2005

On 13 November 2004 the Plenary Session of the Economic and Social Council took decision to draw up and adopt on its own initiative an Opinion on the Problems of Textile and Apparel in Bulgaria.

The Commission on Economic Policy that had been responsible for the preparation of the Opinion approved a draft of the Council's Opinion on 18 January 2005.

Mr. Kamen Kolev was appointed Rapporteur.

The Economic and Social Council approved this Opinion at its Tenth Plenary Session, held on 27 January 2005.

## I. INTRODUCTION

On 1 October 2004 the Economic and Social Council and the Council of European Integration signed an Agreement of Cooperation for the preparation of the country for the accession to the European Union. One of the main objectives of the Agreement is the dissemination of information amongst the structures of the organized civil society and the commitments assumed by Bulgaria in the accession negotiations and the rights and obligations for the Bulgarian nationals ensuing thereof.

In execution of the Agreement the Council, as a permanent institutional form of the social and civil dialogue and ensuring the consultations on the economic and social policy between the government and the civil society structures, has taken up an integrated approach. A review was made on the accession process referring to an individual professional group and its engagements evolving from all negotiation chapters. The Council has identified the textile and apparel sector as the first socio-professional group. Taking into consideration that many negotiation chapters contain the rights, obligations and commitments of the sector, the Council has developed an approach for preliminary identification of issues from the respective group in relation with the EU integration, which will be presented to the governmental institutions for the preparation of the responses.

The questions submitted to the attention of the Council are related with the problems, hardships, and challenges to the textile and apparel sector generated by the economic and social development of the country as well as by the integration of Bulgaria into the European Union.

Considering the above and recording:

- the long traditions of the textile and apparel sector;
- the contribution of the textile and apparel sector to the currency revenues and the high portion of the country's export;
- the difficulties facing the textile and apparel sector, resulting from the economic development of the country and the processes of the European integration and globalization, related with the liberalization of the sector in international aspect;
- the place and importance of the textile and apparel sector for the employment in the production sphere;
- the necessity of improving the institutional social dialogue between the organized civil society and the governmental bodies;

and on the authority of art. 5, para 4 and 5 of the Economic and Social Council Act,

The Economic and Social Council has taken decision to prepare an Opinion on the textile and apparel issues in Bulgaria.

The Council points out that the present Opinion is a follow-up from a number of meetings and discussions organized by the Economic Policy Commission of the Council with the

participation of experts in the field of the legislation and social practice on issues in the textile and apparel sector. The Opinion expresses the interests of the organized civil society considered in its nature of manufacturers, the employed and the users.

In the course of the discussions on the textile and apparel issues the views, standpoints, and suggestions of the branch (sector) organizations of the employers and employees were taken into account as well as many proposals made by institutions of the European Union and other International organizations<sup>1</sup>.

The Opinion of the Council aims at drawing the attention of the public and the governmental bodies to the problems and eventual potentials for the solution.

## **II. SHORT SURVEY OF THE ECONOMIC SITUATION IN THE TEXTILE AND APPAREL SECTOR<sup>2</sup>**

The transition to a market economy, the privatization and restructuring processes, combined with the general stagnation of economy in the past have had a negative effect on a large part of the sub-sectors of the light industry leading to the reduction of the physical volume of the manufactured products, the number of the employed, decrease in the receipts from sales of the production, the research-development-production link has been interrupted, and etc. It should be noted that a number of problems exist and face the textile and apparel sector whose impact can be chastened by the implementation of measures objectively needed and timely on the road to an intensive political, social and civil dialogue. One of the main goals of this dialogue is the creation of conditions for the sustainable development of the sector and the preservation of the job positions for over 20% of the active population in the country.

### ***Production***

Over 90% of the companies are occupied under scheme of the c.t.m. (cut, trim and make) production. At the same time many of them have their own registered product mark (1-3 product marks) and company chain shops throughout the country, which is an indicator for an improved competitiveness.

<sup>1</sup> Communication (communiqué) of the Commission to the Council, European Parliament, European Economic and Social Committee and Committee of the regions: "The Future of the Textile and Apparel Sector in the Enlarged European Union", COM(2003) 649, 29.10.2003;

Opinion of the European Economic and Social Committee regarding Communication (communiqué) of the Commission to the Council, European Parliament, European Economic and Social Committee and Committee of the regions: "The Future of the Textile and Apparel Sector in the Enlarged European Union", COM(2003) 649, CESE 967/2004, 01.07.2004;

Communication (communiqué) of the Commission to the Council, European Parliament, European Economic and Social Committee and Committee of the regions: "Textile and apparel following 2005 – recommendations of the Summit Group for textile and apparel", SEC(2004) 1204;

USAID Study "Adjustments of the Investors to the Competitive Advantages of Bulgaria", Eduardo Tugenhat, President of Carana Corporation, November 2004.

<sup>2</sup> Based on official data of the National Statistical Institute.

The sales for June 2004 compared with those during the same month of the previous year marked an increase as follows: for the production of textile and textile products, apparel excluded – 138,3%, for the manufacture of apparel – 119,5%; for the processing of furs – 104,3%. Exported production formed 62% of the sales receipts while the sales on the domestic market made 38% of the revenues.

### ***Investments***

The textile and ready-to-wear clothes sector are a good potential for development and employment. The biggest investors are Mirolio – Italy – textile, Rollman – Germany – apparel and dressmaking, Mazer Holding – Turkey – textile, “Demo – Bulgaria” – Greece – dressmaking, ADF – France – apparel/dressmaking. At the same time, for the period 1998 – 2004 the foreign investments in the sector were 226 million US dollars or 3,5% of all foreign investments in the country, hence the sector is not attractive.

### ***Export***

In 2003 the sectors realized 24% of Bulgaria's total export of and for the first half of 2004 – 26% where the apparel industry had the predominant share. In the commodity structure of the export in the first half of 2004 the groups of the raw materials, materials and consumer goods had the most important contribution increasing by 8% in comparison with the same period in the year 2003. This growth is due first of all to the positive changes in the apparel and footwear commodity group, which occupies 61% of the consumer goods export.

The export is oriented to different EU countries mostly to Germany – ready-made products and footwear, Greece – knitted fabrics and wear. Italy, France, and Portugal can be indicated as new markets. The export of textile materials to Poland and apparel to Hungary has increased significantly. 84% of the Bulgarian textile and apparel goods export is intended for the member states of the European Union (EU-25) and 10% for the USA and Canada.

### ***Employment and income***

At the end of June 2004 the employed in the branch were 193 575 – by over 12 thousand persons more than in 2003 or a 6% increase. They represent 32% of the employed in the processing industry and 11,3% of the employed in the material sphere.

The portion of those occupied in the apparel branch is quite large – 134 thousand persons. 85% of which are employed in small and medium-sized enterprises (personnel of 25 – 150 persons), involved in over 3 500 companies.

In the textile branch, incl. also the knitwear, the employed are 33 thousand persons in over 700 enterprises.

The average work salary for the first half of 2004 was BGN 186, which is 72% of the average work salary for the country.

The labour productivity is not given deserved account of as a factor for determining the labour remuneration. The development of productivity considerably gets ahead of the work salary growth.

In the period 2000 – 2003 the textile and knitwear industry characterized with the following economic processes: “uneven” increase of the manufactured production by 77%, an increase of employment by 24%, growth of labour productivity by 42%, rise of the work salary by 4%.

The producers in the branch use mainly imported (90%) and in quite low extent local inputs intended for c.t.m. production and subsequent reverse re-export. Referring to the 2004 data of the National Statistical Institute, the increase of inputs and materials is less than 20% while the increase of the export in apparel is a little over 20%.

The main factors that will have impact on the development of the sector in the period 2005 – 2010 are:

- the low rates of economic growth in the countries within the euro-zone;
- the situation on the currency markets;
- the dropping off of the export quotas since 01.01.2005;
- the enlargement of the European Union;
- the building up of the Pan-Euro-Mediterranean free trade zone;
- the regulated reciprocal opening of the markets and strict observation of unified rules, without non-tariff barriers in order to ensure equal in rights trade with the big producers from Asia – China, India, Pakistan, and etc.;
- membership of Bulgaria in EU from January 2007.

The recognition of the main factors discloses the complex situation in the textile and apparel sector on European and world scale. These factors and processes have specific effect in Bulgaria, which may lead to a loss of markets, deterioration of the financial situation, insolvency and subsequent bankruptcy of a large number of companies, compulsory dismissal of work force that will bring about a drop of the GDP and an increase in the unemployment rate. In order to avoid the negative impacts it is necessary to undertake purposeful measures, initiatives and programmes, incl. on the part of the governmental bodies. The measures and programmes, taken up by many countries, producers and exporters of products and goods of textile and apparel, and also some of the more substantial problems of the textile and apparel sector in Bulgaria, give and serve as additional grounds for such proposals.

### III. BASIC CURRENT ISSUES IN THE TEXTILE AND APPAREL SECTOR

1. The restructuring of economy is accompanied also by **an abrupt reduction of the production of local raw materials** for the textile and apparel sector such as cotton, flax, and hemp, real silk, wool. This has in turn determined the orientation of a large number of

companies to use imported inputs, which in some cases led to the increase of the production cost and then to the rise in the end-prices of the products and goods. The competitive advantages of the companies have dropped down considerably and this caused the suspension of the operation of many companies. In 2002 more than 1000 small and medium-sized firms stopped their operation. The predominant part of the companies in the branch has taken up to make c.t.m. production providing them with comparatively guaranteed orders. Nevertheless, the c.t.m. working has also its negative dimensions such as:

- impossibility to define the strategic goals for the development of the companies and the branch;
- low payment for the work done;
- preconditions for overtime working, unregulated labour;
- ensuring competitiveness by low labour costs which are subject to incessant optimization;
- low value added export.

The c.t.m. work gives about 25% of the total export of textile and apparel. The import of raw materials worsens the effectiveness of the branch, makes it dependent on the prices at the international markets, and contributes to the increase of the total deficit in the foreign trade balance of the country.

2. The Economic and Social Council considers that **the non-regulated and uncontrolled import** of textile and apparel goods and products, the downgraded customs values constitute a serious problem that generates losses due to outstanding receipts in the state budget from customs collections, creation of conditions for unfair competition and discontinuation of the operation of a great number of companies, destructuring of the light industry, closure of jobs and lack of motivation for work.

3. The registration regime provided for in the Value Added Tax Act requires the attainment of 50 000 leva total taxable turnover for the last 12 consecutive months. At the same time as early as the beginning of their operation the companies do business that requires registration under the VAT. The basic foreign trade partners accrue the adequate indirect tax on the prices of their goods, services, and products because the registration limit is low in the countries of the Balkan region. For example, in Romania it is 500 euro. Bulgaria applies one of the highest registration limits in the region and this brings about an increase of the portion of the shadow economy and the foundation of companies with the purpose of VAT “draining”. This in turn affects the state budget, the free competition rules are violated, and a great number of enterprises and specialized commercial sites of VAT registration are closed.

The Council regards with great concern that preconditions are created for relatively unequal treating of the correct taxpayers at the expense of the incorrect taxpayers. In addition, the tax policy does not contribute to the technological renovation of the production, for “green field investments” and investing in human resources. These processes are one of the reasons for the lack of motivation for the setting up of large enterprises having their own trade network for Bulgarian textile products and apparel.

4. The policy for **encouraging the investments** gives priority to the big business over the small and medium-sized one, which in turn does not create good climate for attracting investments in the textile and apparel sector. This is characterized by reflux of foreign investments. Foreign investments in the branch are mainly “green field” or it is relied on the selling of enterprises, independent parts of them or long-term tangible assets at low cost, which defrauds both the shareholders and the state revenues.

Bulgaria has to invest considerable resources in order to makes its industries attractive to the foreign companies. The smaller producers dispose of limited potentialities and in short-term period they will lose their export production.

5. The Economic and Social Council notices with anxiety that the **connection between the governmental institutions and the representatives of the employers and employees in the textile and apparel sector has been broken**. The interaction between them is insufficient and it is reduced only to the level of preparing administrative regulations, which do not comply with the concrete problems facing the branch, do not record its specifics and potentials for development. The lack of effective dialogue, including also the lack of general strategy for the development of the sector, leads to the drawing up and adoption of regulatory and strategic documents by the state bodies, which are not coordinated on expert branch level and in some cases they bring about the creation of additional barriers and impediments for the operation of the companies. This, in its turn, conditions the lack of trust in the governmental bodies on the part of the owners, managers, and those occupied in the textile and apparel sector.

6. Serious occasions for concern are also the issues related with **the training and employment** of the work force in the textile and apparel sector. The Council is disturbed by the progressive tendency of outgoing young people due to lack of material facilities for their training, lack of opportunities for study practice and students’ internships in real production environment for acquiring the needed knowledge and skills. The gap gets still larger in the skills acquired by the work force in the educational system and the needs of the economy. Specific close-up of this gap is the impossibility to meet the needs of the companies whose activity is based on high technologies requiring close specialization of the human resources. The refusal of the employers to accept pupils and university students is quite influenced by the lack of regulations for practice and training, inadequate regulation for insurance against employment accident and life insurance in these cases as well as by the inadequate encouragement regimes for internships of school and university students.

7. The Economic and Social Council considers that the most important factor for the economic development of the sector is **the dropping off of the export quotas** since 1 January 2005 and the regulated reciprocal (mutual) opening of the markets, which involves the observation of unified trade rules, excluding the use of non-tariff barriers in order to ensure equal rights for trading with the large-scale producers from China, India and Pakistan.

The dropping off of the export quotas, without adequate taking up of measures and initiatives, will push down the competitiveness of the Bulgarian companies in the low market segments

due to the unrestricted import from China. Many countries, including Bulgaria, that compete on price levels shall be eliminated from the global market. It is possible that a considerable part of the small and even medium-sized companies can go bankrupt, because of decreasing the number of the c.t.m. orders. This will be accompanied by the following: approximately 40 thousand employed in the textile and apparel sector will go to the labour market, a drastic loss of markets for the textile and apparel producers, and impossibility for market competition. The lack of fair competition, the dumping import, the import of false and fraud marks deteriorate the image of the sector.<sup>3</sup>

The cancellation of the quotas will enable the multinational corporations (companies) to become more flexible and experience less restrictions regarding the movement between the different countries and suppliers. On the other hand, the suppliers themselves will compete each other.

The protectionist policies and practices in the textile and apparel industry applied by the industrial states have rich history, which may “impose” the implementation of new “concealed restrictive measures”.

8. The Economic and Social Council pays attention to the fact that the enterprises, incl. those in the textile and apparel sector, do not dispose of enough information about the commitments Bulgaria has assumed during the **negotiations for membership** in the European Union as well as the rights and obligations, engagements and requirements to the business and sector, to the employees, and etc. ensuing thereof. In addition it can be stated that adequate foreign trade information is not available regarding the trade agreements signed with the EU member–states and other countries. The assistance and the services rendered on the part of the governmental institutions are inadequate for the stimulation and development of the trade exchange with other foreign trade partners. The Council expresses its view and is convinced that the lack of information in combination with the absence of an effective social dialogue can turn out to be a “suspensory” factor for the development of the sector. And even it can cause the stoppage of the operation of a large number of companies producing textile and apparel.

9. The Council is united around the opinion that the rules and regulations of the European Union are not observed when related with the stages of the project cycles in the realization of **programmes and projects with funds from the European Union**. The organized civil society is not actively involved in the process of consultations when identifying the procedures for the implementation of and monitoring the funds used under the financial instruments of the European Union, incl. also for the programmes and projects directed to the textile and apparel sector<sup>4</sup>.

<sup>3</sup> Dumping is trade behaviour based on price discrimination and represents incorrect commercial practice against which the Bulgarian enterprises have to fight.

<sup>4</sup> See Joint Declaration of co-chairs of the Joint Consultative Committee EU–Bulgaria, issued on 19 May 2004, Brussels, related with the Participation of the organized civil society in the planning, execution, and assessment of programmes and projects funded by the EU.

#### **IV. Main Conclusions and Recommendations**

The Economic and Social Council,

After making a thorough analysis of the problems incurred in the textile and apparel sector;

After taking into consideration and discussing the statements and suggestions containing therein and made by the representatives of the organizations of the employers and the organizations of the employees and the textile and apparel experts;

And taking into account the opinion of the experts and representatives of the groups represented in the Council;

Executing the commitments set forth in the Agreement for cooperation between the Council of European Integration and the Economic and Social Council;

Guided by the rights and interests of the employers, employees and other structures of the organized civil society and in execution of its function and role of voicing the interests and will of the organized civil society and consulting the governmental bodies on issues of the economic and social development of the country,

Has made the following recommendations and suggestions:

1. The Council notices that Bulgaria disposes of a potential for the production of linen and cotton of high quality. Bulgaria has adequate arable land for the cultivation of flax and cotton and strongly needs cotton as input at the volume of 28 000 tons raw cotton per year; hence the Bulgarian economy is a serious market for this raw material. Systems for subsidizing its production are applied in the member states of the European Union. The practice is similar in other countries, which manufacture cotton and they are not EU members – they have set up and implement systems of incentives and subsidies for the production of raw materials for the textile and apparel. The Council notes, that since the beginning of 2004 Bulgaria has started to implement measures for subsidizing the flax and cotton production but they are absolutely insufficient and they are not an element in a synchronized policy directed towards the sector. Therefore the Council considers that after holding consultations with the social partners and all institutions participating in the decision-making process, it is necessary to formulate a purposeful policy in relation with the textile and apparel inputs. And further it will be necessary to work up sector programmes for the development of stockbreeding, sericulture (worm breeding), cultivation of flax and cotton, jointly with the governmental institutions, the social partners and other organizations of the civil society.

2. The Council is convinced that it is necessary to undertake adequate measures for overcoming the negative effects due to the dropping off of the export quotas since

1 January 2005, including also by pursuing a synchronized policy against the unregulated and uncontrolled import of textile and apparel goods and products.

In order to reduce the negative effects from unfair competition and/or dumping practice, the establishment of which is a long and complicated process, as well as for the export promotion, the Council recommends the implementation of the following measures:

- the import of textile products in Bulgaria has to be accompanied by certificates of origin and quality;
- introduction of a monitoring system for tracking the export volume till the end-user in order to track the taxable charges;
- a more effective use of the protection measures and instruments in accordance with the current regulations in this area<sup>5</sup>;
- introduction of measures for control, for non-admission of importing goods and products, manufactured under conditions which violate the International Labour Standards – the Conventions of the International Labour Organization and the Directives and Regulations of the European Union;
- implementation of the best practices of corporate social responsibility as a warranty for adherence to the minimum social, labour, and environmental standards;
- more implicit implementation of Protocol No 5, Bulgaria has ratified, regarding the inspections of suspicious import and levying sanctions as regulated for the prevention of customs violations in the import of undergraded costs;
- interaction between the customs officers and the representatives of the branch organizations for strengthening the control in the import and export of textile products;
- setting up and support for the operation of specialized laboratories for control and prevention of textile products;
- more efficient export promotion by applying administrative, financial and other instruments;
- specialized services by the governmental institutions and in particular by the foreign trade representations for the diversification of the production and the markets;
- transferring unusual state functions to the branch organizations.

The Council recalls that the import quotas' dropping off is not accompanied by an obligation of reducing the tariffs, the customs duties, and the taxes. In this respect the Economic and Social Council recommends to hold dialogue with the branch organizations from time to time about the eventual measures and other protection forms in observing the commitments set forth in the international documents, under which Bulgaria is a party, and the engagements assumed in the accession of the country to the European Union.

3. The Council considers that there is a potential at hand for making use of the mechanisms and instruments of the tax policy for the development of the economy and in particular the

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<sup>5</sup> Ordinance No 287 of the Council of Ministers dated 4.12.1996 for the protection against dumping and subsidized import of goods.

Ordinance No 300 of the Council of Ministers dated 16.12.1996 for protective measures for the import of goods in the Republic of Bulgaria.

textile and apparel sector. The Council recommends the consultations on the philosophy and parameters of the state budget to be preceded by discussions and taking up of mutually acceptable decisions in the following directions:

- dropping off the registration threshold under the Value Added Tax Act in order to place all economic subjects in equal position;
- introduction a gratis period for the payment of the value added tax for the companies processing agricultural products in the period from April including to September every year;
- exemption from profit tax that is reinvested in modernization and development of production;
- promotion of “green field investments”;
- alleviating the taxation regime for the social costs funds;
- tax encouragement of the employers for investing in human and social capital;
- development of state policy for the promotion of setting up clusters in textile and apparel.

4. The Council considers that it is necessary to pursue synchronised investment and tax policy which will create favourable investment climate for attracting foreign investors and stir up the local small and medium-sized investors. In this relation it is necessary to introduce new regulations which will stipulate the reduction of the barrier of 10 000 000 lv. to 500 000 (or the introduction of an additional threshold with considerably lower value of the present one) in order to use administrative reliefs for investments. The 10 000 000 lv threshold is extremely high for the small and medium-sized business in the country, which prevails in the textile and apparel sector. The general comprehensive approach requires also the planning of gratis periods or exemption from taxable profit during the first years of utilizing the investments.

5. The Council insists that emergency measures would be taken up for the building up of an effective database for the textile and ready-to-wear industry on the basis of which:

- to make economic and social analysis of the sector;
- to prepare and adopt strategic documents for the development of the sector, incl. in case of need – the adequate regulatory acts as well;
- to create and maintain a system for information exchange in relation with administrative procedures, regulations, programmes and projects on the financial instruments of the European Union.

6. The Council expresses its firm position that lawful guarantees have to be provided for the equal in rights participation of the representative organizations of the employers, of the representative organizations of the employees, and of other socio-economic partners in the activities related with consulting, identifying the problems and working up policies, instruments and measures for their settlement. The Council considers that institutional support is also needed for these actions by the establishment of an independent unit at the Ministry of Economy involving specialists in the field of light industry, incl. also ones from the

textile and apparel. In order to enhance the knowledge-based competitiveness of the textile and apparel sector, it is advisable to follow policies as for:

- analysing the professional qualification and professional competencies held in relation with the trends in the sector development and the future needs of work force possessing definite qualification characteristics;
- development of general qualification standards for the textile and apparel sector;
- integration of specialised curricular disciplines for the building up and formation of entrepreneur intelligence in the training programmes;
- setting up a network of educational establishments such as universities, colleges, technical schools, and etc. for the formation of a similar structure of the training courses;
- setting up a specialized technological center, which will realize also the connection with the European and world textile institutes and will contribute to the transfer of knowledge and technologies;
- introduction of normative regulations for internship and training of the university and school students and trainees at the enterprises in the textile and apparel sector.

7. The Council considers the use of all forms and institutions for social dialogue purposive, incl. also the Economic and Social Council. Thus the Council will keep the employers, employees and other representatives of the civil society adequately informed about the commitments and engagements assumed in the course of the negotiations for the accession to the EU and the rights and obligations ensuing for the country thereof.

The Council has pointed out the necessity of holding joint training together with the state and other institutions with respect to the implementation of the environmental standards, the requirements for occupational safety and health and certification under the SA 8000 standard.

8. The Council insists the EU rules will be adhered to in relation with the project cycle. The bodies and authorities that are in charge of the execution of the projects have to disseminate effectively the **information** amongst all nationals who might take advantage of the EU initiatives and in particular the measures pertaining to the innovations, enhancing and upgrading the competitiveness, the training, the employment of the work force and the development of the human resources. It is necessary to improve the **transparency** when making selection, assessment, tender procedures, negotiation, and monitoring under the projects. It is also needed to provide information about the funds supplied that have not been agreed upon. It is advisable to involve the civil society in the management of the structural funds, which will contribute to a better commitment between the plans and needs of the Bulgarian people and hence will **ensure their better utilisation**.

It is necessary to take up steps for making a complete and thorough survey prepared with the participation and involvement of all institutions and organizations concerned on the policies in order to identify the measures and actions for the enhancement of the competitiveness of the Bulgarian economy and in particular the competitive advantages of the textile and apparel sector.