The Recent Development of the Cambodian Garment Industry:
Global Firms, Government Policies, and Exports to the US

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This thesis titled

The Recent Development of the Cambodian Garment Industry:

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ABSTRACT

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The Recent Development of the Cambodian Garment Industry: Global Firms, Government Policies, and Exports to the US

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The shift of the garment industry from Japan to Newly-Industrialized Countries (NICs) and eventually to developing countries in Southeast Asia, including Cambodia, reflects a variety of factors that affect global firms’ strategies, international wage differentials, national government policies and trade negotiations. Over the past two decades, the Cambodian garment industry has grown significantly, ranking tenth among the world’s garment exporters in 2014. The development of the Cambodian garment industry was initially assisted by the Multi-fiber Arrangements (MFA) quotas and other preferential trade agreements imposed by developed countries like the United States and the European Union. In addition, the country’s average wage has been low enough to attract garment firms’ and their (sub) contractors’ production units away from other developing countries, including China and Vietnam. The incentives offered by the Royal Government of Cambodia have also played a key role in attracting foreign investment in its garment industry. Those incentives include Special Economic Zones, profit-tax exemption, and Technical and Vocational Education Training among others. In the 1990s, the Cambodian garment industry started out with a simple process named “Cut-Make-Trim”, which required minimal training for workers and little sophisticated technologies to operate. According to personal interviews with garment factories’ representatives in Cambodia, however, there has been a gradual upgrade to Full-package Format, which
involves fairly advanced technologies and qualities. Although the country’s garment industry is still facing challenges in its competition against other major garment exporters, its exports to developed markets are quickly growing and its position in the global garment value chain is certainly improving.
I would like to dedicate this thesis to my parents, sister, brother in Cambodia and my wife Brenda Young who have been the best supporters in my life for providing endless care and love to me during hard times here in the US. Without them in my life, I will not be who I am today.
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CHAPTER 1: INTRODUCTION

There is a tremendous variety of items that are being exported and imported every day in order to fulfill the demand of consumers in global markets. In international trade, the garment industry\(^1\) is a vibrant industry that brings income to developing countries through exporting garment products to global buyers in developed countries such as the European Union and the United States. The garment industry becomes significant in the global economy because the demand of consumers in fashion is rising among high and middle-income consumers in developed countries. Importantly, clothing is one of the fundamental desires of human beings. Trends in fashion and clothes become popular among high and middle-income consumers in developed countries because they tend to express themselves through their clothing. Nowadays, most of the clothes sold in developed countries are imported from developing countries that have low wages and abundance of labor. Also, Dicken (2011) argues that there are big shifts in the garment producers since China currently is ranked first in producing garment products, followed by Southeast Asia, particularly Vietnam, Cambodia and other South Asian countries, such as Bangladesh, Nepal, India, and Sri Lanka.

Cambodia became an Association Southeast Asian Nations (ASEAN) member in 1999, which was a great opportunity for the country to restore its economy after being isolated from international trade during two decades of political turmoil. Historically, Cambodia was in the Dark Age period from 1975-1979, which is known as “Democratic Kampuchea” and infamously known as the “Genocide Regime” under communism leader Pol Pot. However, after the first reform of the political economy in Cambodia in 1993, the

\(^1\)The garment industry in this thesis is interchangeable with textiles, clothing, apparels, footwear and accessories.
RGC transformed Cambodia from a socialist to a market-oriented capitalist economy, which aims to engage Cambodia in international trade. Importantly, the RGC has also implemented various strategies to attract foreign investors to invest in its manufacturing sectors. Due to the shortage of local entrepreneurs, Foreign Direct Investments (FDI) has played an important role in establishing Cambodia’s industrialization and economy. The vast majority of foreign investors that come to Cambodia tend to invest in its garment manufacturing.

Since the garment industry is one of the components in international trade that involves many countries, this thesis analyzes the geographical shift of the global garment industry to developing countries with particular attention to the recent development of Cambodia as a major manufacturing and exporting site. There are several factors, such as government policies, geographical preferences, demographics, low wages and technological innovation that have made Cambodia one of the world’s leading garment exporters. Since the US is the largest market for Cambodian garment products, the current research also looks into trade agreements and policies between the two countries. This research seeks to examine the following problems: 1) the development of garment exports from Cambodia to developed countries, specifically in the US during the past two decades; 2) the policies that Cambodian and US governments each have implemented to promote export-oriented garment manufacturing in Cambodia; 3) the challenges and opportunities that Cambodian garment manufacturers encounter in their effort to establish themselves as a major garment exporter to developed countries. In fact, it is particularly interesting to choose Cambodia as a case study country because garment products account for three quarters of country’s total commodity exports (CDRI, 2014, p. 5; Lopes-Acevedo &
Roberson, 2012, p. 247). A large part of the existing literature has concentrated on the relocation of garment manufacturers to the so-called Asian Newly-Industrialized Countries (NICs) including Hong Kong, Singapore, Taiwan, and South Korea (Staritz, 2010). However, the recent development of the garment industry in small countries like Cambodia is certainly under researched. In 2015, Cambodia became the ninth largest garment exporter to the US (OTEXA, 2015). It is a great achievement that Cambodia has made, considering the fact that the country started the garment industry as an infant industry in 1996. The development of Cambodia’s garment industry is also worthwhile for research and contributes greatly to the general knowledge on the pattern of the global garment industry, both preferential and bilateral trade agreements between Cambodia and the US have played a key role in global garment firms’ investment in Cambodia.

In order to properly address the research questions posed in this thesis, I have collected statistical data related to exports, imports, GDP per capita, and FDI from online databases such as World Bank, World Trade Organization, Asia Development Bank, Office of Textile and Apparel (OTEXA) and Garment Manufacturers Association in Cambodia (GMAC). Additionally, in order to analyze trade agreements and policies, I have collected policy reports from both Cambodia and the US. Those policies are extracted from government websites of Cambodia’s Ministry of Commerce, Trade Department, Economic Institution of Cambodia, Cambodia Development Research Institute, and United States Trade Representatives. Primary data collection is a core method in this thesis because it provides additional information regarding the current, up-to-date perspectives of garment manufacturers in Cambodia. Thus, I have interviewed ten
garment factory representatives in Cambodia by phone, email, and Skype. I have acquired their contacts from the Garment Manufacturers Association in Cambodia.

The thesis is divided into six chapters, Chapter one introduces the methodology, research questions and objective of the research. Chapter Two examines the existing literature on the global garment industry and how it has changed over in the past two decades. This chapter is important in providing concepts about the shifts in the garment industry including geography and technology shift of the garment industry, the value chain and the recent changes in the global garment industry. In Chapter Three, Cambodia is the main case study in this thesis so overall Cambodia’s economy and politics are analyzed by focusing on its recent industrialization. Chapter Three examines the economic incentives such as the Special Economic Zones, Cambodia’s Law of Investments, and others benefits offered to foreign investors. Chapter Four focuses on the development of Cambodia’s garment industry, which is classified into four phases, and the role of government policies in facilitating exports to the US. This chapter also discusses trade policies from the US government in favoring made-in-Cambodia garments. Chapter Five is based on personal interviews with Cambodian garment factories’ representatives regarding their perspectives on the challenges and opportunities that they have in competing with manufacturers in neighboring countries. Those garment manufacturers being selected in the interview are either contractors or direct suppliers to multinational clothing companies in developed countries. Finally, the concluding chapter summarizes research findings and provides policy suggestions for the future of the Cambodian garment industry and export diversifications.
CHAPTER 2: THE EVOLUTION OF THE GLOBAL GARMENT INDUSTRY

This chapter aims to provide overview of the global garment industry and the technology and geography shifts in the garment industry that have occurred in the past two decades. Additionally, this chapter includes the value chains of the garment industry from the production of raw materials to the marketing of the garment products. Chapter two additionally discusses the factors that the multinational corporations consider in investing in developing countries’ garment manufacturing, and the outsourcing criteria imposed by global buyers. Finally, the last part of the chapter covers brief data analysis on the garment trade between the US and Former Socialist Countries in Southeast Asia (Cambodia, Laos, and Vietnam).

2.1 Globalization of the Garment Industry

The garment industry has become one of the largest export industries in the world. As of 2014, in accordance with World Trade Organization (WTO) statistics, world exports of garments in 2014 reached US$797 billion (World Trade Organization, 2014). In the mid-twentieth century, garment products were locally produced to serve the demand of consumers in developed countries. As a result of globalization, trade has gone beyond borders as the size of the garment industry has expanded and switched from local to international and to multinational origins (Kunz and Garner, 2007 p. 3). The garment industry is the most labor-intensive industry with low-wage labor cost, in spite of significant improvements in technology and computerization aiding manufacturing. The garment industry provides employment to tens of thousands of people, especially women in the rural areas, most of whom migrate to the urban areas in order to search for low-skill jobs related to cutting, sewing and other easy garment-making activities. According to
Dickerson (1999), a nation’s garment industry develops through various six stages ranging from “embryonic to declining”:

1. The embryonic stage: industry scope is narrow and domestic-driven only and it is usually found in the poorest and least developed countries specifically in Africa. The process of producing garment products is simple and basic raw material export such as cotton is the main income-generating source.

2. Early export of apparel: Cut-Make-Trim is a simple process utilized in this stage of the garment industry because low wage labor requires low-skill workers to operate production lines. Exporting countries in this stage export low priced garment products to developed countries. Some countries at this stage are Nepal, Bangladesh, Sri Lanka, and several Southeast Asian developing nations, some South American countries and Caribbean countries as well.

3. More advanced production of fabric and apparel: garment production at this stage is upgraded and more technology-based, in which production becomes large in scale and more diversified. Trading characteristic is enhanced in export of fabric, clothing and synthetic fibers in a large scale. Example countries for this stage are China and India as those countries have developed advanced technology and industrialization.

4. The Golden Age Stage: The garment industry at this stage is increasingly expanding and does not produce locally in domestic country. At this stage, garment corporations start investing in developing countries by supplying ready-made fiber and fabric. Countries, (Taiwan, Hong Kong, and Republic of Korea) at this stage diversify their exports to other more technology-oriented items or high-value added items to the international markets.
5. Full maturity: The production at this stage is rather capital-intensive than labor-intensive although production keeps increasing as technology is more advanced. The United States, Japan and Italy are in this stage but they can be integrated into the final step of the development in global garment industry.

6. Significant decline: Offshore production increases dramatically at this stage. The garment industry is no longer a great source of income for the country’s economy. Export diversification focuses on heavy and capital-intensive industry and the garment manufacturing is shifted to low-wage countries. For instance, the United States is considered in this stage as well. (Dickerson, 1999, p. 141-144)

Regarding to the shift in global trade of the garment industry, there are gigantic shifts in both geography and technology in the garment industry, in which Asia and South America have become great exporters of garment products. Based on global shift of the garment industry, developing countries specifically in Southeast Asia focus on garment production as a typical “starter” toward export-oriented production, which essentially stay at the second stage (Early Exports of Apparel) (Gereffi, 1999, p. 40). However, Dickens’ six stages of the national garment industry that she had proposed in 1999 is a bit outdated, but still insightful in examining why certain countries have emerged as major exporters of garment products, while some others have lost their status in recent years. However, there has been current update on the nation’s garment industry stages, due to the upgrade in technology and increase in capital investments.
2.1.1 Shifts in the Garment Industry

Dating back to the eighteenth century, the garment industry became the leading sector for the industrial revolution, as there was a transformation from handmade clothes to the use of technical skills, and the creations of factories and mills in England, and later in the US (Dickerson, 1999, p. 48). In the US economic history, the garment industry was growing relatively fast among the 11 advancing industries during the eighteenth century in which there was a major increase in industrial productivity in the US (Hughes & Cain, 2011, p. 215-216). The garment industry was also initiated in Europe, particularly France, Germany, Italy and the United Kingdom. This is because those countries were influenced by the industrial revolution and innovation in various economic sectors. Later on, as countries grew to the maturity stage, the garment industry manufacturing process shifted to low-cost labor countries, sparsely allocated in different geographical locations around the world (Dicken, 2011, p. 304).

The first movement in the garment industry was in the 1950s when North America and Western Europe settled the production in Japan, which incurred remarkable exports from Japan to developed countries during that period (Dicken, 2011, p. 317). The shift in the garment industry basically relies on the proximity of the factory-based location to the exporting destinations. As the second shift in the garment industry took place, Japanese corporations established subcontracting arrangement engaging trade offshoring with Newly-Industrialized Countries (NICs) including Hong Kong, Singapore, Taiwan and South Korea. Low cost of labor was a favorable incentive and priority that triggered the Japanese firms to shift offshore to NICs (Dicken, 2007, p. 278). Another factor is the import quota policies imposed by major developed countries (mainly the US and EU).
NICs state governments’ policies weighed heavily in attracting Japanese firms and getting MFAs from the US, Canada and European Unions (EU). The role of the NICs’ government during that time was to attract investors as much as possible because the countries had shortage of capital to start gigantic ventures.

The third shift happened in the form of “Triangle Manufacturing”. “Triangle manufacturing” is a term utilized to describe the cycles of investment in the garment industry by NICs toward developing countries in Southeast Asia (Gereffi, 2002, p. 1) (Dicken, 2011, p. 323). Starting from the Japanese trading company Sogo Shosha, triangle strategies allowed the Japanese firms to move garment production to Hong Kong, Taiwan and South Korea during the 1950s. The Japanese firms coordinated the transfer of knowledge, logistics in machinery, and working capital to NICs. Later on, the US and EU were the potential buyers who placed orders with NICs manufacturers that established trustful relationship due to the quality of exporting garment products during the twentieth century. Then, as countries became more developed and labor costs increased rapidly, the NIC manufacturers mainly Hong Kong, Republic of Korea and Taiwan decided to move their factories and capital for investment offshores to low-cost labor and quota preference locations (specifically in developing countries in Southeast Asia, China, Guatemala etc). NICs have allocated preferences in setting up factories in different locations in developing countries. Hong Kong and Taiwan have developed good relationship with China and Southeast Asia, while South Korea mostly locates factories in Indonesia, Guatemala and the Dominican Republic (Gereffi, 1999, p. 60-61). The preferences are based on social and cultural criteria, which will be further discussed in the outsourcing parts. Due to the fact that technology, skills, capital are relatively low in developing countries, factories in those
countries are owned by NIC manufacturers, joint-venture partners or independent 
oversea contractors (Dicken, 2011, p. 269). The Triangle Strategy is finished when the 
final products are shipped back to destinations of the buyers (Dicken, 2011, p. 323). In this 
context, value chain will be discussed in the following section starting from the beginning 
of raw materials to final outputs. The recent shift toward developing countries in 
Southeast Asia is a good start for those countries to build their economies through the 
garment industry with low-cost operation, affordable start-up capital and simple 
technological operation. Moreover, the garment industry is an active sector leading to 
higher technological advancement in developing countries, by obtaining technical 
knowledge and skills applying within a sector or other sectors.

The development of the garment industry in developing countries specifically in 
Southeast Asia has been affected by major events. For instance, firstly, Most-favored-
nations or Multi-fiber Arrangements, which give special preferences to developing 
countries to export garment products under restraint policy, motivated NICs and 
developed countries to move offshore seeking low-cost countries that are granted those 
quotas. Multi-fiber Arrangement (MFA) was initially created by the US’ government in 
January 1974 with the core principal aiming to enhance trade relationship between 
developing and developed countries by giving rights to export certain amounts of garment 
items with a set price under any circumstances without alterations on the agreement 
(Dicken, 2011, p. 313). In addition, MFA is a type of policy that the US government 
implement in order to protect domestic firms in competing with the low-cost countries. 
The US applied the quota policies to different exporting countries with different volume of 
quotas for exports. Until 1981, it was estimated that 80% of garment imports to the US
were covered by bilateral quota systems with exporting countries (United Nations Conference on Trade and Development UNCTAD, 2005, p. 13; Krishna and Tan, 1997). In the MFA quota system, the quantities of garment items were distributed to exporting countries or foreign firms, in which quota rents were generated from this source and granted to the exporters or the government of foreign countries. Under Voluntary Export Restraints (VER), quotas were created under the agreement of exporting countries and proposed by importing countries (see Appendix A for graph illustration). As quotas restricted the imports to the country, price of garment products increased. In fact, the US incurred deadweight losses of up to 5 billion US dollars; on the other hand, foreign countries earned from import quota licenses from 2 billion to 8 billion US dollars (Feenstra & Taylor, 2008).

Secondly, MFA was phased out in 2005, which allowed developing countries to enter the competition in exporting garment products to developed countries under the Agreement on Textile and Clothing (ATC). Thirdly, the economic downturn in 2008-2009 reduced the demand of garment products, which led to the shutdown of some factories in developing countries in Southeast Asia as well as Caribbean nations.

Eventually, there is a change in sourcing strategies implemented by global buyers mainly to restrict the quality of products, processing time, costs, environmental protection, labor standard compliances, and access to raw materials. Global buyers imposed those sourcing criteria although they do not have direct involvement in manufacturing process (Staritz, 2011, p. 26). From the evidence in Table 1, we can see that top 15 garment exporters are largely dominated by Asian countries (61.7 percent share in the total garment exports in the world). China has dominated largely in exporting garment products,
which is equal to 38.6%. While developing countries in Southeast Asia such as Thailand, Cambodia, Vietnam, and Malaysia have 8.8 percent shares in the total world garment exports.

Table 1:

*Top Garment Exporters 2014*

<table>
<thead>
<tr>
<th>Exporters</th>
<th>2014 (billion USD)</th>
<th>2014 (percentage)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1 China (a)</td>
<td>187</td>
<td>38.6</td>
</tr>
<tr>
<td>2 European Union (28)</td>
<td>127</td>
<td>26.2</td>
</tr>
<tr>
<td>Extra-EU (28) exports</td>
<td>32</td>
<td>6.6</td>
</tr>
<tr>
<td>3 Bangladesh</td>
<td>25</td>
<td>5.1</td>
</tr>
<tr>
<td>4 Hong Kong, China</td>
<td>21</td>
<td>-</td>
</tr>
<tr>
<td>Re-exports</td>
<td>20</td>
<td>-</td>
</tr>
<tr>
<td>5 Viet Nam</td>
<td>20</td>
<td>4.0</td>
</tr>
<tr>
<td>6 India</td>
<td>18</td>
<td>3.7</td>
</tr>
<tr>
<td>7 Turkey</td>
<td>17</td>
<td>3.5</td>
</tr>
<tr>
<td>8 Indonesia</td>
<td>8</td>
<td>1.6</td>
</tr>
<tr>
<td>9 United States</td>
<td>6</td>
<td>1.3</td>
</tr>
<tr>
<td>10 Cambodia</td>
<td>6</td>
<td>1.2</td>
</tr>
<tr>
<td>11 Pakistan</td>
<td>5</td>
<td>1.0</td>
</tr>
<tr>
<td>12 Sri Lanka</td>
<td>5</td>
<td>1.0</td>
</tr>
<tr>
<td>13 Malaysia</td>
<td>5</td>
<td>1.0</td>
</tr>
<tr>
<td>14 Mexico</td>
<td>5</td>
<td>1.0</td>
</tr>
<tr>
<td>15 Thailand</td>
<td>4</td>
<td>0.9</td>
</tr>
<tr>
<td><strong>Above 15</strong></td>
<td><strong>435</strong></td>
<td><strong>90.0</strong></td>
</tr>
</tbody>
</table>

Source: World Trade Organization

Due to the fact that the garment industry is the main industry for developing countries to start up industrialization, garment products are largely exported by them. A number of factors have played a significant role in the shift of the garment industry to developing countries in Asia (mainly Southeast Asia) in the age of globalization. Firstly, the garment industry is a labor-intensive industry. Developing countries in Southeast Asia have a comparative advantage in labor, which is beneficial in producing garment products.
Secondly, the development of developed countries’ government policies to protect their domestic manufacturers as well as help developing countries becomes the main factor in shifting the garment industry offshore. For instance, the Multi-fiber Arrangement (MFA), which is one of the government policies, is highly considered by the foreign investors in moving the garment factory offshores. NICs were at first place granted quotas from the US but this would not help in increasing the exports because NICs already reached their quota limits (UNTACD, 2005, p. 13). As a matter of fact, quota restrictions did not help NICs once the countries had already reached the maturity age. However, MFA benefited developing countries in Southeast Asia because the garment industry was just kicked off and needed a lot of support from the US and EU by giving preferential trade agreements as an opportunity to strengthen the countries’ industrialization. For this reason, NICs take the advantages from preferential trade agreements by investing in developing countries, which received quotas access to the US and EU markets.

Third, low wages generate profits to the NICs multinational corporations by investing in the garment industry in developing countries (ILO, 2014, p. 14). The competition in clothing and fashion industry is very fierce in terms of prices. General assembly production requires a lot of labors, in which the cost of labor accumulates highly if the wages are not low. Thus, by moving factories offshore, the investors wish to benefit from low-cost labor countries while concurrently maintaining good quality of the products (ILO, 2014, p. 1).

In addition, foreign investors always search for incentives created by the government of developing countries. For instance, the governments in Asian developing countries that are the top garment exporters provide strong support to the foreign investors
with the hope to modernize their nation’s garment industry (Adhikari & Yamamoto, 2007, p. 209). Common incentives that are provided by the government in Asian developing countries are tax exemption on exports, the establishment of Special Economic Zones (SEZs), the deduction in the infrastructure costs and better improvement of transportation systems, and the ease of access to credits.

Finally, the development of global value chain shifts the garment industry from NICs to developing countries. NICs have upgraded their industry to higher standard and more technological advancement, which will be discussed in the following section.

2.1.2 Technology Shift in the Garment Industry

In addition to geographical shift in the garment industry, technology shift brings changes in the operations of garment manufacturing process, which is one of the main considerations in shifting offshore production throughout decades. Changing patterns of industrialization is extremely difficult for countries since firms and governments have to improve international trade networks (Gereffi and Tam, 1998). In the garment industry, switching from labor-intensive industry that relies heavily on simple technology to integrated manufacturing strategies such as Original Equipment Manufacturing (OEM) and Original Brand Name (OBM) Manufacturing is a major obstacle and require substantive technology for upgrading. OEM or full-package supply is a process targeting financing inputs and providing production services including finishing, packaging and delivering to retail chain stores (Gereffi & Frederick, 2010). Importantly, in OEM procedures, suppliers follow the orders from buyers in making garment products and reserving the brand names of the buyers.
OEM involves international buyers and local manufacturers to engage in upstream and downstream garment value chain production. OBM, on the other hand, focuses on producing and exporting original brand name by combining their manufacturing specialization and designing materials and sell into domestic and international markets. NICs have initiated a giant step moving from simple processing assembly activities in garment manufacturing called Cut-Make-Trim process (CMT). CMT contractors have to provide assembly services including machines, labor, and thread to sew garment products (Kunz & Garner, 2006, p. 21-22). CMT contractors do not own garment materials and products, however, they are paid to provide cut-make-trim services with expertise in production (Kunz & Garner, 2011, p. 136).

Due to the increase of labor wages in NICs, factory owners moved their factories and capital to invest in developing countries in SEA, Africa and Latin America. Those low-cost countries receive orders from NICs manufacturers to complete only simple process of CMT under the status as contractors. NICs manufacturers have to coordinate in upgrading final products in a full-package form through OEM or OBM (Gereffi, 1999, p. 39-40). Industrial upgrading brought NICs to specialize in high-tech jobs in making and designing the products according to the order from buyers, while sometime the buyers also assign the raw materials for suppliers too. As wages increase, NICs have to shift their simple manufacturing process to low-cost countries. Simultaneously, multilayer complicated sourcing strategies will be added toward developing countries and NICs still manage the roles in facilitating the flows of garment production in high-technology forms. It can be concluded that NICs still dominate the garment industry although they are no longer major exporting countries to the US and EU. Their roles in coordinating flow of
export are extremely important especially the transnational corporations investing in developing countries in Southeast Asia who are the main suppliers of garment products (Staritz, 2011, p. 29).

The combination of the above-mentioned factors has resulted in the list of the top 15 garment exporters that are mainly from Asian developing countries as shown in Table 1. As a result, Cambodia, which is furnished with all the factors, became the tenth largest garment exporters in the world.

2.2 Global Value Chain of the Garment Industry

According to Dicken (2011), there are three types of garment products that are circulated in the market, such as basic garments, fashion-basic garments and fashion garments (Dicken, 2011, p. 306). In contrast to producer-driver commodity chain, which focuses on large-scale production (i.e. aircrafts, automobiles, machinery, computers, semiconductors), buyer-driven commodity usually concentrates on the garment industry that employ great pool of labors. The buyer-driven commodity chains allow large retailers, branded marketers, and branded manufacturers to arrange production circuits in a third world, while importing back the finished goods following the demand of foreign market buyers (Gereffi, 1999, p. 43). In the garment industry, buyer driven commodity chain has a characteristic that decentralization is practiced allowing leading firms referring to NICs firms to design, market, set the price of garment products while the real manufacturing process is located in developing countries.

According to several sources (Gereffi, 1999; Dicken, 2007; Gereffi & Frederick, 2010; Staritz, 2011), final products are shipped to three important categorized buyers which determine on clothing selling prices on the markets.
1. Retailers, which historically produced and sold their own garment products, expand their markets as demand on clothing is increasing. Retailers are differentiated into two types (general and specialty clothing retailers). General retailers in the US are Wal-Mart, Kmart, Sears, Target, Macy’s, J.C. Penny, while in the EU include (Asda, Tesco, Marks & Spencer, Galleries Lafayette, Carrefour etc). Specialty retailers are those stores that have built up popularity in clothing and fashions and that include the US stores (Gap, American Eagle, Abercrombie& Fitch, Hollister), the EU stores (H&M, Zara, Mango, New Look, Arcadia and Benetton etc.). Retailers also sell their own brands as well as buying from marketers and branded manufacturers. Retailers determine their own prices with seasonal on sale discount and clearance prices.

2. Branded Marketers, also known as “factoryless” firms, refer to those large brand name corporations that design, market and brand their own garment products such as Nike, Hugo Boss, Gucci etc. The Branded Marketers’ role is to provide technical skills, knowledge to oversea suppliers in producing garment products complying with high quality standards. As competitors’ challenge became enormously in the garment markets, branded marketers, like Liz Claiborne, discontinued direct supports to manufacturers but rather gave this responsibility to contractors and subcontractors to deal with the rest of the production. Branded marketers have to follow the new trend of competition in global garment market by changing pattern of support functions including marker making, pattern grading and sample testing to the contractors, and allocating responsibilities in production
to the contractors. Thus, Branded Marketers have to choose the best contractors in order to outsource the products from them.

3. Branded garment manufacturers: used to have large in-house manufacturing factories but started to outsource in 1980s. Levi Strauss and Adidas are good example of branded garment manufacturers as they also established their own stores as well as factories in abroad. Branded garment manufacturers supply materials such as cut fabric, thread, buttons, and other trims to manufacturers in other countries such as Caribbean countries, China and Southeast Asia. In the United States and Europe, those manufacturers have an attitude that “if you can’t beat them, you join them”. However, these large firms already have raw materials in hand such as cut fabric, thread, buttons and trim. Factories abroad that accept CMT works from them have to assemble the products together and ship back by charging only labor costs and low tariff rates of imports (Gereffi, 1999, p. 48).

Before clothes could be sold in the market, the clothing value chain has to go through five different stages in which each process adds value to the item. The first stage is related to the supply of raw materials (i.e. natural fibers-cotton, wool, silk, and Synthetic fibers-oil, natural gas, power energy etc.). The second stage is the component network in which yarn and fabric production converts raw materials into component inputs in the production. The third stage involves in garment production, which is allocated to subcontractors in Asia, or Latin America. In this typical stage of production, the garment manufacturers in Southeast Asia adopt two types of production methods, which are CMT and Full-package (see figure 2). The garment manufacturers that practice CMT production method start firms as the assemblers. On the other hand, the garment
manufacturers that practice Full-package method start firms with high-end technology including research and development (R&D) and design capability. In Southeast Asia, countries such as Vietnam, Thailand, Malaysia, and Indonesia have already moved on to Full-package industry. Cambodia is still in the process of functional upgrading from CMT to Full-package (Staritz, 2011). After the final output is transferred from factory, export channels link those garment products to brand name apparel companies, overseas buying offices and trading companies. Finally, all garment outputs are distributed sparsely to retail outlets in department stores, malls, factory outlet etc. Importers, exporters, agents and trading houses, in the global garment value chain, play an important role in generating final products with quality and coordinate in delivering them to the global buyers (see Figure 1).

Figure 1: Diagram of the Overall Process in the Garment Industry.

Source: adapted from Gereffi and Frederick (2010)
2.3 Sourcing Strategies by Global Buyers in the Garment Industry

After the Global Economic Crisis between 2008 and 2009, global buyers only engage in business with suppliers whom they have already had long contact with and are capable in responding to handing back the final products on time. Thus, there are three types of suppliers that are listed by Birnbaum (2009). The first group of suppliers that the global buyers build good rapport with and consider the most important group is China, Vietnam and Indonesia. The second group is the countries that performed well during good time but not during the Global Economic Crisis, of which this group includes India, Pakistan and Sri Lanka. The third group is the marginal producers including Cambodia and Sub-Saharan African Countries. The marginal producers are mostly foreign-owned and affected greatly by the economic recession because buyers and intermediaries in the triangular manufacturing strategies moved orders to core suppliers. Sourcing strategies can be classified into two types-direct and indirect sourcing. Direct sourcing happens when
global buyers contact manufacturers abroad directly. Indirect sourcing requires extra channels, which involve importers, exporters, agents, trading houses and transnational manufacturers (Staritz, 2011, p. 29).

Sourcing strategies implemented by global buyers take two criteria into consideration before deciding on buying garment products from specific countries and firms. The first criteria is looking at the firm’s specific criteria that classically focus on production costs that suppliers incur, quality that suppliers are able to adhere to, and the level of trustworthiness on suppliers. Other criteria for firms to follow are lead times in production, flexibility, labor rules compliance, environment compliance, product development and design knowledge, logistics and financing, communication and merchandising (Staritz, 2011, p. 33). Labor compliance greatly influences the decision of global buyers whether to source from that firm or not. Codes of Conduct (CoC) were initiated by global buyers as a way to determine the level of compliance to labor standards and regulations. Labor problems pose a major concern to customers, who think corporate social responsibility is very important. There are a lot of boycotts from not purchasing garment products from some retailed stores such as H&M, Wal-Mart, etc. because of the rumors regarding sweatshops and the abuse of child labor. Thus, those retail stores pay heavy attention when sourcing the products from certain manufacturers in developing countries.

Aside from a firm sourcing criteria, global buyers also think about country’s condition before deciding to source the garments from specific countries. There are lists of specific criteria that buyers evaluate in order to outsource from specific countries.
1. Trade agreements and preferential market access: Global buyers tend to look at how country’s international trade interacts in the world market. There are some incentives to impress global buyers such as countries that gain Most-favored nations (MFN), Generalized System of preferences (GSP) from the EU and Agreement on Textile and Clothing (ATC).

2. Transit time and cost: Geographical distance play a major role in giving advantage to global buyers because proximity to buyer’s target markets is a great incentive for consideration. This would help buyers in reducing risk and costs in transporting garment products.

3. Physical and bureaucratic infrastructure: Having infrastructure and facilities in the sourcing countries are prerequisite prior to gaining investment from global buyers. On the other hand, the bureaucratic system in the supplier’s countries should be less sophisticated, no red tape procedure. It is very important for vendors (suppliers), buyers, and other related countries where garment products are shipped through to sign legal agreement upon tax or customs levied on products being imported to the country and to ensure that everything complies with country of origin (COO) regulations (Kunz& Garner, 2011, p. 150).

4. Raw materials availability: This factor might not be essential in making a decision but it contributes to the understanding that the country of export has enough supply to produce garment products on time without marginal risks of running out of supply materials.

5. Labor and management skills: Human capital is very important in upgrading manufacturing in the garment industry to another level in order to fulfill the high
demand for clothing in developed countries’ markets. So global buyers care about how workers can increase production’s efficiency and respond innovations to keep up with the new trend in fashions.

6. Exchange rate: Stable exchange rates are important factor contributing to the influence on prices of garment exports. For instance, high currency appreciation in China may affect prices of exports to developed economies.

7. Government incentives: When outsourcing from abroad countries, the sourcing countries’ governments play an important role in providing incentives to attract the global buyers, intermediaries and investors to purchase supply from their countries. The Export Processing Zone (EPZ) is one of several pitfall incentives that reduce or equalize tax to zero. It is one-stop-service zone that manufacturers, buyers, intermediaries and other related agents circulate for trade. EPZ is located in a favorable geographical stratification specifically near seaport, airport or railway station. That way will make shipping garment products more efficient and convenient.

8. Historical, political and cultural ties: finally, historical, political and cultural ties also influence on the decision to outsource from specific countries. Countries with peace and regional stability encourage global buyers to seek outsourcing supply from them. The relationships with the global buyers and the countries in terms of embassy, donor aid, or historical colonies help increasing the exports. (Staritz, 2011, p. 33)

In regards to the above-mentioned sourcing criteria, major garment exporters from developing countries in Southeast Asia have fulfilled most of the criteria. For instance, preferential trade agreements were granted to different countries such as Vietnam,
Cambodia and Laos, which created opportunities for outsourcing. Physical and bureaucratic infrastructures have been the main strategies that the government of developing countries in Southeast Asia implemented. That is also linked to the government incentive criteria, which is favorable for global buyers to outsource products. Typically, Cambodia is a dollarized country with stable exchange rate, which is good thing for exporters. The government controls monetary policy in Cambodia. The exchange rate between Riels and Dollars has not fluctuated much.

2.4 Recent Changes in the Global Garment Industry

Throughout two decades of development in the garment industry, the global garment industry has been influenced by three major influential phases, starting from the phase out of MFA, the Global Economic Crisis and the current stable global economy. Each phase has significant outcomes, as they are either improvements or degradations depending on the variation in the production patterns and quantity. After January 1, 2005, by adopting the Uruguay Round Agreement in establishing new Agreement on Textile and Apparel, WTO completely phased out quota systems after decades of negotiation. As a matter of fact, MFA restricted import competition from big low cost countries such as China and India because quotas were given in a stratification division among exporting countries. However, the elimination of MFA, as expected, would allow the influx of low-cost garment products from China to flow into developed countries’ markets. China’s efficiency in production is very high and the wages are considerably low compared to other developing countries. The phase out of MFA opens the door for Chinese firms to import freely to developed countries, which could potentially kill domestic jobs in the importing countries as well as other foreign countries that import the same garment.
products. China’s exports grew 45% in 2005 after MFA was phased out, in accordance with the Figure 2. To avoid fierce competition in the low price of importing garment products to the US and EU, quotas were re-imposed by the EU in 2007 and the US in 2008 to some products from China during mid-2005 (Fukunishi & Yamagata, 2014, p. 9). Besides China, who is the winner after MFA was eliminated, there were other countries that successfully increased their garment production as well. Quotas elimination gives positive impacts favoring developing countries as those countries can diversify and upgrade garment products, leading to full-package services, for instance in India and China (UNCTAD, 2005, p. 27). By 2005, those countries that overcame the elimination of quotas and increase their growth rate of exports in 2005 include China, India, Cambodia, Bangladesh, Indonesia, Pakistan, Vietnam, Sri Lanka and Honduras.

![Figure 3: Winners and Losers after the Elimination of MFA.](image)

Source: Adapted from James Harrigan and Geoffrey Barrows, 2009
After MFA was phased out, there are some changes in the behavior of the global buyers in sourcing garment products from garment producers’ firm and countries. Global buyers reduced sourcing partners when quotas were removed. Big retailers such as J.C. Penny, Wal-Mart, Liz Claiborne, and Gap, which originally sourced garment products from 50 countries before MFA was phased out, cut down sourcing countries to only 30 (UNCTAD, 2005, p. 19). The sourcing strategies after MFA was eliminated are exclusively based on the past relationship and the performance of the suppliers with access to full-package and the upgrade of technology in the garment industry. Importantly, there was a significant growth in initiatives advocating for improvement of the garment industry, specifically referring to environment, labor, quality standard and codes of conducts. Those initiatives to improve labor standards include Better Factories Work initiated by ILO; Ethical Trading Initiative working to give awareness to brands holders and customers regarding the impacts of their purchase; Fair Labor Association working to protect workers’ rights after MFA was phased out specifically in some countries like Dominican Republic (Forstater, 2010, p. 6).

The second phase that has an impact on the production and consumptions of garment products in developed countries as well as developing countries is the Global Economic Crisis during 2008 and 2009. Recent global economic crisis negatively influenced various sectors leading to the shutdown of a lot of factories in developing countries, mainly Southeast Asia. The unemployment rate in the garment industry increased dramatically as garment is a major source of industry attracting great labor forces. Once factories are shut down, employees are laid off without an income subsidy from the government assisting during unemployment period. According to Gereffi and
Frederick, several developing countries have decreased employment in garment sector, and those countries include China (10 million), India (1 million), Pakistan (200,000), Indonesia (100,000), Mexico (80,000), Cambodia (75,000), and Vietnam (30,000) (Gereffi & Frederick, 2010). At the same time, consumers have reduced their spending on clothing leading to a large decrease in demand. Bank credit is also a big major concern for investors to loan money for investment and financing.

2.5 The ASEAN’s Garment Exports

ASEAN consists of developing countries and developed countries, in which each country has different specialization in exporting products to the world. According to table 2, a list of ten ASEAN countries that export garments in 2014 to the world is reported as following.

Table 2:

*ASEAN Garment Exports*

<table>
<thead>
<tr>
<th>Country</th>
<th>Garment Exports to the World 2014 (in millions of USD)</th>
<th>Share of percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cambodia</td>
<td>6,000</td>
<td>12.47%</td>
</tr>
<tr>
<td>Brunei</td>
<td>6</td>
<td>0.01%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>8,000</td>
<td>16.63%</td>
</tr>
<tr>
<td>Lao People Republic</td>
<td>186</td>
<td>0.39%</td>
</tr>
<tr>
<td>Myanmar</td>
<td>404</td>
<td>0.84%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>5,000</td>
<td>10.39%</td>
</tr>
<tr>
<td>Philippines</td>
<td>1,940</td>
<td>4.03%</td>
</tr>
<tr>
<td>Singapore</td>
<td>2,569</td>
<td>5.34%</td>
</tr>
<tr>
<td>Thailand</td>
<td>4,000</td>
<td>8.32%</td>
</tr>
<tr>
<td>Vietnam</td>
<td>20,000</td>
<td>41.58%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>48,105</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

Source: UN Comtrade
The Vietnamese Garment Industry grabbed the highest percentage share in exporting garments among other ASEAN members, which is accounted for 41.58 percent. In addition, Cambodia is also efficient in exporting garment products and accounted for 12.47 percent share among other ASEAN members.

2.5.1 The Garment Trade between the US and Former Socialist Countries in Southeast Asia (Cambodia, Vietnam and Laos)

Figure 4 illustrates the value of garment exports to the US from three former socialist countries in Southeast Asia (Cambodia, Vietnam and Laos). Vietnam has increased its export share after the Doi Moi policy reform in 1986, which was the period that Vietnam opened its economy and promoted heavy industrialization under the centrally-planned economy. Over 12 years from 2002 to 2014, Vietnam increased value of garment exports to the US from 1 billion to 14 billion USD. Vietnam targets the US market as a major source of exporting countries. After signing of the US-Vietnam Bilateral Trade Agreement, Vietnam increased exports to the US with mass-produced goods, mainly garment products (shirts and casual trousers) (Amakawa, 2010, p. 188). Vietnam has done a great job in boosting garment export growth and production since it has rapidly moved from CMT to OEM or OBM. Importantly, CMT generate incomes to Vietnam minimally through processing commission. Thus, Vietnam currently updates its industry to higher value added activity, which is Free On Board Exports (Amakawa, 2010, p. 186). Noticeably, Vietnam joined WTO in 2007, which provided good opportunities for Vietnam’s garment exporters to increase exports to the US markets. Foreign Direct Investment still dominates industrialization in Vietnam although there is 10% domestic-
owned industry being operated. The garment industry in Vietnam has progressed at a rocket speed. Transpacific Partnership is a newly formed free trade agreement signed by 12 Pacific Rim countries. If TPP is officially approved, Vietnam would greatly benefit because the tariff is zero for exporting garment products to the US, which will be a great incentive for Vietnam to boost export growth in garment manufacture (BBC, 2015).

Besides Vietnam, Lao People’s Democratic Republic (PDR) is known as former socialist countries in the region and members of ASEAN in 1997, established trade relation with the US. Lao PDR’s rate of competition in garment production and export is relatively low comparing to other Southeast Asian Nations. Figure 4 illustrates the value of garment exports from Laos to the US. The trend has fluctuated over time, reaching the peak in 2011 but falling down steadily after that until 2014. Laos faces high competition in producing garment products although it has relatively low-wage labor cost. Garment industry is heavily simple process (CMT). Comparing to Cambodia and Vietnam, Laos’ garment industry is falling far behind. As a matter of fact, the geographical location in Laos is not favorable for investment since there is no deep-coastal port for shipping.

Among the former socialist countries in Southeast Asia, Cambodia is in between Vietnam and Laos in terms of garment exports and production. For the next chapter, Cambodia’s economy is analyzed with new update about the political economic situation. Additionally, Cambodia’s garment industry will be reviewed and discussed in the following chapter as well. There is further update of the literature review on the developing stages of the garment industry, mentioned by Dickerson (1999). Vietnam is no longer in the “early exports of apparel” but shifting to the “more advanced production of fabric and apparel”. However, Cambodia is currently in the process of moving from the
“early exports of apparel” to the “more advanced production of fabric and apparel”. The facts and figures supporting this argument are to be discussed in Chapter 4.

Figure 4: The Garment Trade between the US and Former Socialist Countries in Southeast Asia (Cambodia, Laos and Vietnam)

Source: UN Comtrade and OTEXA
CHAPTER 3: RESTRUCTURING OF THE CAMBODIAN ECONOMY

Chapter 3 aims to provide a brief overview of the current political economic situation that is paralleled with the development of Cambodia’s garment exports. In this chapter, government incentives such as Special Economic Zones (SEZs) and Law of Investments are briefly discussed. Foreign Direct Investment in Cambodia is also mentioned in this chapter.

Cambodia, which is located in mainland Southeast Asia, is bordered by Thailand, Vietnam, Laos and Thai Sea Gulf; and is the center of international trade connecting countries around the globe. Located in tropical Asia, it has total land area of 181,035 square kilometers; Cambodia has a favorable weather for agriculture especially cash crops such as rice, wheat, corn and rubber. Cambodia has a population of 15.14 million, of which about 50.5% are between age group 15-49, as per 2010 census (National Institute of Statistics, Directorate General for Health, and ICF Macro, 2011, p. 11). Cambodia is currently underdeveloped and many sectors need improvement. Cambodia has received support from developed countries through many forms including Official Development Aid (ODA), Foreign Direct Investment (FDI), official loans with zero interest, etc. Most of the aid has been allocated to the re-construction of infrastructure that was almost completely destroyed during two decades of civil war.

3.1 Political and Economic Reform in Cambodia

Having been influenced by political ideologies from both China and the US, Cambodia has adopted a hybrid democracy, in which transparency in national elections requires reformation and trust from citizens. Political clash has been a major concern that has hindered foreign investors from investing in Cambodia. Specifically, national
production has decreased as instability and insecurity has prevailed in the country. Two decades ago, Cambodia had been under the “Pol Pot Regime” (more popularly known as “Khmer Rouge”) when international trade was isolated and domestic infrastructure was completely destroyed. The aforementioned regime committed genocide, leading to mass-migrations abroad into developed countries hoping to survive on the new land. The impact of civil war affected the entire Cambodian society, including its economy, industrial sector and education.

After the Pol Pot Regime completely collapsed due to a Vietnamese military intervention, Cambodia’s society returned to normalcy though the Vietnamese invasion remained a major concern. However, in 1993, the United Nations Transitional Authority in Cambodia (UNTAC) funded by the United Nations restored the entire country’s political economy by organizing the first national election. Cambodia’s People Party (CPP) won the election, and has continued to rule the country since 1993 by winning four consecutive mandates (Chandler, 1991, p. 30).

The conduct of the national election in 1993 signaled the opening of Cambodia’s economy to international trade and welcoming all sorts of foreign investors. The industrial sectors were not strong due to the shortage of capital investment, knowledge, and resources (see Table 3 and Figure 6). The economic transition since 1993 adopted by the RGC allows foreign companies to invest in Cambodia. The economy depended heavily on foreign investors while the RGC was feeble and unable to subsidize production and state-owned enterprises.
The overall trajectory of economic growth in Cambodia’s economy has remained positive since the opening of the economy in 1993. In 2015, Cambodia had a GDP growth of 7.3 percent (Asian Development Bank, 2015). The growth of the GDP is partially because of its admission to Association of Southeast Asian Nations (ASEAN) in 1999, World Trade Organization (WTO) in 2004 and the foreign investments in various economic sectors. The GDP per capita has remained stagnant for the first decade after the economic opening but increased rapidly after joining WTO in 2004. The major increase did not lift Cambodia up from the developing country. Cambodia is still classified as a lower middle-income country because the GDP per capita in 2014 was roughly USD 1,090 (see Figure 5). The country was hit hard by the global financial crisis in 2009 when the GDP growth in percentage dropped to zero percent. However, the country has slowly

Figure 5: Cambodia's GDP Per Capita.

recovered from the low point to a sustained 7% per annum growth, as has been mentioned previously.

3.2 Cambodia’s GDP Composition

As the Figure below shows, share of the agricultural sector in the Cambodian GDP decreased over the years, as the country became more developed and stable. Service industry grew over time and has begun to dominate GDP since 1999. Simultaneously, the industrial sector has fluctuated specifically during the global economic crisis, which slowed down the growth of the industry.

Table 3:

<table>
<thead>
<tr>
<th>Employment Distribution in Cambodia</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employment in %</td>
</tr>
<tr>
<td>Agriculture</td>
</tr>
<tr>
<td>Industry</td>
</tr>
<tr>
<td>Service</td>
</tr>
</tbody>
</table>

Source: World Bank Data

In 2014, the industrial sector contributed 27.1 percent to the Cambodia’s GDP growth. It accounted for 18.6 percent of total labor employments in Cambodia in 2012. Cambodia’s industry is an infant industry and depends on foreign direct investment. Industry in Cambodia is classified into four types. Manufacturing industry accounting for 70 percent of the in industrial sector, followed by construction which accounted for 24 percent, mining and utilities represent 4 percent in 2012 (Asian Development Bank, 2014,
The manufacturing industry is largely dominated by the garment industry in which, from 2006 to 2010, 75.9 percent of garment manufacturing shared the total manufacturing output. In addition, garment manufacturing absorbs a large number of labor force from the agricultural sector. A lot of young workers migrate to work in the city and other areas that are located with the garment factories. This factor may explain why employment stratification of agriculture went down from 77.5% to 51%, while employment in industry increased from 4% in 1998 to 18.6% in 2012. The rest of the manufacturing outputs are extracted from rubber (1.2%), food, beverage and tobacco (10%), paper and publishing (2%), and other manufacturing (11%) (See table 4).

Figure 6: Cambodia's GDP Composition by Economic Activities.

Source: Asian Development Bank 2015
Table 4:

Share of Total Manufacturing Output

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Garments, Textiles, and Footwear</td>
<td>34.6</td>
<td>70.4</td>
<td>75.9</td>
</tr>
<tr>
<td>Rubber</td>
<td>3.1</td>
<td>1.9</td>
<td>1.2</td>
</tr>
<tr>
<td>Food, Beverage and Tobacco</td>
<td>33.3</td>
<td>13.3</td>
<td>10.0</td>
</tr>
<tr>
<td>Paper and Publishing</td>
<td>10.7</td>
<td>2.7</td>
<td>2.0</td>
</tr>
<tr>
<td>Other manufacturing</td>
<td>18.3</td>
<td>11.0</td>
<td>11.0</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
</tr>
</tbody>
</table>

Source: CEIC Global Database (extracted from Asia Development Bank article titled “Cambodia Diversifying beyond Garments and Tourism: Country Diagnostic Study”)

3.3 Foreign Direct Investment

Cambodia’s economy largely depends on Foreign Direct Investment (FDI). With regards to this form of aid, Foreign Direct Investment is of great interest to many developed countries as the donor in improving employment, and manufacturing industry in the recipient country. According to the World Bank definition, Foreign Direct Investments (Net Inflow) are the net inflows of investment in the management of interest of 10 percent or more in stock in the enterprise situated in the host country economy other than that of the investors. The OECD defines FDI as the evolvement of global market integration through international trade between recipient countries (host) usually developing countries and investing countries (home). FDI improves the connection of economies between the two countries. FDI also plays a major role in solving social problems in developing countries such as unemployment, promotion of technology and knowledge in the manufacturing industry and economic growth (World Bank, 2015).
Like other developing countries, the RGC established strategies and built a good environment for the potential investors from abroad to invest the capital in various sectors. The RGC heavily relies on foreign investors because they have capital, knowledge and resources. There are several sectors that receive investment from foreign countries such as garment, electricity, agriculture (mainly rice), rubber plantations, etc. Due to these incentive packages for investment, according to Figure 7, Cambodia’s FDI increased up to 1.3 billion USD by 2013. The correlation between GDP and FDI in Cambodia is 0.9332, which means that FDI and GDP in Cambodia are moving in the same direction as FDI increases the growth of GDP.

![Graph: Foreign Direct Investment, net inflows (BoP, current US$)](image)

*Figure 7: FDI in Cambodia*

Source: World Bank Database

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2 The correlation between GDP and FDI of Cambodia is calculated based on the raw data from World Bank, using excel formula (=CORREL (B2:V2, B21:V21))
Table 5:

Top Countries Investing in Cambodia

<table>
<thead>
<tr>
<th>Country (2015)</th>
<th>In million of USD</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total (including Cambodia)</td>
<td>4,600</td>
<td>100.00%</td>
</tr>
<tr>
<td>China</td>
<td>856</td>
<td>18.6%</td>
</tr>
<tr>
<td>UK</td>
<td>138</td>
<td>3.00%</td>
</tr>
<tr>
<td>Singapore</td>
<td>100</td>
<td>2.17%</td>
</tr>
<tr>
<td>Vietnam</td>
<td>88</td>
<td>1.91%</td>
</tr>
<tr>
<td>Malaysia</td>
<td>74</td>
<td>1.61%</td>
</tr>
<tr>
<td>Japan</td>
<td>59</td>
<td>1.28%</td>
</tr>
<tr>
<td>Thailand</td>
<td>54</td>
<td>1.18%</td>
</tr>
<tr>
<td>Korea</td>
<td>10</td>
<td>0.21%</td>
</tr>
<tr>
<td>Canada</td>
<td>8.74</td>
<td>0.19%</td>
</tr>
<tr>
<td>Others</td>
<td>23.92</td>
<td>0.52%</td>
</tr>
<tr>
<td>Total (excluding Cambodia)</td>
<td>1,413.12</td>
<td>30.72%</td>
</tr>
</tbody>
</table>

Source: Council for the Development of Cambodia

According to table 5, the main FDI inflow to Cambodia is from China, which has several major projects including infrastructure and energy, rice mills, textile and food processing. Due to the strong connection and bilateral agreement between the two countries, China has invested a lot of capital in Cambodia’s market and has earned a lot of profit through the gain from low labor cost and low-tariff exports. Chinese investment in Cambodia accounted for 18.62 percent of the total FDI in 2015. In this matter, China includes Hong Kong as well. Almost one-third of the investment comes from Asian countries. Cambodia largely depends on the FDI inflows, which has contributed a lot of benefits to the young growing economy. The government works relentlessly to improve the policy and beneficial incentives in attracting more foreign investors to capitalize in Cambodia. However, many issues are still prevalent, which include lack of skilled labor,
corruption, and the incapacity to provide subsidies to key sectors, as well as complicated processes in business registration.

There are, however, several reasons why foreign investors may decide to invest billions of capital in Cambodia. First, countries may invest in Cambodia because of the preferential trade agreement, complete with a Most-Favor-Nation status, which allows Cambodia to receive exporting quotas from the US. Secondly, Cambodia has plenty of cheap labors compared to other ASEAN countries in which currently the minimum wage of a garment factory worker is as of February 2014 increased by 25% to $100 per month with the addition of $5 for healthcare benefits (Cambodia Center for Human Rights, 2014). As a result, there is a great rise in the Cambodian garment industry, not only due to peaceful political and social conditions, but also the adoption of an open market economy. At the same time, Cambodia’s low wages, plenty of labor, easy access to Asian raw materials, and favorable tax treatment continued to attract investors during 1999–2005 (USAID, 2007). Additionally, World Bank ranked Cambodia 135 out of 180 in 2009 for the ease of doing business including the factors such as labor cost, intellectual property rights, policy and resources. Third, Cambodia is a member of ASEAN, which influences the foreign investors to consider this good condition. The proximity to other ASEAN nations provides benefits to the investors especially if they can gain the advantage from the low or zero tariff exports to other ASEAN nations. Finally, after the civil war, Cambodia experienced a lack of human capital, which makes it difficult for foreign investors to start a venture in Cambodia. However, due to other incentives that the government offers, foreign investors continue to invest in Cambodia, taking those deals from the government.
With the structural adjustment and foreigner-favored policy created by the RGC, a lot of foreign investors are taking these initiatives as a potential criteria-checking list before deciding to do business in Cambodia. Attracting foreign investment and strengthening Cambodia’s integration with ASEAN regional and global organization (WTO) trading systems with the initiative to privatize or reduce state-owned enterprises were the targeted objectives of the RGC, which was compiled in the National Rectangular Strategy 2014-2018 (Lee, 2011). To attract more foreign investors to improve Cambodia’s economy and compete with neighboring countries, the Law of Investment (LOI) and sub-decree, were written, which contain a number of important guarantees for the investors and is summarized as followed. Firstly, all the investors, regardless of nationalities, are to be treated equally and fairly in the market. Secondly, there is to be no requirement of local equity participation. Thirdly, there is no price control on products and services and no restrictions on Forex convertibility. In addition, free remittance of foreign currency abroad is allowed to circulate in the market. In addition to this, there are no complicated regulations for business registration as a one-stop service has been established to include all processes such as information and applications, visa and work permit, and business registration. Furthermore, there is a special incentive called a “One-Stop-Service”, which is a fast track investment approval process requiring only 28 days for foreign investors to process ownership of their business with a long term lease of up to 99 years of land. Moreover, the market determines the prices of the products and services, which reflects that business owners have the control over the flexibility of their price strategies. Thus, it implies that Cambodia has a great liberal investment regime.
Figure 8: Investment by Sectors in Cambodia from 2011-2015

Source: Council for the Development of Cambodia.

Figure 8 demonstrates the distribution of FDI in Cambodia across various sectors from 2011 to 2015. Infrastructure grabs the highest FDI rate, accounting for 41 percent. It is true that constructions and road buildings are absolutely necessary in responding to the economic growth. There are 35 percent of total FDI going to industries which mainly incorporates the garment industry in that rate. In the garment sector, Hong Kong, Taiwan, Malaysia and Singapore were the initial countries to invest in Cambodia in 1996 (Bargawi, 2005, p. 9). Furthermore, a large proportion of FDI is flowing into Special Economic Zones-SEZs (also known as Economic Processing Zones-EPZs), emphasizing importantly on the garment industry. The rest of the percentages are allotted to agricultural sector (14%) and services (tourism 10%).
3.4 Special Economic Zones in Cambodia

Special Economic Zones (SEZs)\(^3\) is the arrangement under legal and logistical scheme aiming to assist developing country’s economy by boosting export-oriented industry (ADB, 2015, p. 1). The RGC has invested national budgets in establishing SEZs across main geographical locations in the country. SEZs in Cambodia are vibrant international trade areas that link exports of products to other countries abroad. The main purposes of the RGC in establishing SEZs were required to diversify the export beyond electronics, to link urban and rural areas in Cambodia, and to invest factories outside the capital city-Phnom Penh (Lopes-Acevdo & Roberson, 2012). There are several characteristics of SEZs in Cambodia. First of all, SEZs are the centralized places for “One-Stop-Service” mentioned above. SEZs enable firms to settle all related legal documents required for export, import, registration, and other regulatory matters without going directly to associated ministries, which saves a lot of administrative costs and time for firm owners. Second, in order to register legally in SEZs, firms have to reserve a minimum of $500,000 fixed assets. In contrast to non-SEZs, Cambodia’s manufacturing sector is mostly garment-centered while inside SEZs’ industries are electronic, household furnishing products etc. Indeed, there are some footwear industries located in SEZs as well.

\(^3\) Special Economic Zones in Cambodia is a key term specifically referring to Economic Processing Zones.
Table 6:

Special Economic Zones in Cambodia

<table>
<thead>
<tr>
<th>Location</th>
<th>Name</th>
<th>Year of established</th>
<th>Number of firms</th>
<th>Total Employment</th>
<th>Employees per Firms</th>
</tr>
</thead>
<tbody>
<tr>
<td>Phnom Penh</td>
<td>Phnom Penh SEZ</td>
<td>2008</td>
<td>50</td>
<td>17,000</td>
<td>340</td>
</tr>
<tr>
<td>Bavet</td>
<td>Manhattan</td>
<td>2006</td>
<td>26</td>
<td>28,051</td>
<td>1,079</td>
</tr>
<tr>
<td></td>
<td>Tai Seng Bavet</td>
<td>2007</td>
<td>17</td>
<td>7,968</td>
<td>469</td>
</tr>
<tr>
<td></td>
<td>Dragon King</td>
<td>2013</td>
<td>2</td>
<td>280</td>
<td>140</td>
</tr>
<tr>
<td>Sihanoukville</td>
<td>Sihanoukville SEZ1</td>
<td>2009</td>
<td>2</td>
<td>424</td>
<td>212</td>
</tr>
<tr>
<td></td>
<td>Sihanoukville SEZ2</td>
<td>2008</td>
<td>40</td>
<td>8,967</td>
<td>224</td>
</tr>
<tr>
<td></td>
<td>Sihanoukville port</td>
<td>2012</td>
<td>2</td>
<td>416</td>
<td>208</td>
</tr>
<tr>
<td>Koh Kong</td>
<td>Neang Kok Koh Kong</td>
<td>2005</td>
<td>4</td>
<td>830</td>
<td>415</td>
</tr>
<tr>
<td>Poi Pet</td>
<td>Poi Pet O’Neang</td>
<td>2011</td>
<td>2</td>
<td>3,953</td>
<td>988</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td></td>
<td></td>
<td>145</td>
<td>67,889</td>
<td>468</td>
</tr>
</tbody>
</table>

Source: Adapted from ADB Economics Working Paper Series No. 459

The above-listed locations of SEZs in table 6 are situated in active cities and provinces which are on the border with neighboring countries. Phnom Penh is the main city where trade, industrialization, market and other important flow of business take place. Bavet is on the border with Vietnam, which is also the main door of entrance and exit for goods and services. Sihanoukville is the main deep-water seaport, where goods are loaded and unloaded from abroad. Poi Pet and Koh Kong are the main borders to Thailand, of which mostly import products are scanned through these locations.
3.5 International Trade Exports from Cambodia

According to the World Trade Organization trade summary data, Cambodia’s share in the world total export is 0.06% (WTO, 2015). Figure 8 illustrates the volume of exports and imports in Cambodia from 2000 to 2014. There is a significant trade deficit in the Cambodian economy. Cambodia’s exports reached 11 billion USD in 2014 and the imports reach 12 billion USD. The overall trend of exports and imports has been increasing from 1993 to 2014. This has been a result of policies that the RGC implemented to boost export growth. Yet, there are industries that are still vulnerable and unable to produce products to fulfill the demand in Cambodia. Therefore, import’s value surpassed exports, indicating a trade deficit in Cambodia.

![Cambodia's Exports and Imports](attachment:image.png)

*Figure 9: Cambodia Ex-Im from 1993-2014*

Source: World Bank Database
### Table 7:
**Top 10 Exporting Commodities from Cambodia 2013**

<table>
<thead>
<tr>
<th>No.</th>
<th>Code</th>
<th>4-digit heading of Harmonized System 2013 (Exports)</th>
<th>million USD</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>All commodities</td>
<td>9248.1</td>
</tr>
<tr>
<td>1</td>
<td>4907</td>
<td>Unused postage, revenue or similar stamps of current of new issue[^4]</td>
<td>2260.1</td>
</tr>
<tr>
<td>2</td>
<td>6104</td>
<td>Women’s or girls’ suits, ensembles, jackets, blazers, dresses, skirts</td>
<td>1199.6</td>
</tr>
<tr>
<td>3</td>
<td>6103</td>
<td>Men’s, boys’, suits, jackets, trousers etc knitted or crocheted</td>
<td>865.0</td>
</tr>
<tr>
<td>4</td>
<td>6109</td>
<td>T shirts, singlets and other vests, knitted or crocheted</td>
<td>1045.2</td>
</tr>
<tr>
<td>5</td>
<td>6110</td>
<td>Jersey’s, pullovers, cardigans, waist-coats and similar articles</td>
<td>546.4</td>
</tr>
<tr>
<td>6</td>
<td>6108</td>
<td>Women’s or girls' slips, petticoats, briefs, panties, knitted, crocheted</td>
<td>321.3</td>
</tr>
<tr>
<td>7</td>
<td>8712</td>
<td>Bicycles and other cycles</td>
<td>357.6</td>
</tr>
<tr>
<td>8</td>
<td>6403</td>
<td>Footwear with outer soles of rubber, plastics, leather</td>
<td>207.7</td>
</tr>
<tr>
<td>9</td>
<td>4001</td>
<td>Natural rubber</td>
<td>176.9</td>
</tr>
<tr>
<td>10</td>
<td>1006</td>
<td>Rice</td>
<td>258.2</td>
</tr>
</tbody>
</table>

Source: UN Comtrade

### Table 8:
**Top 10 Importing Commodities to Cambodia 2013**

<table>
<thead>
<tr>
<th>No.</th>
<th>HS Code</th>
<th>4-digit heading of Harmonized System 2013 (Imports)</th>
<th>million USD</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>All commodities</td>
<td>9227.4</td>
</tr>
<tr>
<td>1</td>
<td>2710</td>
<td>Petroleum oils</td>
<td>950.3</td>
</tr>
<tr>
<td>2</td>
<td>6006</td>
<td>Other knitted or crocheted fabrics</td>
<td>815.1</td>
</tr>
<tr>
<td>3</td>
<td>6004</td>
<td>Knitted or crocheted fabrics exceeding 30 cm</td>
<td>744.0</td>
</tr>
<tr>
<td>4</td>
<td>5515</td>
<td>Other woven fabrics of synthetic staple fibers</td>
<td>641.6</td>
</tr>
<tr>
<td>5</td>
<td>4907</td>
<td>Unused postage, revenue or similar stamps of current issue</td>
<td>978.5</td>
</tr>
<tr>
<td>6</td>
<td>8703</td>
<td>Motor cars and other motor vehicles</td>
<td>216.6</td>
</tr>
<tr>
<td>7</td>
<td>2402</td>
<td>Cigars, cheroots, cigarillos</td>
<td>184.4</td>
</tr>
<tr>
<td>8</td>
<td>5509</td>
<td>Yarn of synthetic fibers</td>
<td>155.5</td>
</tr>
<tr>
<td>9</td>
<td>8704</td>
<td>Motor vehicles for the transports of goods</td>
<td>152.5</td>
</tr>
<tr>
<td>10</td>
<td>8711</td>
<td>Motorcycles fitted with an auxiliary motor</td>
<td>126.0</td>
</tr>
</tbody>
</table>

Source: UN Comtrade

[^4] “Unused postage, revenue or similar stamps of current of new issue” is uncertain item category that Cambodia exports. It can be other items that are not listed in specific category. Thus, the sum of those unidentified items is greater than other specific items.
Important commodities for exports are depicted in Table 7. Cambodia exports are largely garment-related products to major destinations in Europe and the US, as it is shown in table 9 that the EU was ranked number 1 and followed by the US which are the target countries that Cambodia exports to. Items with prefix 61 and 64 are clothing-related products that are exported from Cambodia in large numbers. There are three other items that started to emerge in the top list of exporting commodities in Cambodia: rubber, rice and bicycles. In 2013, despite largely exporting clothing products, Cambodia also imported garment input materials from China and Hong Kong. Cambodia’s human capital is still limited in producing raw materials. Thus, outsourcing the materials for producing garment products has increased. There are other commodities that are imported into Cambodia such as petroleum, motor vehicles, and cigars (see Table 8). Since the garment industry dominates a large share of the exports in Cambodia, the next chapter content will focus significantly on the development of Cambodia’s garment industry.

Table 9:

Top 5 Major Trading Partners with Cambodia in 2014 (in percentage)

<table>
<thead>
<tr>
<th>By destination</th>
<th>Exports (2014)</th>
<th>By origin</th>
<th>Imports (2014)</th>
</tr>
</thead>
<tbody>
<tr>
<td>European Union</td>
<td>27.2</td>
<td>China</td>
<td>36.2</td>
</tr>
<tr>
<td>(26)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The United States</td>
<td>23.5</td>
<td>The United States</td>
<td>12.2</td>
</tr>
<tr>
<td>Hong Kong, China</td>
<td>17.2</td>
<td>Thailand</td>
<td>11.9</td>
</tr>
<tr>
<td>Singapore</td>
<td>8.6</td>
<td>Vietnam</td>
<td>10.7</td>
</tr>
<tr>
<td>Canada</td>
<td>5.2</td>
<td>Hong Kong, China</td>
<td>7.2</td>
</tr>
</tbody>
</table>

Source: World Trade Organization
CHAPTER 4: DEVELOPMENT OF THE GARMENT INDUSTRY IN CAMBODIA

As discussed in previous chapters, the garment industry plays an important role in the Cambodian economy, which was devastated after long decades of political turmoil and instability. This chapter aims to provide an in-depth and detailed review on the development of Cambodia’s garment industry and the upgrade of the value chain. In its yearly newsletter, the Garment Manufacturing Association in Cambodia (GMAC)\(^5\) reported that both garment and footwear exports account for approximately 80\% of the Cambodia's total exports and international trade (GMAC, 2015). Since 1993, Cambodia’s garment industry has contributed substantially to the economic growth through employment generation, the inflow of foreign currency, the transfer of technologies, the human capital development and the attraction of foreign direct investors (GMAC, 2015).

In 2014, GMAC consisted of 570 export-oriented garment factory members and 58 footwear factory members together with 70 associate members. GMAC has worked in collaboration with the government to facilitate trade in the garment sector mainly to avoid the complication of trade policies.

After opening its economy in 1993, Cambodia focused on the improvement of industrialization, in which the RGC have implemented national strategies to welcome foreign investors to Cambodia. Cambodia did not pass through the import-substitution industrialization stage due to the weaknesses in expanding the export-diversification. During French colonization (1863-1953), Cambodia produced cotton and silk and made

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\(^5\) GMAC stands for Garment Manufacturing Association in Cambodia, which is governed by a 25-Member executive committee (Exco) elected at the biannual General Assembly. The multi-national executive committee sets the policy and direction of the Association in order to ensure a continuous growth and development of the garment and footwear sector in Cambodia. GMAC Bulletin Newsletter is produced yearly in order to keep on track on the overall progress and policy regarding Cambodian garment industry.
them into garments in a small-scale economy (Hossain, 2010, p. 11). Later on, the Pol Pot Regime completely destroyed the garment sector because there was no trade with international countries.

4.1 Characteristics of Cambodia’s garment industry

The Cambodian garment industry is completely an export-oriented industry and involves largely in “Cut, Make, Trim” (CMT) activities. Raw materials are imported from big countries like China, Taiwan, Hong Kong and ASEAN Countries (Fukunishi, 2012). Specifically, the garment industry in Cambodia is a labor-intensive industry that absorbs large amount of Cambodian labor force consisting mainly of women from rural areas. CMT production in Cambodia requires very minimal training in processing output for clothing. Cambodian workers, specifically women, have adopted sewing skills since a young age as a traditional way of living.

According to the official observations from GMAC, 60 percent of the garment industries in Cambodia operate CMT; nonetheless, FOB or full-package firms account for 25 percent and the rest are represented by the subcontracting firms (USAID, 2007, p. 11). The type of the garment industry in Cambodia has different functions and capacities in manufacturing products. For instance, CMT, which is the largest and most common clothing factory-type, focuses on simple assembly production. CMT factories in Cambodia receive orders and instructions from the oversea contractors, which are basically East Asian countries or directly from potential global buyers such as Adidas or Nike. CMT manufacturers have to thoroughly comply with the instructions in sewing, cutting, and packaging and to ensure the final products are safely distributed back to the contractors in East Asia. CMT manufacturers do not have to purchase raw materials that
are necessary for production and to financially deal with international logistics and transportations of the final product to the destination. The intermediaries, mainly NICs, have already covered all those things. This process is called “Triangle Manufacturing” that is commonly practiced in the garment industry of developing countries. However, it can be a disadvantage for CMT manufacturers when they are not able to finish the products by the deadline due to the shortage of fabrics and materials and the delay in sending all those materials. Besides, of the 60 percent of shareholders of CMT manufacturers in Cambodia’s garment industry, 15 percent type of garment industry in Cambodia is related to subcontractor (USAID, 2007, p. 13).

As a matter of fact, CMT and subcontractors are somehow correlated in the case that CMT manufacturers could not complete the production on time as they have already accepted large numbers of orders from the intermediaries. To avoid taking risk, CMT manufacturers seek assistance from small factories and workshops by subcontracting them to help finish the process in a given length of time. After accepting orders from CMT or FOB firms, subcontracting firms in Cambodia are responsible for cutting and sewing, washing, sand blasting in accordance with the instruction. They have to follow all the instructions carefully and accurately. It is more likely that subcontracting firms can upgrade to fully CMT if they are able to market themselves and establish network with international intermediaries or global buyers directly. Subcontracting firms do not have to incur financial risk but they are elastic to the market economy since the downturn affects them enormously (USAID, 2007, p. 14). Finally, FOB full package firm is a new type of the garment industry in Cambodia that acquires 25 percent garment shares. For instance, SL garment in Cambodia, which is interviewed for a case study in this thesis, is a good
example of a FOB firm because this factory is equipped with high-tech machinery, raw materials, and a large labor force. There is also a research and development program created to invent new garment products. FOB firms incur large costs in the production, as they do not only take care of labor wages but also other materials and capital rent costs. FOB firms’ exports final products to designated buyers or retailers that have issued purchase orders and signed contracts in producing goods. Additionally, FOB firms manufacture garment products according to the order from the global buyers. Therefore, the types of fabrics are purchased following the instructions, in which the costs are paralleled to the selections. In Cambodia, the access to financial credit is very complicated, especially for foreign investors. FOB firms in Cambodia may have difficulty in asking for business loans from commercial banks (USAID, 2007, p.15).

Raw materials are imported from ASEAN countries and Sub-contracting countries, which supply materials and half-made fabric to Cambodian garment manufacturers to finish the final outputs. In 2013, Cambodia was still in the developing stage and raw materials are yet to be created locally. China exports the largest amount of textile yarn, fabrics, made-up articles and woven materials including machinery, washing machines, and sandblast machines. According to Table 10, China, Hong Kong and Republic of Korea are the top triangle manufacturers and material importers to Cambodia. China grabs 58% of the total shares of the raw materials for garment production. It was followed by Hong Kong (15%), Vietnam (3%), Korea (3%), Thailand (2%) and Malaysia (2%).
Since Cambodia only recently reconciled from wars, Cambodia’s garment industry would not exist and improve without the assistance of preferential trade agreements from the US and EU. The preferential and bilateral trade agreements consecutively lead to high growth rate in exports and foreign direct investments. The garment industry in Cambodia is generated exclusively for exporting to foreign markets but not for trade transaction in domestic markets. Therefore, clothes, which are sold in Cambodia, are imported from China, Hong Kong and Thailand to serve the demand in the domestic market. In 1996, Cambodia was granted Most-favored-Nation status (MFN) and Generalized System of Preferences (GSP) from the EU, and which went into effect in 1997 (Neak & Robertson, 2009, p.99; Lee, 2011, p. 561). In 1999, Cambodia received quota- and duty-free access for clothing exports to the EU market subject to double transformation Rules of Origin.

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6 The data on raw materials that Cambodia import from other countries are extracted from UN Comtrade by selecting the Standard International Trade Classification (SITC) code 65 Rev 3.
(ROO) under the three-and-a-half year EU-Cambodian Textile Agreement and from 2001 onwards under the Everything But Arms (EBA) Initiative for Least Developed Countries (LDCs) (Staritz, 2011, p. 105). The garment industry in Cambodia has participated vigorously in reducing poverty rates, especially by improving the wage gap between males and females. It also helped reduce the outflow of young Cambodian workers’ migration to neighboring countries such as Thailand, South Korea and Malaysia (Hossain, 2010, p. 28).

*Figure 10: Comparisons of the Minimum Wages of the Biggest Garment Exporters from Asia (2014).*

Source: ILO Wages in Asia's garment sector: Finding new drivers of competitiveness
The requirements to work in the garment industry are low, which means that factory workers in Cambodia do not need higher education. Cambodian workers in the garment industry are able to live above the one dollar a day poverty line, even though the standard of living is considerably poorer. Wages in Cambodia are comparatively low among regions in Southeast Asia, which is one of the greatest incentives in attracting foreign direct investors to invest in the garment industry because this kind of industry is heavily labor-intensive. Thus, lower wages generate high profits and reduce the cost of production. According to the ILO’s releasing statement on October 8th, 2015, the RGC pledged to increase the monthly minimum wage for garment workers in Cambodia up to USD 140 (ILO, 2015). Although wages are increasing rapidly, the rate is lower than other ASEAN countries whose garment industries are also vibrant.

Figure 10 illustrates wages in Asian countries that produce large quantities of garment products. In 2014, a large demonstration of Cambodian garment workers demanding the RGC to increase minimum wages has consequently resulted in slight increase of wages after consecutive protests. Wages in Cambodia only surpass three large garment-producing countries in Asia, which are Sri Lanka (USD 66), Bangladesh (USD 68) and Pakistan (USD 95) (see Figure 10). In addition, workers involved in garment production in Asia tend to work more than 48 hours per week. Thus, although minimum wage is relatively low, they can earn extra income through overtime. Minimum wage in Cambodia was initially adopted by the Cambodian Labor Law 1997. The Cambodian Ministry of Labor and Vocation Training (MoLVT) decides on the minimum wage after

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7 http://www.ilo.org/asia/info/public/pr/WCMS_412780/lang--en/index.htm ILO released press statement regarding to the agreement from RGC upon the increase of minimum wage to USD140 for Cambodian garment workers. The ILO country Office for Thailand, Cambodia and Lao People’s Democratic Republic acknowledge and appreciate the greater step of RGC in together improving welfare of Cambodian garment workers.
receiving recommendations from the Labor Advisory Committee (The Arbitration Council, 2013). Furthermore, the Cambodian minimum wage is determined based on a number of factors such as the cost of living, salary levels, comparative standard of living, productivity, employment, economic development, and inflation rates (The Arbitration Council, 2013).

4.2 The Evolving Phases of Cambodia’s Garment Industry (1996-Present)

Cambodia’s garment industry has developed through four important stages: the beginning of the garment industry, post-MFA, 2008-2009 Global Economic Crisis and post-crisis. Production and exports of Cambodia’s garment industry have been upgraded from one stage to another due to several important factors. Under the RGC’s policies, Cambodia’s various industries, including the garment industry, have performed outstanding within 2 decades after the civil wars. In order to build networks internationally, mainly by gaining the trust from global buyers, the garment industry in Cambodia has been the focal point linked to the development and innovations.
The database of Cambodia’s total garment exports and total commodities and services exports from 1995 to 2014 are reported and recorded from GMAC and World Bank. The data on the Cambodia’s garment exports is slightly different from WTO database. However, data on Cambodia is reported lower in value than in WTO report, except the years of 2007, 2011, and 2012. To remain consistency, I am selecting data from GMAC to report on the total garment exports from Cambodia and exports to the US. For instance in this table, the total Cambodia’s garment exports in 2007 based on GMAC database is 2,866 million USD while WTO database is 2,684 million USD.

Table 11: Value of Cambodia’s Garment Exports and Total Exports. (in millions of USD)

<table>
<thead>
<tr>
<th>Name of phase</th>
<th>Special events and descriptions</th>
<th>Year</th>
<th>Garment Exports</th>
<th>Total exports</th>
<th>Share of the total exports</th>
</tr>
</thead>
<tbody>
<tr>
<td>Newly-open garment industry</td>
<td>-Infant Garment Industry</td>
<td>1995</td>
<td>63</td>
<td>1073</td>
<td>5.87%</td>
</tr>
<tr>
<td></td>
<td>-MFA applied</td>
<td>1998</td>
<td>579</td>
<td>975</td>
<td>59.40%</td>
</tr>
<tr>
<td></td>
<td>-“Everything But Arms” trade agreement with EU</td>
<td>2000</td>
<td>1207</td>
<td>2374</td>
<td>50.84%</td>
</tr>
<tr>
<td></td>
<td>-US increased quotas to Cambodia 9 percent from 2000-2001 and 12 percent from 2001-2004</td>
<td>2002</td>
<td>1196</td>
<td>2374</td>
<td>50.37%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2003</td>
<td>1644</td>
<td>2633</td>
<td>62.43%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2004</td>
<td>2026</td>
<td>3395</td>
<td>59.67%</td>
</tr>
<tr>
<td>Post-MFA Phase</td>
<td>-MFA was completely phased out on January 1, 2005.</td>
<td>2005</td>
<td>2228</td>
<td>4033</td>
<td>55.24%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2006</td>
<td>2711</td>
<td>4990</td>
<td>54.32%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2007</td>
<td>2950</td>
<td>5644</td>
<td>52.26%</td>
</tr>
<tr>
<td>Post-MFA Phase</td>
<td>-Cambodia is the winner after MFA was phased out</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>-BFC monitor the factories</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>The Global Economic Crisis Phase</td>
<td>-Global Economic Crisis affects Cambodia’s Garment Industry</td>
<td>2008</td>
<td>3069</td>
<td>6785</td>
<td>45.63%</td>
</tr>
<tr>
<td></td>
<td>-Loss of jobs, shutdown of factories</td>
<td>2009</td>
<td>2529</td>
<td>5120</td>
<td>52.38%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2010</td>
<td>3185</td>
<td>6080</td>
<td>52.38%</td>
</tr>
<tr>
<td>The Current Trend of the industry</td>
<td>-Cambodia’s garment industry is moving from CMT to Full-package</td>
<td>2011</td>
<td>4709</td>
<td>8825</td>
<td>53.35%</td>
</tr>
<tr>
<td></td>
<td>-Export diversification takes place</td>
<td>2012</td>
<td>4756</td>
<td>8825</td>
<td>53.89%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2013</td>
<td>5320</td>
<td>10016</td>
<td>53.11%</td>
</tr>
<tr>
<td></td>
<td></td>
<td>2014</td>
<td>5784</td>
<td>11425</td>
<td>50.62%</td>
</tr>
</tbody>
</table>

Source: World Bank and GMAC

Note: The data in the table is reported and recorded from GMAC and World Bank. The data on the Cambodia’s garment exports is slightly different from WTO database. However, data on Cambodia is reported lower in value than in WTO report, except the years of 2007, 2011, and 2012. To remain consistency, I am selecting data from GMAC to report on the total garment exports from Cambodia and exports to the US. For instance in this table, the total Cambodia’s garment exports in 2007 based on GMAC database is 2,866 million USD while WTO database is 2,684 million USD.

The first major development for Cambodia’s garment industry occurred when the RGC switched the economy from a centrally-planned economy to a free market economy in the mid-1990s. This attracted foreign investors from Hong Kong SAR, Taiwan, China, Malaysia, and Singapore to operate export-oriented factories in Cambodia (Lee, 2011). During the 1990s, there were some changes in the East Asian garment industry for several reasons, such as increasing competitive garment suppliers from Southeast Asia and the restrictions of export to the EU and the US for some countries such as Hong Kong, South Korea and Taiwan. As a result, in addition to the low cost of labor production, some of the corporations from East Asian countries shifted factories from their own countries and directly invested in Southeast Asia such as Vietnam, Laos, and Cambodia because these countries were given a Multi-Fiber Arrangement (MFA). During the first period of the evolution, Cambodia’s garment industry, basically started as an infant industry, strongly relied on the preferential trade agreement. According to Table 11, the first period of Cambodia’s garment industry has shown good performance, in which the value of exports jumped from 63 million USD in 1995 to 1.98 billion USD in 2004.

In the NICs investors’ consideration, Cambodia was one of the targeted countries because of the unused quotas that Cambodia gained from the US under MFA preferential trade agreements and GSP signed together with the EU. The MFA quota systems and GSP preferential market access from the EU accelerated the production and exports of Cambodia’s garment industry greatly. In 2001, Cambodia signed another trade agreement with the EU called “Everything But Arms” (EBA), which significantly helped Cambodia’s
garment industry. However, the greatest garment market that Cambodia exports to is the US. The US market plays important role in expanding Cambodia’s garment industry. The US and Cambodia’s Bilateral Trade Agreement on Textile and Apparel was signed by both parties, establishing fixed quotas for export from 1999-2001. The three-year fixed quota period allowed Cambodia to export the 12 largest categories of clothing (Staritz, 2010, p. 106). The progress of Cambodia’s garment industry increased after signing the agreement. The extension of the agreement was prolonged another three years from 2001-2004. As there was higher demand from the US in regard to the clothing and fashion, Cambodia was granted another extra 9 percent of quotas from 2000 to 2001, 12 percent for 2002 and 18 percent for the following years till 2004 (Polaski, 2009). Cambodia benefited greatly from quotas, which exceeded that of its competitors such as Bangladesh (10% per annum from 1995-2004), China (average growth of 1.5 percent a year from 1997-2004), and Sri Lanka (7.5% per annum from 1995-2004) (Bargawi, 2005, p. 15).
Cambodia’s Quota Fill Rates from the US under Bilateral Trade Agreement.

<table>
<thead>
<tr>
<th>Quotas fill-up rates of Cambodia's garment exports to the US (in %)</th>
<th>1999</th>
<th>2003</th>
</tr>
</thead>
<tbody>
<tr>
<td>331/631 Gloves and Mittens (Dpr)</td>
<td>81.9</td>
<td>0</td>
</tr>
<tr>
<td>334/634 Men's and Boys' coat (Doz)</td>
<td>90.7</td>
<td>79.0</td>
</tr>
<tr>
<td>335/635 <strong>Women and Girls' coats</strong></td>
<td>45.5</td>
<td>91.8</td>
</tr>
<tr>
<td>338/339 Men's and Boys' Knit Shirts &amp; Blouses (Doz)</td>
<td>94.7</td>
<td>80.8</td>
</tr>
<tr>
<td>340/640 Men's and Boys' Shirts, Not knit (Doz)</td>
<td>49.7</td>
<td>65.1</td>
</tr>
<tr>
<td>345 <strong>Women and Girls' Shirts/Blouses, Not Knit (Doz)</strong></td>
<td>41.2</td>
<td>57.5</td>
</tr>
<tr>
<td>347/348 /647/648 Trousers, Cotton and man-made Fibres (Doz)</td>
<td>97.1</td>
<td>93.4</td>
</tr>
<tr>
<td>352/652 <strong>Underwear (Doz)</strong></td>
<td>57</td>
<td>67.7</td>
</tr>
<tr>
<td>435 Women and Girls' Wool Coats (Doz)</td>
<td>0</td>
<td>5.3</td>
</tr>
<tr>
<td>438 Wool Knit Shirts (Doz)</td>
<td>95.9</td>
<td>25.6</td>
</tr>
<tr>
<td>445/446 Women/ Girls' &amp; men/ Boys' Wool Sweaters (Doz)</td>
<td>49.8</td>
<td>6.0</td>
</tr>
<tr>
<td>638/639 Men &amp; Boys' Knit Shirts, Man-made Fibres &amp; Blouses (Doz)</td>
<td>89.0</td>
<td>50.2</td>
</tr>
<tr>
<td>645/646 Men's &amp; Boys' Sweaters, man-made Fibres (Doz)</td>
<td>9.1</td>
<td>4.6</td>
</tr>
<tr>
<td>Average in total</td>
<td>66.8</td>
<td>48.2</td>
</tr>
</tbody>
</table>

Source: OTEXA

Cambodia’s garment exports from 1999 till 2003 depended heavily on quotas.

Voluntary Export Restraint (VER) is the type of quota that Cambodia and the US implemented in the garment trade exchange. Cambodia followed the request of the

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9 Quota fill rate data table is taken from article titled “Cambodia’s Garment Industry-Origins and Future Prospects” by Omar Bargawi. But the original data is taken from OTEXA. The calculation to confirm the accurate data number is conducted once again. Please see the appendix page for detailed quotas and fill up rates based on actual number from OTEXA.
importing country, the US, but quota rent went to Cambodia’s exporters. Table 12 displays the percentage of quota fill rates that were completed by Cambodia’s garment manufacturers from 1999-2003. On average, Cambodia’s garment manufacturers did not manage to fulfill 100 percent of the quotas provided by the US. There are only 4 items that increased which include Women and Girls’ Coats, Men’s and Boys’ Shirts, Women and Girls’ Shirts and Underwear. However, item 435 was added later after the extension of the agreement and the growth of quota rates. As a matter of fact, Cambodia’s garment manufacturers were unable to fulfill the quota rates provided by the US mainly because of the specializations and the productivity of the workers. It can be implied that the number of garment factories in Cambodia kept rising due to the unused quotas.

4.2.2 Post-MFA Phase (2004-2008)

Cambodia joined WTO on October 13, 2004 and later on, MFA was phased out completely after an agreement and negotiations in Doha Round of trade talks. Members of the WTO were no longer limited in exporting garment products to developed countries, which is both a good thing and a bad thing for Cambodia to challenge itself as a main exporter of garment products. The first stage began with the phasing out of MFA on January 1st, 2005. As expected, this was initially considered unfortunate news for Cambodian firms that would have to be confronted with even more competition with other developing countries. However, after MFA was phased out, there was no significant decline in production and exports as had previously been expected (Bargawi, 2005; Lee, 2011; Natsuda, Goto & Thoburn, 2009; UNCTAD, 2013; Yamagata, 2006). Data on the Cambodian garment exports from 2004 to 2008 are illustrated in Table 11. The result after The MFA was phased out in Cambodia’s garment industry sector was astonishing, due to
a significant increase in the total exports of garment products from USD 1.98 billion USD in 2004 to USD 2.19 billion USD in 2005, and USD 2.9 billion USD in 2008. Cambodia was a clear winner after the MFA was phased out.

One of the reasons that Cambodia’s garment industry could have been in a panic was that when the MFA was phased out, it was feared that the quota agreement between Cambodia and the US would also be terminated. However, the RGC extended the agreement with the ILO monitoring program. That required Cambodian garment manufacturers to pledge to comply with the adoption of standard working conditions imposed by the International Labor Organization (ILO). Quotas for export to the US and EU increased dramatically because of the great overall performance and good evaluation by the ILO. Better Factories Cambodia (BFC) was established in 2001 in order to monitor the progress of Cambodian garment manufacturers. Better Factories Cambodia is one of the programs initiated by the ILO to monitor factories, and train management teams and workers. BFC also provides guidance and advice on factory improvements that help maximize firms’ profits while maintaining adherence to workers' rights and regulations. According to Polaski (2009), BFC’s initiative is dependent on two important policy innovations. First, it initiates market access incentives to manufacturers who have complied with the labor and environmental standards. Secondly it began the use of a new type of monitoring scheme. BFC has conducted door-to-door monitoring and evaluation in factories by relying on transparent, honest, and fair guidelines and without getting bribery from the factory owners. A team of local staffs who are Khmer-speaking officers working with the ILO/BFC assesses factories based on the checklist provided by the ILO offices.
The data information is computerized efficiently and both buyers and suppliers can get access to this information.

According to Asuyama et al. (2012), between 80 percent and 90 percent of garment factories in Cambodia followed Cambodian labor laws, and standards of working conditions including wages, hours of working, and union freedom of speech, as well as occupational safety and health. Better Factories Cambodia generates two important policies, which are to create trade agreements or extensions if there is a positive assessment of garment manufacturing in Cambodia and to introduce new monitoring standard rules to enhance labor standards in Cambodia (BFC, 2015). It is in contrast to what had been forecasted which is that Cambodia’s garment manufacturing production was going to decrease because of the elimination of quotas and especially, the fear that China was going to obtain the lead in producing garment products.

However, it has been argued that the garment industry from China is not likely to affect Cambodia’s garment industry or other developing industries negatively. For instance, Asuyama and Neou (2014) conducted an empirical study testing the factors contributing to the high productivity for garment products in Cambodia. The variable, which is related to the fact that China does not affect Cambodia, is associated with China-quota-free item and China-quota-re-imposed items. Before the MFA was phased out, production led to higher volume because of lower price competition as the MFA guaranteed the export amounts. After the MFA was phased out, Cambodian garment firms increased their shares of China-quota-re-imposed items due to the fact that some products from China were restrained from entering the EU and the US market. Another variable for testing is the material cost share, which dropped from 45.6 percent in 2002 to 31.6 percent
in 2008. The transportation cost is considerably low and it is affordable to operate fabric layer machines and cutting machines in Cambodia. Importantly, improvement in human capital and high frequency of training led to higher productivity. Cambodia’s education system was seen to have an upward trend as well as the experience of the labor workers who have undergone vigorous and regular trainings conducted by foreign technical experts. At this phase, Cambodia’s garment industry is classified in the second stage of the global garment industry, which is the early export of apparels.

4.2.3 Global Economic Crisis Phase (2008-2010)

Not only did developed countries get strongly affected by the global economic crisis, Cambodia’s economy was also hit. The global economic crisis began in 2008, in which financial systems collapsed. The job market was very narrow and unemployment rates soared very high, making people cut down spending. The employment in Cambodia’s garment industry was cut down from 414,789 in 2007 to 407,927 in 2008 and continued to decrease till 405,245 in 2009 (see Table 13). Given that Cambodia is a small country, it was affected greatly by the global economic crisis due to its high dependence on international trade. Specifically, Cambodia’s garment industry largely depends on the US and EU markets as the potential markets for export. The most affected segment of the garment industry in Cambodia was the one operating in small scale or local-owned firms. Subcontracting firms were also affected due to the reduction of the orders from big firms.

Total exports of garment in Cambodia fell abruptly after the second quarter in 2008. From 2008 to 2009, exports fell from 2.9 billion to 2.4 billion, which accounted for 18 percent reduction in exports. Exports to the US fell from 2.3 billion to 1.9 billion in 2008 and 2009. The decline in export of garment products was mainly caused by the
slowdown of demand from developed countries including the EU and the US. Additionally, China’s re-imposed quota safeguard was phased out at the end of 2008, which led to high competition in exporting garment products. Not only did Cambodia have to compete with China, but also neighboring and nearby Asian countries such as Vietnam and Bangladesh, which are considered leading garment exporters. Vietnam had become a member of WTO in 2007, which meant that Vietnam was no longer restricted by quotas.

Table 13:

*Cambodia’s Operating Garment Factories and Number of Employments*

<table>
<thead>
<tr>
<th>Years</th>
<th>Number of firms</th>
<th>Number of employment</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>233</td>
<td>200,861</td>
</tr>
<tr>
<td>2002</td>
<td>248</td>
<td>226,484</td>
</tr>
<tr>
<td>2003</td>
<td>266</td>
<td>254,535</td>
</tr>
<tr>
<td>2004</td>
<td>300</td>
<td>300,043</td>
</tr>
<tr>
<td>2005</td>
<td>351</td>
<td>328,466</td>
</tr>
<tr>
<td>2006</td>
<td>398</td>
<td>379,293</td>
</tr>
<tr>
<td>2007</td>
<td>432</td>
<td>414,789</td>
</tr>
<tr>
<td>2008</td>
<td>455</td>
<td>407,927</td>
</tr>
<tr>
<td>2009</td>
<td>487</td>
<td>405,249</td>
</tr>
<tr>
<td>2010</td>
<td>515</td>
<td>451,900</td>
</tr>
<tr>
<td>2015</td>
<td>666</td>
<td>542,795</td>
</tr>
</tbody>
</table>

Source: GMAC 2015
4.2.4 Current Trend in Cambodia’s Garment Industry (2010-Present)

After having weathered the storm of global economic crisis, Cambodia’s garment industry started to grow again in 2010 reaching USD5 billion of the total garment exports in 2014 (see Table 11). Although the statistics show the upward trend of overall export growth, the industry still faced with vulnerability including political instability, strike, rising of lower wage countries such as Myanmar and People’s Democratic Republic of Laos. The industry has not been entirely developed to OEM or full-package, yet as skills of labor remain critical issues especially the policy of the government in subsidizing the industry. Therefore, it can be assumed that Cambodia’s garment industry is in the process of moving on to the third stage of global garment industry, which is more advanced production of fabrics and apparels. Other indicators, such as electricity cost, raw materials, government policy, and human resources remain critical issues that delay the upgrade to OEM and full-package industry. Importantly, a high percentage of investment in the garment manufacturing industry is from NICs while the locally-owned firms are very small in percentages. Locally-owned firms usually have subcontracting activities. Importantly, Cambodia does not have primary industries to produce raw materials such as cotton, fabric, plastic and other accessories. Thus, Cambodia imports ready-made raw materials such as thread, fabric, paper carton, labels, bands, and embroidery from China, Taiwan, Hong Kong and the US (Hossain, 2010, p.11). Given the fact that Cambodia’s garment industry has not been fully transformed into full-package or OEM industry, the garment industry still contributes greatly to Cambodia’s GDP. The correlation between the total exports of Cambodia’s garment products and the total GDP is positively related, 0.966.
After the global economic crisis began to recede, Cambodia’s garment industry started to recover by gaining another potential exporting market from Japan. The GMAC has promoted Cambodia’s garment industry to China and Japan by associating the label name “Made in Cambodia” with good quality and standards. To bring this label up to the international market, GMAC has sought after new market access by trade negotiation, displayed the garment-manufacturing activities, and initiated promotions and marketing to attract global buyers from other developed countries (Staritz, 2010, p. 115). Importantly, GMAC has rights to distribute data information to global buyers or potential investors as requested anytime, which is an efficient and convenient way not to get involved in bureaucratic administrative work with the government. Cambodia’s garment exports to the Japanese markets kicked off officially in 2011 with the total value of 116.4 million USD (see Table 14). The exports to the Japanese market peaked in 2014 with the value of 261.8 million USD. Cambodia has established good connections with the new market niche in Japan. The trend is increasing although the export value is lower than other giant markets such as the EU and the US. GMAC has successfully diversified Cambodia’s garment industry’s targeting markets by retaining the trade relationships with the US and the EU but exploring new market opportunities in Japan as well as other countries (Staritz, 2010, p. 115). As we can see in Table 14, the exports to the EU dramatically rose in 2011; on the other hand, the exports to the US declined but have remained stable. Additionally, if we take a closer look at the Canadian garment importing market share, there is a huge increase in exports of the garment products in 2006. The number of exports has increased starting from 5.8 million USD and continued increasing consecutively in 2006 with the value of 116.47 million USD and five times increase till 2014 with the value of 491.31
million USD. The reason behind this dramatic growth of exports to Canada is because of the trade policy initiated by the Canadian government to extend Canada’s Generalized System of Preferences scheme in January 2003 (Lopes-Acevdo & Roberson, 2012, p. 235). However, among all the destinations, the exports of garments to the US still remain on the top list due to several reasons to be discussed in the following section.

Table 14:

<table>
<thead>
<tr>
<th>Country of imports/Year</th>
<th>2001</th>
<th>2006</th>
<th>2011</th>
<th>2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>US</td>
<td>828.51</td>
<td>2,151.00</td>
<td>2,670.00</td>
<td>2,671.00</td>
</tr>
<tr>
<td>EU</td>
<td>309.12</td>
<td>571.00</td>
<td>1,170.20</td>
<td>2,225.60</td>
</tr>
<tr>
<td>Canada</td>
<td>5.80</td>
<td>116.47</td>
<td>382.74</td>
<td>491.31</td>
</tr>
<tr>
<td>Japan</td>
<td>-</td>
<td>-</td>
<td>116.43</td>
<td>261.78</td>
</tr>
<tr>
<td>Other Markets</td>
<td>13.40</td>
<td>57.97</td>
<td>309.67</td>
<td>502.14</td>
</tr>
</tbody>
</table>

Source: GMAC and UN Comtrade

4.3 The Roles of the Royal Government of Cambodia

The RGC has been working relentlessly in improving the conditions of the garment industry in Cambodia. As a matter of fact, the garment industry is one of the four revenue-generating pillars in the Cambodian economic growth, which include tourism, agriculture and construction. The garment industry has helped restoring Cambodia’s economy, developing every sector, attracting more investors and generating revenues. The RGC promotes international trade pursuit through joining international organizations such as World Trade Organizations (2004), and ASEAN (1999). Simultaneously, the RGC also signed a long list of mutual and bilateral trade agreements with the US, EU, Australia,
New Zealand and ASEAN member states in order to find markets for exporting the
garment products that are made in Cambodia. His Excellency Sun Chanthol, Minister of
Ministry of Commerce in Cambodia has claimed in GMAC 2015 newsletter as followed:

In order to stimulate the growth of Cambodia’s garment industry after the open of
the economy, Garment Manufacturing Association in Cambodia was established
and has cooperated effectively with the RGC. As a result, there are many
remarkable successful stories that the RGC and GMAC have achieved, which
include the acceptance on MOU between Cambodia and BFC/ILO program, duty
free market access to the EU and the US, participation in the ASEAN Federation
of Textiles Industry (AFTEX) to promote the brand name and quality of ASEAN
garment products” (GMAC, 2015, p. 2).

The garment industry in Cambodia does not receive direct incentives (cash support)
from the RGC like the Bangladeshi garment industry (Hossain, 2010, p. 23). Bargawi
(2005), Fukunishi (2012), Hossain (2010), and UNCTAD (2013), conducted several
studies regarding Laws of Investment (LoI) in Cambodia that are favorable to foreign
investment and ensure that effective policies are highly implemented to achieve good
results. In fact, LoIs were enacted in 1994 and 1997 to provide incentives to the investors
such as exemptions from corporate income tax, import duty tax on material and equipment,
export tax and promote exports as also listed in National Development Triangle Strategy.10

Any Qualified Investment Projects (QIPs) are exempted from tax during the first three
years, which means that the owner of the project must pay income tax after three years
based on the actual profits of the firms. Indeed, a lot of garment industries in Cambodia
enjoy this kind of incentive because newly created foreign industries take a longer time to
adjust to the business environment in Cambodia. Additionally, Special Economic Zones

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to-the-law-on-investment_030324.html
(SEZ)\textsuperscript{11} were initiated as a one-stop service which provides a lot of favorable incentives for foreign direct investors including full import duty exemption, no export tax, reinvestment of profit etc (Hossain, 2010, p. 23), (Council of Development Cambodia, 2015). One-stop service is a policy allowing foreign investors to register company, patents, and any other legalized documents in an expressway without involving more than one department. In addition, the MNCs in SPZs are entitled the rights to transfer profit to their home countries.

The RGC plays an important role in coordinating smooth flow of garment export and production in the country. The RGC have also reduced the corruption rate specifically the custom clearance so as to ensure that there is no bribery and illegal money. In addition, the RGC has successfully implemented fiscal and monetary policy in controlling the exchange rate between the Cambodian Riel and the US Dollar to not fluctuate too much. The exporters in Cambodia are secured with the stable exchange rate.

The Cambodian labor productivity is lower than its neighboring countries like Thailand, and Vietnam. Cambodia’s garment industry is highly labor-intensive. Therefore, the RGC has listed labor training in the Cambodia Trade Integration Strategy 2014-2018. The main goals are to transfer skills and knowledge to Cambodian workers and to improve the productivity levels. Related to this issue, the RGC has worked closely and supported the nutritional promotion program of the Better Factories Cambodia (BFC/ILO) that aims to enhance workers’ wellbeing and health. The Technical and Vocational Education Training (TVET) in Cambodia has been reconsidered in Cambodia’s development strategies since the Global Economic Crisis, in which many employees were laid off

\textsuperscript{11} Cambodia SEZ was officially launched for investors on 15 February 2006 after the MFA was phased out for one year.
Dasgupta, et. al. 2011, p. 197). The program is designed to furnish Cambodian workers with practical skills in responding to the need in the labor markets. The RGC collaborated with private firms in providing skills to the workers. Furthermore, the RGC has increased the budget for allocation for education and vocational training in 2015 by 21.4% (Cambodia Daily, Education to Receive 20% Boost in 2014 Budget, 29 October 2013; CDRI, 2014, p. 14).

After 2013’s national election took place in Cambodia, the Cambodian People Party (CPP) won the election, which caused the instability in the country due to the dissatisfaction of Cambodian people especially workers, who demand real justice and transparent elections. Strikes, which were violent confrontation, were created and the workers boycotted working in the garment factories. Many factories in Cambodia encountered with losses due to the delay of the final products that are needed to ship back to the global buyers by certain deadlines. The RGC tried to negotiate with union leaders and opposition parties in order to solve this issue. Thus, the negotiation resulted in a positive way that wages were increased for workers. The RGC plays an important role in securing foreign investors through peaceful negotiation and ensures that both parties benefit from this way.

In upgrading Cambodia’s garment industry, the RGC has included this policy into Cambodia Trade Integration Strategies 2014-2018. The RGC encourages the shifting from CMT to full-package production by concentrating on improving supply chains that are linked with garment production (Cambodia Inter-ministerial Committee, 2014, p. 197). The RGC also encourages the joint-venture of the local and multinational corporations so that the local companies are able to establish themselves as major exporters and suppliers.
of the garment products. In addition, the RGC suggested to the foreign investors to focus not only on the production but also the components of raw materials that are essential in the production. Importantly, research and development should be highly placed into consideration. Last but not least, the RGC includes that strategy aiming to decrease non-wage production costs, which can increase efficiency in the supply chain.

4.4 International Trade Between Cambodia and the US

Cambodia’s trade with international countries contributes dramatically to the national economic growth when the country’s effort to establish strong networks with other countries is improving. Representing the superpower country with huge geographical location and large diversified demography, the US is the potential market for exporting. The trade relation of the US and Cambodia on exports and imports shows that the amount of US exports to Cambodia is less than the US Imports from Cambodia.

Figure 11: Cambodia-US Trade 1989-2013

The blue line indicates the exports from the US to Cambodia, which is slowly increasing, below 0.5 billion US dollars in 2013. However, the imports from Cambodia to the US noticeably increased and reached the peak in 2013 in the value of 2.7 billion USD. Cambodia’s exports to the U.S started to grow because of MFN. In 2013, Cambodia is ranked 129th among the countries that import items from the US. Simultaneously, Cambodia is ranked 60th for the country that exports large amount of items to the US market (USTR, 2015).

![Figure 12: Cambodia’s total exports and garment exports to the US Markets](http://tse.export.gov/TSE/TSEReports.aspx?DATA=NTD)

Among all the major partnered countries, the US plays an important role in helping Cambodia’s economic situation and providing labor employment to Cambodians in the
manufacturing industry. Cambodia has formed a better connection with the US, which resulted in the US Government subsequently designating Cambodia as a beneficiary under the Generalized System of Preferences (GSP) in 1997. The quotas system under MFN policies did not help Cambodia boost up the exports to the US markets. However, the quotas system allowed Cambodia to strengthen the garment industry and prepare to expand the industry later. The garment industry in Cambodia had not been developed until 1999, that Cambodia and the US signed a Bilateral Textile Agreement (BTA), a unique agreement that increases quotas for exports (United States International Trade Commision, 2010). The bilateral trade agreement provided detailed legal information of what items that Cambodia could export, the number of exports and the deadlines. If the actual exports are over the limits that are stated in the agreement, the US will not only allow for entry but also penalize the exporters in the succeeding period. However, if the exports do not achieve the target, it is possible to carry forward for certain amounts next year.

Cambodia’s garment industry started to flourish since that time and consequently generated labor employments. There was actually a slight drop in 2009 as the U.S encountered a financial crisis. Garments are the main items that Cambodia exports to the US market. In 2014, Cambodia exported various products to the US, equal in value of 2.8 billion USD, in which garment exports (illustrated in red striped graphic) account for 2.6 billion USD, representing more than 90 percent of the total exports (see Figure 12). According to personal interview with ten garment manufacturers in Cambodia, the representatives have provided common top buyers from the US (shown in Table 15), that they receive orders and instructions from, in order to manufacture products for those companies.
Table 15:

**Top US Buyers Buying “Made in Cambodia” Garment Products, 2016**

<table>
<thead>
<tr>
<th>Name of top buyers</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Adidas, Abercrombie and Fitch, Banana republic, Old Navy, Levi’s, H&amp;M, GAP, Dayton Hudson, Targets, Walmart, JC Penny, Sears, Carter’s, Kohl’s, Macy, Forever 21, Zara, Clark, Sketcher, Solomon, JMA, Kmart, Nautica, Camel, AEO, American Eagle.</td>
<td></td>
</tr>
</tbody>
</table>

Source: personal interview (2016)

Table 16:

**Top 10 Countries Exporting Clothes to the US in 2015 (in millions of USD)**

<table>
<thead>
<tr>
<th>Country/year</th>
<th>2015</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>World</td>
<td>103,782</td>
<td>100%</td>
</tr>
<tr>
<td>China</td>
<td>40,220</td>
<td>38.7%</td>
</tr>
<tr>
<td>Vietnam</td>
<td>10,472</td>
<td>10.1%</td>
</tr>
<tr>
<td>India</td>
<td>6,751</td>
<td>6.5%</td>
</tr>
<tr>
<td>Indonesia</td>
<td>4,814</td>
<td>4.6%</td>
</tr>
<tr>
<td>Bangladesh</td>
<td>5,191</td>
<td>5.0%</td>
</tr>
<tr>
<td>Mexico</td>
<td>4,298</td>
<td>4.1%</td>
</tr>
<tr>
<td>Pakistan</td>
<td>2,796</td>
<td>2.7%</td>
</tr>
<tr>
<td>Honduras</td>
<td>2,470</td>
<td>2.4%</td>
</tr>
<tr>
<td>Cambodia*</td>
<td>2,368</td>
<td>2.3%</td>
</tr>
<tr>
<td>Korea, South</td>
<td>862</td>
<td>0.8%</td>
</tr>
</tbody>
</table>

Source: OTEXA

At the end of the fiscal year in 2015, the International Trade Administration, Office of Textiles and Apparels released statistical data describing the top 10 countries that import large amount of garment products to the US. Cambodia is ranked the 9th country that exports 2.3 billion USD worth of total garment exports to the US markets in 2015. China is the top exporter of garment products to the US market (see Table 16).
The main garment items exported to the US are listed in Table 17. Code 61, 62, and 64 are the most popular exporting items to the US market. According to the UN Comtrade commodity list, code 61 covers men/women coats, shirts (knitted/crochet), blouses, underwear, nightwear, pullovers, and basic garments. Code 62 covers clothes that are not knitted, which include overcoats, capes, jackets, coated fabric, suits, etc. Code 64 covers all sorts of shoes. NICs specifically Hong Kong and Taiwan have built solid connections with the global buyers in the US. In this regard, the Cambodian garment manufacturers have received purchase orders from top clothing buyers in the US, who make orders through intermediaries in NICs. Among the top buyers of the garment products made in Cambodia, US buyers represent the largest percentage of the global buyers.

Table 17:

The Cambodian Garment Products that the US Imports (in Actual Value).

<table>
<thead>
<tr>
<th>HS Code</th>
<th>Items (2014)</th>
<th>Total US Garment Products Imports from Cambodia</th>
</tr>
</thead>
<tbody>
<tr>
<td>61</td>
<td>Apparel Articles and Accessories; Knit or Crochet</td>
<td>1,882,753,039</td>
</tr>
<tr>
<td>62</td>
<td>Apparel Articles and Accessories; not Knit etc.</td>
<td>597,396,761</td>
</tr>
<tr>
<td>64</td>
<td>Footwear; Gaiters etc. and parts, thereof</td>
<td>128,412,120</td>
</tr>
<tr>
<td>58</td>
<td>Spec Wov Fabric; Tufted Fabric; Lace; Tapestries etc.</td>
<td>1,779,764</td>
</tr>
<tr>
<td>63</td>
<td>Textile Art Nesoi; Needlecrafts sets; Worn Text Art</td>
<td>30,324,667</td>
</tr>
<tr>
<td>42</td>
<td>Leather art; Saddlery etc.; Handbags etc.; Gut Art</td>
<td>25,292,814</td>
</tr>
<tr>
<td>60</td>
<td>Knitted or Crochet Arts</td>
<td>25,889</td>
</tr>
<tr>
<td>52</td>
<td>Cotton including Yarns and Fabrics</td>
<td>19,357</td>
</tr>
<tr>
<td>Total</td>
<td>Total Cambodian Garment Export to the US</td>
<td>2,666,004,411</td>
</tr>
</tbody>
</table>

Source: OTEXA
As discussed in the literature review, Cambodia’s garment products are distributed accordingly to the global buyer’s orders and through a network built by NICs’ overseas buying office and trading companies. Brand-name apparel companies in the US as listed such as Adidas, Levi Strauss, GAP, H&M, Abercrombie & Fitch, and Hollister, received the products from NICs as intermediaries or directly received from Cambodia. There are also other large retailer chain stores such as Wal-Mart, Target, JC Penny, Kohl’s, DSW, and Factory Outlet etc, which are very popular in America in terms of selling fashionable clothes and footwear. According to the personal interview, a list of buyers from the US is recorded and those buyers represent the active merchants. The relation between the US and Cambodia in terms of trade has been very impressive in that the superpower country can help Cambodia’s economy to thrive. Asides from this, the US has goals in Cambodia to promote good governance, democracy, and human rights, reducing the threat of terrorism, and facilitating trade. (Lum, 2007).
CHAPTER 5: GLOBAL GARMENT COMPANIES IN CAMBODIA

In order to obtain updated information from the current garment industry in Cambodia, interviews were conducted with 10 garment factories’ representatives in Cambodia through phone calls and Skype. This chapter aims to provide the findings from the interview that are related to the perspective of the garment factory representatives in Cambodia on the overall performance of the factory, the exports of the garment products to developed countries, the challenges and opportunities in manufacturing garment products in Cambodia, and the strategies in boosting production and exports.

5.1 Foreign Direct Investment in Cambodia’s Garment Industry

Cambodia’s garment industry lives under the reign of foreign investors since it lacks capital investment, leadership, entrepreneurship in industrialization, and existing networks with global buyers. The best thing that we have in the country is the low wages and incentives created by the RGC. Approximately 95 percent of Cambodia’s garment industry are owned by foreign parent companies (Staritz, 2010, p. 107). The highest rate of foreign garment firms in Cambodia is Taiwan (25%), followed by Hong Kong (19%), China (18%), Korea (10%), Malaysia (5%), Singapore (4%), and others (12%) (see Figure 13). However, Cambodia’s garment factories are owned by more than just a layer of foreign countries. There are multiple ownerships of the industry based on the establishment of the triangle strategies. It depends on the nature of the investment. For instance, during the interview, it was found that there is a factory whose headquarter is in China while there is also a capital share from Hong Kong. Cambodia is one of the Southeast Asian Countries where the population of Chinese descendants is particularly large, which is beneficial for foreign investors, specifically from Chinese-speaking
countries. That is one of the reasons why Chinese-speaking countries like Taiwan, Hong Kong, and China invest in a large proportion of Cambodia’s garment industry.

![Pie chart showing foreign ownership in Cambodia's garment industry](image)

*Figure 13: Foreign Ownership in Cambodia's Garment Industry*

*Source: GMAC 2010*

On the other hand, the foreign ownership of Cambodia’s garment industry does not exclusively depend on the Chinese ethnicity in Cambodia. Triangular manufacturing plays an important role in placing foreign investors in Cambodia. Triangular manufacturing links Cambodia with the international trade through channeling with the intermediaries in NICs. The subcontracting arrangements are implemented in this industry, which allows Cambodia’s final exports to arrive at final destinations in the US and EU. Thus, the practical application of triangle strategies is that Taiwan, Hong Kong SAR and Singapore, which used to be the main producers and exporters of garment products in early 1980s, invested in Cambodia through the investment in the garment manufacturing factories. The
process of CMT starts in the factories, where imported raw materials and ready-made fabrics are produced into final outputs for exports. In contrast, parent companies in NICs control production and decision in design, sample making, costs, and exports from Cambodia (Staritz, 2010, p. 118). Generally, the parent companies conduct marketing promotion, brand strategies, and network connections with the global buyers. Additionally, parent companies also send technical experts from their countries to supervise and train workers in Cambodia. For instance, all ten factories that accepted the interview responded that the high-ranking officers in the factories, including general manager, quality controller (QC), quality assurance (QA), and technical officers are from parent companies mainly Taiwanese, Hong Kong, Chinese, Japanese, and Korean.

In addition, Cambodia’s garment factories do not involve only in triangular strategy. For instance, there is a case where a Chinese-owned garment factory in Cambodia is a sub-contractor of the parent factory in China. The parent factory in China is the direct contractor for NICs. It works in the way that Chinese factories in China expand their branches outside the country to other developing countries, such as Cambodia. Another implication that can be drawn from the interviews is that big garment factories in Cambodia that have opportunities to expand the factories outside the country can become the intermediary. For instance, when this happens, they start to move offshore to another low-wage country such as Laos, Myanmar. The process of moving offshore is complicated and require more than a layer of triangle manufacturing strategy.

The foreign garment factories in Cambodia are not permanently settled. It is mobile based on the orders, performances and the problems happening in the country (for instance, political instability, strikes, fire disasters, and debt insolvency). As a matter of
fact, lack of local ownership in Cambodia’s garment industry is due to the network establishment with the global buyers and the capital to run a business. It is noticed that Cambodian investors are not willing to invest large capital in setting up factories because the return earnings are not sufficient to cover the production costs. In addition, local investors are not able to compete with large factories from NICs.

![Figure 14: Cambodia's Productivity Rate Comparing to ASEAN Nations (2009) in USD](image)


Employment is increased following the growth of the factories. However, Cambodia’s productivity rate is still a major concern to foreign investors although number of factories keeps expanding over the years. Cambodia’s productivity rate was around 3000 USD (see Figure 14), which is lower than other ASEAN nations. Lower productivity
rates generate costs to the manufacturers because they have to pay for training, hiring expats and the costs that are associated with lateness in production and opportunity costs. Cambodia’s labor productivity is measured based on the real GDP produced by one hour of Cambodian labor (Staritz, 2011, p. 123).

5.2 Value Chain in Cambodia’s Garment Industry

The Global Value Chain (GVC) emphasizes differently on how the products are made and transported to the customers’ hands. Typically, internationalization of trade comes in different forms, in which two types of international production networks are classified as follows. As discussed in Chapter 2, producer-driven commodity chains largely coordinate big-scale production, such as automobile, aircraft, semi-conductor or heavy machinery, electrical equipment like computers. The second type is the buyer-driven commodity chain, in which values of the products are added through each process of manufacturing, marketing, and administrative related works. The garment industry is one of the best examples to illustrate the buyer-driven commodity chain. Cambodia is a developing country in Southeast Asia in which industrial knowledge and capacity are still a major concern for further development. Therefore, Cambodia’s garment industry focuses heavily on the buyer-driven commodity chain. In the process of upgrading, according to Gereffi et al (2010) and Humphrey and Schmid (2002), upgrading in the Global Value Chain constitutes four different types including process upgrading, product upgrading, function upgrading, and chain upgrading. Function upgrading applies to the garment industry in Cambodia, which is in the process of moving forward to FOB or OEM production. Currently, there are 25 percent of garment factories processing FOB in Cambodia.
Compared to other top garment exporting countries, Cambodia’s garment value chain upgrading process still falls behind Malaysia, Thailand, Pakistan, Turkey, India, Bangladesh and China. Cambodia’s garment industry is relatively smaller in size than its border countries, mainly Thailand and Vietnam. Cambodia’s ability to upgrade to high-tech garment industry is still constrained because of the low productivity rate of each worker and the scarcity of local owned industry. Cambodia’s garment industry’s value-added activities concentrate on the CMT process. The overall process will be discussed the following points.

Low wages provide positive benefits to Cambodia’s garment industry because of the diminishing in the costs of the production. Cambodia’s garment industry usually involves the following process, such as finishing the products that are already designed or sampled by NICs, printing or embroidering on shirts, T-shirts, other textile products, washing, cleaning, packing and shipping back to the requesting buyers (USAID, 2010, p. 1). According to the interview conducted through a phone call, a manager of factory A, which practice CMT, mentioned that her factory receives order samples, materials and the instruction on the purchase order of the specific products from global buyers. Factory workers have to follow all the instructions carefully so as to ensure the quality of the products assigned by the global buyers. Basically, Adidas is factory A’s buyer but the head office of the factory is in Hong Kong. Therefore, the branch of factory A in Cambodia receives raw materials like leather, fabric, and labels, washing chemicals from Hong Kong, in which the cost of materials is covered by Adidas. Factory A in Cambodia has to work on Cut-Make-Trim and ship back the final products to Adidas, in which the cost of shipping back is incurred to the factory in Cambodia. In the case of lateness,
Factory A has to ship through express airway and may have to discount the products. In addition, in the case of CMT factory, factory A’s shipping manager reported the costs involved in producing one unit of sport shirt for Adidas. Factory A does not have to design the samples as they will be prepared by the office in Hong Kong, which is the intermediary for factory A in connecting with the global buyer-Adidas. However, factory A does not ship the final products to Hong Kong but to Adidas in the US and Europe based on the destinations set in the instructions. Factory A is only incurred with the costs of wages, energy, rent, transportation and local customs commission.

Table 18:

Costs of Producing One Unit of Sport Shirt in CMT.

<table>
<thead>
<tr>
<th>Descriptions/items (Sport Shirts)</th>
<th>Costs (USD)</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Labor (workers and office staff)</td>
<td>1.4</td>
<td>40%</td>
</tr>
<tr>
<td>Administrative costs (tax, custom)</td>
<td>0.35</td>
<td>10%</td>
</tr>
<tr>
<td>Energy</td>
<td>0.35</td>
<td>10%</td>
</tr>
<tr>
<td>Electricity</td>
<td>0.175</td>
<td>5%</td>
</tr>
<tr>
<td>Rent</td>
<td>0.28</td>
<td>8%</td>
</tr>
<tr>
<td>Transportation</td>
<td>0.175</td>
<td>5%</td>
</tr>
<tr>
<td>Embroidery/ printing shirts</td>
<td>0.525</td>
<td>15%</td>
</tr>
<tr>
<td>Finishing (Packing, washing, rinsing, Sand wash)</td>
<td>0.245</td>
<td>7%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>3.5</strong></td>
<td><strong>100%</strong></td>
</tr>
</tbody>
</table>

Source: Interview and USAID, 2010

In the general pattern of the garment production process, Nathan Associates Inc. has drawn a diagram of the steps that garment manufacturers follow in order to export the products to the international destinations (see Figure 2, on page 20). Indeed, Cambodia’s garment industry that operates FOB process has to follow all the steps in the diagram. In
contrast, Cambodia’s garment factories that are hired as contractors or sub-contractors practicing CMT start from factory production and post-production.

In the personal interview I have conducted through phone call, one of the ten factories selected for interview functions as full-package but the head office is in Hong Kong. The “PGC”’s shipping and operating manager has provided a detailed process of the production in her company. The “PGC” factory has been upgraded to full-package service in 2009. The “PGC” factory imported sewing machinery, packing machine, and embroidery machine and dry/wet washing machine. The “PGC” factory has been receiving purchasing orders from multiple giant clothing corporations such as JMA, Kohl’s, Kmart, FILA (Sport shirts), and some stores from Korea and Japan.

The “PGC” factory depends on head offices, in Hong Kong to network with the global buyers. In the process of the purchase order, initially, global buyers issue the instructions including types of products (e.g. shirts, t-shirts, denim jeans, skirts, blouse), the design (designer from the global buyers), materials, and deadline for samples and final products. Sometimes, the global buyers decide on the shipping courier companies. After receiving the purchasing order, factory’s production team has to produce samples, first following the instruction given. They have to go through testing and evaluation before sending back to the global buyers for evaluation. Few samples are made and shipped through express air services, which is fast and convenient but costly. After shipping the first sample to the global buyers, they will check the quality and evaluate if everything complies with the standard guidelines. In case that the samples do not meet the requirements, “PGC” factory has to make another sample for adjustment. Raw materials are imported from Hong Kong and China, which have been specified by the global buyers.
The costs of raw materials are solely borne by “PGC”. Certain deadlines are placed on samples and “PGC” has to satisfy global buyers. When samples are accurately approved, “PGC” can process the production. Since “PGC” is fully equipped with the machines, CMT production is conducted in the factory by Cambodian workers with minimal instructions. However, PGC will transfer CMT jobs to subcontractors in Cambodia when the production is overly ordered or workers cannot finish them by the deadlines.

Subcontractors are locally or foreign-owned small workshops that have built direct networks with “PGC” before. Quality Control teams, which are dominated by Chinese, Hong Kong, and Taiwanese foreign employees, check the quality and the quantities. Finally, products are packed and labeled according to the rules of origins (Made in Cambodia). In this step, Cambodia’s mobile customs and CamControl usually come to inspect the factory or right at the port of shipping (Sihanoukville port) to process the custom clearance. “PGC” shipping officers have to show bill of lading, shipping licenses, manifestation of the products, and factory license registration to process at the custom office. The final products are shipped directly to the global buyers and further continue to various retail stores. For the worse scenario when the production cannot be shipped by the deadline, “PGC” has to discount the products and choose the fastest transport method to ship the product, which is costly to the factory. It is considered risky for a full-package firm like PGC. In terms of setting the price, the managers provided components of full-package cost that are associated in producing one unit of pajamas.
Table 19

Costs of Producing One Unit of Pajamas in Full-package Factory.

<table>
<thead>
<tr>
<th>Description/Items</th>
<th>Costs USD</th>
<th>Percentage</th>
</tr>
</thead>
<tbody>
<tr>
<td>Raw materials (Fabrics, buttons, threads, labels)</td>
<td>5.95</td>
<td>70%</td>
</tr>
<tr>
<td>CMT Cost</td>
<td>2.125</td>
<td>25%</td>
</tr>
<tr>
<td>Local transportation (factory to port)</td>
<td>0.425</td>
<td>5%</td>
</tr>
<tr>
<td><strong>Total FOB (paid by PGC)</strong></td>
<td><strong>8.5</strong></td>
<td><strong>100%</strong></td>
</tr>
<tr>
<td>Shipping (Waterway)</td>
<td>0.255</td>
<td>3%</td>
</tr>
<tr>
<td>US Import Duty</td>
<td>1.4</td>
<td>16.5%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>10.15</strong></td>
<td></td>
</tr>
</tbody>
</table>

Source: interview and USAID, 2010

In general, Cambodia’s garment industry is still being operated in a low-level of value chain activities due to the lack of human resources, technology, energy sources, and the subsidies from the government in protecting the firms from going bankrupt. However, the government also intervenes a lot in boosting Cambodia’s garment export growth, which is to be discussed in the following sections.

5.3 Cambodia’s Garment Manufacturers

In order to obtain specific data from Cambodian manufacturers’ perspectives, I have compiled a list of garment manufacturers in Cambodia, which are members of GMAC for interview purpose. The data sampling follows the random sampling from a list of GMAC members. The method of collecting data is through semi-structured interview via phone and emails. Before conducting the interview, I sent emails to the contact persons basically referring to production managers or CEO. Interview questions are

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12 The costs of producing Pajamas are recorded from the interview with the manager of PGC. However, the guidelines of the costs are followed by the article in USAID, 2010 titled “Value Chain Analysis of Cambodia’s Apparel Industry.”
attached as appendix B. A set of ten questions, which was inquired to the managers, was in open-ended format and sought to explore challenges and opportunities that Cambodian garment manufacturers confront in dealing with the competition in the garment industry and especially on the overall performance of the factory. Additionally, the interview sought to find information on the potential buyers that factories export the products to. Therefore, in order to thoroughly analyze the data collected, questions and answers were categorized and I have summarized the information received from the interviewees.

Ten factory representatives, including managers, shipping officers, administrative officers, and trading officers, agreed to participate in the interview through phone calls and Skype. In order to keep confidentiality of the company profiles, real names of the factories are replaced by letter A to J. Factory A is one of the biggest garment factories in Cambodia, which is owned by triple foreign investors from Hong Kong, Singapore, Malaysia, China, and the Philippines. In the interviewing samples, there are five factories reported that they practice CMT production while two other factories fully operate full-packaged production in which the design and sample making are also part of their responsibilities. The three other factories reported that they practice mixed production. However, they design and make samples for some products that are not complicated and require extra machinery. They also follow the designs that are determined by the global buyers. The total employees in the factories are also listed, which also include labor and non-labor employee (mainly office workers).
Table 20:

*Factory Profiles*

<table>
<thead>
<tr>
<th>Factory</th>
<th>Ownership</th>
<th>Type</th>
<th>Production</th>
<th>Employees</th>
</tr>
</thead>
<tbody>
<tr>
<td>A</td>
<td>Singapore, Malaysia, Hong Kong, The Philippines, China</td>
<td>Full-Package</td>
<td>Jeans, Short, Skirt, Pants</td>
<td>5000+</td>
</tr>
<tr>
<td>B</td>
<td>Japan</td>
<td>CMT</td>
<td>Men denim jeans, Jackets, Suits</td>
<td>1000+</td>
</tr>
<tr>
<td>C</td>
<td>Hong Kong</td>
<td>Mixed</td>
<td>Vest-like garment, cardigan, anorak, blouse, T-shirt, Trousers, Top (knitted fabric), skirt, pullover,</td>
<td>5500</td>
</tr>
<tr>
<td>D</td>
<td>Hong Kong</td>
<td>CMT</td>
<td>Sport shirts, pants</td>
<td>1000+</td>
</tr>
<tr>
<td>E</td>
<td>Taiwan</td>
<td>CMT</td>
<td>Denim Jeans, skirts, shirts, men's clothes</td>
<td>1500+</td>
</tr>
<tr>
<td>F</td>
<td>Taiwan</td>
<td>CMT</td>
<td>Babies’ clothes, Pajamas, underwear’s</td>
<td>1500+</td>
</tr>
<tr>
<td>G</td>
<td>Singapore, Hong Kong</td>
<td>Mixed</td>
<td>Women's robe, jeans, trousers, shorts,</td>
<td>1000+</td>
</tr>
<tr>
<td>H</td>
<td>Taiwan (90%), (10%)</td>
<td>Mixed</td>
<td>Men's sportswear (sneakers)</td>
<td>4300+</td>
</tr>
<tr>
<td>I</td>
<td>Hong Kong</td>
<td>Full-Package</td>
<td>Baby shirt, sport shirt, pajamas, J&amp;A</td>
<td>2000+</td>
</tr>
<tr>
<td>J</td>
<td>Taiwan</td>
<td>CMT</td>
<td>General Garment</td>
<td>1000+</td>
</tr>
</tbody>
</table>

Source: Personal Interview
Table 21:

**Global Buyers and Shipping Destinations of the Factories**

<table>
<thead>
<tr>
<th>Factory</th>
<th>Global Buyers</th>
<th>Destinations</th>
</tr>
</thead>
<tbody>
<tr>
<td>Factory A</td>
<td>AEO, Banana Republic, Blue Note, Camel, Camel, Cargo, Convington, Levi's Nautica, Old Navy, Zara, Union Bay, Wrangle, Yessica</td>
<td>USA (60%), EU (40%)</td>
</tr>
<tr>
<td>Factory B</td>
<td>H&amp;M, Wal-Mart, JC Penny, GAP, Target</td>
<td>USA (100%)</td>
</tr>
<tr>
<td>Factory C</td>
<td>H&amp;M, Armani Exchange, Li &amp; Fung, GAP, Abercrombie &amp; Fitch, Zara</td>
<td>80% EU, 15% US, 5% Others</td>
</tr>
<tr>
<td>Factory D</td>
<td>Adidas</td>
<td>EU, ASEAN, US</td>
</tr>
<tr>
<td>Factory E</td>
<td>Abercrombie &amp; Fitch, SEARs</td>
<td>USA (100%)</td>
</tr>
<tr>
<td>Factory F</td>
<td>Carters, JC Penny, Macy's, Targets, Kohl's</td>
<td>USA</td>
</tr>
<tr>
<td>Factory G</td>
<td>Forever 21, H&amp;M, Zara</td>
<td>US and EU</td>
</tr>
<tr>
<td>Factory H</td>
<td>Clark, Sketcher, Solomon,</td>
<td>Asia, EU (70%), UK, US (30%), ASEAN, China, Japan</td>
</tr>
<tr>
<td>Factory I</td>
<td>JMA, Kohl's, Kmart, FILA (Sport shirt) Store: Korea, Japan, 4 countries</td>
<td>Canada, US</td>
</tr>
<tr>
<td>Factory J</td>
<td>Kohl's, H&amp;M, Macy's, Wal-Mart's, Targets</td>
<td>EU (50%) and US (50%)</td>
</tr>
</tbody>
</table>

Source: Personal Interview

The common destinations, in which the factories’ representatives in the interview export the final products to, are the US, EU, Japan, China, and ASEAN countries. All of the factories’ interviewees claimed that they do not have to find buyers because they are the contractors. The head offices are located based on the foreign ownership of the firms. Head offices build networks, receive orders from the global buyers and then inform their factories the amounts of orders, instructions and samples (for CMT case). The
interviewees continued explaining that normally the global buyers pay much more attention to the quality, labor, and environmental standards imposed by BFC. They also reported that global buyers nowadays are very strict in terms of quality and mainly production lead times as it takes at least 20 days to ship to the US and the EU. Factory D and H reported that besides the US and EU market; their exporting destinations also include ASEAN member nations. The main reason is they have branch office in ASEAN countries mainly Thailand, Vietnam, and Indonesia. Thus, their head offices are able to find a market niche in ASEAN.

5.3.1 Overall Performance of the Factory

When asked about the overall performance of the factories, 70 percent of the interviewees reported that their factories (factory A, B, C, E, G, H, I) are estimated to perform very well, and the manufacturing outputs have been increasing. In addition, more orders will be requested by the global buyers due to the high demand in their markets. Factory H’s shipping manager emphasized that her factory has increased its export of shoes roughly from 28,000 pairs to 38,000 pairs per month during 2015 (estimated based on interviewee’s experience). There are several reasons that the representatives from successful factories explain why their factories perform well. First, they try to follow the instruction guidelines carefully in producing items. Importantly, they struggle to obey labor laws and regulations imposed by the BFC and the RGC. Last but not least, they are able to ship final products in time as requested by the global buyers. However, three other factories (D, F and J), which are considered small in size, reported that production was slow during 2014. But an administrative officer in factory J is optimistic that production will increase in 2016. All of the factories’ representatives added that their factories’
production went down during the strike in 2013 after the national election. They encountered losses due to the lateness in production and shipping because laborers boycotted the work and joined union leaders in protest to demand higher wages and other benefits.

5.3.2 Challenges and Opportunities

Although the RGC has facilitated easing the burdens of the garment manufacturers, investors in Cambodia still find stressful problems that hinder the growth of the industry in general. Ten representatives from the different factories being interviewed mentioned that they all encounter challenges in producing and exporting garment products in Cambodia. According to the responses from different interviewees, there are several challenges that they find disadvantageous in Cambodia’s garment industry. First of all, workers’ skills and education are constrained because those workers migrate from rural areas, in which quality of education is typically poor. Factories’ representatives added that they have to spend money and time on training new employees. Moreover, some employees who are well trained and knowledgeable in the field usually resign and move to work in another factory for various personal reasons. The language barrier is another problem in training those employees. Normally, the majority of technical experts in garment production is sourced from abroad (for instance, Taiwanese, Hong Kong, Chinese, Malaysian), and speaks different languages. Thus, to reduce language barriers, Cambodian translators are hired, in which more costs are added and misunderstandings in the production happen occasionally. Secondly, the respondents argued that Cambodia’s electricity cost is more expensive than neighboring countries like Thailand, Vietnam, and Laos. Moreover, there is not sufficient power to run the whole factory as sometimes the
power is cut off during production. All the factories being interviewed are equipped
with power generators as backups when electricity is cut off. As a matter of fact,
Cambodia still imports electricity power from Vietnam and Laos because hydroelectric
power produced in the nation is unable to supply the whole country. One of the factory’s
managers complained during the interview:

Sometime the electricity is cut off in the middle of the testing sample process. But
luckily our factory has power generator to help when the power outage happened.
Having had power generator might not be a good thing after all because the costs
of buying oil to run the power generator are high especially during dry season
since we use it very often.

Another challenge that Cambodia’s garment manufacturers have confronted is
dealing with strike. Roughly 7.7 percent of the Cambodian labor forces are in unionized,
and most of them are garment workers (Danish Trade Union, 2014, p. 2). Strikes become a
common problem that all of the respondents in the interview consider it as an obstacle to
the growth of the garment production. Most of the respondents said that they do not like
union leaders, who are the main activists in creating strikes. Factory A’s manager
commented that:

The factory I work in now is very infamous for strikes. The shareholders and CEO
issued warning to the government and workers that they would withdraw capitals
and move factory to another country if workers do not resume back to work.
Demanding higher wages is suitable because I can see that inflation is also high in
Cambodia. Workers need to support their families back in countryside. They do
not have enough money for saving after spending on daily activities. However,
low-wage countries arise just like Laos and Myanmar. I am afraid that factory
owners will shift the factory if there is no solution with strikes. Actually, I am not
in favor of union leaders because they always create problems, which slow down
our manufacturing flows.

Third, the scarcity of raw materials, which are not readily available in Cambodia,
leads to the critical problems for all of the respondents. It takes a lot of work and time to
coordinate in dealing with the shipment of raw materials, even though the RGC has lessened taxes and regulations on importing raw materials. A quote by a representative of five factories symbolizes wider industry concerns.

When raw materials are shipped to the factory, not all of them are usable, due to the long distance shipping and careless handle. When the materials are late, everything in the production is late. For instance, labels are late so workers wait for them to arrive. While sometime the suppliers forget to ship parts of the materials, we cannot complete them. If the materials are broken a lot, we may have to request more from them, which take quite a lot of time. It’s not as fast as materials that are available locally.

Last but not least, Cambodia’s corruption and bureaucratic systems are not favorable to garment manufacturers, according to the views from ten interviewees. Most of them answered similarly that they have to pay small commission money to local customs when they come to inspect the products. Cambodia is ranked number 98 in the world based on the “Trading across Border” category (Ease of Doing Business, 2016). There are some concerns regarding the procedures, time, and costs in dealing with customs at borders. Factory I’s shipping officer added that “she normally paid small commission fee to local customs whenever they ask so that the shipping process will not be complicated and it becomes the culture.” However, there is also another challenging experience in dealing with BFC. Since BFC strictly monitors the factory’s standards, there is a lot of pressure, which is useful for Cambodian garment manufacturers to follow. Thus, when asking about this matter, the interviewee thinks that it was obligatory to obey the rules; although, there are hardships in satisfying the BFC.

Although challenges sometimes obstruct the process of Cambodia’s garment production, six factories’ representatives answered that they are optimistic about the future growth of their industry, while the other four are neutral. From the interview, I have
observed that big factories are more likely to stay positive about the growth of Cambodia’s garment industry. Factory G and H’s representatives asserted that their factories will be upgraded to full-package soon, as the head offices start thinking of transferring machinery and training to Cambodia’s branch factory. Importantly, factory A plans to buy property by signing an agreement with the RGC for 99 years ownership. In addition, most of the respondents think that attracting more orders from global buyers is a good opportunity if the factories follow the regulations set by BFC.

5.3.3 Solutions

Representatives of ten factories being interviewed gave similar and different solutions to the challenges that they have encountered in production and exports. First of all, in order to boost the production, it is important to provide workers good incentives such as paying them the salary on time, solving conflicts effectively as a team, managing the workers so they are not lazy and do not free ride others’ labors. Secondly, improving workers’ welfare, environmental standards and organizing the factories with enough ventilation and safety exits in case of the emergency is necessary. In the production line, it is also important to ensure the best quality of the products and satisfy the buyers by following the guidelines. Quality of the production alone is not sufficient, but delivery on time is taken as an utmost consideration by the factories. The interviewees added that it is very significant to satisfy the global buyers’ needs, as now the competition in the garment industry is very fierce. Several interviewees claimed the same statements about the global buyers.
Our factories are able to process until now because of the trust from the global buyers that accept the quality and working process that we have made. It’s really important to strengthen the quality and cut down the lead-time. As now, we do not only have to compete locally with other factories but also other neighboring countries especially Vietnam in receiving orders from the global buyers. We are also concerned about the requirements set by the global buyers. However, they are our customers so we need to maximize our efforts in delivering the best quality products to them to retain the factories in Cambodia.

Another solution that the interviewees addressed is related to the raw materials. Raw materials are frequently checked and monitored to make sure that there are enough for production. The responsibilities of non-labor staff are allocated efficiently so that production flows smoothly. Third, factories’ owners have built good rapport with Cambodia’s government. They meet regularly with GMAC and the RGC to solve various issues, specifically strikes. Cambodia’s garment industry is volatile to the neighboring competitor, Vietnam. However, Cambodia’s garment manufacturers still work their best in order to grab the exporting markets in developed countries.
CHAPTER 6: CONCLUSION

After Cambodia is opened its economy to engage worldwide, the manufacturing industry particularly the garment industry has been upgraded rapidly. In spite of being a small-size country, Cambodia has been portrayed as a potential investing country by a lot of investors from developed countries. The Cambodian economy has thrived from the investment in the garment industry. At the same time, the shifts in the garment industry to Cambodia provide the country an opportunity for GDP growth. Initially, thanks to the preferential trade agreements provided by developed countries, Cambodia’s garment industry has developed from time to time, leading to the upgrade to the full-package format. Preferential trade agreements, such as MFN and GSP, benefit Cambodia and support the start-up of industrialization in Cambodia. Having been challenged by significant events, such as the removal of the MFA, the Global Economic Crisis, and the continuation of the trade agreement, Cambodia’s garment industry is becoming stronger and stronger, which positively signals that Cambodia’s economy will be further improved.

The RGC has significantly played a role in coordinating the smooth flow of garment exports and production in Cambodia. Due to the establishment of trade incentives, foreign investors (from Newly-industrialized Countries and China) build confidence in investing capital and operating ventures in the garment industry in Cambodia. Importantly, in this research finding, Cambodia’s garment industry has achieved another goal in diversifying garments’ exports to other developed countries’ markets rather than exclusively depending on the US markets. The US markets remain the potential market for the Cambodian garment industry, while there are emerging exporting markets such as the EU, Japan, Canada, and ASEAN members. The RGC and GMAC have collaborated and
managed to obtain the trade agreements with Canada, Japan and other ASEAN countries in exporting garment products from Cambodia.

As a matter of fact, Cambodia’s garment industry is 95 percent owned by foreign investors (mainly Newly Industrialized Countries). Since foreign investors own the factories, a large part of the revenues is flowing out of the country through remittances. However, it is not about the cost, as we can perceive some advantages that Cambodia can benefit from. The garment industry is a labor-intensive industry, which requires a large labor force to operate. This is a fabulous way for Cambodia to solve unemployment issue and labor migration to other countries. However, the RGC has included a new strategy into the Cambodian Trade Integration Strategies 2014-2018 and the Cambodian Industrial Development Policy, aiming to encourage the merge of local firms and multinational firms. The RGC has to improve the credit access system in Cambodia, which is one of the main concerns to the majority of the investors. Another great thing is that Cambodia is able to prepare for a high-tech manufacturing industry, basically the Original Brand Name (OBM). Cambodian workers are adjusted to manufacturing production in the garment industry. Thus, it is easier to train them the next level of complicated manufacturing process.

On the other hand, competition among major clothing export countries is very fierce and tough. Cambodia is vulnerable to the competition if we take a look at labor productivity, stability of the country, government policies and human capitals. Human resources in Cambodia are scarce, especially in the Science, Technology, Engineering, and Math (STEM) fields. Those are very important in strengthening the industry. The RGC should allocate extra national budgets into education and vocation training program, in
order to enhance human resources in Cambodia. In addition, Cambodia has partially managed to succeed in obey the labor standards set by the ILO. It is just that the compliance level is not yet reaching the most satisfactory point. On the other hand, Cambodia does not satisfy the global buyers with the lead time (including manufacturing process until final delivery to the global buyers). Staritz (2011) has conducted a study on several countries that export garment products. The results show that Cambodia’s lead time is from 80-110 days, compared to Bangladesh (60-80 days), Thailand (50-60 days), Vietnam (60-90 days), and China (50-60 days) (Staritz, 2011, p. 122). Another problem that the RGC has to effectively solve is the strike, formed by union leaders and garment workers. It is common problem for some developing countries. However, investors find this an obstacle in building trust to invest in Cambodia. Strikes advocate for the concerns and rights of the workers, however, it constraints the development of the nation’s economy and development. The RGC has to find an effective method in dealing with union leaders and providing fair solution to the workers.

Back to Table 11 on page 65, there is a big gap between Cambodia’s total exports and total garment exports starting from 2008 to 2014. Cambodia started to diversify its exports rather than just focusing on the garment industry as there have been factories starting to produce products other than garments. On the other hand, it is also important to notice that specialization in a certain type of garment product can increase market segments from Cambodia. For instance, Sri Lanka started to specialize in producing women’s underwear and active wear; Mexico focused on denim trousers and image-wear (UNCTAD, 2013, p. 20). Export diversification is absolutely significant in raising Cambodia’s living standards and economic growth. The exclusive dependence on the
garment industry is uncertain for the future of Cambodia’s economy (Park, 2014). If Cambodia is not able to diversify into higher value-added industry, the country’s export competitiveness will fall behind other neighboring countries such as Vietnam and Thailand (Park, 2014). As mentioned in Table 7 (page 55), agricultural products (natural rubber and rice) have become major exporting commodities for Cambodia. Therefore, the RGC has concentrated on producing them on a large scale and finding markets for exporting them. According to Asian Development Bank, there are 29 new products for Cambodia to diversify its exports, including bicycles, footwear, plywood, maize, vegetables, sand, sugar, palm oil, wood products, Cassava, light manufacturing (electronic and automobile parts), and other 11 categories of garments (ADB, 2014, p. 135).

Cambodia is still classified as developing country, where industrialization is upgraded slowly comparing to other developed countries. Based on the measure conducted by Asian Development Bank, Cambodia’s rate on overall product sophistication surpasses only Lao People’s Democratic Republic’s and Myanmar’s in ASEAN region (ADB, 2014, p. 130). Export diversification in Cambodian products requires efficient competence in producing products with high skilled, highly technological-oriented, and the connection of goods to other goods (forward-linkages and backward-linkages products).

After almost two decades of rapid development, Cambodia’s garment industry has been given an “ethical” reputation, thanks to Better Factories Cambodia Program. Global buyers and international investors have built confidence in outsourcing garment products from Cambodia because of the compliance report from BFC, which is considered highly reliable and accurate. Securing original trademark “Made in Cambodia” is necessary in developing Cambodia’s garment industry. The Cambodian garment manufacturers’
representatives involving in this research interview have positive visions in the 
Cambodian garment industry and see the opportunities to upgrade it with the possibility of 
additional investment.

Since the scope of the research is small, interviews were not conducted with the 
contractors in NICs and China. The interview was only conducted with the garment 
manufacturers in Cambodia. Obtaining information from contractors is beneficial in 
accumulating data information regarding their perspectives on the garment trade as a 
whole. For the future research, interviewing with multinational companies in NICs and the 
government in Cambodia would strengthen the research and make it more informative.
REFERENCES


http://otexa.ita.doc.gov/msrpoint.htm


APPENDIX A: VOLUNTARY EXPORT RESTRAINT

Note: The red area in the US graph represents the loss from the US side when implementing VER. Cambodia, as the garment exporter, benefited from the quota rents generated from the US. When a VER is imposed by the US to Cambodia, the supply of the garment products in the US increases as the demand goes down because the price goes up. While on Cambodian side, due to the quota restrictions, the supply decreases from S2 to S1 as price decreases.
APPENDIX B: INTERVIEWING QUESTIONS

Dear Sir or Madam:

My name is Uymeng Tang and I am graduate student at Ohio University pursuing Master of Arts in International Studies, focusing on Southeast Asia. Presently, I am doing thesis research on the topic titled “The Recent Development of the Cambodian Garment Industry: Global Firms, Government Policies, and Export to the US”. As included in part of my research methodology, I am conducting a survey in order to gather information from Cambodian garment manufacturers. Your participations are very important in contributing to information for my thesis. I hereby guarantee that all the information will be kept confidentially and utilized for anything other than academic purpose. In thesis writing, your name and company name will not be shown.

Thank you,

Best regards,

Uymeng Tang

I. Background of company:
   1. When was your factory established? What country is this factory based in?
   2. What kinds of garment products does your factory produce?
   3. How many employees are there in the whole factory?

II. Global Exports and Perspectives:
   1. Who are the potential buyers for garment products that your factory has produced?
   2. Which countries does your factory export garment to? What are the shares of export to each country abroad?
   3. What is the overall performance of factory in producing garment products? Is it declining or increasing in terms of production?
   4. In order to promote greater production and export, what are the challenges that your factory has encountered?
   5. Could you discuss how you overcome some or all of the challenges you have listed?
   6. What new opportunities do you think you gained by resolving these challenges, if any?
   7. What are your perspectives on the future Cambodia’s garment industry?