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The expansion of textile and clothing firms of China to Asian Least Developed Countries: The Case of Cambodia

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Executive summary

Since the 1990s, the rapid expansion of China's textiles and clothing enterprises to Cambodia has been closely linked to the phenomenon of industrial clustering of textiles and clothing firms at the Yangtze River Delta, Pearl River Delta and Bohai Rim. The report adopts the case study approach to examine the pattern and features of overseas foreign direct investment (OFDI) of textile and clothing firms in Zhejiang province and Jiangsu province of the Yangtze River Delta to the least developed countries (LDCs) in the Asian and Pacific region, particularly Cambodia, and make the corresponding policy suggestions on the sustainability of South-South investment and cooperation.

The fieldwork in Zhejiang province for this study showed that the subsidiaries of Chinese textile and clothing firms in Cambodia had been gradually integrating into the vertically-integrated value chain of textile and clothing firms in China, thereby becoming an important node in global textile and clothing value chain. Interviews (see annex 1) by the authors in the Yiwu specialized wholesale market indicated that business linkages between the specialized wholesale market and the Asia-Pacific LDCs have been developing fast in the past decade, although the ratio of businessmen from the Asia-Pacific LDCs is relatively limited compared with those from the LDCs in Africa. The internationalization of specialized wholesale markets has promoted commercial activities between China and LDCs in the Asia-Pacific region and led to an increase of OFDI from Chinese textile and clothing firms to LDCs.

The fieldwork in Jiangsu province has demonstrated that Chinese textile and clothing firms have started to change their investment behaviour from voluntary overseas expansion by individual firms to the establishment of overseas economic and trade cooperation zones, such as Sihanoukville Special Economic Zone (SSEZ) (see annex 2) in Cambodia, which facilitates the collective expansion of Chinese textile and clothing firms and improves the textile and clothing manufacturing capability in Cambodia.

The OFDI from China to LDCs has not had a great impact on local employment. However, the global financial crisis has led to a rising number of unemployed textile and clothing workers in China. The factors constraining sustainable OFDI from China in Cambodia include poor infrastructure, relatively high labour costs compared with other LDCs, low efficiency of government assistance and inadequate financial services.

The policy suggestions on facilitating sustainable investment from China to the LDCs from the perspective of Cambodia are to: (a) encourage OFDI by Chinese textile and clothing firms in overseas economic and trade cooperation zones in the Asia-Pacific LDCs; (b) forge the regional production network between China and the LDCs; (c) upgrade the financial package to support Chinese textile and clothing firms' FDI; and (d) improve the infrastructure facilities and government efficiency in the LDCs.

Introduction

According to the United National Conference on Trade and Development (UNCTAD), the South-South FDI increased from US$ 2 billion in 1985 to 60 billion in 2004 (UNCTAD, 2006). The multinational companies from the South have become important investors in the LDCs. The LDCs that have the highest dependence on FDI from developing and transition economies include Cambodia, Bangladesh, Ethiopia, the Lao People's Republic, Myanmar and the United Republic of Tanzania (Fredriksson, T., 2008).One important phenomenon resulting from recent economic globalization has been the large-scale relocation of certain production processes to developing countries. Although the textile and clothing clusters in China can still take advantage of cheap land and low-cost labour, labour costs are nonetheless on the rise. At the same time, the clustered firms have to deal with more and more anti-dumping allegations and the appreciation of the Chinese currency as part of the globalization process. Some textile and clothing firms in the cluster have taken collective action by establishing overseas industrial parks in least developed countries (LDCs) to avoid the trade barriers and expand their production. For example, Chinese enterprises signed contracts with Cambodia for labour services and design consultation totalling US$ 380 million in 2005, US$ 320 million in 2006 and US$ 560 million in 2007, respectively. By the end of 2007, they had signed labour services, design and consultation contracts totalling US$ 1.97 billion, with a total realized turnover of US$ 860 million (Xinhua News, 2008).

However, few studies have been carried out on the formation of a production network between China and the LDCs in the Asian and the Pacific region in terms of the increasing intraregional FDI, the role of industrial parks that promote the sustainable FDI from China to the LDCs and the benefits arising from south-south FDI. More research needs to be done on the inclusive development of the LDCs with the deepening south-south cooperation between those countries and China.

Currently, OFDI by textile and clothing firms in China has mainly been made in Bangladesh, Cambodia, Myanmar and Viet Nam as well as some African countries such as Nigeria. This report focuses on the Sino-Cambodia economic linkage because Cambodia has overtaken Viet Nam as the best investment destination for Chinese textile and clothing enterprises in the Asia-Pacific region in recent years. After 10 years of development, Viet Nam has established its own economic system. Because it does not belong to the LDC group, the United States and European Union impose import tariffs and quotas on textile and clothing imports from Viet Nam. Due to border disputes, the Sino-Viet Nam relationship remains unstable. In addition, the financial instability of Viet Nam in June 2008 affected the confidence of Chinese investors.

This report deals with the following three research questions:

(a) How are the firms in Chinese textile and clothing clusters making the spatial expansion to the LDCs in the Asian and Pacific region, particularly Cambodia?
(b) How can the governments of LDCs in Asia and the Pacific improve their investment environment in order to make south-south investment sustainable?
(c) What effective means exist for facilitating the integration of the textile and clothing industry in China and LDCs into the global value chain (GVC)?

I. Change in the global textile and clothing regime, and its impacts on China and least developed countries in Asia and the Pacific

A. Evolution of the global textile and clothing trade regime

Under the auspices of the General Agreement on Tariffs and Trade (GATT), in 1962, the developed countries and developing nations reached a Long-Term Arrangement Regarding International Trade in Cotton Textiles and Substitutes. In 1974, it was replaced by the Multi-Fibre Arrangement (MFA).

1. Multifibre Arrangement, 1974-1994

The MFA provided for the application of selective quantitative restrictions when surges in imports of particular products caused, or threatened to cause, serious damage to the industry in the importing country. It was an explicit attempt to protect developed country producers by restricting exports of textiles and clothing from developing to developed countries. Theoretically, it sought to provide temporary protection to textile and clothing firms in developed countries to enable them to undertake the necessary changes for competing against lower cost producers in developing countries. In practice, the MFA not only provided an effective framework for extending the protected position of garment manufacturers in developed countries, but also gave some LDCs preferential quota access to the leading markets around the world. However, the MFA was a major departure from the basic GATT rules, particularly the principle of non-discrimination (World Trade Organization, 2008).

2. World Trade Organization Agreement on Textiles and Clothing, 1995-2004

On 1 January 1995, the MFA was replaced by the World Trade Organization (WTO) Agreement on Textiles and Clothing (ATC), which sets out a transitional process for the ultimate removal of quotas outside GATT rules. The 10-year transitional programme has been applied in four stages under the agreement, allowing those countries affected by the MFA to make adjustments to a new “free trade” environment. It was designed to terminate the series of trade-distorting regimes that had governed the textile and clothing trade over some four decades.

3. **Post-**Agreement on Textiles and Clothing **era, 2005-present**

On 1 January 2005, all special quotas on textile and clothing were finally eliminated for WTO member countries. However, there is still a mixed picture in textiles and clothing trade in a quota-free environment (Mayer, 2005).

B. Development of the textile and clothing industry in China in the post-Agreement on Textiles and Clothing era

In the post-ATC era, China remains a major players in the global textile and clothing industry, accounting for 22.3 per cent of world textile exports and 30.6 per cent of world garment exports in 2006 (tables 1 and 2). In 2005, China signed Memoranda of Understanding with the United States of America and the European Union on restricting the rapid growth of Chinese textiles and clothing exports to these markets; however, in 2005, 2006 and 2007, overall exports of textiles and clothing from China to the world increased by 21 per cent, 25 per cent and 18.9 per cent, respectively (World Trade Organization, 2008).

However, the textile and clothing firms in China still face many challenges including industrial upgrading and new forms of trade protectionism. Although a large number of labour-intensive clustered firms have strong international competitiveness, they rely principally on low-price competition. The constant low-price competition not only affects the bargaining power associated with export earnings, but has also resulted in constant international trade friction over Chinese textile and clothing exports from both developed and developing countries since 2005. Therefore, more and more textile and clothing firms in China have chosen to make OFDI in other developing countries including the Asia-Pacific LDCs.

Table 1. Leading exporters of textiles, 2007

(Units: US$ billion and percentage)

Exporters	**Value**	**Share in world exports**			
	2007	**1980**	**1990**	**2000**	**2007**
European Union (25)	80.62	-	-	36.2	33.9
Extra-European Union (25) exports	23.72	-	-	9.9	10.0
China[a]	55.97	4.6	6.9	10.3	23.5
Hong Kong, China	13.42	3.2	7.9	8.6	5.6
Domestic exports	0.46	1.7	2.1	0.8	0.2
Re-exports	12.95	1.6	5.8	7.8	5.4
United States	12.39	6.8	4.8	7.0	5.2
Korea, Republic of	10.37	4.0	5.8	8.1	4.4
Taipei, Chinese	9.72	3.2	5.9	7.6	4.1
India	9.45	2.4	2.1	3.6	4.0
Turkey[b]	8.73	0.6	1.4	2.3	3.7
Pakistan	7.37	1.6	2.6	2.9	3.1
Japan	7.11	9.3	5.6	4.5	3.0
Indonesia	3.83	0.1	1.2	2.2	1.6
Thailand	3.11	0.6	0.9	1.2	1.3
Canada	2.32	0.6	0.7	1.4	1.0
Mexico[a]	2.21	0.2	0.7	1.6	0.9
United Arab Emirates[b]	4.02	0.1	0.0	2.0	1.7
Total for above 15	**217.67**	**-**	**-**	**91.7**	**91.4**

Source: World Trade Organization, 2008

[a] Includes significant shipments through processing zones.

[b] Includes Secretariat estimates.

Table 2. Leading exporters of clothing, 2007

(Unit: US$ billion and percentage)

Exporters	**Value**	**Share in world exports**			
	2007	**1980**	**1990**	**2000**	**2007**
China[a]	115.2	4.0	8.9	18.2	33.4
European Union (25)	103.4	-	-	28.4	29.9
Extra-European Union (25) exports	24.8	-	-	6.5	7.2
Hong Kong, China	28.8	12.3	14.2	12.2	8.3
Domestic exports	5.0	11.5	8.6	5.0	1.4
Re-exports	21.7	0.8	5.7	7.2	7.0
Turkey[b]	14.0	0.3	3.1	3.3	4.1
India	9.7	1.7	2.3	3.0	2.8
Bangladesh[b]	10.1	0.0	0.6	2.1	2.8
Mexico[a]	5.1	0.0	0.5	4.4	1.5
Indonesia	5.9	0.2	1.5	2.4	1.7
United States	4.3	3.1	2.4	4.4	1.2
Viet Nam[b]	7.2	...	...	0.9	2.1
Romania	4.4	...	0.3	1.2	1.4
Thailand	4.1	0.7	2.6	1.9	1.2
Pakistan	3.8	0.3	0.9	1.1	1.1
Morocco[a]	3.6	0.3	0.7	1.2	1.0
Tunisia [b]	3.6	0.8	1.0	1.1	1.0
Sri Lanka [b]	3.3	0.3	0.6	1.4	1.0
Total for above 15	**298.1**	**-**	**-**	**79.2**	**86.3**

Source: World Trade Organization, 2008.

a Includes significant shipments through processing zones.

[b] Includes Secretariat estimates.

C. Textile and clothing industry development in Asia-Pacific least developed countries in the post-Agreement on Textiles and Clothing era

The textile and clothing industry play a very significant role in the economic development of some LDCs in the Asia-Pacific region, which account for 37 per cent of the world's total LDC population. It was widely predicted that the main winners would be the larger exporting countries, such as China and India, which were previously constrained by quotas; the losers were expected to be some of the smaller countries that took advantage of quotas within the MFA after the removal of all special quotas on textile and clothing (United Nation Development Programme, 2006). However, following the termination of the quota regime in 2005, the situation has not been so clear-cut among LDCs in Asia and the Pacific.

Some LDCs in the Asia-Pacific region, such as Bangladesh and Cambodia, have increased their ready-made garment (RMG) exports to the developed countries since the termination of ATC. In terms of value and volume, Bangladesh's RMG exports grew by 35.4 per cent and 37.4 per cent in 2005, and 32.0 per cent and 31.87 per cent in 2006, respectively (table 3). Cambodia also maintained significant growth of garment exports to the United States, with its RMG share in the United States rising from 2 per cent in 2003 to

2.9 per cent in 2006 (Yamagata, 2007). Nonetheless, Bangladesh is likely to face fiercer price competition in the United States market, particularly in the woven garments segment, which accounts for more than 60 per cent of its total garment exports(table 4). Meanwhile, Bangladesh is still facing funding and implementation constraints in improving its infrastructure, which is essential to attracting additional FDI and strengthening its competitiveness (World Trade Organization, 2006).

Table 3. Growth of ready-made garment exports from Bangladesh, 2000-2006

(Unit: Percentage)

Year	Value	Volume
2000	17.8	15.90
2001	-2.5	20.80
2002	13.3	9.10
2003	29.9	32.40
2004	31.3	31.10
2005	35.4	37.40
2006	32.0	31.87

Sources: Export Promotion Bureau of Bangladesh; and International Monetary Fund, 2007.

Table 4. RMG shares of some Asian low-income countries in the European Union and United States markets, 2003-2006

	European Union				United States			
	2003	**2004**	**2005**	**2006**	**2003**	**2004**	**2005**	**2006**
Bangladesh	6.6	7.5	6.6	7.7	2.8	2.8	3.2	3.8
Cambodia	0.9	1.0	0.9	0.9	2.0	2.1	2.4	2.9
India	5.0	5.0	6.0	6.3	3.3	3.4	4.3	4.4
Pakistan	1.7	1.8	1.4	1.5	1.6	1.7	1.8	1.9
Sri Lanka	1.5	1.6	1.5	1.6	2.3	2.3	2.3	2.3
Viet Nam	1.1	1.3	1.3	1.7	3.7	3.7	3.8	4.3

Sources: Eurostat; United States Department of Commerce; and International Monetary Fund, 2007.

However, some smaller LDCs, such as Nepal and Maldives, were affected severely by the removal of quotas in 2005 due either to being landlocked or small island economies, or to supply-side problems. Foreign investors relocated production bases after the expiry of quotas. For example, Nepal's textile and clothing exports in 2005 and 2006 to the European Union and United States markets failed to return to their pre-ATC levels due to the fiercer competition from other countries in the region. Nepal regained some orders after the imposition in 2005 by the European Union and United States of safeguards on Chinese textile and clothing imports, but clothing exports from Maldives to the European Union and United States in 2006 continued to decline. Although 2,478 expatriates from Sri Lanka were employed by the clothing industry in Maldives at its peak, that number started to decline in 2004 and was reduced to 431 by the end of 2005 (Adhikari and Yamamoto, 2007).

Despite several decades of reform, the LDCs remain marginalized in the world economy (UNDP, 2007). The Asia-Pacific LDCs will continue to face challenges such as tariff barriers, non-tariff barriers and the phase-out of trade preferences in the coming decade. According to the rule of origin requirements within the preferential trading arrangement (PTA) by the European Union, those LDCs that fail to meet the "double transformation" process will only have a low level of preference utilization. The utilization rates for clothing preferences of the Asian LDCs under the Everything but Arms (EBA) initiative were 33.8 per cent for Bangladesh and 65.8 per cent for Nepal in 2004 (World Trade Organization, 2005). This implies that LDCs must continue to pay most favoured nation (MFN) tariffs on their exports to the European Union market and that the preferential market access has distorted the tariff structure. Exporters in Bangladesh pay tariffs that are 82 times higher than in Canada on exports of knitted apparel and 107 times higher on exports of woven apparel (Adhikari and Yamamoto, 2007).

In addition, non-tariff barriers such as environmental requirements, labour standards and trade remedy measures are imposed. From 1999 to 2001, environmental trade barriers had an impact on 41 per cent of the merchandise exports of LDCs compared with 20 per cent of merchandise exports from other developing countries (UNDP, 2007).

II. Spatial expansion of Chinese textile and clothing firms to Asia-Pacific least developed countries

Currently, outward FDI in Asian and Pacific region LDCs by textile and clothing firms in China has mainly been made in Bangladesh, Cambodia and Myanmar (table 5).

Table 5. China's outward FDI stock to some Asia-Pacific least developed countries, 2003-2006

(Unit: US$ million, non-financial portion)

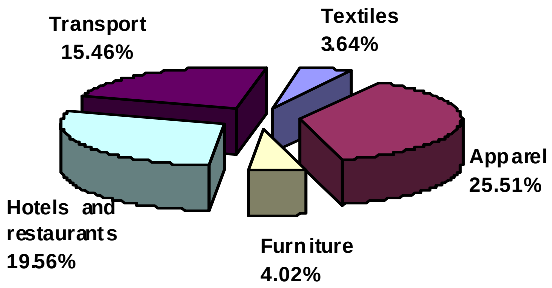
Country	2003	2004	2005	2006
Afghanistan	0.43	0.45	0.45	0.67
Bangladesh	8.45	8.66	32.96	39.66
Cambodia	59.49	89.89	76.84	103.66
Lao People's Democratic Republic	9.11	15.42	32.87	96.07
Myanmar	10.22	20.18	23.59	163.12
Nepal	1.81	3.32	2.99	3.59

Source: Statistical Bulletin of China's Outward Foreign Direct Investment, 2006.

According to the *Statistical Bulletin of China's Outward Foreign Direct Investment, 2006*, The total accumulated value of China's outward FDI to Cambodia, increased from US$ 59.49 million in 2003 to US$ 103.66 million in 2006 (Ministry of Commerce, 2007). At the end of 2007, China's non-financial FDI in Cambodia had reached an accumulated total of US$190 million while Cambodia had accumulatively invested US$ 84 million in China.

Many multinational enterprises from the Republic of Korea, Japan and Singapore have established production bases in Cambodia since that country began its economic reform in 1998. In the past decade, inward FDI in Cambodia has mainly been in the labour-intensive sectors such as the textile, garment and tourism industries (figure I). In 2006, the foreign share of the Cambodian garment industry accounted for 56.5 per cent of investment projects in industries in Special Economic Zones (table 6). Cambodia's MFN status and the fact that it is a beneficiary of the Generalized System of Preferences (GSP) from Canada, the European Union, Japan and the United States have contributed to the constant inflow of FDI. The majority of inward FDI in Cambodia is market-seeking and export-oriented.

Figure I. Realized FDI in fixed capital in selected industries of Cambodia, 1994-2004



Source: Cuyvers, Reth Soeng and van Den Bulcke, 2006.

The first Chinese garment enterprise in Cambodia, Cambodia Blue Bird International Garment Enterprise Co., Ltd., was established in 1994. In the 1990s, a few large-scale textile and clothing enterprises in China began making OFDI in Cambodia. At the end of 2004, 104 Chinese clothing firms and 3 textile firms were operating in Cambodia, accounting for 56.6 per cent of China's total Cambodian OFDI projects. Investment reached US$ 136.5 million at the end of that year, accounting for 33.3 per cent of China's total investment. According to Cambodia's Garment Manufacturers Association membership list in 2004, some 40 per cent were Chinese solely-funded enterprises plus about 40 per cent joint ventures between China and (a) Hong Kong, China, (b) Macao, China, (c) the United Kingdom of Great Britain and Northern Ireland, (d) Switzerland and (e) the United States; Sino-Cambodia joint ventures accounted for only 20 per cent of the members (table 7). Total investment by Chinese companies in Cambodia amounted to US$ 240 million in 2005, ranking first among all the investing countries. Most Chinese investments were in the garment industry (*China Daily*, 2006)

More and more Chinese textile and clothing enterprises have chosen Bangladesh for making OFDI. Bangladesh has an ample market for Chinese textile machinery and equipment. In fact, high-quality Chinese textile machinery and equipment have gained a steadily growing market share in Bangladesh due to competitive prices. Garment enterprises in Bangladesh have had to postpone deliveries because of a shortage of processed fabrics as well as inadequate weaving and dyeing-finishing capacity. More than 2 billion m^2 of fabrics need to be dyed and finished every year. Although the output of fabrics by Bangladesh textile companies has risen by 10 per cent annually, a supply shortage of fabric and yarn still exists. Only half of the existing demand has been satisfied. Projected demand for yarn has been projected as 30,700 tons in 2008-2009 (Business Section of Chinese Embassy in Bangladesh, 2007). Thus, Bangladesh is expected to establish more spinning and weaving factories with domestic investment or foreign capital in the next decade.

Table 6. FDI in Cambodia by sector, 1 January-28 December 2006

Sector	Projects	Local share (%)	Foreign share (%)	Registered capital (US$ million)	Fixed assets (US$ million)	Equities (US$ million)
Agriculture	**19**	**49.74**	**50.26**	**21.0**	**481 206 599**	**481 206 599**
Agriculture	2	10.53	-	2.0	146 578 540	146 578 540
Agro-Industry	17	39.21	50.26	19	334 628 059	334 628 059
Industries	**60**	**16.85**	**83.15**	**149.4**	**552 395 917**	**552 395 917**
Cement	1	1.67	-	78.0	132 000 000	132 000 000
Electronics	1	0.00	1.67	1.0	2 051 096	2 051 096
Energy	3	1.67	3.33	7.0	194 201 764	194 201 764
Garments	39	8.50	56.50	40.9	138 478 665	138 478 665
Mining	1	0.00	1.67	1.0	2 644 530	2 644 530
Shoes	5	0.85	7.48	7.0	24 799 024	24 799 024
Socks	2	0.00	3.33	2.5	4 144 785	4 144 785
Services	**10**	**61.10**	**38.90**	**17.3**	**2 594 116 070**	**2 594 116 070**
Construction	3	16.00	14.00	6.0	2 444 713 436	2 444 713 436
Engineering	1	0.00	10.00	1.0	9 373 400	9 373 400
Health services	1	5.10	4.90	1.0	10 000 000	10 000 000
Service energy	1	10.00	-	3.3	2 271 840	2 271 840
Service	4	30.00	10.00	6.0	127 757 394	127 757 394

Tourism	**7**	**61.86**	**38.14**	**17**.0	**352 009 643**	**352 009 643**
Hotels	4	33.29	23.86	5.0	21 754 690	21 754 690
Tourism	3	28.57	14.29	12.0	330 254 953	330 254 953
Total	**96**	**0.31**	**0.69**	**204.7**	**3 979 728 229**	**3 979 728 229**

Source: Cambodia Special Economic Zone Board, www.cambodiasez.gov.kh/investment_Infor.asp (accessed 4 August 2008).

Table 7. Chinese garment manufacturers in Cambodia, 2004

Company	Owner from
Belgian Industries C/L	Hong Kong, China
Cambo Fashion C/L	Republic of Korea, China
Cinkamp Apparel Corp.	China, Japan, Taiwan Province of China and the United States
Cung Sing (Cambodia) Garment Factory Ltd.	China, Hong Kong, China
Ecent Cambodia Knitting C/L	China
Four Seasons Garment (Cambodia) C/L	China, Hong Kong
Franco Knitting Garment Factory Ltd.	Macao, China
Gold Kamvimex Garment Factory Ltd.	China, Hong Kong
Grace Sun Cambodia Garment C/L	China
Guangda (Cambodia) Garments C/L	China
Hang Fung Shing (Cam) Garment Factory C/L	United Kingdom, China
Huiying Enterprises (Cambodia) C/L	China
Jiangsu Diao (Cambodia) Garment C/L	China
Jin Chan (Cambodia) Clothing C/L	China
Kenetex International (Cambodia) C/L	Hong Kong, China
Kog Veng Garment C/L	China, United Kingdom
Lucky Zone Apparel (Cambodia) C/L	Hong Kong, China
Luen Thai Garment (Cambodia) C/L	China, United States
Mekong Textiles Ltd.	Cambodia, Macao, China
M.G. Garment Manufacturing C/L	China
Min Yue Australia (Cambodia) Garment C/L	China
New Orient (Cambodia) Garment C/L	China
Pak Shun Knitting Factory Ltd.	China
Shandong Demian Group (Cam) Textile C/L	China
Shing Tex (Cambodia) C/L	China, Cambodia
Splendid Chance International Ltd.	Cambodia, China
Su Tong Fang Group Ying Kan (Cam.) Garment	China, Cambodia
Supreme Choice (Cambodia) Garment Ltd.	China, Switzerland
Trico (Cambodia) Textile Co., Ltd.	China, Cambodia
Universal Apparel (Cambodia) Co., Ltd.	China, Cambodia
Wong's Enterprise Ltd.	China
YGM (Cambodia) Ltd.	China
You Cheng Garments Co., Ltd.	China
Zheng Yong Garment Factory Co., Ltd.	Taiwan Province of China, China

Source: Garment Manufacturers Association, Cambodia list of members, www.embassy.org/cambodia/government/manufacturelist.pdf (accessed 3 August 2008).

Textile and clothing firms in China undertake spatial expansion to Asia-Pacific LDCs because of overcapacity within the domestic market, increasing international trade friction on Chinese textile and clothing exports, the adjustment of domestic industrial policy and tax policy , and the implementation of the "Go Global" strategy of the Government of China.

A. Overcapacity in the domestic market

The textile and clothing industry in China has achieved strong competitive advantages in the past two decades. China has become the world's biggest textile and clothing producer and exporter. Its synthetic fibre output accounts for one third of total world production. The production capacity in the textile and clothing sector has expanded so dramatically that the domestic market finds it difficult to accommodate the output. The OFDI of textile and clothing enterprises in China can help to ease the excessive domestic production capacity as well as promote the structural adjustment and industrial upgrading.

B. Increasing international trade friction on Chinese textile and clothing exports

Due to increasing international trade friction on Chinese textile and clothing exports from developed and developing countries, the Ministry of Commerce in China issued "Provisional Measures for the Administration of Textiles Exports" on 18 September 2005.[1] Under these Measures, The Ministry of Commerce, the General Administration of Customs, and the General Administration for Quality Supervision, Inspection and Quarantine (AQSIQ) compiled a *Catalogue of Textiles Products Subject to Interim Export Administration*, which lists textiles and clothing exports subject to restrictions imposed by countries or regions unilaterally, and those subject to temporary quantitative control under bilateral agreements (World Trade Organization, 2008). A new quota allocation system was applied to textiles and clothing exporters. The textile and clothing quotas, which are subject to an annual review, were allocated at lower prices because the exports to the United States and European Union did not come to expectation in 2006. In addition, Ministry of Commerce adopted various means of invitation for bid and the quotas were allowed to be transferred by agreement in 2007.

China and the European Union have also reached a new agreement on textiles and clothing trade. Since 1 January 2008, all the textile and clothing exports from China to the European Union have not been subject to any quota or quantity cap. However, both parties agreed to implement a 'Dual Approval and Supervisory System'. China has imposed export licence system on eight types of textile products including T-Shirts, pullovers, trousers, blouses, sheets, dresses, brassieres and linen shirts while the European Union has implemented a voluntary import licence system. The adoption of export licence system has reduced the exports of above eight types of textile products.

However, the LDCs in the Asia-Pacific region can still enjoy the preferential access to the United States and European Union markets. The foreign RMG enterprises in Bangladesh can obtain Certificate of Origin easily if they make use of over 70 per cent local fabrics. The European importers can have 13.5 percent tax redemption if the textile products have Certificate of Origin from Bangladesh (Adhikari and Yamamoto, 2007).

C. Adjustment of domestic industrial policy and tax policy

Chinese textile and clothing firms not only need to meet new trade rules but must also confront fiercer competition from other developing countries in terms of product, pricing and technology. The sustainable development and overall interests of textile and

[1] The measures are based on the Interim Measures for the Administration of Textiles Exports, issued on 19 June 2005, and revised with effect from 22 September 2005.

clothing firms might be harmed if they fail to make industrial adjustments and technological innovations. Currently, technological innovation is still limited in the textile and clothing industry, and the ratio of research and development (R&D) expenditures to total sales is less than 1 per cent. The textile and clothing firms need to establish their own original brands in international markets.

On 23 July 2007, the Government of China issued a *Catalogue of Commodities under the Restricted Categories in the Processing Trade*, which lists 1,853 types of restricted commodities including textiles (but excluding clothing) and furniture. At the end of December 2007, an additional catalogue of 589 restricted types of commodities was published. These policies are aimed at reducing the widening trade surplus and promoting domestic industrial adjustment. The Government will take further measures to (a) restrict high levels of energy consumption and high pollution, resource-based exports, (b) encourage exports with indigenous intellectual property rights and (c) expand domestic demand. China will move from the manufacturing of labour-intensive products, such as textiles and clothing, to more capital-intensive products, such as electronics in the coming decades. For example, the Yangtze River delta is maintaining its high growth in the share of national exports because it is shifting to more capital-intensive industries while maintaining and upgrading the labour-intensive industries. The global credit crunch has accelerated the industrial upgrading and transformation in China.

The adjustment of the tax policy has further reduced corporate profits in China. The Government of China has started to implement a new corporate income tax law since 1 January 2008. According to *Notice on Implementation Measures on Transitional Policy of Preferential Corporate Income Tax*, all the enterprises including the SMEs that previously enjoyed a preferential tax rate will transit to the statutory tax rate gradually in the following five years. The enterprises enjoying a 15 per cent corporate income tax rate are subject to a new tax rate of 18 per cent, 20 per cent, 22 per cent, 24 per cent and 25 per cent in 2008, 2009, 2010, 2011 and 2012 respectively while those enterprises with an existing 24 per cent tax rate are subject to a tax rate of 25 per cent from 2008.

D. ‘Go Global’ strategy of the Government of China

The Government of China has been encouraging and supporting efforts by textile and clothing firms to go global with a series of promotion policies. In 2005, the Ministry of Finance and the Ministry of Commerce jointly issued a “Circular on Administrative Measures on a Special Fund for Foreign Economic and Technological Cooperation” ([2005] No.255) to subsidize earlier stage expenses of enterprises undertaking foreign economic and technological cooperation, such as expenditures on composing a project feasibility report, technological and consultancy fees, a subsidy for loan interest not exceeding five years, and overseas business expenses. According to Zhejiang province’s “Measures on the Administration of the Fund to Support Companies to ‘Go Global’” (7 December 2005), the fund is aimed at: (a) supporting the establishment of overseas specialized wholesale markets, manufacturing enterprises and R&D institutions; (b) the implementation of a “market diversification” strategy; (c) the promotion of overseas marketing by small and medium-sized enterprises (SMEs); and (d) participation in overseas trade and investment fairs by the enterprises (Zhejiang Foreign Trade and Economic Cooperation Bureau, 2005).

On 26 July 2006, a Special Fund was set up to support the restructuring of the textile industry and the efforts of Chinese textile companies to “Go Global. The Ministry of

Finance, the State Development and Reform Commission and the Ministry of Commerce issued a “Circular on Relevant Policies to Promote Chinese Textile Industry to Shift New Ways of Growth in Foreign Trade and Support Chinese Textile Enterprises to Go Global”, allocating a special government fund of Y 1.36 billion for encouraging technology innovation, industrial upgrading and OFDI by textile enterprises. In particular, the Government supports the establishment of overseas economic and trade zones by granting subsidies for loan interest, land supply, manufacturing facilities, infrastructure and supporting services. The initial fund was Y 560 million to be provided to provincial governments, which were required to formulate their own measures on the administration of the fund in accordance with the guidelines set by the central Government. The amount received by each province varied proportionately with exports and overseas investment of each province (World Trade Organization, 2008). For example, on 26 October 2006, Jiangsu province issued “Measures on the Administration of the Fund to Support Companies to ‘Go Global’” allocating the fund to support the establishment of overseas economic and trade zones, OFDI by textile companies, overseas marketing and sales networks, and activities of service companies in facilitating overseas investment by textile companies (Department of Foreign Trade and Economic Cooperation, Jiangsu, 2006).

The establishment of overseas economic and trade zones has been actively promoted by the Government of China. The Ministry of Commerce hopes that industries with domestic competitive advantages and massive production capability, such as textiles, clothing, electronic appliances, construction materials, non-ferrous metals and processing of agricultural products, will be transferred gradually to overseas economic and trade zones in order to avoid trade friction as well as establish international marketing networks. Currently, 19 overseas economic and trade zones in Cambodia, Egypt, Indonesia, Republic of Korea, Mauritius, Mexico, Nigeria, Pakistan, Russian Federation, Thailand, Venezuela, Viet Nam and Zambia have been approved by the Ministry of Commerce. These zones are mainly attracting Chinese enterprises including SMEs. Most of these economic and trade zones have completed the construction of infrastructure and are serving as an important platform for OFDI by domestic textile and clothing firms in China. In addition, since the beginning of 2008 the Ministry of Commerce has been sponsoring a series of foreign economic and trade fairs to promote the overseas economic and trade zones.

III. Case study: Spatial expansion to Cambodia by textile and clothing clusters in the Yangtze River delta

The main research method used in preparing this report was a case study of textile and clothing clusters in eastern China, particularly Zhejiang, Jiangsu, Guangdong, Shandong and Fujian provinces as well as Shanghai. Two-thirds of the textile clusters are located in Zhejiang and Jiangsu provinces while one-third and one-fifth of the clothing clusters are located in Guangdong and Zhejiang provinces, respectively.

Zhejiang and Jiangsu provinces are located in the Yangtze River delta and their economic integration has been further strengthened since 2000.. The development of textile and clothing clusters in Jiangsu province has followed the same route as those in Ningbo City and Shaoxing City of Zhejiang province. However, as the textile and clothing clusters in China have become one of the main sourcing bases for exports, the industrial clusters have also become more export-oriented and are actively participating in original equipment manufacture (OEM). Therefore, the textile and clothing clusters in the Yangtze River delta are typical of such clusters in China and suitable for case studies. The industrial agglomeration has important economic and social implications given the creation of a large number of enterprises, entrepreneurs and employment in the region. The Yangtze River delta mainly comprises Shanghai City, Zhejiang province and Jiangsu province.

The original data were collected from the Yangtze River delta region, mainly in Zhejiang province and Jiangsu province. In Zhejiang province, the sample textile and clothing firms were in Ningbo City and Yiwu City. In Jiangsu province, the sample textile and clothing firms were mainly located Wuxi city, Nantong City and Kunshan City. Interviews were also conducted with government officials in charge of foreign economic cooperation at the Zhejiang Economic and Trade Commission (Annex 1). The report also makes use of a descriptive analysis of secondary data on OFID by Chinese textile and clothing firms in Asian and Pacific region LDCs. The secondary data include that given in the *Statistics Bulletin of China's Outward Foreign Direct Investment* (2003-2006) and *The Statistics Yearbook* (2004-2007) for Zhejiang and Jiangsu provinces.

Table 8 lists the main textile and clothing companies interviewed. The majority of large-scale textile and clothing companies in China are expanding business to Cambodia through joint ventures, except for Ningbo Mingda Knitting Group Co., Ltd., Jiangsu Diao Garment Group Co., Ltd., Jiangsu AB Group Co., Ltd. and Wuxi Guangming Co., Ltd, which remain under sole Chinese ownership. Almost all the enterprises interviewed acknowledged that they seldom subcontracted to, or formed some other type of strategic partnership with local firms because very few integrated cotton and textile production facilities were operating in Cambodia. Cotton farming still lacks effective organization and only a few local enterprises are engaged in processing cotton into yarn and fabric (Yasuo, 2003). However, these companies have already established a complete value chain in China. All the enterprises interviewed reported that they had recouped their investments within two to five years.

Chinese textile and clothing firms can enjoy many advantages through OFDI in Cambodia. The interviewed firms provided FDI to Cambodia mainly for the following reasons:

(a) China has a sound political relationship with Cambodia. Chinese leaders of different generations have been very close to King Sihanouk and cultivated profound friendship with him, thus laying a solid foundation for long-standing and stable development of Sino-Cambodian relations. The two countries signed the agreement on trade, investment promotion and protection in 1996 and set up an economic and trade cooperation committee in 2000. In order to help Cambodia with its post-war reconstruction, China has provided Cambodia with a certain amount of economic aid (Ministry of Foreign Affairs of the People's Republic of China, 2003).

(b) Cambodia has adopted many favourable policies aimed at attracting overseas FDI. For example, enterprises investing in Cambodia will be exempt from all taxes for nine years and imports of raw materials are free of import tariffs. The entrepreneurs in the interviews agree that there is more ample room for economic development in Cambodia compared with other neighbouring countries such as Vietnam and Thailand.

(c) Exports from Cambodia still have duty-free and quota-free market access to Australia, Canada, the European Union and Japan. In addition, the United States has granted loose quotas and favourable import tariffs for Cambodian textiles and garments. The United States imposed an average 17 percent tariff on Cambodian garment exports in 2007. As for China, the highest general tariff rate ranges from 3.9% to 32.0% and the peak tariff rate can range from 60.0% to 113.5% (Martin, M., 2007).

Avoiding trade barriers to entering the European Union and United States markets is a major consideration. The European Union, Japan and the United States are the main export destinations for Chinese textile and clothing products. In order to restrict the rapid growth of such exports, China signed Memoranda of Understanding with the European Union and the United States in 2005. Meanwhile, the Government of China issued provisional rules on a new quota allocation system for domestic textiles and clothing companies.

Since 22 September 2005, textile and clothing producers in China have been granted a quota by the Ministry of Commerce in terms of each affected market and category when they export to countries or regions that have either imposed restrictions on China's textile and clothing exports or signed agreements with China regarding affected categories of textile and clothing products. However, some developed countries are still granting Cambodian imports favourable treatment. Cambodia enjoys favourable treatment of its textile and clothing exports to the European Union market through the EBA Initiative introduced in March 2001. Cambodian textile and clothing exports also have duty-free and quota-free market access to Australia, Canada and Japan. All the interviewed firms admitted that they had established production bases in Cambodia in order to enter the European Union and United States markets more smoothly. The implementation of China-ASEAN Regional Trade Agreement has strengthened the trade and investment relationships between China and ASEAN member states. Compared with Laos, Cambodia has better geographical conditions. The economic linkages between China and ASEAN member states are deeper than south Asian countries such as Bangladesh.

A second important issue has been the appreciation of China's currency as well as rising domestic factor prices. All the interviewed firms indicated that the profit margin in the textile and clothing sector had declined rapidly, due to the appreciation of China's currency since 2005 as well as to increasing factor prices such as the costs of labour, land and raw materials in 2007 and 2008.

On 21 July 2005, the People's Bank of China issued an "Announcement on Improving the Exchange Rate Regime of Renminbi" in order to establish a more flexible exchange rate regime by abandoning the policy of pegging to the United States dollar and adopting a managed floating exchange rate based on market demand and supply with reference to a basket of currencies. By the end of 21 July 2008, the yuan renminbi had appreciated by 21 per cent compared with the beginning of reform on 21 July 2005. The rapid appreciation of the yuan renminbi within a short time has reduced the profit margins of export-oriented textile and clothing firms in China and many enterprises have declined to accept large long-dated orders.

The cost of labour has risen rapidly since the implementation of the new labour contract law on 1 January 2008, which gave staff with more than 10 years of service with a company the right to sign contracts that would protect them from dismissal without cause.

It also required employers to contribute to their employees' social security accounts and set wage standards for workers on probation and overtime. There has been a shortage of rural labour in the coastal provinces of China including Zhejiang and Jiangsu in recent years. In contrast, the average monthly salary of Cambodian workers is around US$ 56 – much lower than that paid in China.

Meanwhile, the shortage of electricity and cotton supplies has constrained the expansion of production capacity. In 2007, the international cotton price increased steadily due to the drought in Australia and the reduction of the cotton planting area in the United States. Cotton production in China in 2007 was 6,728,000 tons, but total consumption reached 10,886,000 tons, so imports of cotton amounted to 4,158,000 tons. Most of Chinese textile and clothing firms believe that they will benefit in the long run if they relocate some of their production to the LDCs because the prices of factors of production in China have been going up in the recent years. Some forward-looking entrepreneurs are willing to make OFDI in the LDCs even if the infrastructure is poor and there is the shortage of electricity.

A third important issue is that of China-Association of Southeast Asian Nations (ASEAN) regional trade agreements. Because Cambodia is a member country of ASEAN and is located in the Greater Mekong Region, the deepening China-ASEAN regional trade agreements have further encouraged OFDI in Cambodia by the textile and clothing enterprises in Zhejiang and Jiangsu provinces.

Table 8. Main textile and clothing companies covered during fieldwork

Province	**Sample enterprises**	**Subsidiary**	**Ownership**
Zhejiang	Shenzhou International Group Holdings Ltd.	Shenzhou (Cambodia) Co., Ltd.	Joint venture with Cambodia
	Ningbo Mingda Knitting Group Co., Ltd. (Mingda Group)	Ningbo New Mingda (Cambodia) Manufacture Co., Ltd.	Sole Chinese ownership
	Ningbo Hongmei Textile & Garments Co., Ltd.	Ningbo Hongmei (Cambodia) Textile and Clothing Co., Ltd.	Joint venture with Chile
	Yiwu China Commodity City • Bing Wang Clothing Market • International Trade City	Ten local SMEs operating within the market such as Yiwu Wei Hai Zipper Company and four businessmen from Bangladesh,	

		Cambodia Ethiopia and India	
Jiangsu	Wuxi Guangming (Group) Co., Ltd.	Gold-Kamvimex Garment Factory Ltd.(Cambodia)	Joint venture with Hong Kong, China
	Hong Dou Group Co., Ltd.	Sihanoukville Special Economic Zone	Joint venture with Cambodia
	Jiangsu Diao Garment Group Co., Ltd.	Jiangsu Diao (Cambodia) Garment Co., Ltd.	Sole Chinese ownership
	Jiangsu AB Group Co. Ltd.	Xinlan Garment Making Co., Ltd.	Sole Chinese ownership

A. Zhejiang province

In Zhejiang province, the interviews were mainly with Shenzhou International Group Holdings Ltd., Mingda Knitting Group Co., Ltd. and Hongmei Textile & Garments Co., Ltd. In Ningbo, the interviews were with 10 medium and small-sized enterprises and four businessmen from Cambodia, Bangladesh, India and Ethiopia at Yiwu specialized wholesale market.

1. Integrating Cambodia into its vertically-integrated value chain

The fieldwork showed that Shenzhou International Group Holdings Ltd., Mingda Knitting Group Co., Ltd. and Hongmei Textile & Garments Co., Ltd. in the Ningbo clothing cluster had a relatively complete vertically-integrated value chain and rich experience in OEM for world-famous brands.

(a) Shenzhou (Cambodia) Co., Ltd., (Shenzhou Cambodia)

This company is a wholly owned subsidiary created by Shenzhou International Group Holdings Ltd. (“Shenzhou International”) (see annex 3), with an investment of US$ 3.8 million in June 2005 (figure II). It specializes in the manufacture and sale of knitwear products at two rented factory buildings covering 15,500 m^2 and newly-built auxiliary buildings totalling 5,000 m^2 in Vattanac Industrial Park, Phnom Penh. Shenzhou Cambodia started production in September 2005 and realized a profit in June 2006. It mainly serves

North American customers and has successfully gone through factory inspections by world-famous clients including NIKE, ADIDAS, PUMA and UNIQLO. In June 2006, the board of directors decided to increase its investment by US$ 300 million.

Shenzhou International Group Holdings Ltd. and its subsidiaries (the "Group") is the largest integrated knitwear manufacturer in China. The Group mainly specializes in manufacturing high-quality knitwear on an OEM basis. It is also the largest knitwear exporter and Chinese garment supplier to Japan according to a report on the development of China's garment industry and the annual reports on China's international trade in textile and clothing in 2006 and 2007. The Group currently has more than 35,200 employees. The factories cover 900,000 m^2 and the annual output of various types of knitwear is more than 110 million pieces in the Ningbo Economic and Technical Development Zone.

The product line of the Group ranges from casual wear to sportswear with the major international renowned sports wear clients including NIKE, ADIDAS, PUMA an UNIQLO. The export destination has been extended from Japan to the whole Asian and Pacific region, and the European and the United States markets. In November 2005, Shenzhou International was listed on the Main Board of Hong Kong Stock Exchange, thus realizing the corporate objective of becoming the most competitive knitwear manufacturer in the world. In addition, in 2007 the Group continued to expand its dyeing and finishing capacity by acquiring additional dyeing and finishing equipment. To complement the expansion of its the dyeing and finishing capacity, the Group also increased its knitting, printing, embroidery and manufacturing processes. The factory particularly designated for ADIDAS started operating in 2007 in order to meet increasing orders from ADIDAS.

(b) Ningbo New Mingda (Cambodia) Manufacture Co., Ltd.

The company was established in 2006 in Vattanac Industrial Park, Phnom Penh with an investment of about US$ 3 million. Its annual production capacity has reached 5 million pieces of knitted clothing with 1,500 units of sewing machinery and 2,000 sewing employees. The company is a subsidiary of Ningbo Mingda Knitting Group Co., Ltd. (Mingda Group), which is controlled by Ningbo Shanshan Co., Ltd., and which was listed at Shanghai Stock Exchange in 1997. It is one of the leading textile and clothing enterprises in the cluster. All the knitted products made by Mingda Group target the international market. The sound regional industrial environment and the scale effects by local textile and clothing clusters partly provide a trade-off against the negative effects of trade friction and yuan renminbi appreciation. The Mingda Group started producing knitted products in 1974. Currently it is ranked in the top three in the knitting sector of the Ningbo textile and clothing cluster. It has a relatively complete production line, owning one trading company and 12 factories handling weaving, dying, embroidering, cutting out and sewing. The Group has 3,800 employees.

(c) Ningbo Hongmei (Cambodia) Textile and Clothing Co., Ltd.

The company was established in March 2006 in Canadia Industrial Park, Phnom Penh by Ningbo Hongmei Textile & Garments Co., Ltd with an investment of US$ 1 million. It has a production capacity of 1 million shirts annually. Ningbo Hongmei Textile & Garments Co., Ltd. is a joint venture with Chile that was established in March 2003. It is an integrated export-oriented enterprise with a total investment of US$ 2.1 million. The company is mainly engaged in R&D, design, production, marketing and service of garments. Its main products include jackets, casual and beach trousers, and men's, women’s and children’s shirts. Its products are not only exported to Hong Kong, China but also Australia, Canada, the Republic of Korea, New Zealand, the United States, plus Europe and South America.

The production capacity and ancillary facilities of Shenzhou Cambodia have progressively expanded, which has contributed to the formation of complete garment value chain in Cambodia. For example, Shenzhou Cambodia set up a printing and embroidery production line in 2007 in order to better satisfy the needs of customers. In fact, Shenzhou Cambodia has become a stable production base in the South-East Asian region for the Group.

Both Ningbo Mingda Knitting Group Co., Ltd (Mingda Group) and Ningbo Hongmei Textile & Garments Co., Ltd have also successfully included Cambodia in their respective vertically-integrated value chains. In the interview, Qiu Miaofa, General Manager of Mingda Knitting Group Co., Ltd. (Mingda Group), remarked:

> “We have our own weaving factory, dying factory, embroidery factory and printing factory. We are competitive because we can conduct overall production and deep processing with high technological contents. [Our] 70 per cent profit on one ready-made garment lies in the initial fabric processing. We have passed the factory inspection by American Disney Co., Ltd., which has strengthened our cooperation. The direct cost of establishing a factory in Cambodia is not lower than that in China, but we can make profits from the fabrics we have produced and exported.”

The clients of Ningbo Hongmei Textile & Garments Co., Ltd are mainly in South America, so the company does not face high trade barriers to its exports. However, the fiercer domestic competition and appreciation of the yuan renminbi have forced the company to relocate some of its production in Cambodia. The manager of the company told us that there was a profit margin when the subsidiary moved on the right trajectory. The profit margin of exports from Cambodia can be 2-3 per cent higher than those from China, particularly to the United States and European Union markets.

The fieldwork in the Ningbo clothing cluster showed that the subsidiaries in Cambodia had gradually been integrating into the vertically-integrated value chain of textile and clothing firms in China, thereby becoming an important node in global textile and clothing value chain.

2. Realize inclusive development by training local workers and improving the working environment

The three textile and clothing firms interviewed have created a set of effective management methods to develop successful subsidiaries in Cambodia. They have contributed to inclusive development through the training and improvement of local employees, and upgrading technological capability.

Shenzhou International Group Holdings Ltd. is a typical successful example. First, it has adopted an intensive management model and introduced its corporate culture to Cambodia. The company sent about 70 Chinese managerial and technical staff to teach Cambodian workers by personal example and verbal instruction so that Cambodian staff would form good working habits, improve their skills gradually and strengthen their awareness of quality. The company quickly took the right path. Within three years, the number of garment workers increased to 5,000 and monthly output rose from 150,000 to 1,300,000 pieces. More job opportunities have been created for the local workers. In addition, the company has met global manufacturing standards set by famous international brands such as NIKE and ADIDAS, and have passed the factory inspections successfully. The knowledge spillover of Shenzhou Cambodia has undoubtedly improve the local production and managerial capability.

Second, Shenzhou Cambodia has strengthened its communication with local workers. Ma Jianrong, General Manager of Shenzhou Group, remarked during the interview that the workers' representatives and trade union could become the driving force of corporate growth if the enterprise cooperated well with them. In addition, he said, the enterprise had set up a suggestion box at each workshop so that employees could put forward suggestions and viewpoints to the managers. If their problems cannot be solved satisfactorily in the context of Cambodian law and regulations, the managers will provide explanations to the employees concerned. All problems should be nipped in the bud so that garment workers will be able to work happily. The Chinese managers have also grasped the local language and communicate with local workers effectively.

Third, a good working environment has contributed to the improvement of the Cambodian employees' efficiency. At the start of operations, local workers' efficiency was only 50 per cent of employees in China, but it increased by 20 per cent after adopting piecework wages. The incentives of local workers have been stimulated with the new reward system, in which the local workers can enjoy higher salaries if they can produce more. As a result, the monthly salary of each worker is about US$ 80 on average and the maximum can be as high as US$ 100. It is higher than the average salary of US$ 56 in Cambodia. In addition to increasing income, Shenzhou Cambodia also established a new canteen for its Cambodian workers, which covers 2,000 m^2. It is the first special canteen for local employees in Vattanac Industrial Park, Phnom Penh. In the past, the Cambodian workers had to sit on the ground to eat their lunch.

3. Forging business linkages between China and Asia-Pacific least developed countries through the specialized wholesale market

The prosperity of the specialized wholesale market is itself a good example of reducing poverty and promoting rural development in China. As a county-level city located in the middle of Zhejiang province, Yiwu City covers 1,105 km^2 and a population of 1.67 million, of which 1 million people are not permanent residents but are there to do business. In 1988, Yiwu county was changed into Yiwu City. Since China's adoption of the open-door policy, Yiwu has been making unremitting efforts to implement the strategy of developing the city through promoting commerce and to foster a market system based on trade in "small commodities". This, in turn, has promoted regional economic development and realized an historic transition from a traditional agricultural county to a prosperous modern commercial city. Yiwu has become the biggest distribution and exhibition centre of small commodities in China. The turnover of Yiwu China Commodities City Group Co., Ltd reached US$ 42.43 million in 2005 (table 9).

Table 9. Turnover of Yiwu China Commodities City Group Co., Ltd.

Year	Turnover (US$ in real terms)	Percentage change
2001	31.18	9.8
2002	33.82	8.5
2003	36.51	8.0
2004	39.25	7.5
2005	42.43	8.1

Sources: Yiwu Statistics Bureau, 2007, Yiwu Statistics Yearbook 2006.

The specialized wholesale market has gone through three stages of development in the past 26 years: (a) an agglomeration market; (b) a wholesale market; and (c) an exhibition and trade market. It has been moved five times and expanded nine times in that period. Since it was established at the beginning of the 1980s, the specialized wholesale market in Yiwu has mainly targeted 900 million farmers in rural areas. It became a national market in the mid-1990s and an international market in 2002. Since then, it has become an international distributing centre, circulation centre and international trade platform for SMEs around China as well as a magnet for SME buyers at home and abroad.

Yiwu China Commodity City has expanded its international market since the mid-1990s, and the annual export growth rate has been more than 40 per cent since the millennium year. The commodities have been exported to 212 countries and regions. About 8,000 foreign businessmen visit for procurement purposes at the market every year. The number of containers sent abroad from Yiwu exceeds 1,000 daily. In 2005, exports to Asia accounted for 39.68 per cent, followed by Europe (27.32 per cent), the United States (17.32 per cent), Africa (11.62 per cent) and Oceania (2.58) per cent (Yiwu Yearbook Leading Group of Editing Office, 2005). The volume of international trade in Yiwu now exceeds that of domestic trade.

The prosperity gained from international trade at the specialized wholesale market has not only encouraged local businessmen to establish a China Commercial City in countries such as Brazil, Cambodia, South Africa and the United Arab Emirates, but also to set up more and more subsidiaries in those countries to promote their business. The frequent visiting of Yiwu specialized wholesale market by the businessmen from the LDCs such as Cambodia, Bangladesh, Ethiopia and so on has led to the expansion of local SMEs to the LDCs through conducting international trade, setting up overseas trading offices and undertaking OFDI in the end. Thus, more and more OFDI by local SMEs can be expected in Asian and Pacific LDCs through the platform of the Yiwu specialized wholesale market. For example, some Yiwu sock manufacturing companies have provided OFDI to Cambodia. Zhuji Tairong Knitting Co., Ltd, a joint venture with the Republic of Korea in the local sock cluster that was established in 2001, set up Tairong (Cambodia) Knitting Co., Ltd. in 2005. The export volume from Cambodia to the United States and the European Union by Tairong (Cambodia) Knitting Co., Ltd reached US$ 2.5 million in the first two months of 2008.

The fieldwork in the Yiwu specialized wholesale market showed that the business linkages between Yiwu and Bangladesh, Cambodia and Viet Nam have been developing fast during the past decade, although the ratio of businessmen from the Asian and Pacific LDCs is relatively limited compared with those from other developing countries in Africa and the Middle East. The interviews with local SMEs at the Yiwu Bing Wang Clothing Market in August 2008 indicated that most of the visiting foreign businessmen were from

India, Africa and the Middle East. One local businesswoman, who owns her own clothing factory, remarked while making deals with two Ethiopian clients that:

> "Most of my clients are from African countries and the Middle East. Occasionally, there are some businessmen from Bangladesh, Cambodia and Viet Nam. I have never thought of setting up a factory in a foreign country. However, some of my relatives are pushing sales of local small commodities in South Africa".

However, at least five interviewees dealing in clothing accessories and raw materials at Yiwu International Trade City said they were exporting zippers, buttons, lapping cloth and other accessories to Cambodia and Bangladesh. The marketing manager at Yiwu Wei Hai Zipper Company noted that:

> "We deal with businessmen from both Bangladesh and Cambodia. Our annual exports to the two countries amount to Y 500,000 (about US$ 60,000). But up to now, we do not have any plans to invest abroad. "

Although many foreign businessmen are to be found at the Yiwu specialized wholesale market each day, it is not easy to meet businessmen from the Asian and Pacific LDCs. One Cambodian businessman provided the following explanation:

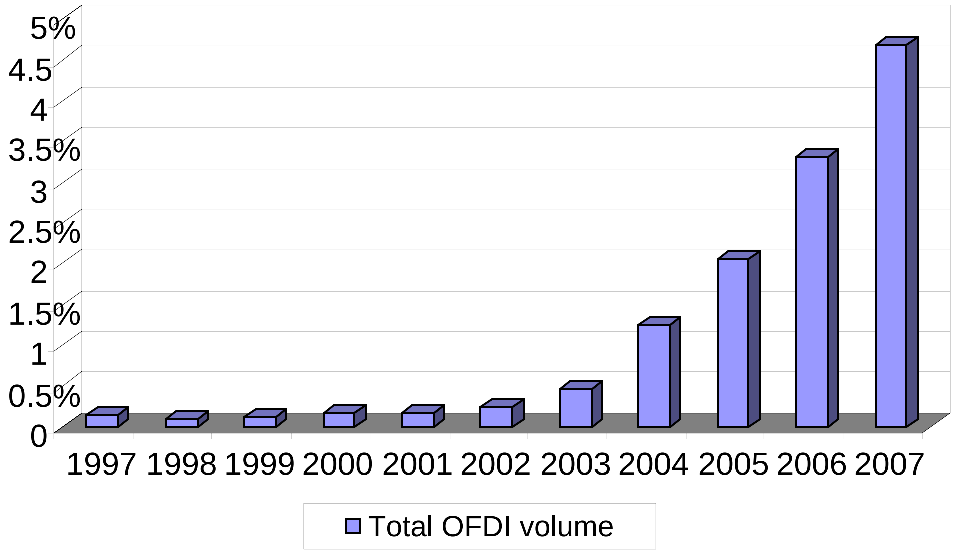
> "There is also a China Small Commodity City in Cambodia. I learnt about Yiwu there three years ago. Then I started to introduce local garments and clothing accessories to Cambodia. Cotton farming, yarn spinning and textile fabric production are not competitive at all in my country. More Cambodians need to know the market and their entrepreneurship might [then] be nurtured. The Governments of China and Cambodia both need to further promote the specialized wholesale market."

The Yiwu specialized wholesale market will play a more important role in the regional development of Asia and the Pacific with its economy of scale and sound commercial facilities. Therefore, the business linkages between China and the Asian and Pacific LDCs can be further strengthened through the specialized wholesale market because its small commodities can meet the demands of people living in the LDCs. The businessmen from the LDCs in Asia and the Pacific are encouraged to attend annual trade fairs held by the specialized wholesale market in the Yangtze River delta and the rest of China to promote inclusive development and reduce the poverty in the region. In addition to creating business opportunities for businessmen from the LDCs, the specialized wholesale markets have encouraged more and more Chinese businessmen to do business with, and promote economic development in the LDCs.

B. Jiangsu province

In the past decade, OFDI in Jiangsu province has been steadily rising. The total volume of OFDI increased from US$ 14 million in 1997 to US$ 468 million in 2007 (table 10). The annual growth rate has exceeded 50 per cent in past four years (figure II). The OFDI has helped the enterprises to enter the international market directly and promote the exports of parent companies by effectively avoiding international barriers. According to a survey in Wuxi City, Jiangsu province in 2007, exports increased by US$ 255 million while OFDI increased by US$ 100 million. In addition, some enterprises have introduced advanced foreign technology. Moreover, OFDI has promoted the inflow of scarce natural resources from foreign countries to China.

Figure II. Total volume of OFDI in Jiangsu province, 1997-2006 (US$ 100 million)



Sources: Jiangsu Yearbook of Statistics,1998-2007; and Jiangsu Foreign Economic and Trade Commission.

Table 10. Growth rate of total OFDI in Jiangsu province, 2003-2006

Year	Growth rate of OFDI (%)
2003	83.4
2004	169.5
2005	63.1
2006	61.7

Sources: Jiangsu Yearbook of Statistics, 2004-2007; and Jiangsu Foreign Economic and Trade Commission.

More and more of the textile and clothing enterprises that have made OFDI in ASEAN countries are starting to reap the harvest. Interviews with the following four garment enterprises in Jiangsu province showed that Chinese textile and clothing firms had changed their investment behaviour from voluntary overseas expansion by individual firms to the establishment of overseas economic and trade cooperation zones in Cambodia. This was facilitating the collective expansion of Chinese textile and clothing firms, and the formation of industrial clusters in Cambodia.

1. From voluntary overseas expansion by individual firms to the establishment of overseas economic and trade cooperation zones

(a) Gold-Kamvimex Garment Factory Ltd. (Cambodia)/Wuxi Guangming (Group) Co., Ltd

Wuxi Guangming (Group) Co., Ltd. used to be a state-owned enterprise. It was established in 1955 and completed ownership transformation in 2005. The company mainly specializes in the production of garments for export. In 1978, Guangming Group started to extend the compensation trade with Hong Kong Esquel Enterprises Ltd. The compensation trade means that the inward foreign direct investment is repaid from the revenues generated by that investment. Afterwards, it became one of the biggest clothing factories in South-East Asia, with an annual production capacity of 3 million units and sales revenue of RMB 30 million. However, with strengthening globalization, domestic competition became much fiercer with the rapid growth in the number of textile and clothing factories in the region. Meanwhile, the expansion into international markets was constrained by many types of trade barriers such as high tariffs, quotas and anti-dumping allegations and so on. The company decided FDI was the answer to meeting the challenges and it established Gold-Kamvimex Garment Factory Co., Ltd in Phnom Penh with a registered capital of US$ 1.6 million in 1997. After 10 years of development, its subsidiary in Cambodia now has an annual production capacity of 2.5 million units of shirts and leisurewear. All the products are exported to the European and United States markets.

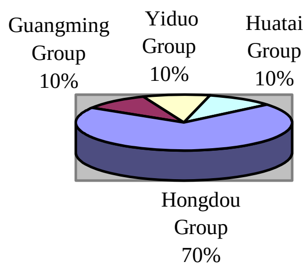
In order to ensure the security of overseas capital, some Chinese textile and clothing firms mainly outsource production in Cambodia. The Guangming Group accepts orders, supplies raw materials and makes payments at its headquarters in China. Gold-Kamvimex Garment Factory Ltd. in Cambodia is mainly responsible for production, quality control and timely delivery. Except for some vault cash, other expenses are reimbursed by the parent company on time. The management model has proved effective because the parent company has absolute control of overseas companies, which facilitates unified regulation and management. The company has not only created job opportunities for local people, but has also improved production capability in Cambodia. The successful operation of the company in Cambodia has led to its participation in the establishment of the SSEZ, which will promote local economic development and greatly increase employment opportunities for local people.

(b) Sihanoukville Special Economic Zone (SSEZ) /(Hong Dou Group Co., Ltd)

The Sihanoukville Special Economic Zone (SSEZ) Co., Ltd., the first overseas business and economic cooperation zone of Jiangsu province, was launched in Cambodia on 23 February 2008 as a joint venture between Jiangsu Taihu International Economic Cooperation Zone Co., Ltd. and Cambodia International Investment Development Co., Ltd. The SSEZ, which covers an initial area of 1 km^2, will be expanded to 11.08 km^2 with an estimated investment of US$ 3 billion by 2015. After completion, the zone will be able to accommodate about 300 companies, offer 80,000 job vacancies and achieve an export volume worth US$ 2 billion. The major industries will include textiles and garments, machinery and electronics as well as high-technology businesses. It will be the largest export processing zone in Cambodia.

Jiangsu Tai Hu Cambodia Economic Zone Investment Co., Ltd. was founded in October 2006. The main shareholders include Jiangsu Hongdou Industrial Co., Ltd. (70 per cent) (see annex 4 for organizational structure), Wuxi Guangming (Group) Co., Ltd. (10 per cent), Wuxi Yiduo Investment and Development Group Co., Ltd. (10 per cent) and Hua Tai Investment and Real Estate Consultancy Co., Ltd. (10 per cent) (figure III). The company undertakes overseas direct investment, overseas processing and international trade in commodities and technology.

Figure III. Main shareholders of Jiangsu Tai Hu Cambodia Economic Zone Investment Co., Ltd.



Source: Compiled by the authors.

Six companies in Wuxi signed agreements with the developers to establish their subsidiaries within the SSEZ in February 2008.[2] The initial annual output was expected to be 1.5 million to 2 million pieces, mainly for export to the European Union and United States markets. Meanwhile, infrastructure construction has been further promoted within the SSEZ. A heat-engine plant is under construction by the Nanguo Heat-Engine Factory, which is another subsidiary of the Hongdou Group. The completion of the plant will meet the demand for electricity and steam by new enterprises within the zone. It can be expected that the textile and clothing clusters in Cambodia will be nurtured in the near future as a result of the successful experience gained from establishing industrial parks in Jiangsu province.

The firm support provided by the Government of China for overseas economic and trade zones is helping to reduce overseas investment risks of single enterprises. In addition, OFDI by dozens of enterprises can bring about the cluster effects, which can lead to the agglomeration of production and innovation activities, the easy transmission of new ideas, the availability of intermediate inputs, the supply of skilled labour, the organization of linkages among business actors, and greater bargaining power with the host country. Moreover, the overseas economic and trade zones can contribute towards enriching the OFDI experiences of Chinese enterprises as well as increase their international competitiveness. Overseas economic and trade zones have offered SMEs in China a platform for increasing corporate capability in undertaking international production and forging international marketing network.

2. Implementing internationalization strategy with the establishment of a large-scale production base in Cambodia

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[2] Wuxi Nanguo Co., Ltd. (a subsidiary of Jiangsu Hongdou Industry Co., Ltd.), Wuxi Tian Xiu Textile Products Co., Ltd., Jiangsu Shen Xi Construction Machinery Co., Ltd., Wuxi Han Shen Electric Co., Ltd., Wuxi Li Jia Packaging and Decorating Co., Ltd., Wuxi Xing Da Plastic New Material Co., Ltd. Wuxi Nanguo Co., Ltd. already entered the SSEZ in July 2007.

The interviews in Jiangsu Diao Garment Group Co., Ltd. and Jiangsu AB Group Co., Ltd. showed that both companies regarded the establishment of a production base in Cambodia as part of their internationalization strategy in addition to the avoidance of trade barriers.

Jiangsu Diao Garment Group Co., Ltd. established Jiangsu Diao (Cambodia) Garment Co., Ltd. in Phnom Penh in 1998. The company's manufacturing capacity in Cambodia increased from 520,000 pieces in 2006 to 640,000 pieces between January and September 2007. The export volume of RMG reached US$ 5.5 million and profits grew by Y 1.6 million with increasing exports from Cambodia to the United States. The company is expanding its production base in Cambodia through integrating garment-making, product development, brand operation and international marketing. Meanwhile, its subsidiary in Cambodia has further contributed to the internationalization of the whole group. The group has also established business partnerships with famous American garment firms through its production base in Cambodia.

Likewise, Jiangsu AB Group Co. Ltd. is one of several famous export brands supported by the Ministry of Commerce in China, but the quota system has constrained the group's business expansion to European and American markets. In 2006, the company invested US$ 16.5 million in creating Xinlan Garment Making Co., Ltd in Cambodia. The factory covered 6,000 m^2 and production started in the middle of May 2007 with about 300 employees. The relocation of some low value-added underwear production to Cambodia has helped the company to solve quota issues and avoid trade barriers. The AB Group sends raw materials from China to Cambodia and then exports the underwear to Europe and the United States.

The infrastructure of Cambodia is still underdeveloped and the steady supply of water, electricity and raw materials cannot be guaranteed. Thus, the AB Group has had to send manufacturing machinery and raw materials from China to Cambodia. It is planning to expand its production capacity in Phnom Penh and increase the annual sales volume of Xinlan (Cambodia) Garment Making Co., Ltd. to Y 200 million in the near future. The group is further promoting its internationalization process of establishing an international marketing network by setting up a large-scale production base in Cambodia.

IV. Is OFDI from China to Cambodia sustainable?

The large-scale textile and clothing enterprises interviewed during this study have mainly expanded their production capacity in Cambodia instead of shifting their whole production process from China to Cambodia. This is because the textile and clothing clusters in the Yangtze River delta still enjoy the advantages of sound infrastructure and relatively complete industrial linkages, with which LDCs unable to compete in the short term. Therefore, the relocation of some production from China to LDCs has not had a great impact on local employment. In fact, the global financial crisis has led to a rising number of unemployed textile and clothing workers in China.

A. The global financial crisis and OFDI from China to Cambodia

The global financial crisis has had a negative impact on economic growth in China. The growth of textile and clothing exports has slowed to single digit levels. According to

China Customs, the growth rate of Chinese textile and clothing exports rose by only 8.6 per cent, year-on-year, from January to October 2008. The orders received by textile and clothing companies at the China Import and Export Fair declined by 30 per cent in the autumn. In order to combat the global financial crisis, on August 2008 the Ministry of Finance increased tax rebate rates on some textile and clothing exports from 11 per cent to 13 per cent (Zhao, 2008).

A large number of the enterprises in the textiles, plastics, electronics, ceramics and construction materials sectors of the Yangtze River and Pearl River delta regions have gone bankrupt, including Zhejiang Jianglong Textile Printing & Dyeing Co., Ltd., China's biggest printing and dyeing company, due to the complete depletion of capital. The statistics compiled by the administration for SMEs in Guangdong province in southern China indicate that 7,148 companies have closed or been moved out the Pearl River delta between January and September 2008 (Chen, 2009).

Qiu Miaofa, General Manager of Mingda Knitting Group Co., Ltd. (Mingda Group), commented:

> "Our profits in 2007 amounted to US$ 8.82 million, but in the first half of this year [2008], our costs rose by US$ 9.32 million. For example, the appreciation of the yuan renminbi reduced our profits by US$ 2.65 million while our labour costs increased by US$ 4.41 million, our water, electricity and coal bills rose by US$ 1.76 million and the costs of raw materials reduced our profits by US$ 500,000.
>
> However, our profit margin has still been about 6 per cent, thanks to our production base in Cambodia. If it had been otherwise, it would have been impossible for us to accept profitable orders. Foreign businessmen usually subcontract producers in different countries in order to diversify their business risks. The enterprises that own multinational processing bases usually enjoy high favour and have stronger bargaining power. It is easier for them to win big orders. In 2007, an American company placed a US$ 7 million order with us. The order has been increased to US$ 20 million this year [2008]. Thirty per cent of the order is being executed in Cambodia. Meanwhile, another American order specified that 70 per cent was to be produced in Cambodia. If we had not relocated some of our workshops to Cambodia three years ago, our business would have been affected dramatically."

Although the global financial crisis has seriously affected the textile and clothing industry in China, the firms that were interviewed were still operating their Cambodian manufacturing bases smoothly. However, they may have to adjust their production capacity according to the demand of their major customers.

B. Factors constraining sustainable OFDI from China to Cambodia

The interviews conducted in the Yangtze River delta region showed that the sustainable OFDI from China to Cambodia can be further stimulated if the business environment in Cambodia can be further improved.

1. Poor infrastructure

Cambodia underwent political turmoil and chaos for many years, and its infrastructure was seriously damaged by war. The constant short supply of water and electricity cannot guarantee manufacturing output. Usually, no advance notice is given of stoppages of water and electricity supplies. All the interviewed textile and clothing firms have their own electric generators in case of power cuts.

2. Relatively high labour cost compared with other LDCs

According to Cambodian law, a garment worker's legal minimum monthly salary is US$ 56. Garment enterprises are not required to buy life insurance for their employees. However, Cambodian workers can still enjoy good social benefits because the garment enterprises have to take responsibility for all medical expenses of employees who fall ill during their work period.

Meanwhile, Cambodian workers are relatively inefficient compared to Chinese workers. The labour law in Cambodia stipulates that a certain number of workers' representatives should be elected in proportion to total employees. For example, Shenzhou Cambodia has 3,000 employees and about 50 workers' representatives. The workers' representatives in Cambodia are very powerful because Certificates of Origin are not issued to the enterprise after any workers' representatives make complaints to Ministry of Commerce. Trade unions in Cambodia are very active. When workers receive unfair treatment in garment enterprises, they complain to their trade union. Trade unions can enter garment enterprises, and they must be treated well and allocated offices. Garment enterprises cannot fire workers until several warnings have first been given with permission from the representatives.

3. Serious corruption

The Government of Cambodia is usually inefficient and permeated by serious corruption. Land purchases, applications for business certificates and work permits for foreign employees of enterprises with foreign investment need to bribe government officials at various levels.

4. Insufficient financial services

The financial services in Cambodia usually fail to meet the demands of enterprises with foreign investment because of the complicated lending procedures and high loan interest rates. Meanwhile, the Chinese banks have not set up enough branches or representative offices in Asia-Pacific LDCs to support FDI by Chinese textile and clothing firms. In addition, they impose strict lending conditions for corporate long-term investment. It is difficult for textile and clothing firms to obtain favourable financing arrangements when making OFDI. Moreover, the repayment period is too short in terms of gross profit margins of the textile and clothing industry.

C. Policy suggestions, from the Cambodian perspective, for facilitating sustainable investment by China in least developed countries

In the post-ATC era, the textile and clothing clusters in China are trying to extend the vertical value chain, coordinate cluster development with local specialized wholesale markets and carry out spatial expansion to other developing countries including the Asia-Pacific LDCs. The objective is to reduce production costs in the long term, avoid trade barriers, establish new marketing networks and trade off negative effects arising from the appreciation of RMB. The low-end textile and garment firms in the coastal provinces of eastern China have been under great pressure to meet workers' demands for higher wages as well as the impact of the constant appreciation of the Chinese currency. Some of those firms have gone bankrupt as a result of the global financial crisis.

More and more textile and clothing factories have been forced to relocate to the middle and western regions of China or to Asia-Pacific developing countries such as Bangladesh, Cambodia, Thailand and Viet Nam. However, the coastal provinces of eastern China continue to maintain their unique competitive advantages arising from local textile and clothing industrial clusters with a comprehensive production chain, a pool of skilled labour, innovative fabric technology, sound infrastructure and economies of scale within the textile and clothing industry. The trend of relocating medium or high-end textile and clothing OEMs will continue in the foreseeable future. However, the enterprises in the textile and clothing clusters of China will continue to relocate some workshops to other developing countries.

1. Encourage OFDI by Chinese textile and clothing firms in overseas economic and trade cooperation zones in Asia-Pacific least developing countries

The Government of China should continue to encourage the domestic large-scale textile and clothing enterprises to establish textile industrial parks in other developing countries, including LDCs, which can serve as a good platform for the survival and growth of overseas Chinese textile and clothing enterprises. The successful establishment and operation of SSEZ by the Hongdou Group will undoubtedly encourage OFDI in Cambodia by more Chinese textile and clothing firms as well as promote the rapid development of the Cambodian textile and garment industry.

The overseas economic and trade cooperation zones can provide both Chinese and overseas textile and clothing enterprises with basic production facilities and comprehensive services such as investment consultancy, licence application, employee recruitment and international trade services. They not only reduce all types of investment risks, but also attract more supporting enterprises – both upstream and downstream – to enter the zones, leading to the formation of textile and clothing industrial clusters in LDCs. The leading enterprise in the establishment of overseas economic and trade cooperation zones should be granted more capital support from the Government of China in order to attract business in addition to being able to enjoy the favourable policies for overseas Chinese textile and clothing firms such as the subsidy for lending interest rates, start-up capital and insurance premiums.

Localization plays an important role in the successful operation of overseas economic and trade cooperation zones. First, the construction and development of economic and trade cooperation zones need to be localized because local experts can communicate more effectively with the local people and enterprises. Second, the operation of the economic and trade zones also needs to be localized. Since local experts have better knowledge about natural conditions and administrative procedures of LDCs, they can deal with the local divisions of security, tax, banking, logistics and trade unions more efficiently.

2. Forge a regional production network between China and least developing countries

The Asian and Pacific region LDCs can be part of the regional production network of China. That inclusive development can be further promoted when the textile and clothing industry in Asian and Pacific region LDCs such as Bangladesh and Cambodia are integrated into the global value chain through forging industrial linkages with China. The Chinese textile and clothing firms have firm and specific advantages over those in Asian and Pacific region LDCs. South-South cooperation can range from outsourcing to technology transfer, the dissemination of an advanced management model and the implementation of cluster policy in the Asian and Pacific region LDCs. More and more of the Chinese textile and clothing enterprises that have invested in Cambodia have a relatively complete value chain in China. They have the capability to establish a more complete value chain within SEZs in Cambodia.

However, the positioning of some overseas economic and trade cooperation zones is vague. Some aim to become an integrated and omnipotent area including trade, commerce, logistics, services and leisure. Although such positioning is ideal, it ignores the basic conditions of LDCs. Thus, it is highly recommended that the establishment of overseas economic and trade cooperation zones by Chinese enterprises should follow the path of industrial specialization with regard to national endowments of LDCs such as land availability, abundant labour and natural resources. In addition, these overseas economic and trade cooperation zones mainly target SMEs in China that have achieved their rapid growth thanks to sound industrial linkages and sufficient cheap labour. The Government of China needs to grant the SMEs greater support and consultancy services on how to cooperate and integrate themselves into the local production network. In addition, the local textile and clothing enterprises should be encouraged more to enter the economic and trade cooperation zones to promote cooperation with Chinese firms.

The LDCs in Asia and the Pacific can be integrated into the value chain of Chinese textile and clothing enterprises because of their great demand for Chinese raw materials and textile machinery. The exports from the Asian and Pacific LDCs to China are very limited and China maintains a trade surplus with all LDCs. In 2007, the volume of bilateral trade between Cambodia and China totalled US$ 933 million, up 193.6 per cent up from 2004. China's exports to, and imports from Cambodia amounted to US$ 882 million and US$ 51 million, respectively; these figures represented increases of 195.1 per cent and 170 per cent, respectively, from 2004. In terms of commodity categories, China mainly exported yarn, fabrics and related products, apparel and clothing accessories, agricultural products, vessels and rolled steel to Cambodia while imports from Cambodia mainly included logs, natural rubber, sawn timber, yarn, fabrics and related products, and apparel and clothing accessories (Xinhua News, 2008). The OFDI from Chinese textile and clothing firms has also promoted exports of yarn, fabrics, textile machinery and other equipment to the Asian and Pacific LDCs.

The governments in China and the Asian and Pacific LDCs need to cultivate the vertical market linkages in the textile and clothing sector by implementing more powerful industrial promotion schemes, because the textile and garment exports by LDCs usually rely on a few foreign companies. Some of the large-scale textile and clothing firms in China are already making efforts to set up supporting industries in the LDCs. For example, Shenzhou International established an embroidery workshop in Cambodia in 2007. The voluntary efforts by Chinese enterprises need to be guided and supported by the host country’s industrial policy and blueprints. The Asian and Pacific LDCs should be given greater incentives and support for developing the backward linkages of local enterprises in order to strengthen and expand the supply chain. Meanwhile, the Government of Cambodia should try to increase its textile production by the reduction of material costs so that the textile industry and the garment sector can become more competitive.

3. Provide a better financial package to support foreign direct investment by Chinese textile and clothing firms

The textile and clothing firms that were interviewed demand greater policy support in financing, tax and insurance from the Government because the current promotion policies are not sufficient to encourage the SMEs to make outward foreign direct investment . The Government will need to establish a venture capital fund to encourage OFDI in Asian and Pacific LDCs by the small and medium-sized textile and clothing firms. The Chinese banks could offer more favourable credit or financing guarantees in terms of enterprise scale, anticipated profits and investment risks.

Different financial support packages could be designed to meet diversified demands of different types of enterprises in order to make OFDI sustainable. The Export-Import Bank of China should increase the scale of special loans and extend the repayment period. The interviewed enterprises suggested that a more favourable repayment period (10-15 years) could be granted according to the lending scale. The Ministry of Finance could subsidize the interest rate in full for loans to those textile and clothing firms making OFDI in LDCs.

In addition, the China Export & Credit Insurance Corporation could offer more effective credit insurance support to textile and clothing firms “going out” to LDCs. New types of insurance, such as sovereignty risk insurance and exchange risk insurance, could be launched to protect textile and clothing firms from huge losses arising from political and social force majeure as well as large depreciation of the currency of the host country. The Ministry of Finance could subsidize the insurance premiums for sovereignty risk insurance.

4. Improve infrastructure facilities and government efficiency in the least developed countries

The LDCs in Asia and the Pacific should increase their investment in improving their infrastructure facilities. FDI in the construction of infrastructure should continue to be encouraged by the LDCs. It is important to establish more and more supporting institutions in the LDCs so as to reduce the production cost of foreign-invested companies in addition to the advantages of cheap labour and favourable polices by the host countries. The LDCs should add more of other location advantages in addition to the favourable market entry to developed countries. For example, the analysis of administrative costs in the garment sector of Cambodia has shown that the imports of inputs, export clearance charges, export document processing, and packing and loading constitute over 66 percent of the imported input costs. It is highly important for the LDCs in Asia and the Pacific to lower high undocumented administrative charges, to reduce unnecessary in-factory inspections and to simplify the cumbersome export procedures. Meanwhile, the energy pricing policy should be more competitive because the Chinese subsidiaries in the LDCs have to bear the high cost of electricity and diesel.

V. Strengthening inclusive development and South-South cooperation between China and Asia-Pacific least developed countries

Currently, China is strengthening regional inclusive development and South-South cooperation by taking an active part in regional trade agreements and offering aid to LDCs in the form of infrastructure construction, technology transfer and training local staff.

The implementation of China-ASEAN regional trade agreements (RTAs) will further promote the intraregional trade, investment, and technical and social cooperation. Cambodia, the Lao People's Democratic Republic and Myanmar are the member states of ASEAN. China is also the member of the Bangkok Agreement, together with Bangladesh, India, the Republic of Korea, the Lao People's Democratic Republic and Sri Lanka. China acceded to the Bangkok Agreement in May 2001. It is the first real preferential trade arrangement that China has participated in. The agreement is aimed at promoting trade among member countries by granting preferential tariffs and by removing non-tariff barriers. Nonetheless, trade among member countries has remained low despite the fact that China's accession resulted in a significant increase in the proportion of trade flow among members. In addition, China has been taking an active part in regional economic cooperation with South Asian countries, such as Bangladesh, Bhutan, India, Maldives, Nepal, Pakistan and Sri Lanka, who are member States of the South Asian Association for Regional Cooperation (SAARC).

China has been granting aid to the LDCs in order to promote regional inclusive development without adding extra political conditions. China remains committed to boosting economic cooperation in the Greater Mekong Subregion (GMS) with Cambodia, the Lao People's Democratic Republic, Myanmar, Thailand and Viet Nam. A total of US$ 9.87 billion has been poured into 34 projects by China, the above five countries and the Asian Development Bank. An additional 146 technological aid projects have been implemented at a total cost of US$ 166 million. Model projects facilitated by China under the GMS economic cooperation framework include:

(a) The one-third section, in the Lao People's Democratic Republic, of the western line of the south-north economic corridor (the Kunming-Lao-Bangkok road);

(b) Cooperation on the Pan-Asia railway and research into the China and other sections;

(c) The 110 kW power line connecting Hekou in Yunnan province, south-western China and Lao Cai in Viet Nam;

(d) The GMS Information Highway (GMS IS) phase I project;

(e) The first GMS Agriculture Ministers Meeting and the GMS Agriculture Information Network Service;

(f) The implementation of the Action Framework for the GMS Strategy of Facilitation of Trade and Investment; and

(g) Its own country action plan (Xinhua news, 2008).

In 2007, total aid and loans provided by China to Cambodia reached US$ 546 million (Minder, 2008). China has helped Cambodia to train a large number of workers to meet the latter country's economic development requirements. From 1993 to the first half of 2007, China trained 364 government officials, technicians and engineers. Thirty-five Chinese experts were sent to Cambodia to provide training programmes and technical guidance in health, finance, commerce, industry, agriculture and transportation.

Meanwhile, China has launched some large-scale bilateral economic cooperation projects with Cambodia. For example, the state-owned Sino-hydro Corporation is constructing the Kamchay Hydropower Station in Cambodia with an investment of US$ 280 million.

Other Chinese firms are helping Cambodia to construct roads, bridges and office buildings. In addition to the garment industry, OFDI by China is being extended to the underdeveloped natural resources sector for such subsectors as pulp, palm oil, rubber, oil and gas (Embassy of China to Cambodia, 2007). China can and will play an important role in promoting inclusive development of LDCs in the Asia-Pacific region by strengthening South-South cooperation.

The limitation of this study is that the report has mainly focused on the spatial expansion of textile and clothing clusters in the Yangtze River delta to Cambodia without taking into account the OFDI performance of other Pearl River delta and Bohai-Rim delta textile and clothing clusters in other Asia-Pacific LDCs. Currently, OFDI by increasing numbers of cluster firms in China is being made other Asia-Pacific LDCs. Regional integration processes such as those between Cambodia-ASEAN-China and Bangladesh-SAFTA-China have had great impacts on OFDI from China to the LDCs. How will these regional integration processes affect the South-South OFDI pattern? What effective means are there for leading to inclusive development between China and the LDCs in the Asia-Pacific region? The strengthening trade and investment linkages between China and the Asia-Pacific LDCs should and will continue to contribute to welfare improvement in the whole region.

Annexes

Annex 1. Interview outlines

Interview outline 1:
Textile and clothing firms in Zhejiang province/Jiangsu province

Part one: Company background

1. Company name
____

2. Year of establishment
____

3. Location/city
____

4. Number of plants/sites in LDCs
____

5. Company status (please tick all that apply)

a. Private
b. Listed company
c. Joint venture (please give percentage of foreign ownership) %

6. Total employees (average full-time equivalents in each year)
____

7. Gross value of plant and equipment (current book value)
____

8. What are your company's main products?
____

Part two: Foreign direct investment in LDCs

13. Why did your company make foreign direct investment in LDCs?

14. What do you think of the investment environment in LDCs?

15. Do you cooperate with local firms?

16. What are the obstacles and challenges you are facing in your business expansion in LDCs?

17. Do you plan to make more investments in LDCs? Why?

18. What do you think of government support programmes in LDCs? What are your suggestions?

Part three: Respondent's details

19. Name ____
20. Position in firm ___________________________________
21. Address____
22. Telephone number_____________________________________
23. Fax number ____
24. E-mail address ______________________________________

Interview outline 2:

The government officials at the Economic and Trade Commission of Zhejiang Province, Ningbo City, Shaoxing City and Yiwu City.

1. Please give an overview of outward foreign direct investment to LDCs in Asia and the Pacific by local textile and clothing clusters.

2. How does the Government encourage the local textile and clothing firms to make outward foreign direct investment in the LDCs, particularly in the Asia-Pacific region?

3. How will the Government facilitate sustainable foreign direct investment in LDCs by the textile and clothing firms in the cluster?

4. Has the support programme of establishing industrial parks in Asia-Pacific LDCs been successful?

Interview outline 3:

Businessmen from LDCs in Asia and the Pacific at the specialized wholesale market in Yiwu/ Shaoxing.

1. How long have you been doing the business at the specialized wholesale market?

2. Can you make comparisons between China and your home country in terms of the business and investment environment?

3. Do you plan to introduce Chinese textile and clothing firms to your home country?
4. What are the potential business opportunities between China and LDCs?

5. What do you think of the business barriers between China and your home country?

6. Can you make suggestions on foreign direct investment in local textile and clothing firms in your country?

Annex 2. Main shareholders of Sihanoukville Special Economic Zone

Jiangsu Hongdou Industrial Co., Ltd. is the core subsidiary of the Hongdou Group and it chose Cambodia as one of its overseas production bases in April 2007. It exports its apparel products to many countries, such as Australia, Canada, France, Italy, Japan, the Russian Federation and the United States. The Hongdou Group is ranked second among the top 100 textile and clothing enterprises in China. It owns nine subsidiaries with 20,000 employees.

Wuxi Yiduo Investment and Development Group Co., Ltd., which were established in October 1992, are mainly engaged in the development of real estate business. The sales volume reached Y 1.7 billion in 2006.

Hua Tai Investment and Real Estate Consultancy Co., Ltd. was set up in February 2004 and specializes in making investments in property and in providing consultancy for house purchases. Its subsidiaries mainly undertake the construction of road and drainage systems.

Cambodia International Investment and Development Co., Ltd., which was established in July 2004, is engaged in the construction and development of special economic zones, forestry, gold mining, iron ore mining and water conservation.

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