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**Skills for Trade and Economic
Diversification in the Kyrgyz garment
sector**

Trade and
Employment
Programme

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Preface

The primary goal of the ILO is to contribute, with member States, to achieve full and productive employment and decent work for all, including women and young people, a goal embedded in the ILO Declaration 2008 on *Social Justice for a Fair Globalization*¹, and which has now been widely adopted by the international community.

In order to support member States and the social partners to reach the goal, the ILO pursues a Decent Work Agenda which comprises four interrelated areas: Respect for fundamental worker's rights and international labour standards, employment promotion, social protection and social dialogue. Explanations of this integrated approach and related challenges are contained in a number of key documents: in those explaining and elaborating the concept of decent work², in the Employment Policy Convention, 1964 (No. 122), and in the Global Employment Agenda.

The Global Employment Agenda was developed by the ILO through tripartite consensus of its Governing Body's Employment and Social Policy Committee. Since its adoption in 2003 it has been further articulated and made more operational and today it constitutes the basic framework through which the ILO pursues the objective of placing employment at the centre of economic and social policies³.

The Employment Sector is fully engaged in the implementation of the Global Employment Agenda, and is doing so through a large range of technical support and capacity building activities, advisory services and policy research. As part of its research and publications programme, the Employment Sector promotes knowledge-generation around key policy issues and topics conforming to the core elements of the Global Employment Agenda and the Decent Work Agenda. The Sector's publications consist of books, monographs, working papers, employment reports and policy briefs⁴.

While the main findings of the research initiatives are disseminated through the Employment Working Papers, the *Employment Report* series is designed to consolidate the major evaluations of employment programmes, conclusions and resolutions of workshops and seminars, and other information details that are particularly, though not exclusively useful to the work of the ILO and its constituent partners.

José Manuel Salazar-Xirinachs
Executive Director
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¹ See http://www.ilo.org/public/english/bureau/dgo/download/dg_announce_en.pdf

² See the successive Reports of the Director-General to the International Labour Conference: *Decent work* (1999); *Reducing the decent work deficit: A global challenge* (2001); *Working out of poverty* (2003).

³ See <http://www.ilo.org/gea>. And in particular: *Implementing the Global Employment Agenda: Employment strategies in support of decent work*, "Vision" document, ILO, 2006.

⁴ See <http://www.ilo.org/employment>.

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Foreword

“Skills development is [...] essential to address the opportunities and challenges to meet new demands of changing economies and new technologies in the context of globalization.”

Conclusions on skills for improved productivity, employment growth and development,
International Labour Conference, 2008

This report, produced upon request from ILO constituents, presents an application of the Skills for Trade and Economic Diversification (STED) methodology to the Kyrgyz garment sector. STED has been developed in recognition of the fact that having the right skills among workers is crucial for firms or industries to succeed in trade, and vice versa understanding trade is important to provide workers with the right skills. Availability of skilled workers contributes to higher and more diversified exports, more FDI, higher absorption of technology, and more sustainable growth and productive employment creation. At the same time, skills are the key determinant for a worker's success in finding a good job and making a living.

Providing the right skills at the right time is anything but easy, and it is not just a question of putting in more resources. Around the world, we observe situations where highly educated workers remain unemployed, while at the same time firms find it difficult to fill vacancies for skilled positions. Such mismatches, where the skills taught by the education and training systems do not fit with what is in demand on the labor market, constitute a large economic loss, as well as a personal tragedy for those affected by it. In order for skills supply to match skills demand in the labor market, it is necessary to take a forward looking perspective, and to ask not just what skills are in demand today, but what skills will be in demand in the future. This is what STED does.

The application of STED in Kyrgyzstan represents cooperation between the ILO's Trade and Employment Programme and Enterprise Department in the context of ILO's work to promote an enabling environment for sustainable enterprises. The STED methodology was developed jointly by the ILO Skills and Employability Department and the Trade and Employment Programme. STED builds upon the ILO's unique tripartite structure and its ability to bring together governments, workers, and employers to work for more and better jobs.

STED has completed its development and testing phase in 2011/2 with applications in Bangladesh, Ukraine, Macedonia, and Kyrgyzstan. The methodology is now taking an important place in the ILO's toolbox to promote decent work. We expect it to inform technical assistance in the area of skills and trade, and to make a strong contribution to their effectiveness in the future.

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It was edited by Erik von Uexkull with substantial support from Katharina Lehmann (both ILO Trade and Employment Programme).

A team of researchers from CSR Business Network, including Asel Arstanbekova, Elvira Ilibezova and Larisa Ilibezova, conducted the survey in Kyrgyzstan and wrote substantial sections of the report with guidance from Ritash Sarna (ILO Enterprise Department) and Erik von Uexkull.

Con Gregg (ILO Skills and Employability Department) made substantial contributions to the design of the survey questionnaire and the recommendations section. Jan Loeprick (World Bank Foreign Investment Advisory Services) gave valuable advice for the section on the patent system. Erik von Uexkull provided the analysis of external challenges and sector outlook. Merten Sievers (ILO Enterprise Department) contributed to the sections on the upstream and downstream value chain. Graeme Buckley (ILO Enterprise Department) provided comparative analysis of key elements of the business enabling environment.

Bolot Orovkov (ILO National Coordinator Kyrgyzstan) and Aziz Kirgizbaev (ILO TC project office, Kyrgyzstan) made substantial contributions to defining the scope of the work and facilitating its implementation in Kyrgyzstan. Ritash Sarna and Walter Verhoeve (ILO Moscow office) also made important contributions to defining the scope of the work undertaken. The report has benefited greatly from comments from the ILO Decent Work Technical Support Team and Country Office for Eastern Europe and Central Asia. Helpful comments were also received from Gulmira Asanbaeva (ILO Enterprise Department).

Many experts and stakeholders in the sector generously gave their time and shared their knowledge by responding to the survey or participating in a validation workshop organized in Bishkek on March 14th 2012.

The STED methodology was developed jointly by the ILO's Trade and Employment Programme and Skills and Employability Department under the leadership of Marion Jansen and Christine Evans-Klock.

Funding from the Swedish International Development Cooperation Agency (Sida) under the ILO project "Promoting Inclusive Job-Rich Growth" is gratefully acknowledged⁵.

⁵ http://www.ilo.org/employment/Whatwedo/Projects/WCMS_144422/lang--en/index.htm

Executive summary

Background and Methodology

The report addresses challenges and makes recommendations to promote employment creation through sustainable enterprise development in the Kyrgyz garment sector. It applies the ILO's Skills for Trade and Economic Diversification (STED)⁶ methodology to look in particular at current and future needs for skill development among workers. The methodology used is a combination of topical analyses and recommendations contributed by various ILO experts and structured interviews with garment firms and other key informants in Kyrgyzstan through a local consulting firm.

Current Situation and Outlook

The report characterizes the current situation and business model of the sector, which has led to high export growth over the last years. According to official export data, Kyrgyz garment exports grew strongly between 2001 and 2010 with an average annual growth rate of 29 per cent. However, due to low labor productivity in comparison to competitors, the sector's competitiveness is mainly based on very low labor costs, the flipside of which are low wages and often precarious working conditions. Most companies in the sector are small and operate informally or semi-informally.

The sector exports a large share of its output and also depends on importing intermediate inputs. Exports remain very concentrated in the lower value segment of the Russian and Kazakh markets, with most distribution channels organized along traditional linkages with buyers or intermediaries. Only very few firms have been able to develop exports to other countries and have in place strategies for product and market development. Inputs are imported mainly from China.

The garment sector faces several adjustment challenges in terms of its external business environment that the report covers in detail:

- Most small companies depend on the patent system, a simplified scheme for business tax and social contributions for small enterprises. The government has recently increased the cost of patents, but the system remains problematic both in terms of revenue generation and with respect to the incentives it poses for business formalization. There currently does not appear to be a clear reform agenda for the patent system, but any changes to it are likely to have a substantial impact on the sector, whether positive or negative.
- Kyrgyzstan's upcoming accession to a Customs Union with Russia, Kazakhstan and Belarus will lead to the adaptation of a common external tariff that has higher tariff rates on inputs imported by garment factories. The report suggests that actual tariff increases are likely to be small. On the positive side, the Customs Union entails possibilities for substantial reductions in non-tariff trade costs, which many garment exporters currently highlight as a particular concern.
- Russia's recent accession to the WTO will lead to an erosion of the preferential margin that Kyrgyz garment producers currently enjoy in the Russian and Kazakh markets and thus significantly increase competition in these markets.

Despite the industry's strong export growth over the last years, there are several indications that the current business model based on cheap labor, low taxes (for firms in

⁶ www.ilo.org/sted

the patent system), preferential market access, and concentration on traditional markets and distribution channels may soon reach its limits. Low wages and precarious working conditions are leading to high labor turnover, including migration abroad, which presents a serious problem for companies and reduces their ability to build up skills among their workers. The patent system generates inefficiencies and unsatisfactory fiscal revenue and is likely to be reformed in the medium term. Preferential margins in traditional markets are eroding and thus competition is likely to increase significantly.

The report concludes that the sector is facing significant adjustment challenges which will likely lead to a consolidation towards fewer, but possibly larger and more productive enterprises with more diversified export profiles. Based on information collected from companies which are already “pioneers” in new markets, the report analyzes current and future skill and training needs and existing deficits in skill supply in order to identify critical gaps⁷.

Skill Gaps and Training Needs

The report assesses current and arising skills gaps in all levels of employment in the garment sector. The top-rated occupations for which companies report difficulties in finding suitable applicants are skilled craft and professional level occupations such as dyers, designers, gaugers, and cutters. Companies indicate that they expect increasing demand for cutters, designers, universal sewing machinists, and process engineers over the coming years. Currently, most firms train their own workers on the job for rather specific tasks. They often do not see an advantage in hiring graduates from the public education institutions and argue that the skills taught there are not relevant for their operations.

In terms of training and skills development on the job, many firms highlight their interest in training courses in particular for sewing machinists, designers, marketing, procurement and sales personnel, cutters, gaugers, machine operators, packaging workers, and administrators. The report also stresses the importance of specialized training for top and middle management to deal with the particular challenges of developing new products, integrating into international value chains, and developing new export markets.

Recommendations

The report concludes that a forward looking perspective on skills will have to be a central element of the ongoing revision of the sector export strategy. For this, stakeholders will have to choose between radically modernizing existing education and training systems, or an approach that largely by-passes existing institutions. The report favors the former path.

At the institutional level, the report makes detailed recommendations for improvements of the existing education and training system, including for strengthening cooperation between the industry and education institutions, reform priorities for each occupational level, and revitalization of the Shvei-Profi training center.

The report emphasizes that firms in the sector have an important role to play in skills upgrading and improvement. A key challenge is to reduce labor turnover and to

⁷ This methodology is sometimes referred to as “Sector scouting”. Sector Scouting is a tool for determining trend qualifications in different sectors by grouping only trendsetting or pioneer firms, i.e. firms that stand out in terms of size, productivity, development of new products and access to foreign markets. See Abicht et al, 2002 for details.

promote a more sustainable culture of employment that gives both employers and workers an incentive to invest time and resources into training and skills development. Improving working conditions and social dialogue at the enterprise level can have very positive effects in this regard and at the same time promote labor productivity.

Chapter 1. Introduction

The garment sector is considered one of the most promising sectors of the Kyrgyz economy. It has exhibited substantial export growth over the past years and thus contributes substantially to economic diversification and, given its labour intensive nature, to employment creation in Kyrgyzstan. At the same time, the sector is facing significant challenges. Internal factors include serious decent work deficits in terms of employment conditions and high levels of informality. External challenges include increasing competitive pressures in key export markets. As a result, the sector has an urgent need to improve its labour productivity.

This report addresses challenges and makes recommendations for promoting more productive employment in the Kyrgyz garment sector in the context of the ILO's work on supporting an *Enabling Environment for Sustainable Enterprises*¹. It focuses on the availability of adequate skills among workers as a key prerequisite for enterprise development and employment creation.

Given the export orientation of the sector and the importance of skills for its development, this report is based on a new methodology developed by the ILO called *Skills for Trade and Economic Diversification (STED)*². The analytical process underlying STED recognizes that trade and skills development are strongly interrelated. Having the right skills among workers is crucial for firms or industries to be competitive in the global economy, and a firm's success in export markets often requires new skills that its workers may not yet possess.

The methodology used is a combination of topical analyses and recommendations contributed by various ILO experts and structured interviews with garment firms and other key informants in Kyrgyzstan through a local consulting firm. Interviews focused on successful large enterprises (referred to as "pioneer" companies) in the garment sector. The idea is that skill demand of these firms is likely to reflect the trends that the rest of the industry will follow over the coming years. In total, 20 interviews with textile and garment enterprise leaders and 10 in-depth interviews with key informants were conducted for the study. The group of key informants included representatives of government agencies who deal with issues under review in this study, independent experts in labour resources, independent experts in technical and vocational training and education, and representatives of donor-supported projects working on labour issues. A validation workshop was held in Bishkek on March 14th 2012 to discuss a draft version of the report with industry stakeholders.

The remainder of the report is structured as follows: Chapter 2 characterizes the current state of the industry in terms of major trends in output, industrial organization, exports and imports, investment, employment, etc. Chapter 3 discusses three major upcoming external challenges, namely a potential reform of the small business tax system, Kyrgyzstan's accession to a Customs Union with Russia, Kazakhstan, and Belarus, and Russia's WTO accession. Based on the findings from these chapters, Chapter 4 gives an outlook on likely developments of the industry over the coming years and its current strategic vision. Chapter 5 analyses current and future demand for skills based on the outlook developed in the previous chapter. Chapter 6 reviews current sources of skill supply and their adequacy in meeting the industry's skill demand. Chapter 7 concludes by making specific recommendations on how the identified shortcomings can be addressed through measures at the policy, institutional and enterprise levels.

¹ www.ilo.org/eese

² www.ilo.org/sted

Chapter 2. Current Situation and Industry Profile

2.1. Industry Profile

2.1.1. History and Development of the Garment Industry

During the Soviet period Kyrgyzstan's light industry comprised three main sectors – textile, garment making, and leather and fur. The textile industry consisted mainly of large- and mid-scale enterprises, which were concentrated in Bishkek city and the Osh and Chui provinces, and which produced wool, cotton, and silk fabrics that were used as raw materials for garment production. Prior to 1990, the garment sector was generally made up of 10 large factories and public ateliers. Light industry employed up to 300,000 people and created nearly 40 per cent of state budget revenue. At the start of the 1990s, the total number of employees in the light industry was still over 250,000. Manufacturing and fibre processing used to account for a major share of the sector³.

The crisis of the early 1990s seriously undermined the whole sector. Output dropped, enterprises had to close or downsize, the integrated textile-garment making production chain fell apart, and adjacent sectors started to develop independently of one other and at present are considered to be at different stages of development. The decreasing availability of local raw materials (in particular cotton and wool) forced garment production to reorient to use imported fabrics from China, Turkey, and other countries.

The end of 2008 and early 2009 marked again a grave period for the Kyrgyz garment sector. The three main reasons were the global economic crisis, which affected purchasing power of Russian and Kazakh customers and which in turn led to a drop in garment exports to these countries; the rolling blackouts of electricity that forced extended idling at garment enterprises and caused damage to equipment; and changes in the taxation system (cancellation and later doubling of the tax patent payable by garment producers). However, recovery was relatively quick in 2009 / 10.

2.1.2. Size and Growth of the Garment Sector

According to official statistics, there has been a notable increase in textile and garment production over the past six years. Output in the textiles and garment sectors in 2010 exceeded the 2009 level by almost 38 per cent, according to official statistics.

Estimates provided by key informants confirm the strong growth; study participants in fact think that the sector is growing even faster than indicated by official data. The growth in the sector is supported only by the garment firms, while fibre and fabric production are in deep crisis.

Table 2.1. Changes in Output Volume in Textile and Garment Industries⁴

	2006	2007	2008	2009	2010
Production volume in the textile and garment industries (KGS million)	4 642	4 194	5 935	4 519	6 238
Physical output in the textile and garment industries (million items)	44.2	37.7	53.9	33.8	56.0

³ National Statistics Committee of the Kyrgyz Republic. Most data from the National Statistics Committee goes until 2009 or 2010.

⁴ National Statistics Committee of the Kyrgyz Republic.

The industry mostly produces apparel (for men and women of all ages) as well as underwear. Some entities also produce uniforms, sportswear, and knit-wear items. Survey respondents indicated that most enterprises are concentrated on a relatively low number of products, with some only producing one single item.

Table 2.2. Production of Main Garment Items (thousands of units)⁵

	2005	2006	2007	2008	2009
Men's apparel	6 200	4 642	6 242	2 988	5 383
Women's apparel	19 972	19 723	25 957	19 639	28 744
Underwear	18 002	13 339	21 676	11 157	21 827

According to data from the National Statistics Committee, in 2010 the republic's light industry employed around 158,000 individuals. Key informants, however, estimate the number at a much higher level due to the important amount of informal economic activities⁶. According to the textile and light industry labour union, there are around 2,500-3,500 garment making units and enterprises in the country. Survey respondents think that the garment industry consists of around 300 mid-sized (50-80 employees) and around 1500 small-scale (5-15 employees) enterprises. It is estimated that around 40 per cent of the sector's enterprises operate in the informal economy⁷. Most garment units are concentrated in Bishkek city, as well as the provinces Chui, Osh, and Jalal-Abad.

The textile and garment industry is classified as one of the country's five core economic sectors, together with metallurgy, the energy sector, the food processing industry and the production of construction materials. However, its share in the output volume of these core economic sectors (5.4 per cent) is still far below the level at which it was in the 1990s (35 per cent). The production of ready-made garments currently makes up over 80 per cent of the industry's output. Textile and garment production accounted for 3 per cent of the country's GDP in 2010.

2.1.3. Informality

The following legal forms of enterprises in the garment sector were identified by the survey:

- Registration as legal person (most often as a limited liability company with settlement account and a stamp);
- Registration of physical person as "private entrepreneur" (can include having a settlement account in the bank and a stamp);
- Economic operation based on voluntary tax patent basis;
- Economic operation without registration and without purchase of voluntary tax patent.

In-depth interviews revealed that regardless of the form of registration, some enterprises work in the informal economy, i.e. have been legally registered but report

⁵ National Statistics Committee of the Kyrgyz Republic.

⁶ Presentation by Ryskul Babaeva, The state of textile and garment sector of the Kyrgyz Republic, Press conference of the Chairwoman of the Textile and Light Industry Labor Union, 8 June 2010.

⁷ UNDP (2008): Assessing the impact of trade policy on the development of the Kyrgyz Republic, Bishkek, Kyrgyzstan.

officially only part of the production volume, the number of workers, or profits. Other enterprises work without registration and have no legal papers or reporting.

As estimated by survey participants, practically all registered enterprises work half "in shade" and use various means to hide data on actual production output. Regarding the number of enterprises that work fully in the informal economy⁸, the estimates vary; experts estimate them to make up between 30 and 50 per cent of the number of registered garment companies. Other key informants estimate it as "quite a lot", but can't give more precise figures. One third of the key informants think that the State has done everything to bring the garment makers from the shade and at present only few remain unregistered.

Key informants said that informality of activities in the sector of fabric, accessories, and equipment supply also has a significant influence on garment production. Managers of garment units said that they often have to buy fabric, accessories, or equipment without proper documentation because materials with proper fiscal papers cost on average 10-12 per cent more than without fiscal documents. Managers also noted that they are forced to hide their profits in order to compensate for informal payments to various inspection bodies. Another reason why the number of staff is distorted is that garment operations are frequently seasonal. During maximum load the number of staff doubles and triples compared to quiet times. According to managers of garment companies, such changes in the number of workers often raise many questions among inspection bodies, and thus it becomes more convenient to show minimal number of workers year-round. Among other reasons, managers mentioned that female workers who come from rural areas often do not have documents and thus legal payments (taxes and other) cannot be made for such workers. High turnover of staff also complicates the signing of labour contracts.

Live voices

...Usually I have two girls who do the straight stitching. The job is low-paid and unskilled. I never sign contracts with them because they usually don't have proper documents, and besides, sometimes they come to work, sometimes they don't. Where will I find them if they leave? And if I report 30 workers in one month and 10 in another, the tax inspectors will give me a hard time. That is why I report 10 workers year round, and nobody asks unnecessary questions. In terms of volume of production, the situation is the following: everybody knows that a certain share of fabrics and accessories are imported without proper documentation, and consequently it is sold also without documentation. We also often produce garments and sell them without proper papers. I also know that wholesalers export a part of the final products without papers, that is, they arrange customs clearance only for part of the lot.

(In-depth interview with a manager of a garment unit)

It should be noted that government bodies did take steps to legalize garment enterprises that operated in the informal economy. The Government Decree of 23 December 2005 no.615 and the Law no.86 of 12 May 2006 provisioned measures to stimulate development and legalization of garment production through patent based taxation and payment of social insurance at the rate of 25 per cent of the cost of the patent.

These measures seem to be fruitful. As reported by the State Committee on Taxes and Collections⁹, the number of registered private entrepreneurs in the garment sector increased to 584 entities in 2005 and to 855 entities in 2006. 823 entities were reported in 2007 and

⁸ The term "informal economy" refers to "all economic activities by workers and economic units that are – in law or in practice – not covered or insufficiently covered by formal arrangements. Their activities are not included in the law, which means that they are operating outside the formal reach of the law; or they are not covered in practice, which means that – although they are operating within the formal reach of the law, the law is not applied or not enforced; or the law discourages compliance because it is inappropriate, burdensome, or imposes excessive costs". See ILO (2002) for details.

⁹ Report of the State Committee on Taxes and Revenues outgoing no.14-9-2-3651/4601 of 13 June 2008.

710 entities over the first five months of 2008. 327 entities operating on a patent basis were reported in 2006, 475 entities in 2007 and 359 entities in the first five months of 2008¹⁰.

Nevertheless, key informants think that it is necessary to further review registration and taxation in the garment sector in order to reduce the number of quasi legal and informal entities.

2.1.4. Premises

According to survey participants, small enterprises or garment producing units (up to 100 workers), are usually located in basements of multi-storey buildings, private homes or on the territory of abandoned large industrial buildings, such as the industrial plants “Frunze”, “Lenin”, “40 Let Oktyabrya”, and “Kozhzavod”. The former garment factory “8 Marta” houses nearly 40 small garment units. Key informants estimate that most units rent the premises. Sanitary norms, work place requirements, and safety rules in such garment enterprises are usually ignored, while control on the part of supervisory bodies is insufficient according to the interviews. Entities that work informally do not bother to follow relevant norms and rules. However, several more profitable enterprises bought offices and expanded their business recently and constructed production premises.

2.1.5. Equipment

The situation with equipment and production machinery has changed significantly over the years since Kyrgyzstan gained independence. The sector is gradually replacing out-dated Soviet-era equipment with modern, cheap, and simple in maintenance Chinese-made machines, such as garment machinery for knitting and overlocking, presses, cutters, modern equipment for design and cutting, as well as computer programs for developing design. According to key informants, nearly one third of newly imported equipment replaces old one, while two thirds are used to expand production, i.e. create new jobs. This led to significant improvements in the technical capacity of many garment enterprises. Starting from 2006 after the tariff on imports of technological equipment to Kyrgyzstan was lifted, Kyrgyz enterprises also started to bring in Japanese equipment. In 2011 UNDP (United Nations Development Programme) provided 1.5 million Kyrgyz Soms (KGS) credit for the procurement of new equipment by garment enterprises that were members of the “YuzhLegprom” association (Light Industry Association of the Kyrgyz Republic)¹¹.

¹⁰ Report of the State Committee on Taxes and Revenues outgoing no.14-9-2-3651/4601 of 13 June 2008.

¹¹ *Kyrgyz Garment Makers Review Results of 2011*, Time is Money newspaper, 28 December 2011.

2.2. Marketing and Sales

2.2.1. Exports and Imports

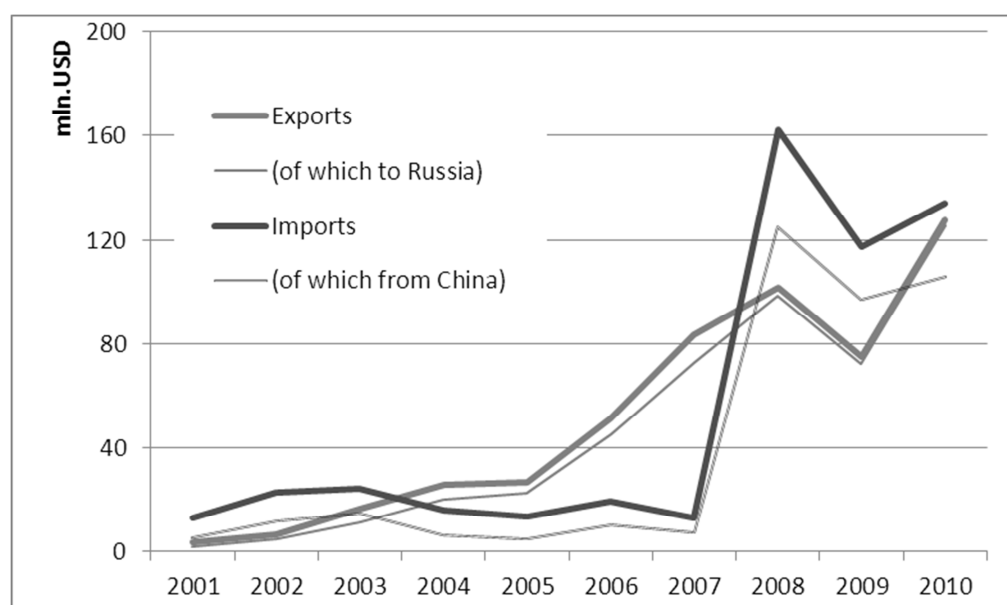
It is estimated that up to 80 per cent of the garment sector's output is exported¹², while at the same time a significant share of its intermediate inputs are imported, making the sector highly exposed to both import and export trade. This also makes the sector susceptible to changes in trade policy and international markets, some of which will be discussed in the following chapter.

Women's and girl's clothing account for the largest share of garment exports abroad¹³. Some enterprises are fully export-oriented and sell only in bulk, many other producers work both on local and foreign markets and some firms produce goods only for the domestic market.

Given the high level of informal trade, official trade statistics, as shown in Figure 2.1, only capture a fraction of garment exports. In fact, according to these figures, Kyrgyzstan would be a net importer of garments, which is not likely to hold true once informal trade is taken into account. This data pattern may also be driven by garments that are imported to Kyrgyzstan from China and then re-exported informally to other neighbouring countries. Overall, the official trade data show a very high concentration of exports in the Russian market, and also a rather strong concentration of imports from China.

According to official export data, exports grew strongly between 2001 and 2008, dropped significantly during the crisis year of 2009, and recovered in 2010, when official garment exports reached a total of 130 million USD with an average annual growth rate of 29% for the decade. More recent data indicate that export growth accelerated as Kyrgyz clothing exports increased by 17 per cent in the first three quarters of 2011¹⁴.

Figure 2.1. Imports and Exports of garments



Source: UN COMTRADE.

¹² Ryskul Babaeva, Press conference of Textile and Light Industry Labor Union, June 8, 2010. Information Agency IA "24.kg"

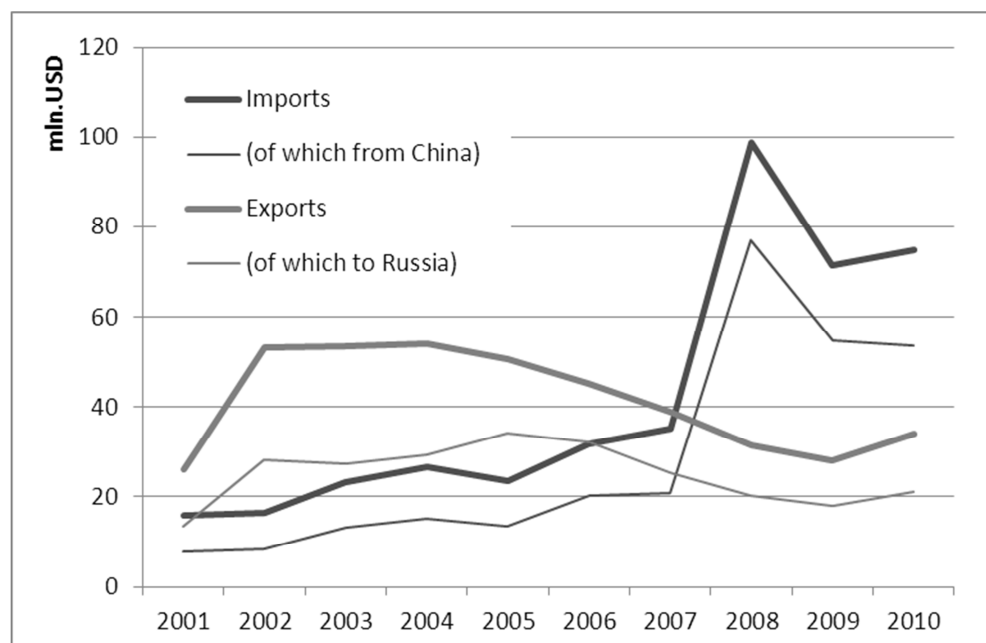
¹³ USAID (2009): Economic effects from Kyrgyzstan's participation in the multilateral trade system (WTO): Textile Sector, Bishkek, Kyrgyzstan.

¹⁴ ITC (2011): ITC's role acknowledged, ITC website, quoting official data from the Kyrgyz Statistics Committee.

Managers of garment firms interviewed in the survey confirm a strong dependence on the Russian, but also on the Kazakh market, although less extreme than in the official data. According to them, nearly 90 per cent of all exports go to Russia (46.3 per cent) and Kazakhstan (41.5 per cent). Other export destinations include Uzbekistan (7.3 per cent), Israel (2.4 per cent), and the USA (2.4 per cent).

Exports of garments are closely associated with imports of textile materials used in garment production (Figure 2.2). Imports of textiles typically used to produce garments follow a similar trend as export of garments, and amounted to nearly 70 million USD in 2010, with 78 per cent of official imports coming from China.

Figure 2.2. Imports and Exports of Textiles used for garment production



Source: UN COMTRADE.

2.2.2. The Garment Value Chain

Upstream

The garment sector depends on the availability of cheap fabric. Local wool and cotton production declined over the past two decades. As more than 80 per cent of cotton is grown on small plots by private farmers using out-dated equipment, productivity in the sector is very low. In addition, production costs increase and markets are unstable, which make cotton production inefficient. Farmers often prefer to sell to wholesale buyers who take the cotton abroad. Therefore, raw materials are mainly imported. According to official data, the main supplier of fabrics are China (over 70 per cent of the market), as well as Turkey, South Korea, and the United Arab Emirates¹⁵. In addition to fabric, China and Turkey also supply garment accessories, thread, yarn, and components for fabric making.

Most garment makers buy fabric and accessories through three large markets (two in Bishkek and one in Kara-Suu in the Osh province) and generally keep long-term relationships with their suppliers. If necessary, garment makers can order special supplies through market sellers who act as intermediaries. Only few enterprises have established

¹⁵ USAID (2009), Economic effects from Kyrgyzstan's participation in the multilateral trade system (WTO): Textile Sector, Bishkek.

direct contacts with fabric producers. Payments for fabrics, accessories, and component materials are usually made upon receipt of the goods and mostly in cash.

However, according to some key informants, further development of the garment sector and exploration of new markets in developed countries will be linked to the use of natural fabrics – wool, cotton, and silk. Thus, according to these key informants it is important to develop adjacent sectors. Some key informants think that such development will stimulate not only garment production but also the country's economy at large.

Key informants noted that in spite of active support from international donors GIZ (German International Cooperation Agency), KfW (German Bank for Reconstruction), USAID, Soros Foundation, JICA (Japan International Cooperation Agency), and the government, there was little success in achieving progress in the textile sector to date.

Almost all survey participants think that the development of adjacent sectors will require time, and in the medium term the sector will therefore continue to rely on imported fabrics.

Downstream

In many cases, the Russian and Kazakh market presence of Kyrgyz producers is linked to Kyrgyz immigrants in these countries. A sector study commissioned by the ILO in 2009¹⁶ states: "At present the apparel industry in Kyrgyzstan targets low-income population strata in Russia and Kazakhstan. (...) Most of the output is marketed by 'shuttle merchants' at the Dordoy market, while direct supplies under contracts are insignificant."

The main reason for choosing a certain country for export is for 90 per cent of the managers the presence of repeat clients. 35 per cent of the companies choose a certain country for export because consumer preferences match their products. Other factors such as low transportation costs or tax incentives appear to have lesser influence.

Key informants estimate that the producer – wholesaler scheme prevails at present with practically no direct contact with the buyers. According to managers of garment enterprises, the main foreign partners who deal with the sale of garments abroad are small and medium-sized retail traders (35 per cent). The survey also revealed that frequently sales partners abroad are the relatives and acquaintances of the managers of garment companies. A quarter of survey participants (25 per cent) reported having foreign wholesale buyers with their own marketing channels. Only 5 per cent of respondents work with large department stores and chains for exporting. 55 per cent of surveyed garment enterprises have long-term (exceeding two months) contracts or oral agreements with their buyers.

The majority of managers of garment enterprises (83 per cent) reported problems with selling garments outside of Kyrgyzstan. Respondents said that exporting goods outside the country is complicated not only by imperfection of the customs system (37 per cent), breach of delivery time (10 per cent), but also corruption (10 per cent). Other problems mentioned included high competition and market saturation, lack of trade places, high transportation costs, limited financing possibilities, clients falling behind on payments and the taxation system (5 per cent each).

Almost half of the survey participants report selling garments through specialized containers in the local markets (mostly the Dordoi and Kara-Suu market or through the "Legprom" Association). Approximately one in five producers works under purchase contracts and does not deal with marketing matters. 14 per cent of producers sell garments

¹⁶ PBD Association (2009): Report on Results of Survey: Overview of the Situation in the Apparel Industry, Report commissioned by the ILO.

through their own specialized stores or boutiques in department units, as well as through private retail sellers. 5 per cent sell through specialized shops in trade centres.

2.2.3. Product Development

According to key informants, marketing in the garment industry is underdeveloped. Survey participants noted that the absence of professional sales and marketing skills is one of the sector's weaknesses. Surveyed managers said that they do not have any specific marketing strategies except for participation in exhibitions in Russia (by large companies).

In practice the following scheme is often used: the garment maker examines European and Turkish ready-made goods in the local shops and markets and estimates demand for such garments. If in his/her opinion there is demand for this garment, the garment maker buys one item and carefully disassembles it along the seams. After that, experienced gaugers prepare the templates based on the disassembled garment. The new garments are then produced and put up for sale. The development of a new garment, from design to sale on the market, takes on average 14 days. There are also cases when entrepreneurs who work on the Russian and Kazakh markets commission production of a certain item. In such cases, a garment of certain design or size which is popular in Russia is sent from Russia, and then the product is copied and delivered to the destination.

Key informants also noted that there are approximately 20 leading garment makers who develop original models and have well-established marketing practices. Such companies study the demand and develop various marketing strategies. As an example experts named several fashion shops that produce custom-made modern women clothes and dresses with ethnic designs.

2.3. Employment

2.3.1. Personnel

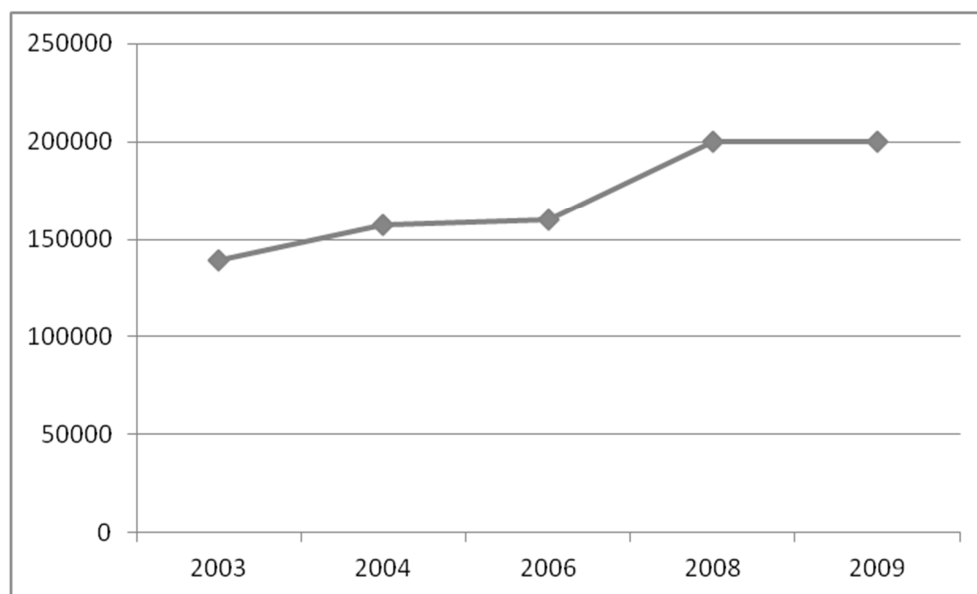
The study found that garment production is a highly feminized sector, with 92 per cent of the employees being women. More than half (57 per cent) of the workers in the garment sector come from rural areas¹⁷. Women form the majority at all levels of the garment sector; they work as managers, process engineers, designers, production foremen and sewing machinists. Men employed in the sector are mostly engaged in machinery repairs and maintenance, as well as in attaching garment accessories, ironing, packaging, driving, and delivering final products.

According to managers, the main personnel of garment units (fitters, designers, gaugers, production foremen) are highly skilled and experienced workers. Sewing machinists and ironing staff are usually low skilled labourers from rural areas who learn on the job and have no special education. New employees are usually found through acquaintances and relatives, through ads, or cooperation with vocational schools. Unregistered enterprises usually prefer to find new workers through acquaintances in order to have ways of social influence on them.

Key informants estimate the number of garment sector workers at 100,000-300,000 individuals. Official data put employment directly in the sector at 200,000 and indicate strong growth between 2003 and 2009. In addition, roughly 150,000 Kyrgyz citizens are estimated to work in garment related trading activities outside of the country.

¹⁷ USAID (2011), Gender Aspects in the Kyrgyz Republic's Garment Sector, Regional Trade Liberalization and Customs Reform Project.

Figure 2.3. Official Employment Figures for the Garment Sector



National Statistics Committee of the Kyrgyz Republic

An analysis of social security records suggests that most of the employees who work in the sector do not make social security contributions. The Social Fund has only 2,275 individuals registered as working in the garment sector. This is a dangerous situation since these workers will receive very low pensions or will not be eligible for any pension at all in the future. Considering the feminization of the garment sector, this can lead to growth in female poverty as early as in the next decade.

According to key informants, many enterprises work without any supervision, with sanitary and safety norms constantly violated. Many employers also do not observe labour regulations; workers often have to work 14-17 hour a day. Respondents also mentioned unreported or hidden cases of labour accidents.

2.3.2. Remuneration of Labour and coverage for sick leave

Table 2.3 shows that while wages in the garment sector have risen in recent years, increases have not been in line with increases of the national average wage and have barely covered the simultaneous increase in consumer prices. The data also suggests that wages in the garment sector are much lower than average country wages and wages in the manufacturing industry.

Table 2.3. Increase in Wages of Textile and Garment Industries (KGS); base year for real wages is 2005

	2005	2006	2007	2008	2009
Average nominal (real) monthly wage, nation-wide	4740 (4740)	5781 (5474)	6596 (5672)	8216 (5674)	9900 (6395)
Average nominal (real) monthly wage of workers in the manufacturing industry	5033 (5033)	6129 (5804)	6889 (5923)	8572 (5920)	11061 (7145)
Average nominal (real) monthly wage of workers in textiles and garment sectors	1767 (1767)	1916 (1814)	2142 (1842)	2660 (1837)	2878 (1859)
Inflation, consumer prices (annual percentage change)	4.4	5.6	10.2	24.5	6.9

ILO (2009): *Improving prospects of youth employment in the textile and garment sector*, ILO Subregional Bureau.

In the opinion of some key informants, actual wages in the garment sector during peak season almost double and according to various estimates range from 4,000 to 6,000 KGS per week with a 17-18 hour work day. Women receive 2-5 per cent higher wages than men.

Nearly 60 per cent of the survey respondents reported increased wages of their workers compared to the previous year by 5-50 per cent, with the relative majority of the respondents reporting a 20 per cent average increase in wages. Only 14 per cent of respondents said that the average wage for workers in their enterprises did not change since last year and almost 10 per cent reported lower wages.

92 per cent of managers said that they do not cover the medical bill in case of a labour accident. One third of the companies do not even pay the sick leave, while 57 per cent of the enterprises covered by the study say that they do so.

Furthermore, survey participants indicated that the size of the compensation for a labour accident or sickness is very subjective. Highly skilled specialists and individuals favoured by the managers tend to receive special treatment.

Table 2.4. Answers to the question “Do your workers receive any compensation in case of injury of sickness?”, percentages

	In case of injury			In case of sickness		
	Always	Sometimes	No	Always	Sometimes	No
Paid sick leave	58.8	5.9	35.3	42.9		57.1
Monetary compensation	10.0	90.0			88.9	11.1
Payment for medical treatment		8.3	91.7		88.9	11.1

ILO (2009): *Improving prospects of youth employment in the textile and garment sector*, ILO Subregional Bureau.

2.4. The Role of Industry Associations

There are two associations in the garment industry at present: "Legprom", which unites garment enterprises and "Soyuztextile", which unites knitwear-making and garment enterprises. "Legprom" counts 400 large, medium and small garment sector enterprises as its members and "Soyuztextile" 26 enterprises.

"Legprom" and "Soyuztextile" are well-known public organizations and according to survey participants play a major role in the development of the sector.

Key informants noted that these associations provide assistance to their members on various legal and production-related matters. In the opinion of managers of garment enterprises, the associations assist with the exploration of new markets, the provision of information about international markets and the defence of the rights and interests of garment makers in government and other state agencies. Another important function of these associations according to key informants is developing legislative proposals to improve sector regulation. Many key informants positively assessed the actions taken by the associations when the tax patent was cancelled for garment producers.

Key informants made proposals to establish an entity under one of the associations that will deal with procurement issues. According to key informants, this structure would be able to attract regional and international suppliers of wool, wool yarn, fabric and sewing accessories. In case of joint procurement of a certain raw material or a product this will allow to save more due to economies of scale and offer wider choice. Key informants think that such procurement structure could also warehouse some raw materials and sell it at affordable prices to garment enterprises.

Associations could also participate in subcontracting. According to key informants, this would help smaller enterprises to participate in implementation of large orders, which in turn would develop the sector and ensure technological upgrading of enterprises.

In the opinion of some survey participants, associations should help with collecting information about fashion trends, cooperate with leading international fashion houses, and in future should support the establishment of a Kyrgyz School of Fashion and Design.

It is through associations, according to key informants, that producers can join large whole-sale supply chains that will help increase sale of products.

For these reasons all study participants voiced the need to develop and support existing associations.

Chapter 3. External Factors

3.1. Taxation and Patent System

Kyrgyzstan currently maintains three different business tax systems of relevance to the sector: the general tax system, a simplified business tax system, and the patent system.

Under the patent system, the entrepreneur buys a tax patent from the tax office for a certain amount, which depends on the number of work places, but not on the production output. The single tax (patent) is then paid on a monthly basis at a certain specified rate. The use of a patent thus helps producers plan the size of payments, which creates predictability and stability and reduces scope for corruption due to the elimination of inspections.

The patent-based taxation in the garment sector went through several stages of evolution. During the early days of the sector, small and medium-size enterprises that made up the majority of enterprises, had no capacity to pay taxes at the officially established rates as they were producing at a very low level. Tax legislation thus arguably forced the majority of enterprises to go into informality. This led to economic stagnation of the sector. To simplify taxation, the government introduced the voluntary patent system of taxation in 2005. This contributed to bringing many small and medium businesses into the legal field.

Live voices

...The tax patent is vital for garment makers. Let's not forget that the sector legalized exclusively due to the introduction of patent-based taxation.

...Patent helps to address three main issues: the legalization of the informal economy, the creation of a microclimate for development of enterprises, and the elimination of corruption.

(Interview with key informant Asanova, "Legprom" leader, <http://tazar.kg> Viktor Glumskov)

The patent-based system continued until its cancellation in December 2008. This negatively affected the sector and some businesses closed down. Business expansion loans were frequently taken under the collateral of private property, and in the case of stable economic conditions it was not very difficult to repay the loan within a year. However, taking a loan during the unstable period of 2008/9 was considered very risky, and some firms found it safer to close until things stabilized.

Sector representatives fought to return to the patent-based taxation, which the government did, but the cost of patents practically doubled. According to almost all study respondents, taxation under the current system is not differentiated and the current tax system does not lead to increased state budget revenues. Government bodies often say that a new taxation system is needed for the further development of the sector, but there currently does not appear to be a clear reform agenda.

Live voices

...We will continue with the patent basis until we see that the industry is ready for gradual move to another system. Patents should eventually die out since with this system the revenue of the state does not rise with the rise in production.

(Interview with key informant)

"Pioneer" enterprises tend to think that the current tax rate is quite acceptable. However, respondents who represented small garment enterprises felt that the current

taxation system forces businesses into the informal economy, and does not stimulate or support garment producers.

The relative majority (43 per cent) of the interviewed managers, mainly coming from well-established and successful “pioneer” enterprises that operate under the general tax system, feel that the current tax legislation is equally acceptable for all garment enterprises, regardless of the size of the company. However, a quarter of the managers feel that the existing tax legislation is more suitable for large enterprises, but is inappropriate for smaller companies who are forced into the informal economy. About one in five respondents voiced the concern that no enterprise could adequately follow current tax legislation. Interestingly, nearly 14 per cent of the managers, mostly of large “pioneer” enterprises, think that nothing needs to be changed.

Live voices

...Taxation should take into account the size of an enterprise and whether it is doing well or not. In reality there are some large, medium, and small garment enterprises. The small units that are just starting up should make lower payments.

...The taxation system should stimulate development and growth of garment producers. For instance, a small enterprise should be allowed to work one year with reduced tax payments. During this period the company needs to make some profit in order to operate in the second year as well, and only then move to regular tax rates. This will attract new businesses into the sector, will make it easier for them and will serve as incentive.

(Interview with key informant)

In a study on the investment climate in the Kyrgyz Republic¹⁸, the World Bank found that the total average labour costs associated with tax accounting and mandatory reporting are indeed regressive, which means that small and medium enterprises bear the greatest burden in fulfilling reporting and accounting requirements. The report highlights that, in particular, the simplified tax regime is not very attractive to companies and does not fulfil its intended role to encourage graduation from the patent system. Instead, many SMEs (Small and Medium-Sized Enterprises) take advantage of the relatively high turnover threshold for the patent system and / or organize part of their activities in the informal economy or under commercially counterproductive arrangements (e.g. splitting up firms) that allow them to remain in the patent system. The report concludes that therefore, the current tax system establishes a bottleneck to firms’ growth beyond the threshold of leaving the patent system, and recommends a simplification of the simplified tax regime along with a reduction of the turnover threshold for the patent system. It also points out that companies see important long term advantages from graduation into the regular business tax system, including the opportunity to buy from and sell to a large number of companies.

Any reform steps of the business tax and patent system can have serious implications for the garment sector, both in a positive or a negative direction. On the one hand, the events of 2008/9 have shown that the sector’s export growth is very vulnerable to changes in the patent system that can generate costs and insecurity among garment producers. On the other hand, a reform that would address the above mentioned issues of graduation would have the potential to remove a critical bottleneck to firm growth in the sector, and encourage more firms to operate in the formal economy. This would also be important in order to enable them to pursue export development strategies beyond traditional channels and integrate into global value chains.

¹⁸ World Bank (2010) Investment Climate in the Kyrgyz Republic as seen by Small and Medium Enterprises, Investment Climate Advisory Services, World Bank Group, International Finance Cooperation, www.ifc.org/beekg.

3.2. Customs Union

Live voices

...Growth in production volume depends not on internal but external conditions. We need concessional export treatment to Russia. Currently Kyrgyzstan's share in the total volume of Russian imports is 4 per cent. For our country it is a huge number.

(Key informant interview)

On 19 October 2011, Kyrgyzstan was admitted to join the Customs Union of Russia, Kazakhstan and Belarus. The government justified this decision by the increased market for various domestic sectors, increased jobs, and attraction of investment. This issue was hotly debated in Kyrgyzstan and up to now there is no unanimity concerning Kyrgyzstan's accession. An independent country-level task force was supposed to come up with a final expert conclusion on this matter. However, the formation of that group was delayed and many key informants justify the final decision of accession more by political reasons than economic ones. Overall, implementing the Common External Tariff (CET) of the Customs Union will lead to substantially higher average tariff levels and may bring Kyrgyzstan in conflict with its WTO obligations. This report does not deal with the question whether accession overall is a good decision, but highlights some of the potential consequences for the garment sector, both positive and negative.

Live voices

...At present 90 per cent of textile products manufactured in our country are exported to Russia and Kazakhstan. We are not supposed to enter products to Russia because we don't have a compliance certificate. If we stay out of the Customs Union zone, the garment sector will face major difficulties.

...If we can get some preferences in terms of raw materials, we could become the 'sewing machine' of EurAsEC (Eurasian Economic Community). It is up to the government to make sure that that happens. If we join the Customs Union, garment makers would need to pay from 30 to 40 per cent in fees plus the VAT for the raw materials.

...We are very concerned, it is crucial that the cost of component materials stays as it is at present. Compensation can be achieved only if there will be no borders. A lot of costs are incurred during transfer through the border with Kazakhstan and Russia, this will no longer happen if we join the Customs Union. Because barriers are made up not of tariff policy, but bureaucracy and corruption, which will be eliminated once we join the Union.

(Asanova S., "Legprom" Manager, Vechernyi Bishkek Newspaper, 15 December 2011)¹⁹

Survey respondents in particular highlighted the following concerns:

1. The price of component materials, fabric and garment accessories that Kyrgyzstan fully imports from China, Turkey, and Korea will increase from around 5 to up to 10 per cent²⁰. As a result, the prices of Kyrgyz-made garments will rise and the industry will lose competitiveness in export markets.
2. Unified economic borders with Russia and Kazakhstan will lead to outflow of highly skilled labour from Kyrgyzstan's garment sector to other countries with higher pay. The garment sector risks facing a problem of lack of skilled labour. Moreover, "pioneer" enterprises already experience shortage of skilled workers.
3. Higher tariffs would likely bring up prices for a number of important consumer articles, which could lead to social unrest as well as higher wage demands.

¹⁹ www.vb.kg

²⁰ Central Asiam Free Market Institute (CAFMI), Bishkek, 20 December 2011.

Live voices

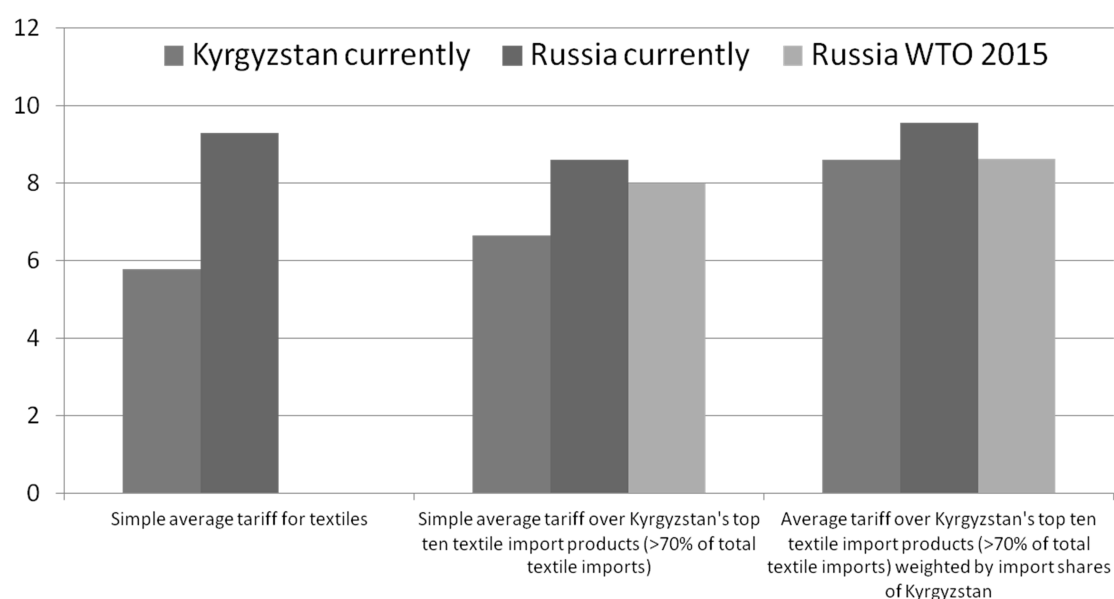
...After we join the Customs Union the raw materials will become more expensive. Currently, under WTO rules it is cheap to import goods from China. However, if we join the Customs Union, according to Russian Federation's tariffs we will pay more, and consequently our exports will rise in price. As far as I know if we join the Customs Union the rules of WTO will be automatically replaced by Customs Union agreements. That is why from the perspective of the garment sector it is a disadvantage for us.

(Key informant interview)

On the positive side, most respondents think that the Customs Union presents a chance to expand the markets for Kyrgyz garment products and in particular reduce costly non-tariff barriers with the Russian and Kazakh markets. This could strengthen the industry's competitiveness in export markets. They also highlighted that it might be possible for Kyrgyzstan to negotiate at least temporary exemptions or an adjustment period for tariffs on key inputs for the garment sector, and that not joining the Customs Union would have led to a substantial deterioration in market access to member countries. Ultimately, a majority of survey respondents believed that benefits of joining the Customs Union could outweigh the costs to the sector.

A simultaneous analysis of trade and tariff data reveals that the anticipated increase in tariffs on intermediate inputs may actually not be very substantial. According to Figure 3.1, survey respondents are correct in pointing out that the Customs Union's Common External Tariff on textiles used as inputs for garment making is almost twice as high as Kyrgyzstan's current average tariff on these products. However, the differences are substantially smaller for the textile inputs that Kyrgyzstan imports the most. The second set of bars in Figure 3.1 shows that the difference in tariff rates declines importantly once it is calculated only over Kyrgyzstan's top ten textile import products, which jointly account for over 70 per cent of total imports. After the implementation of Russia's WTO commitments by 2015, the difference becomes even smaller. The last set of bars shows that once tariffs are weighted by the relative size of Kyrgyzstan's top ten textile imports, the difference disappears.

Figure 3.1. Import Tariffs on textiles before and after Kyrgyzstan's accession to the Customs Union



Source: Data from ITC Market Access Map and Russia's WTO accession documents and authors' calculation

3.3. Russia's Accession to the WTO

While most surveyed managers tend to think that Kyrgyzstan's accession to the Customs Union may ultimately have positive effects for the sector, they do believe that Russia's membership in the WTO will negatively affect the competitive position of the Kyrgyz garment sector. The concern is that Russia, under its WTO commitments, will reduce tariff barriers against other exporters of garments – namely China – and thus Kyrgyz producers would lose some of the preferential margin they are currently enjoying in the Russian market. In addition, given that Russia is already in a Customs Union with Kazakhstan, any tariff reductions would have to take place through the Common External Tariff and therefore also affect the Kazakh market.

Live voices

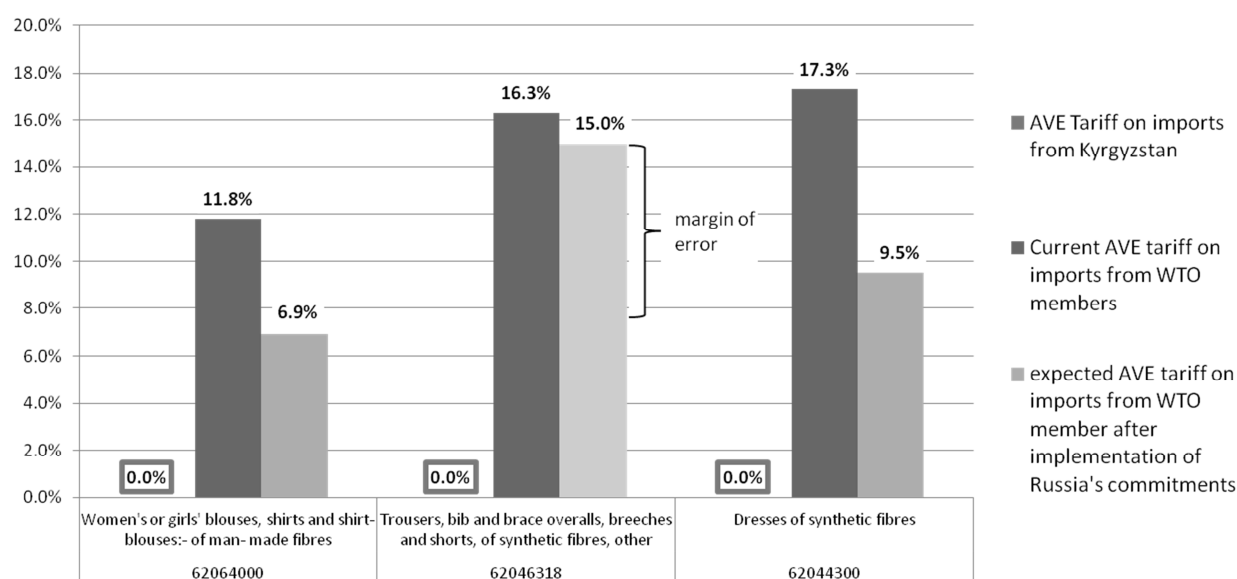
...Russia's potential membership in the WTO will seriously affect the situation. Because when it happens, Russia will be forced to reduce customs duties for Chinese imports. And Chinese goods will be cheaper for Russia and they will clearly put us in disadvantage. Nobody will need our garments. What is our current advantage? High customs duties for Chinese goods to Russia make Chinese goods more expensive. When China gets easier access to the Russian market, our sector will be at loss.

(A. Maslov)

The potential loss of market access preferences due to Russia's WTO accession is illustrated in Figure 3.2 for the three single most important Kyrgyz garment export products. For each of these products, Kyrgyzstan, China, and Turkey in varying orders are the three most important suppliers of the Russian market. Kyrgyz producers already enjoy duty free market access under the preferences granted by Russia to CIS countries, while competitors like China and Turkey face relatively high tariffs, consisting of a combination of an ad valorem rate and a minimum amount per unit. Figure 3.2 shows the calculated ad valorem equivalent (AVE) tariff rates, which are defined as total tariff revenue from a given product divided by total imports of that product.

The tariff concessions specified in the agreement for Russia's WTO accession, to be implemented in most cases by 2016, call for substantial reductions in the tariffs for all three products shown in Figure 3.2. For two products, the AVE tariff rate unambiguously declines by almost half. In the case of the third product, the new tariff structure is too complex to calculate the new AVE rate with certainty, but the expected margin also falls well below the current rate.

Figure 3.2. Preference Erosion due to Russia's WTO Accession



Source: Data from ITC Market Access Map and Russia's WTO accession documents and authors' calculation

The example illustrates that Russia's WTO accession is likely to lead to substantial preference erosion for Kyrgyz garment producers in the Russian and Kazakh markets. For instance, the reduction of AVE tariffs on HS code 62044300 (dresses of synthetic fibres) from 17.3 per cent to 9.5 per cent would imply a price reduction of nearly 7 per cent²¹ on imports from competitor countries such as China and Turkey, putting substantial competitive pressure on Kyrgyz manufacturers.

²¹ In practice, in the absence of perfect competition, this gain in market access is likely to manifest itself in a combination of consumer price reductions and an increase in the profits of producers from countries benefiting from enhanced market access.

Chapter 4. Sector Outlook and Strategy

4.1. Sector Outlook

Despite the industry's strong export growth over the last years, there are several indications that the current business model based on cheap labour, low taxes (for firms in the patent system), preferential market access, and concentration on traditional markets and distribution channels may soon reach its limits. Low wages and precarious working conditions are leading to high labour turnover, including migration abroad, which presents a serious problem for companies and reduces their ability to build up skills among their workers. The patent system generates inefficiencies and unsatisfactory fiscal revenue and is likely to be reformed in the medium term. Preferential margins in traditional markets are eroding and thus competition is likely to increase significantly.

Interviewed managers are well aware of these issues and the need for the sector to increase its competitiveness. Table 4.1 shows survey responses on the top 5 priorities managers identified to boost the sector's competitiveness. Interestingly, further reducing labour costs (or wages) is not among them; there appears to be a consensus that this is not a viable option.

Managers' top priority is the reduction of non-tariff barriers. Joining the Customs Union may provide opportunities for Kyrgyzstan to push for improvements in this area, but these are not likely to come automatically with accession and progress will require continuous policy attention. A more detailed analysis of the textile value chain, aimed at identifying critical cost factors and bottlenecks along the way, could greatly enhance the effectiveness of policy measures in this area.

The second top priority is to expand the assortment of products. This reflects an interest and perceived need by companies to diversify their operations. New products and enhanced capabilities for product development make it possible to target new consumer groups and new markets, and establish new marketing chains. This will be particularly important given the expected increase of competition in traditional markets. In order for companies to remain profitable, it will be crucial for them to develop the ability to quickly respond to changes in market conditions and adjust their production if necessary to target market segments where they can compete successfully. Similar arguments can be made with respect to the need to upgrade machinery and introduce new technologies. All these changes will be crucial in order to further develop and diversify production and increase Kyrgyz producers' ability to identify and compete in new market segments.

Achieving the above described objectives will inevitably require higher demand for specific skills in the areas of product development (e.g. designers) and the introduction, use, and maintenance of new technologies. This is reflected in the anticipated skill demand discussed in the next chapter as well as in managers' responses that rank improving worker's skills as the third highest priority for improving competitiveness.

Table 4.1. Actions that need to be taken to increase competitiveness of Kyrgyz garments exports

Top 5 actions that need to be taken to increase competitiveness of Kyrgyz garments abroad (multiple answers possible)	per cent
Reduce nontariff barriers	43.3
Expand assortment of products	38.3
Improve workers' skills	34.8
Install new production machinery/ equipment	34.0
Introduce new technological lines	28.6

Source: STED Kyrgyzstan survey (2011)

International experience suggests that over time and with increasing competition in its main markets, the garment industry is likely to undergo a process of consolidation towards fewer, but larger and more productive enterprises. In the course of this process, average productivity is likely to increase, as weaker firms leave the market or are absorbed by stronger firms. This can have significant implications for the industry's labour demand, as larger, more productive firms tend to use more sophisticated technology and carry out more advanced business processes both upstream (product design, inbound logistics etc.) and downstream (sales management, logistics, marketing etc.). The methodology used in this report to anticipate the implications of such an adjustment process on labour and skill demand is to focus the survey on "pioneer" firms; firms that stand out in terms of size, productivity, development of new products and access to foreign markets. The idea is that over the years, the strong firms in the sector will grow and become more like these "pioneers", while some of the weaker ones may eventually disappear.

4.2. Sector Strategy

The existing sector export development strategy for the years 2009-11, which was written with the support of GIZ, mentions five priority targets for the sector²²:

1. Increase exports to Russia and other CIS countries (+35 per cent over the two year time frame of the study).
2. Enhance marketing and sales capabilities.
3. Strengthen the sector associations (Legprom and Soyuztextil) and the Shvei-Profi training centre.
4. Increase productivity across firms.
5. Establish sourcing cooperatives for raw materials

Survey responses and evidence presented in this report have shown that these strategic priorities remain valid and important. The revision of the strategy, which is under way as this report is written, should however recognize changing external conditions, in particular due to Russia's WTO accession. Without diminishing efforts to establish new products and marketing channels in traditional markets, a wider focus on export market diversification might be considered.

The 2009-11 strategy also dedicates some space to skills and education, but relies mainly on a static analysis of current skill needs. With the need for firms to strengthen their competitiveness and develop new capabilities over the coming years, skills will

²² GTZ (2009): Broader strategy for the textile and clothing industry in Kyrgyzstan 2009 to 2011, Bishkek, Kyrgyzstan.

become an even more important factor for the sector's success, and new areas of skill demand are likely to arise. Given that the development of new skills can take several years, a forward looking view to anticipate changing skill needs would be useful in the revision of the strategy. The following chapter provides this type of analysis.

Chapter 5. Skill Demand

5.1. Existing Skill Demand

All managers of surveyed companies were asked to rate on a 5-point scale how difficult it is to find skilled workers, where 5 stands for very difficult to find and 1 for very easy to find. Averaged scores are presented in the table below. The answers show that in spite of high unemployment rates in the country, it is not easy to fill vacancies with skilled workers. It is particularly difficult to find skilled craft workers and technicians as well as candidates for professional level occupations, such as skilled dyers (4.5 points), designers and gaugers (3.8 points each) and machine repairmen (3.7 points). Skilled machinists, such as cutters (3.3 points), sewing machine operators and others production related workers (3.1 and 2.9 points, respectively) also seem to be difficult to find.

According to key informants, difficulties with finding dyers are mostly related to the fact that training in this narrow field is basically absent due to the decline of textile production. Survey respondents argued that the labour markets for specialized occupations such as dyers, designers, gaugers, repairmen and dress cutters are quite small, which makes matching of workers to available jobs more difficult.

According to key informants, demand for highly skilled gaugers led to a new type of entrepreneurship: There are companies that specialize only in production of gauges. The lack of skilled designers is compensated by taking a blueprint of other ready-made garments produced abroad.

Table 5.1. Assessment of difficulties related to finding workers with certain skills; 5-points scale (where 5-very difficult to find, 1- not difficult to find)

Main specializations	Total, points
Machinists	
Sewing machine operators	3.1
Knitting machine operators and technicians	2.4
Other machine operators	2.9
Skilled craft and technician level occupations	
Delivery and security personnel	1.5
Cutters	3.3
Workers processing final garments, packaging	2.4
Machine adjusters	3.2
Repairmen and technicians	3.7
Gaugers	3.8
Drivers/ transportation unit	1.9
Professional level occupations	
Dyers	4.5
Administrators	3.1
Designers	3.8
Highly skilled personnel with technical knowledge (dyers, textile scientists, engineers)	3.0
Procurement personnel	2.0
Marketing department	2.2
Sales department	2.2
Administrative/office workers, accountants	2.7
Operations manager	
Final product managers and other production managers	1.4
General managers and entrepreneurs	
Chief operating officers, and other non-production managers	2.1

Source: STED Kyrgyzstan survey (2011)

5.2. Expected Skill Demand

Most managers (63 per cent) had difficulties responding to a survey question on expected vacancies in the sector over the next five years. This illustrates that the sector itself is having difficulties to assess its pathway forward and the resulting skill needs.

Managers that did respond to this questions mentioned 9 different occupations for which they expect increasing demand on the labour market in the next several years. Professional level occupations, and in particular designers, are expected to be most demanded in the future. This suggests that garment enterprises are striving to develop their own models and produce unique designs. According to key informants, “pioneer” enterprises already feel the shortage of highly skilled designers today. The growing demand for process engineers and dress cutters is fuelled by growing competition and, according to key informants, the desire of producers to satisfy new customer needs. This illustrates the strong linkages between skills demand in the sector and export performance and diversification.

Skilled craft workers and technician level occupations, as for example universal sewing machinists, are also highly demanded specializations in the future. The adjective “universal” implies the ability to operate various types of professional equipment and perform operations skilfully. This indicates a trend among “pioneer” firms to deviate from the current pattern of hiring unskilled workers as sewing machinists and training them for specific tasks only.

The table below presents a ranking of the expectations for most demanded occupations in the garment sector in the near future.

Table 5.2. Occupations that will be the most demanded on the garment sector's labour market in the next several years

Occupations that will be the most demanded on the garment sector's labour market in the next several years	per cent
Designers	23.7
Universal sewing machinists	18.4
Process engineers	15.8
Dress cutters	15.8
Sewing machine operators	7.9
Cutters	5.3
Engineers	5.3
All skills/occupations	2.6
Embroiderers	2.6
Highly specialized skills	2.6

Source: STED Kyrgyzstan survey (2011)

5.3. Training Needs

While the two previous sections of this chapter focus on current and expected quantity of labour demand across different occupations, the survey also attempted to assess employers' views on the suitability of skills of their current employees in different occupational profiles. The first step was to ask employers "What kind of help does your enterprise need in terms of training/skills enhancement of your workers?" 80 per cent of respondents were able to name at least one area in which their firms needed help in this regard, mainly in the following areas:

- Professional training of all workers;
- Training of designers;
- Training in new technologies;
- Training of sales personnel;
- Training of dress cutters;
- Internships/ study tours.

The responses strongly reflect an apparent interest among managers of interviewed firms to strengthen skills relevant for diversification and upgrading of business activities in terms of developing new products and markets.

Live voices

...The lack of good training for middle-level personnel and managers prevents recovery of our sector and moving to the higher level of development, i.e. international markets. There is an objective need to raise professionalism of managerial staff in business, planning, marketing and other relevant fields.

...Educational institutions need to strive to provide services at the level of international standards that meet the requirements and needs of the labour market.

(Key informant interview)

In a second question of this section, managers were asked to assess the professional skills of their workers and indicate what skills are in most need of additional training by occupation. This led to the following ranking:

Table 5.3. Occupations in need of training

Occupations	Rank in the Ranking of Training Needs
Machinists	
Sewing machine operators	7
Operators of "other" machines	9
Knitting machine operators and technicians	16
Skilled craft and technician level occupations	
Operators-cutters	4
Gaugers	8
Machine technicians/adjusters	11
Drivers/transportation unit	12
Repairmen and technicians	13
Delivery and security personnel	19
Professional level occupations	
Marketing personnel	1
Procurement personnel	2
Sales department	3
Designers	4
Workers processing final textile products, packaging, and other internal assets	5
Administrators	6
Administrative/office workers, accountants	10
Dyers	17
Highly skilled technical staff (dyers, textile and process engineers)	18
Operations manager	
Final product managers and other production-related personnel	15
General managers and entrepreneurs	
Chief operating officers, and other non-production managers	14

Source: STED Kyrgyzstan survey (2011)

The ranking shows that marketing and professional sales skills in particular are underdeveloped in the garment industry. Until now, the only marketing strategy of survey participants is participation in exhibitions in Russia. Key occupations currently mentioned such as designers and gaugers / cutters also rank high on the scale of training needs.

Chapter 6. Skill Supply

One of the most important factors that limit supply for skilled labour, according to key informants, are the relatively low working conditions and wages. Skilled workers with good education and experience usually command higher salaries and certain social benefits. Thus, highly skilled workers are crowded out from the garment production and only domestic labour migrants who agree to work for lesser pay and longer hours stay. According to key informants, there is an outflow of highly skilled sewing machinists to Russia and Kazakhstan where they receive housing, employment, and higher wages than in Kyrgyzstan. As a result, the country loses young, skilled workers who have been trained in the vocational schools of the Kyrgyz Republic.

Live voices

...I know entrepreneurs who openly say that instead of taking a sewing machinist with higher productivity it is easier for them to hire two unskilled and untrained girls who came from rural areas. They can be given on-the-job training, paid small wages, and work long hours. These girls do not demand any social support.

(Key informant interview)

One third of the interviewed managers assert that the poor quality of labour and the lack of skilled workers on the market have become a hindrance for the development of the sector.

To look for better skilled workers, the interviewed enterprises use different channels. One third of all interviewed garment enterprises uses newspapers to look for new workers. The second most used channel is acquaintances (17 per cent), followed by the use of employment services and internet advertisement (15 per cent each). Television as a means of finding new workers is used rarely (12 per cent) due to high advertisement cost and employers also look only rarely among graduates of vocational schools and colleges directly (7 per cent).

Several structures and institutions train workers for the garment sector, but these are not well coordinated among each other. They include the following:

- The system of vocational technical lyceums
- Institutions of higher education, such as the Kyrgyz Technical University in Bishkek city
- Training courses
- On-the-job training at garment enterprises

6.1. Vocational Technical Lyceums

The system of technical and vocational education and training (TVET) has schools all over the country, both in urban and rural areas, and thus has large potential for training highly skilled labour for the garment sector.

According to the Agency for Vocational and Technical Education for Garment and Textile Sectors, vocational lyceums offer education and training mainly for machinists, in particular sewing machinists with various specializations such as in tailoring, embroidery, ethnic garments, spinning and operators of knitting-sewing equipment, and for skilled craft workers and technicians, such as tailors and gaugers.

These specializations are offered in Bishkek city by 6 lyceums, in the Osh province by 15 vocational lyceums, in the Batken province by 10, in the Jalal-Abad province by 19, in the Issyk-Kul province by 5, in the Naryn province by 7, in the Talas province by 6, and in the Chui province by 12 vocational lyceums.

However, training of specialists for the garment sector by the TVET system tends to decline. In 2010, 34 per cent less students graduated than in 2009 (3404 persons), despite increasing employment in the sector.

The duration of studies in TVET system varies from 10 months to 4 years, substituting for other forms of secondary education. As shown by Table 6.1, 55 per cent of the students prefer to study in TVET under 10 month programs, and 35 per cent under the 3-year scheme²³. Garment sector stakeholders expressed their dissatisfaction with this relatively long duration of education and argued that the necessary skills could be acquired much more quickly if the system was streamlined.

Table 6.1. Number of TVET graduates by duration of the studies and specialization, persons (year 2010)

	Duration			
	10 months	3 years	2 years	4 years
Total:	1227	780	227	15
Sewing machinist	579	401	95	15
Tailor	531	182	87	
Tailor-embroiderer			19	
Sewing machinist-embroiderer		27		
Sewing machinist, maker of ethnic garments/crafts	50	87	26	
Sewing machinist-tailor	31	28		
Sewing machinist-spinner		30		
Operator of knitting and sewing equipment		25		
Gauger-sewing machinist	36			

Source: STED Kyrgyzstan survey (2011)

Generally it can be said that the TVET system is directed at training socially vulnerable groups of the population, including orphans and half-orphans, and thus addressing the problem of poverty and employment. The system often offers meals and accepts students that have difficulties studying in the regular high school. But it is not only the social benefits offered by the TVET system but also the social environment— parents, relatives, and friends – that often affects the decision of young person to study in a vocational school or lyceum. The main incentives for choosing a certain field of study in the vocation system are market demand, the level of pay for such occupation, and the prestige of the occupation. However, in the perception of society there is certain negative stereotype concerning vocational education.

Survey respondents expressed strong dissatisfaction with the performance of the TVET system. The quality of education offered by vocational schools often falls behind the needs of modern manufacturing companies. The situation is partially due to the lack of

²³ *Demand for labor in Kyrgyz garment making and knitting enterprises*, <http://www.mz.kg/news/view/id/341>, 18.07.2011.

professional analysis and monitoring of labour market needs in occupations produced by the system (at the government and/or the level of vocational schools), lack of the linkage "production - vocational training - production", insufficient competitiveness of vocational school graduates due to poor teaching and insufficient material endowments of vocational schools. Training in vocational schools is done on technologically outdated equipment, practically without reference to popular fashion trends. Career counselling in the vocational system, according to the people who work in the system, is done poorly.

Respondents' answers indicate that only one third of enterprises employ graduates of relevant vocational technical schools and colleges; nearly 14 per cent of the surveyed enterprises do not have graduates of vocational colleges among their workers. Strikingly, the majority (52 per cent) of managers had difficulties recalling whether their workers had special vocational education and training or not, indicating that managers do not see a high value added in a worker having this type of education.

Key informants have also mentioned weak cooperation between businesses and training institutions. There is no system of "orders" from businesses to educational institutions in which enterprises can request a certain number of graduates with a specific set of skills and which would allow businesses to have skilled workers and graduates to obtain jobs.

Live voices

...The problem is that our lyceums, especially those that are located in rural areas, use outdated equipment in providing the training. Besides, lyceum graduates have very little practice. As a result, when graduates go out to find jobs, it turns out that they don't know how to operate the machinery provided by the entrepreneur.

...Machinery technicians also have difficulties finding employment because they are simply unacquainted with new equipment installed in the actual productions.

(Key informant interview)

A survey of vocational schools showed that the management of educational institutions does not monitor employability of their graduates. In turn, many graduates don't find employment in their field of study and contribute to the unemployment level.

Several international donors and aid agencies are currently providing support on different levels to reform the TVET system, including a 10 mln US\$ project by the Asian Development Bank.

6.2. Higher Education

The Kyrgyz Technical University in Bishkek offers higher education diploma for professional-level occupations, such as sewing machinist-process engineers or apparel designers. Training of specialists for the garment sector should yet be differentiated from training of specialists for middle and higher management level, which should be offered by the higher education institutions. Interviews with the garment enterprise managers suggest that businesses rate the quality of education in universities of Kyrgyzstan as poor.

Live voices

...Quality of education in Bishkek-based universities is very low. Education has become corrupted. There are even known rates of payments for 'fixing' an exam or a test in various universities. Among universities that do offer good education and are not so corrupt we can name only two, but then these do not produce workers for our sector.

(Key informant interview)

6.3. Training Courses

A number of lyceums and private providers offer specialized training courses for specific subjects of varying quality. The individual training courses commissioned by the employment services trained and retrained in 2010 192 unemployed persons in 3-months courses, 20 individuals in 2-month courses and 15 individuals in 3.5 month courses to specialize in sewing. In tailor courses, 42 individuals were trained in 3-month courses and 4 individuals in 2-month courses. 15 individuals were trained in 3-month sewing machinist-embroiderer courses. And 74 individuals passed a 1 month for-pay course under the employment service to specialize in pant-sewing.

A major initiative in the area of training provision was the foundation of the Shvei-Profi training centre in 2008, an initiative of the industry associations. Shvei-Profi operates as a commercial training provider for firms in the industry and provides modular training courses of 1-3 months, as well as longer part-time courses. These are intended for current employees of the textile sector, as well as retraining of currently unemployed workers.

With the support of GIZ, Shvei-Profi was equipped with state of the art technical equipment, including modern sewing machines as used by firms in the sector and different computer based design software packages. The centre can also provide direct cutting and design services to firms in the sector. In addition, it was intended as an innovation hub that would contribute to the dissemination of knowledge and upgrading of skills and technology in the industry through the organization of seminar and workshops.

The experience with the operation of Shvei-Profi has not fulfilled the expectations of the industry so far. The centre is intended to operate on a cost-covering basis, and relatively high costs of training deter some potential students or employers to get their staff trained. After the crisis of the industry and political unrest, demand for the services offered by the centre dropped in 2010 and did not recover. Industry representatives complained about managerial and communicational problems with the centre's leadership, which eventually led to the installation of a new director at the end of 2011. Since then, the centre has been undergoing an extensive audit and is currently not operational as a training provider.

6.4. On-the-job training

Survey respondents indicated that due to the lack of skilled labour in the market and poor quality of available education and training institutions, companies have to train and enhance skills of new workers. That is why garment makers spend their own funds to train newly hired workers. This is done in particular by "pioneer" enterprises. Many attribute success of their enterprises to highly skilled professional workers.

56 per cent of the training sponsored by surveyed garment enterprises was on-the-job training. One third of the enterprises who decided to train their own skilled workers sent them to refresher courses. One in ten leading companies prefers to send their staff to retraining courses. Other venues for training courses included Master Classes and courses organized by BNP as well as the "Legprom" Association.

The most frequently trained occupations by the garment enterprises are machinists and technicians, such as cutters (35 per cent) and sewing machine operators (20 per cent). Overall, respondents have named around 13 occupations and skills, among which figure also professional level occupations and operations managers, in which they train workers.

6.5. Migration

High unemployment rates, deteriorating social welfare, poverty, and higher wages in the neighbouring countries have become the main reasons for outward labour migration of skilled workers. According to UNDP (2010)²⁴, 100'000 to 700'000 Kyrgyz citizens work abroad and the number is growing. One of the principal countries of destination for the Kyrgyz labour migrants is Russia. According to a World Bank study²⁵, 400'000-700'000 migrant workers from Kyrgyz Republic work in the Russian Federation and the number is 70'000 for Kazakhstan which is another major destination country for migrant workers. This seems to be a natural trend given that Russia and Kazakhstan are the most viable economies of the former Soviet Union and that there is a visa-free regime between these countries.

Outward labour migration has both positive and negative aspects to it. On the one hand, migration does not only ease the oversupply of labour and offer opportunities for young people to build their professional capabilities while there are abroad, it also plays a huge role in supporting private consumption which contributes to poverty reduction and economic growth. According to the World Bank, Kyrgyzstan's remittance inflows totalled \$1.2 billion in 2008 and represented 28 per cent of Kyrgyzstan's GDP²⁶.

One of the main negative aspects of outward labour migration is that it reduces human capital and considerably undermines the overall workforce potential in the home country. Migration can thus create a risk of degradation of human resources available for the national economy. The most active part of the population is involved in the outward migration. About 70 per cent of Kyrgyz emigrants are working age persons²⁷.

Moreover, it was found that demand for skilled workers on the Kyrgyz labour market and in CIS countries are in many ways similar, meaning that the national labour market is competing with foreign markets for the same categories of labour. Due to the wage differences Kyrgyzstan is losing qualified workers to the CIS countries²⁸.

The garment sector as a mainly export oriented sector is unlikely to benefit substantially from the positive domestic demand effect of remittances, and at the same time, key informants mentioned that outward migration was already aggravating the shortage of skilled labour for garment producers, contributing to high labour turnover, and at the same time aiding their competitors in neighbouring countries. Unfortunately, precise data on migration by occupation or by professional education is not available, which makes it difficult to evaluate the precise magnitude of the effect on the garment sector.

In addition, there are also other negative aspects related to labour migration such as the separation of families. According UNDP, men represent 73 per cent of Kyrgyz labour migrants, a phenomenon that contributes to an increase in low-skilled female and child labour.

²⁴ UNDP (2010), Kyrgyzstan: Successful Youth-Successful Country.

²⁵ Joint country support strategy for the Kyrgyz Republic 2007-2010 World Bank, p 7.
http://siteresources.worldbank.org/INTKYRGYZ/Resources/JCSS_ENG_07.pdf

²⁶ World Bank (2010), Migrant Remittance Flows: Findings from a Global Survey of Central Banks.

²⁷ Kyrgyz Republic Country Development Strategy (2009-2011),
<http://sgdatabse.unwomen.org/uploads/Kyrgyzstan%20-%20National%20Development%20Strategy%202007-2010.pdf>

²⁸ Labour Migration and Productive Utilization of Human Resources, Kyrgyz Republic, Bishkek 2009, ILO.

Chapter 7. Recommendations

7.1. Policy Level

The report has highlighted the importance of skills for the sector's development. However, while it may currently be the most pressing one, this is clearly not the only critical area of the enabling environment that needs to be addressed. Other urgent elements mentioned in the report include reducing trading costs, maintaining access to affordable inputs, finding a sustainable solution for business taxation that encourages firms to grow and formalize, and strengthening the industry associations. In order for the sector to continue its recent growth, these and other issues need to be addressed in a coherent and strategic manner. The ongoing development of a new sector export strategy provides an important opportunity for this and skills and education should take a central role in the process.

Any strategy to enhance the availability of relevant skills for the garment sector has to choose between an approach based on radically modernizing education and training systems, or an approach that largely by-passes existing institutions. The garment sector may be the best candidate out of all sectors to drive reform forward, so it appears preferable to take a wider view and not establish a parallel industry-led education and training initiative for the garment sector only. Indeed, the government of Kyrgyzstan is interested in upgrading its education and training systems and also the garment industry would like to see the existing system improved. If upgrading Kyrgyz education and training is to be more than an abstract goal, the change should be led by the needs of sectors where change will yield economic and employment benefits. This will be helpful in terms of justifying government spending, attracting support from donors, and overcoming institutional resistance to change.

Live voices

The garment sector is currently in a difficult period due to lack of labour and lack of professional specialists. High turnover is apparent in the sector [...]. The Government of Kyrgyzstan intends to apply all efforts to create a favourable legal basis and support the institutional development of the education sector and build the capacity of institutions of higher and vocational education"²⁹.

Sanjar Mukanbetov, Deputy Minister of Economic Regulation of the Kyrgyz Republic.

²⁹ Bishkek, December 3 2011, <http://www.kginform.com/>.

7.2. Institutional Level

Survey participants' recommendations and a general analysis of the situation point to the following areas of action to improve skills of garment sector workers and to upgrade the system in general:

7.2.1. *Improvement of cooperation between the industry and the education system.*

Better links between industry and education institutions are crucially important. Some progress has been made in this area through several consultative meetings between industry and representatives of the education institutions, and the ownership of the industry in the Shvei-Profi training centre. However, stakeholders indicated that attempts to create a more formal and permanent mechanism for skills dialogue have so far failed and cited lack of funding as well as a lack of interest from participating companies as the main reasons. At the same time, survey respondents were quite unanimous in pointing out that better coordination between firms' needs and education and training institutions is crucially important.

International experience from supporting the promotion of industry skills dialogue suggests a number of lessons for establishing successful mechanisms.

- There are different levels at which such an initiative can be established, ranging from arrangements for occasional consultation on course content to groupings that undertake significant research, develop curricula, and get involved in the allocation of resources. It is important for stakeholders to agree beforehand on what they see as an appropriate level of activity.
- It is quite common for businesses to quickly lose interest in such initiatives. Businesses may initially engage without allocating specific resources for a few meetings, but they have so many other calls on their attention that it will be difficult for them to keep this up for long unless they are willing to dedicate time and energy of a specific high level qualified manager.
- In order to fully engage in an initiative, business will need to see a clear pay-off in the short term. This can, for instance, take the shape of immediate responses to short term training needs through the development of appropriate courses. The Shvei-Profi centre appears to be a natural counterpart for this.
- Availability and dedication of adequate staff at different levels is key. Models seen elsewhere often use a combination of making the initiative part of the job of a focal person in the industry association, making contributing to it part of the job of a small number of corporate affairs or HR managers in the sector, and appointing industry experts to study groups/research projects with a limited time commitment that lasts for a limited period.
- Any initiative in this field requires substantial resources for staff, research, implementation of recommendations etc. If companies are not convinced that the required resources are available, they may not see an initiative as relevant and hesitate to dedicate time and funds themselves. Given the unanimous agreement of stakeholders on the importance of skills for the sector, the declared interest of the government to address these issues, and the presence of multiple international agencies in the sector, a coordinated effort to plan and mobilize the required resources over a medium term period appears to be the most promising way forward.

Specific suggestions from survey participants on how to improve coordination between industry and the education system include the following points:

- Regularly monitor market demand in the garment sector and train professionals with necessary specializations.
- Develop measures that contribute to raising cooperation of educational institutions and businesses in terms of employment of graduates. For instance, conduct competitions with participation of entrepreneurs and award the winners "gold certificates" that ensure the employment of graduates who demonstrate high results.
- Develop a set of measures aimed at stimulating entrepreneurs who provide internships to lyceum students.
- Promote lyceums that can demonstrate high levels of employability of their graduates.

7.2.2. Reform priorities by occupational types

An analysis of the education system by type of occupation shows that there is need for a fundamental re-examination of machinist education and training in Kyrgyzstan: The system has to be designed in a way that skills, technologies and working practices fit the new requirements for high labour productivity garment manufacturing. A reform initiative for TVET would collaborate with the sectoral institution for skills dialogue discussed in the previous section, but would take the lead on issues like quality assurance and curriculum reform, and would probably have a system-wide brief, taking training for garment related occupations as the pioneering vehicle for change across the whole of the TVET system.

While the numbers involved are lower, there is also a need to re-examine education and training for all the other major existing occupations, plus some (such as designer) that are not yet well represented in the sector, but will be important to its future.

Finally, enhancing management skills in training institutions is clearly important, given the existing deficiencies in the quality of the system, and given the wider range of activities that will be required into the future.

Sorted by the different types of occupation, the following actions on training and education are required:

Machinists
<ul style="list-style-type: none"> • Reform of institution-based TVET courses; • Provision of good entry level training for new recruits entering the sector directly (which could possibly extend to the introduction of a low level apprenticeship mechanism); • Continuing TVET to broaden and update skills.
Skilled craft and technician level occupations
<ul style="list-style-type: none"> • Reform of institution-based TVET courses, and new courses for occupations that are not yet covered by institutions; • Possible introduction or formalization of apprenticeship systems; • Continuing TVET to improve and broaden skills, and perhaps give those working in these occupations who enter by a non-TVET route a credible qualification.
Professional level occupations
<ul style="list-style-type: none"> • Introduction of university level courses (bachelor and masters at least) in these areas to qualify new entrants. The establishment of a university level centre of excellence in apparel and textile technologies, design and business, probably at a single university, but possibly spread across a couple of places if existing distribution of expertise demanded could be beneficial. • Arrangements for continuing learning to raise the skills of people already in these roles are also needed.
Operations managers
<ul style="list-style-type: none"> • As people are likely to move into operation management roles from other jobs, rather than directly from initial education, the emphasis needs to be on measures fostering continuing learning (see above).
General managers and entrepreneurs
<ul style="list-style-type: none"> • There is a need for a range of techniques to be used to raise skills and professionalize senior managers. Other types of intervention include executive education courses in apparel industry management, mentoring, networking events, foreign study visits, etc.

Source: STED Kyrgyzstan survey (2011)

7.2.3. Other priority areas

- Revitalizing Shvei-Profi: Given the sector's substantial training needs, revitalizing the Shvei-Profi training centre is an urgent priority. Management consulting and training to the centre's leadership could support the development of a business model that is financially sustainable, and at the same time attractive to companies in the sector in terms of costs and services offered. In addition, the function of the centre as an innovation hub for the sector should be extended. Creation of learning networks for professionals in relevant technical, professional, and managerial positions could be envisaged. Having a service oriented provider of high quality professional training available will remain of utmost importance to enterprises in the sector even if progress is made with enhancing the education provided by technical lyceums.
- An effective mechanism for quality assessment linked to curriculum development is crucially important. The absence of feedback on quality and curriculum between industry and the education and training system appears to be the biggest problem in the system – even greater than under-resourcing. A concrete suggestion by survey participants was to increase the number of hours dedicated to practical classes.

- Lifelong learning is crucially important for skills in the apparel sector. If an education system is not already involved deeply in supporting lifelong learning with part time provision, short courses etc., moving into this can be challenging. Key obstacles are the cultural shift required to become sufficiently highly responsive, and the fact that institutions that are accustomed to delivering a highly structured suite of provision that changes only slowly may have significant practical organizational difficulties in making itself sufficiently flexible.
- Equipment of specialized lyceums with modern material. New curriculum materials will be essential for changed and new courses, particularly at TVET level, which tends to be more reliant on standard materials relative to higher education where there are better prospects that academics can develop their own and draw on international sources.
- Training of teachers. Improving teacher training is crucially important, both to update the skills – in particular skills on the operation of new equipment – of those currently engaged, and to train the many new teachers/trainers who will be required if the system is to be properly resourced, and as the existing aging teaching workforce retires.
- A more effective national employment service could also play a very useful role in providing career counselling, providing information on labour market needs, and supporting re-training of currently unemployed workers for occupations demanded by the garment sector.
- A program to up-skill workers already in the sector, particularly in terms of converting low skilled sewing machinists to universal machinists, could be considered. The practicalities of this would have to be worked out, and tested through pilots. With the support of a donor, industry associations, the Svey-Profi centre and one of the more advanced lyceums could work together to develop a pilot that could later be expanded. The expansion could make use of the lyceum infrastructure and provide extra impetus to improve initial TVET provision from the lyceums, or could possibly be firm based with a system to develop in-house trainers with external quality assurance on the training and assessment.

7.3. Enterprise Level

Firms themselves have an important role to play in the process of skills upgrading and improvement. A key challenge, mentioned prominently by all key informants, is to reduce labour turnover. A more sustainable culture of employment, based on a long-term relationship between worker and employer, gives both an incentive to invest time and resources into training and skills development.

Central elements of a strategy to reduce labour turnover are improvements in working conditions and career prospects for workers at the enterprise. Social dialogue and better cooperation between workers and management can have very positive effects in this regard. This would also help to reduce the outflow of skilled workers to neighbouring countries.

The ILO has developed enterprise level tools to promote improvements in the above mentioned areas. Experience has shown that this creates a win-win situation for employers and workers, because such improvements can enhance working conditions while at the same time significantly increasing productivity.

In the case of the Kyrgyz garment sector, the use of the ILO's SCORE (Sustaining Competitive and Responsible Enterprises)³⁰ methodology could yield substantial benefits. SCORE is an SME training program that is designed to strengthen collaboration and communication between managers and workers in order to improve working conditions, boost quality and productivity, and thus make enterprises more competitive. SCORE works through training of local consultants. Participating enterprises select two workers and two managers to take part in classroom training and, with the support of the consultant, set up and implement an action plan to implement improvements in their firm. SCORE takes a modular approach and can cover the following areas of enterprise operation:

- Module 1: Workplace Cooperation
- Module 2: Quality Management
- Module 3: Productivity and Cleaner Production
- Module 4: Human Resource Management
- Module 5: Safety and Health at Work

There is already substantial engagement by the International Trade Center (ITC) and the European Bank for Reconstruction and Development (EBRD) in providing consulting services to firms in the sector in areas related to module 2 and 3. Integration of SCORE modules 1, 4 and 5 in these areas could add substantial value to the sector by contributing to lower labour turnover, and thus strengthening labour productivity and prospects for skills development in the sector.

³⁰ www.ilo.org/score

Abbreviations

AVE	Ad Valorem Equivalent
CDS	Country Development Strategy
CET	Common External Tariff
CIS	Commonwealth of Independent States
EESE	Enabling Environment for Sustainable Enterprises
EurAsEC	Eurasian Economic Community
EBRD	European Bank for Reconstruction and Development
GDP	Gross Domestic Product
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit (German International Cooperation Agency), formerly GTZ
ILO	International Labour Organization
ITC	International Trade Center
JICA	Japan International Cooperation Agency
KfW	Kreditanstalt für Wiederaufbau (German Bank for Reconstruction)
KGS	Kyrgyz Som
KR	Kyrgyz Republic
MER	Ministry of Economic Regulation of the Kyrgyz Republic
NBKR	National Bank of the Kyrgyz Republic
SCORE	Sustaining Competitive and Responsible Enterprises
SME	Small and Medium-Sized Enterprises
STED	Skills for Trade and Economic Diversification
TVET	Technical and Vocational Education and Training
UNDP	United Nations Development Programme
USAID	United States Agency for International Development
VAT	Value Added Tax
WTO	World Trade Organization

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