

Factors behind the Success of International Competitiveness of Apparel Industry in Sri Lanka with Special Reference to Vertical Integration Strategy

Dilshan Rathnayake#, Hashini Malsha, Chathuri Dissanayake and Lahiru Gunathilaka

Department of Management and Finance, General Sir John Kotelawala Defence University

dilshanrathnayke@gmail.com

Abstract: Textile and apparel industry occupies a prominent position in the Sri Lankan economy as the main export income earner. However, the imported raw materials for apparel industry is recorded as the second largest import of the country, while most of the apparel manufactures do contract manufacturing for world renowned brands. Accordingly, it is a challenge for the apparel producers in Sri Lanka to increase total value addition in both downstream and upstream. With this background, the study aims to identify factors behind the international competitiveness of Sri Lankan apparel industry associated with the vertical integration strategy. The secondary data were initially gathered from reliable sources, and the primary data were collected using semi-structured in-depth interviews with the industry experts. The gathered data were transcribed and then analysed using the thematic analysis. As per the findings, the two main apparel producers have successfully implemented the vertical integration strategy while other companies do not focus on such strategy. When analysing the findings, it is revealed that the sub codes, codes and themes that were found through data analysis are quite relevant to the famous theory of "Michael porter's diamond model". As such researchers were able to theorize the Porter's Diamond Theory as the complement to achieve a successful vertical integration strategy.

Keywords: Apparel industry, Vertical integration, International competitiveness

Introduction

A. Background of the study

1) *Apparel industry in Sri Lanka:* The apparel and textile industry in Sri Lanka is one of the largest contribute to the economy and the major foreign exchange earner (export.gov, 2019). Sri Lanka has traditionally been agricultural based economy but with the time government of Sri Lanka interpret the need to have an industrialization strategy for development of the economy of Sri Lanka (Embuldeniya, 2015).

According to Central bank of Sri Lanka in (2014) the improved performance of all categories of Factory Industry contributed to the overall growth, specially export market oriented industries such as textile, wearing apparel and leather products category (wanaguru, jegajeevan, & samarathunga, 2012). Among the sub sectors, Apparel sub sector is the one of leading export oriented industry and that contribute continued Sri Lanka's growth. Individual growth of wearing apparel sub sector recorded a 19.7 percent in 2014 (Embuldeniya, 2015).

Apparel sector of Sri Lanka has been recognized for its excellence in speedy delivery and reliability. The maintaining quality and reliability to meet with global brands such as, Victoria's secret, Nike, triumph, speedo. (Gunathilake & De Mel, 2016). Moreover, good industrial practices

(free of forced labour, free of child labour, eco-friendly international standards), and environmental conservation has made for apparel industry. Confirming to Export, earnings from exports of textile and apparel is accounted for 43 percent of total exports earnings of the country (Sri Lanka export development board, 2015).

Considering the country classification of Apparel Exports, there is a high demand for Sri Lankan apparels to export in European countries including United Kingdom, Italy, Germany, Belgium, Australia, Netherlands, etc. Also similar demand in United States America as well as Canada, China, Hong Kong, Japan and United Arab Emirates are also the buyers of Sri Lankan apparels overseas who bring export earnings to the country (Central Bank of Sri Lanka, 2014). Sri Lankan apparel industry can catch the global market but that is not enough prove for Sri Lankan apparel industry is can sustain for long time. The reason is price, quality and on time delivery are only be entry qualifications to enter the global market. Today, with the globalization, consumers ask more value for less money. Therefore, Sri Lankan apparel industry should increase its competitive advantage in order to be sustainable in the global apparel market. Further the integration of apparel sector within the country is at a lower level. This would cause adverse impact on competitive of the industry as well as economic implication due to less value addition.

Textile manufacturing reported growth of 3.6 percent in 2018, compared with growth of 2.3 percent in the previous year. Together, the wearing apparel and textile subsectors contributed approximately 78 percent of the overall growth in the manufacturing sector in 2018. Despite the local clothing and textile industries have the potential for further growth, the lack of economies of scale, infrastructure limitations and high input costs adversely

affect the industry's competitive power. In addition, the advent of relatively new textile production hubs in the area has continually challenged the role of Sri Lanka in a competitive global market. Even though the GSP+ system has been restored to demand in the recent past has required constructive action by the clothing industry to minimize continued dependence on such schemes, enabling increased resilience to external vulnerabilities.

Sri Lankan exports are could be copied by other competitive export countries easily because of the most of the products are simple. Value of high-tech exports in Sri Lanka have hit a low level from US \$102 million in 2008 to US \$ 57million in 2010. Sri Lankan apparel industry contributes in High-tech exports averages at 1.8 percent comparing to 75 percent in Korea, 27 percent in Thailand and 50 percent in Singapore and Malaysia (Dilanthi, 2015). In the other hand lack of solid raw material base is also a huge challenge to the industry. In Sri Lankan apparel industry, it has been identifying as a major issue and it has affected the competitiveness of local garment exports and as comparison with the other competitors in Asia. 70 percent of total raw fabrics used in the industry and 70 percent - 90 percent accessories used in production are accounted as imported to the Sri Lanka (Dheerasinghe, 2016). Country is in difficult situation because regard to this dependence in importing raw materials which simultaneously increases the production cost and the cost of final output. These areas can identify as main challenges to the apparel industry in Sri Lanka.

The purpose of this study is to explore the factors behind the success of international competitiveness in global apparel market using vertical integration strategy and find how to overcome the challenges in apparel industry.

2) *Vertical integration:* With the globalization there have been a drastic change in some sectors in the economy. That change could have led market to customized market requirements (Gunathilake & De Mel, 2016). In that scenario manufacturers believed supply chain management can raise customer value and achieve an enduring competitive advantage. Development of the integrated supply chain is the most considerable contribution to the delivery of goods and services in the past decade (Gunathilake & De Mel, 2016). The Organization which has adopted the vertical integration strategy can gain control over supplier, increased competitiveness, increased market share, decreased cost and secure suppliers. Vertical integration is when a company controls more than one stage of the supply chain. Vertical integration ensure control over the supply of the raw materials to manufacture its product as well as empowered it in market place. In vertically integrated organizations, Activities which were formerly being outsourced would tend to be brought under a one roof. This means that the organizations now has to undertake the responsibility of performing all its upward and downward processes in equally efficient a manner as it was being formerly done, as the long term perspective is on information accuracy, cost saving, and organizational control (Scudder & Byramjee, 2012). Vertical integration can be carried out in two ways such as backward integration and forward integration. Where as backward integration, is a business model where by a company takes direct control how its products are supplied (Sharma, Khatri, & Mathur, 2014).

Forward integration, is a model where a company takes direly control of how product are distributed (Bawaba, 2014). Accordingly, forward integration may involve the company acquiring the retailer

Literature Review

Sri Lanka's economic growth has been among the fastest in south Asia in recent years. Apparel sub sector is one of the leading export oriented industry in Sri Lanka. It gives dynamic contribute to the economy. According to world context Sri Lankan apparel industry is at a reputed place (Embuldeniya, 2015). Today, with the globalization, consumer ask more value for less money. Therefore, Sri Lankan apparel industry should increase its competitive advantage in order to be sustainable in the global apparel market. The integration of apparel sector within the country is at a lower level. This would cause adverse impact on competitive of the industry as well as economic implication due to less value addition (Mataaraarachchi & Heenkenda, 2012).

A. Backward Integration

Examining the Sri Lankan context, due to the higher capital requirement and lack of local raw material base having local textile miles to meet total requirements needed for apparel industry. However, it is a difficult task even with less backward linkages, the apparel industry in Sri Lankan has contribute significantly. According to these reasons expanding possibilities raw material base is very important. With the expansion of raw material base apparel manufactures can reduce the lead time in raw material procurement and also shipping cost (Fernando, 2002). This certain strategy of backward vertical integration is using for achieving two major objectives, mainly increasing the control of the business and to gain cost related advantages. Through the process of integrating backward, companies control their value chain in a more efficient manner (Gunathilake & De Mel, 2016).

B. Forward Integration

When firms applies forward integration it can gain control operational reach to

product retailing, tightening its grip on the demand side (Parlakt & Swaminathan, 2012). According to the industry survey the evident that most of the Sri Lankan apparel manufactures are not in a position having their own design and development units as well as market unit (Embuldeniya, 2015)

C. Porters Diamond Theory

While we collecting data and once we analyze the data we can found that, these data can be conveniently group under porter's diamond theory, accordingly we identified porter's diamond theory as our theoretical framework.

a) Factor Condition.

1) *Human Resource:* Traditionally low labor cost which is main advantage for Sri Lanka, but that factor no longer being deciding factor achieving competitive advantage. Now cost advantage moving to countries like Vietnam and Bangladesh (Mataraarachchi & Heenkenda, 2012).

2) *Material:* Under material factor raw material base is a major weakness for Sri Lankan apparel and textile industry. Since larger amount of raw materials are imported which wants to apparel industry (Mataraarachchi & Heenkenda, 2012).

3) *Knowledge:* Knowledge in design and product development technical knowledge and market knowledge, which are the important in apparel manufacturing industry (Mataraarachchi & Heenkenda, 2012).

4) *Capital:* Sri Lanka provide positive capital facilities towards foreign investments (Mataraarachchi & Heenkenda, 2012).

5) *Infrastructure:* The cost of infrastructures like electricity and water which mostly wanted to apparel industry remains higher in Sri Lanka (Mataraarachchi & Heenkenda, 2012).

b) Demand Condition.

Demand condition is based on buyer's requirements about price, quality and service in an industry. Demand condition effect on the product development and direction of innovation of product.

Examining the local apparel industry demand conditions are not up to the standard to competing in apparel industry. Compared to USA and EU, Sri Lankan consumers do not have very fashion conscious / brand conscious (Mataraarachchi & Heenkenda, 2012).

c) Supportive and related industries.

According to porter there are no single successful industry without strong supportive and related industry. When considering international competitiveness rivalry is very important. Reason for that, when there is a strong challenging competitors, firms compete energetically and develop innovative creations (Bakan & Dogon, 2012).

d) Strategy, Structure and Rivalry.

Companies ' strategy, structure, and rivalry are circumstances that describe how a sector is formed, systematized, and controlled, and the essence of domestic competition that could help a nation attain a sustained competitive advantage.

Rivalry is very relevant in global competition when successful firms compete aggressively at home and constrain each other to grow and innovate (Bakan & Dogon, 2012)

Methodology

With the aim of understanding the situation in sri lankan apperal industry the researchers used realism research philosophy to understand the nature of study by its reality. The researchers have used deductive research approach and adopted a qualitative embedded secondary data review at initial stage and later carried out several interviews with the Industry

Experts (Supply Chain Managers, Operations Managers, merchandise manager, human resource manager) through in-depth semi-structured interviews using open ended questionnaires in order to gather primary data. Under deductive approach, Thematic analyses was used to analyses qualitative data. Secondary data have been gathered from related research articles, publications and internet search and it was necessary to verify the accuracy of the primary data specially provided by interviewee of different apparel manufacturers.

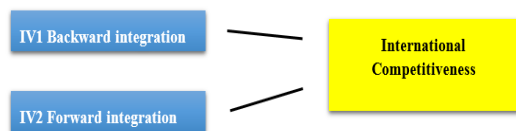


Figure 3.1 conceptual framework
Source: Developed by researches.

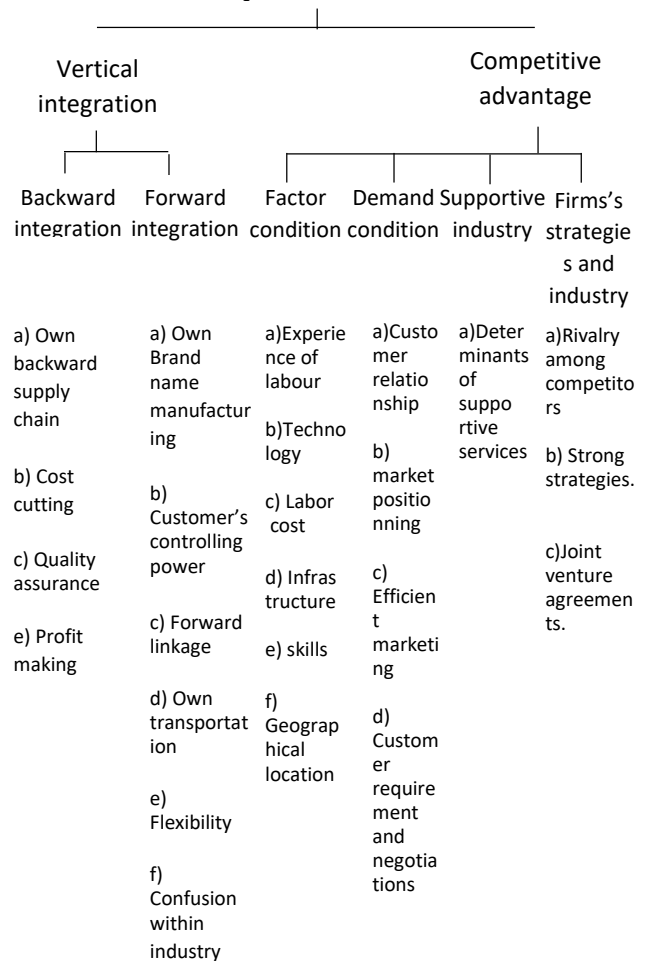
According to the conceptual framework researchers measured the integration impacts mostly towards international competitiveness. These Propositions were identified as below

- i. Companies applied backward vertical integration to create international competitiveness.
- ii. Companies applied forward vertical integration to create intentional competitiveness.

The possible methodological limitations can be identified regarding the sample population; the selected sample size as it was limited only to an industry among large scale apparel industry in Sri Lanka.

Findings

International Competitiveness



1. Own backward supply chain

With regards to respondent 1, by maintaining an own backward supply chain process, they can improve the efficiency and cost savings rather than acquiring or merging with other outside companies

2. Cost cutting

As the respondent acknowledge that they make their own price quotas and cost reductions and get more price advantages by their own fabric supplies, rather than getting supplies by outer supplies

3. Quality assurance

The respondent insists that before take decisions to be fully integrated particular company needs go through a brief cost benefit analysis with equally concern about the qualitative side of the products.

4. *Profit making*

The respondent also acknowledges that the make profits in their apparel sector provide the raw materials them and meantime selling to other companies.

5. *Own Brand name manufacturing*

By making company's own brand name it helps to achieve the home market first. After enter to the market company can increase own brands by efficient promotion and then can have access to the international market as well.

6. *Customer's controlling power*

As per the information it has found that Most of the customers are nominated their raw materials suppliers, therefore sometimes companies cannot integrate in downstream as per it is effortless if they produce their own raw materials because even if they made their own they unable to use for production

7. *Forward linkage*

One of interviewee mention that they have their own medium for distribution process. When company able to take control of distribution channels to offer products directly to consumers it helps to eliminate the middleman cost and able to save cost

8. *Own transportation*

Respondent 2 has mention that they have their own transportation service for their employees. Through this might able to cost savings. Otherwise they may incur additional transporting cost for external transporting channels.

9. *Flexibility*

Respondent 2 has mention that they have their own transportation service for their employees. Through this might able to cost savings. Otherwise they may incur additional transporting cost for external transporting channels.

10. *Confusion within industry*

There must be wiser knowledge to conduct and good managers' needs to take strategic decisions. according to interviewee to conduct vertical integration strategy there must be good evaluating process at all.

11. *Experience of labour*

According to respondent 1, Firms having long time running in the industry have experienced labor. Through that they can achieve working efficiency and competitive advantage too.

12. *Technology*

As per the interviewee apparel industry cannot fully automated due to some functions like designing garments. According to respondent 1 they believed that company has enough technology by compared to other players within the industry

13. *Labor cost*

in the view of respondent 2.all apparel manufacturer's major objective is produce lower price product with high quality.to satisfy that objective it is easy if labor cost can minimize further such as taking actions to prevent labor turnover.

14. *Infrastructure*

Infrastructure is a main factor which is indirectly affect for the supply chain process. The apparel industry has been influenced by industrialization and globalization.it is need for investments in infrastructure development and process standards.

15. *skills*

The technical skills and soft skills are lesser than other countries according to respondent 2. However, labor productivity in apparel sector is improved slowly. Good working conditions and job training centers has been established in their companies in order to that

16. Geographical location

According to respondent it is stated that international customers intended to choose their supplier as Sri Lanka because of the location benefits.

17. Customer relationship

As respondent 1 said, to go for international competitiveness there must be long time customer relationship. By having long term relationship it leads for a strong bond. As long as customer associate supplier for a longer period they may not be shift or change to another supplier at any circumstances. To ensure strong customer relationship it is important for having service agreements like joint ventures.

18. Market positioning

Market according to respondent 2 opinions, to go for that there must be home market as first. Because international customers assign their orders by reviewing home market position

19. Efficient marketing

Reference to respondent 3 it is mentioned that that company own brand market failure because of lack of promotion

According to respondent 2 it is found that verbal marketing is the most powerful marketing as an example when international customer looks for garment manufacturer supplier customer looks for their website reviews as first.

20. Customer requirement and negotiations

Always customer looks in to lowest price from multiple choices. One of customer requirement is they nominate their raw material supplier. Also that is one of barrier to go for vertical integration strategy according to respondent 2.

21. Determinants of supportive services

When supply chain process expanding with vertical integration Strategy Company

needs supportive services like financial institutions.

22. Rivalry among competitors

According to respondent 2 rivalry among competitors affects for the success of the vertical integration because when there is a competition one company tries their best than other one, therefore final outcome is all are performing quality product to rise up in the competition

23. Strong strategies.

It is found that one of strong strategy followed by the company is there are considerable material stock is remaining when company is going to full fill the minimum order quantity because there are more excessive materials

24. Joint venture agreements

Joint ventures are the One of most successful agreements to collaborate with customer and to maintain the favorable relationship at all according to respondent 2 point of view. In this occasion both customer and supplier experience the benefits through industry

Discussion

In this chapter concentrated on discussing the factors behind the international competitiveness of apparel industry in Sri Lanka with special reference to vertical integration strategy. By using this successful strategy company can achieve international competitiveness. In the production stage developing Asian countries cannot make adequate profits because of low value addition to overcome this problem some of the firms are vertically integrated. The main objective is to go for vertical integration is to gain competitive advantage from this study it has been identified the factors behind successful vertical integration strategy in

this research those factors is discussed through the identified propositions.

A. Proposition 1

Companies applied backward vertical integration strategy to create international competitiveness.

B. Proposition 2

Companies applied forward vertical integration to create international competitiveness.

Conclusion

Since apparel industry has become prominent industry in worldwide, Sri Lanka needs to pay more attention for strategies using to perform value added product in order to achieve international competitiveness. Therefore, Sri Lanka needs to follow specific strategies like “vertical integration”.in order to get the advantage of vertical integration there are some factors behind the success of that vertical integration. However, the functions of vertical integration are massive, it is necessary to invest high technology and automatically vertical integration becomes capital intensive. Even though it is capital intensive it is able to get more benefits. Most companies that larger in size currently understand the price offering to the customers can be controlled better by vertical integration than being traditional manufacturer in the industry. When considering the price points, the apparel manufacturer should provide the product under lowest price with high quality as per the findings it is stated that obviously manufacturer can produce profit margins and make the price advantages of it. With the development of the industry import dependency for raw materials could be reduced through backward vertical integration where fabrics are produced domestically. Accordingly, industry as a whole it is important to having joint

ventures as the most sufficient strategy to minimize risk and maximize profits.

According to the findings it has identified there are various factors affect for the vertical integration in apparel industry. Most of factors are directly influence the success of vertical integration too. Companies following vertical integration strategy can achieve more advantages as well as some disadvantages due to lack of factors presence within the country. Some factors need to be developed more to achieve international competitiveness and existence of the industry such as efficient infrastructure including communication, transportation and technology.

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Abbreviations

GDP - Gross Domestic Product

HR - Human Resource

VI - Vertical Integration

Author Biographies



Lahiru Gunathilake
Senior Lecturer-Grade II
Department of
Management and Finance
Faculty of Management,
Social Sciences and
Humanities. General Sir John Kotelawala
Defence University.



Dilshan Rathnayake
Undergraduate.
Department of
Management and
Finance. Faculty of
Management, Social
Sciences and Humanities. General Sir John
Kotelawala Defence University



Chathuri Dissanayake
Undergraduate
Department of
Management and
Finance. Faculty of
Management, Social
Sciences and Humanities. General Sir John
Kotelawala Defence University



Hashini Malsha
Undergraduate
Department of
Management and
Finance. Faculty of
Management, Social
Sciences and Humanities. General Sir John
Kotelawala Defence University