The Competitive Position of the Tourism Cluster in Palestine

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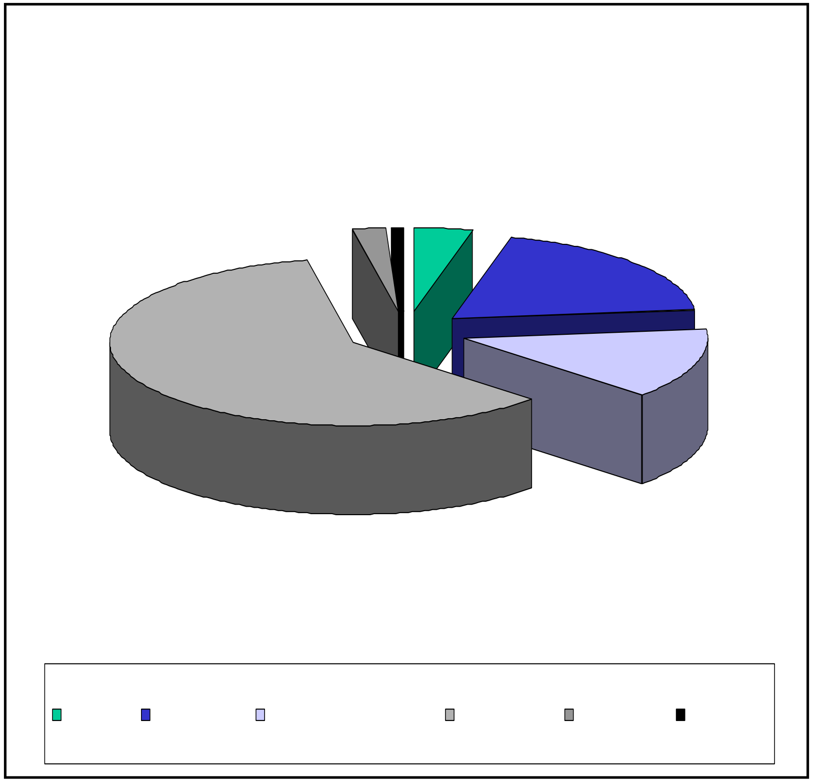
International Tourist Arrivals

(millions in 1998)

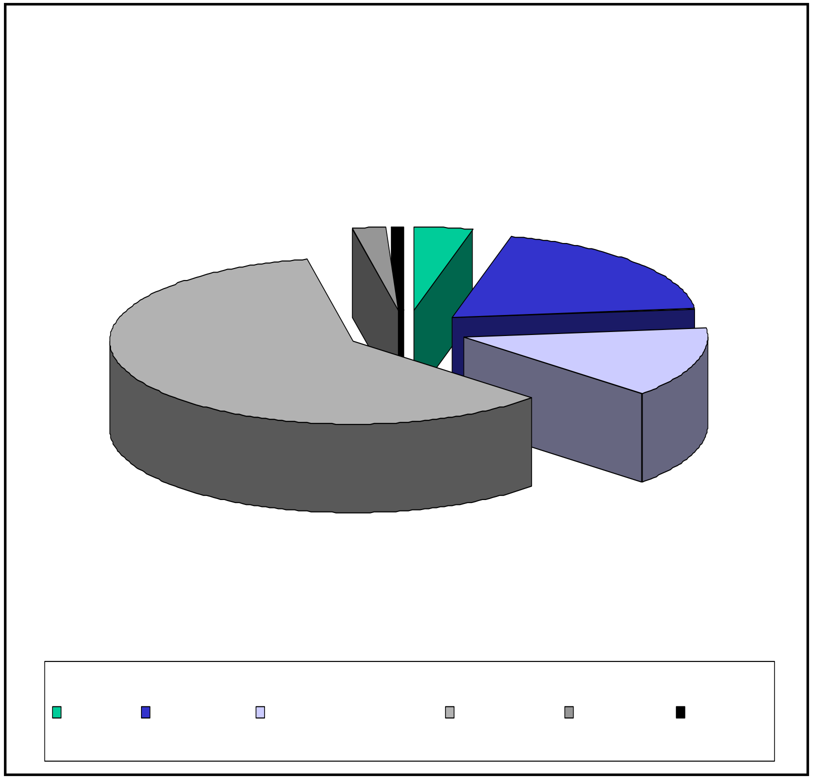
- International Arrivals have reached 535 million people in 1998.
- International Arrivals are expected to reached 700 million people in year 2000 and one billion people in 2010.
- Tourist arrivals in the Middle East reached 15 million people in 1998. Growth rate of tourist arrivals over the past decade was 6.9%.



International Tourist Receipts

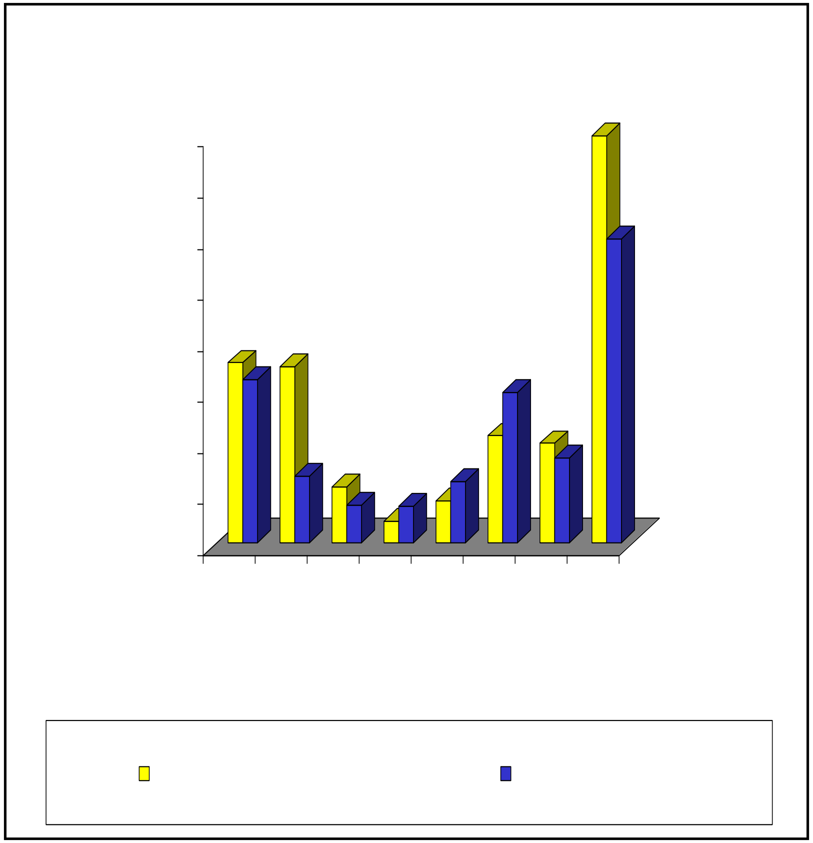
(U.S.$ billion in 1998)

- Receipts from international tourism reached $439 billion in 1998. (Exceeded $500 billion if transportation is included)
- Receipts from international tourism are expected to reached $621 billion in year 2000 and $1,550 billion in 2010.
- Receipts from tourist in the Middle East reached $8 billion in 1998. Tourism receipts have increased by 6.4% in 1998.



Tourist Arrivals and Receipts in Selected Countries in the Middle East (1996)

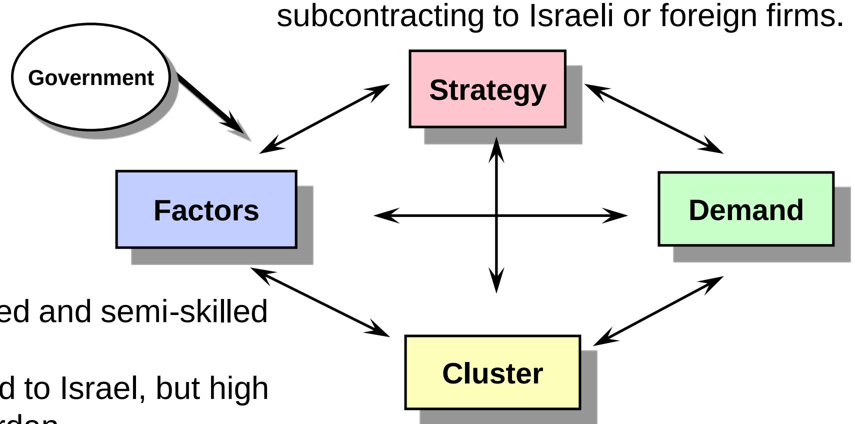
- There has been steady growth in tourist arrivals and receipts in the Middle East during the last decade.
- Turkey and Egypt are among top tourism centers in the region.
- According to WTO, the number of tourists is expected to reach 21 million people in 2010.



Competitive Environment: The Palestinian Textile and Wearing Apparel Cluster

Government
- Unstable political situation
- Limited scope for PNA
- Many governmental institutions are still not effectively operational
- Lack of intellectual property rights and antitrust regulation

Strategy, Structure and Rivalry
-/+ Industry is dominated by a large number of small, family owned and family run, firms
- Rivalry is weak and usually focuses on prices.
- Due to political and economic uncertainty, most firms pursue short-term goals and do not make enough long term investments.
+ Strategies of most firms are based on cheap labor. Many of these firms engage in subcontracting to Israeli or foreign firms.



Demand
- Local demand is, generally, not sophisticated.
+ Foreign buyers (mainly holesalers and large retailers) are demanding and highly sophisticated.

Basic Factors
+ Adequate supply of unskilled and semi-skilled labor.
+/- Wages are low compared to Israel, but high compared to Egypt and Jordan.
- High transportation and utility costs
- No airport or seaport.
- Frequent breakdown of electricity.

Specialized Factors
- Inadequate infrastructure.
- Lack of training centers and R&D institutions
- Low to moderate productivity of labor.
- Heavy reliance on Israel

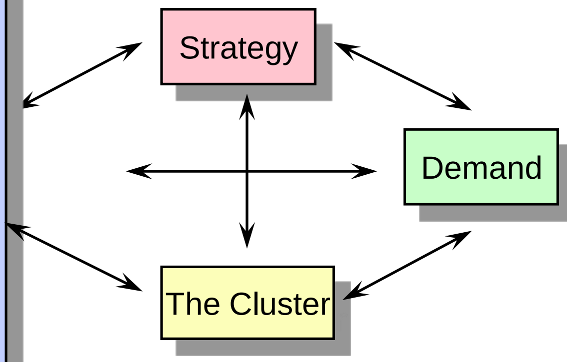
Cluster
- Weak cluster with few competitive supporting and related industries.
- Most inputs are imported.

The Palestinian textile and wearing apparel cluster is incapable of supporting strong industry. Part of this situation is due to historical reasons that are related to Israeli occupation and many other parts are due to the strategies pursued by textile and wearing apparel manufacturers.

Factor Conditions

- A large proportion of the labor force in the industry is owners and family members.
- Labor, in general, is unskilled or semiskilled, with preparatory or secondary education. Most of their experience has been gained from working in Israeli factories.
- productivity is low to moderate, due to lack of formal training and inadequate capital. Productivity is also low because of frequent closure of the Palestinian territories.
- Wages are low compared to Israel, but high compared to Egypt and Jordan.
- Most machinery are imported from Japan through Israel. Maintenance is done by Israeli firms or local technicians.
- Wearing apparel industry is labor intensive (one of the lowest Capital/Labor ratios in the industrial sector).
- Raw materials (Fabrics, etc..) are bought from Israel or imported through Israeli firms from Turkey and East Asia.
- Infrastructure is inadequate and does not enable local firms to compete in open markets.

Heavy reliance on Israel



Factor Conditions

Labor

- Around 25% of workers in wearing apparel industry and 40% of the workers in the textile industry are owners and family members. Around 37% of the workforce in textile and wearing apparel industries are female, many of them are home workers (paid per piece).

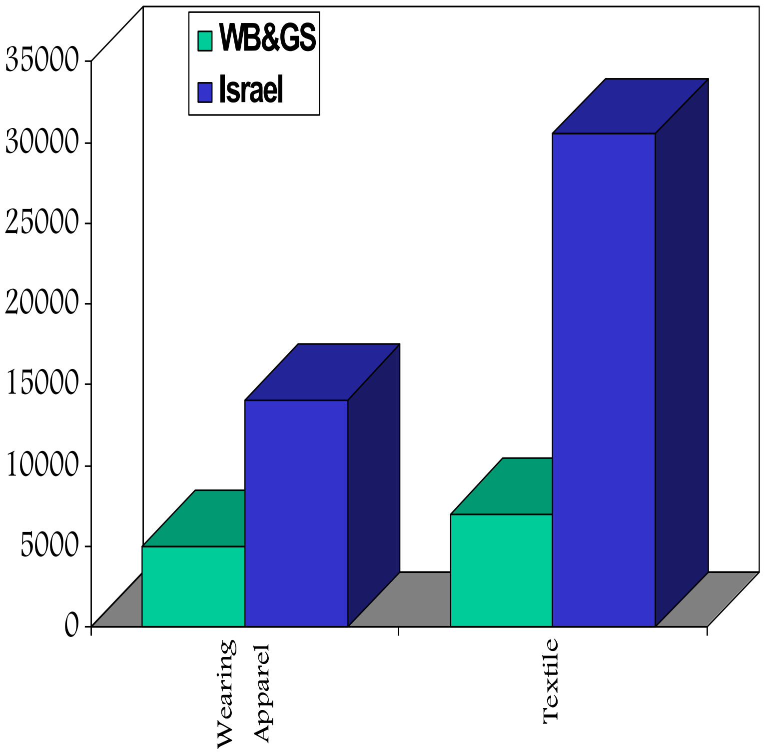
  Source: PCBS, Press Conference on the Economic Surveys Series, 1994 Results.

- Workers are fairly-well educated, but lack formal training. Many workers develop their own experience and skills during their work in Israeli firms or in local factories.

No investment in human resources to meet industry needs.

Factor Conditions
Labor Productivity

- Productivity of labor (measured by the value added per worker) is low to moderate.
- In the wearing apparel industry, productivity in WB&GS is almost one third of that in Israel, while in the textile industry productivity in WB&GS is less than one fourth of that in Israel.

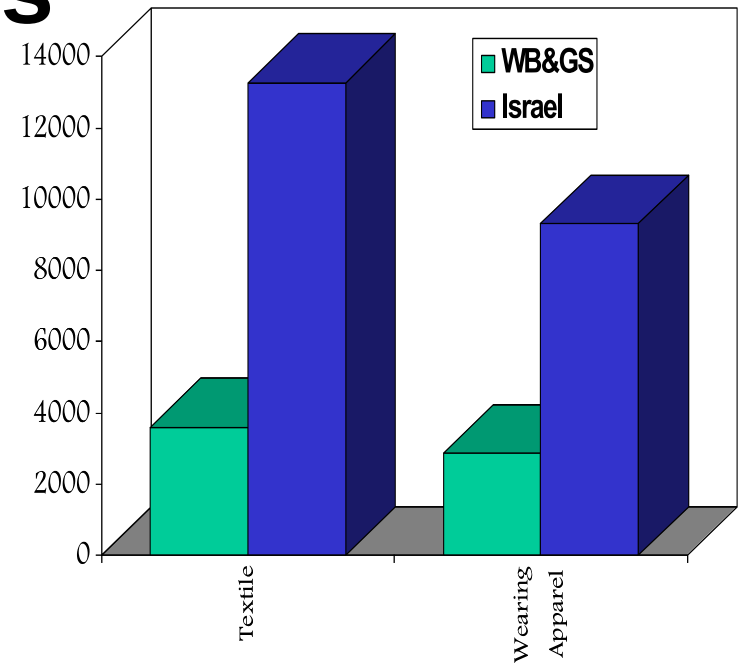


Sources: PCBS, Unpublished Data;
CBS, Statistical Abstract of Israel.

Factor Conditions

Wages

- Productivity is higher in Israel because of better technology, better machines, and better training of workers.
- Higher productivity in Israel results in higher wages. Wages in the textile and wearing apparel industries in Israel is three to four times those in Palestine.



Sources: The Industrial Survey - 1994: Main Results, Report No. 1; CBS, Statistical Abstract of Israel

Wages are low in Palestine because productivity is low

Factor Conditions
Machines

- Machines are mainly imported from Japan, but some machines are imported from Italy, Germany and Taiwan.
- Most machines are bought new from local market or from Israel. Some second-hand machines are sometimes bought from Israeli firms
- Most of the sewing machines are electrical. Some machines are computerized. Few machines are manual.
- Most of the maintenance services are made by local technicians. In case of serious problems, the machine is sent to Israel for repair and maintenance.

Factor Conditions
Machines (continued)

- Capital / Labor ratio is $7672 per worker in the textile industry, and $1773 per worker in the wearing apparel industry.

Source: PCBS, The industrial Survey - 1994, Main Results, Report No. 1

Wearing apparel industry is labor intensive (one of the lowest Capital/Labor ratios in the industrial sector)

Factor Conditions

Raw materials

- Fabrics are mostly imported from Turkey and South East Asia through Israel, or purchased from Israeli textile sources such as Polgat (usually during end of season sales).
- Accessories are bought from local wholesalers or from Israel.
- Nylon and cartons used in packaging is also bought from local and Israeli manufacturers.

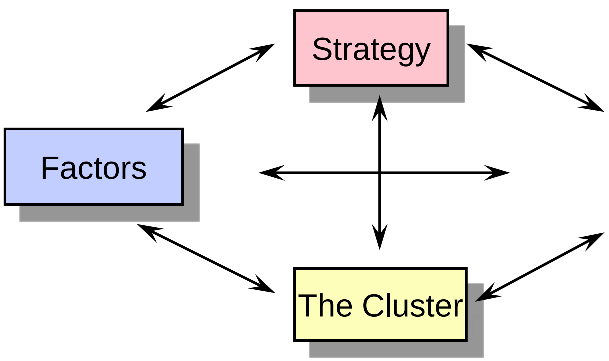
Factor Conditions

Infrastructure

- Many factories are located in residential areas, and therefore face many problems, especially breakdown of electricity and water.
- Breakdown of electricity occurs frequently in some areas, especially in Gaza, which causes the factory to close.
- Storage facilities are expensive and lack handling equipment.
- Transportation is costly and sometimes blocked by Israeli closure of the area.

Infrastructure in its current form does not enable the private sector to compete in an open economy.

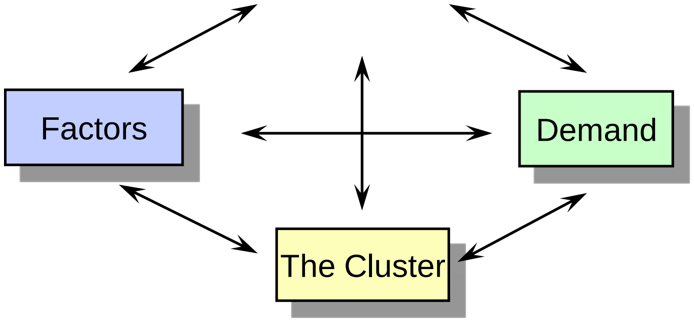
Demand Conditions



- Local demand is weak, and mostly concentrated on simple clothing and uniform by unsophisticated groups (military, hospitals, schools, etc.)
- Foreign demand is strong and sophisticated. Foreign buyers are generally wholesalers and large retailers who represent various groups of consumers in U.S.A. and Europe.
- Local demand is influenced by proximity to Israeli market, exposure to TV shows, catalogues and other media forms.
- Demand is more sophisticated by young generation (seek well-known brands) and young mothers (for children clothing).
- Unsatisfied local customers usually make shopping in Israel, Jordan or other places outside Palestine, where they find different choices.

Firm Strategy, Structure and Rivalry

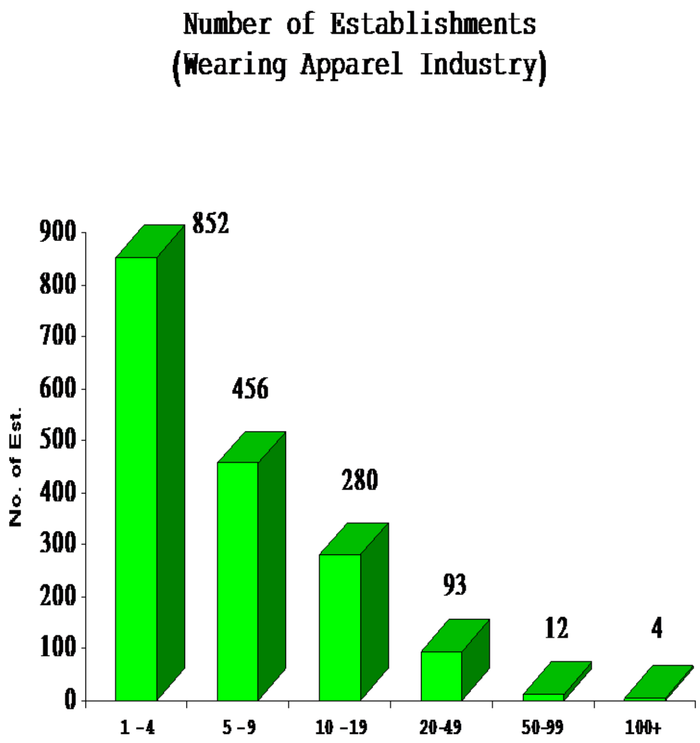
- Structures of textile and wearing apparel industries are dominated by a large number of small establishments.
- Rivalry is not intense and usually focus on price. However, competition is growing as barriers to entry are falling.
- Most firms are run by owners and family members.
- Due to political and economic uncertainty, local firms focus on short-term goals, with minimal investment in machinery and equipment capabilities, supporting technologies, R&D, or training.
- Product imitation is very common.
- Currently, most firms pursue strategies based on cheap labor and subcontracting to Israeli or foreign firms.
- Subcontracting is attractive for local firms due to lack of an access to foreign markets and technology, and the need for a less working capital.



Firm Strategy, Structure and Rivalry

Structure

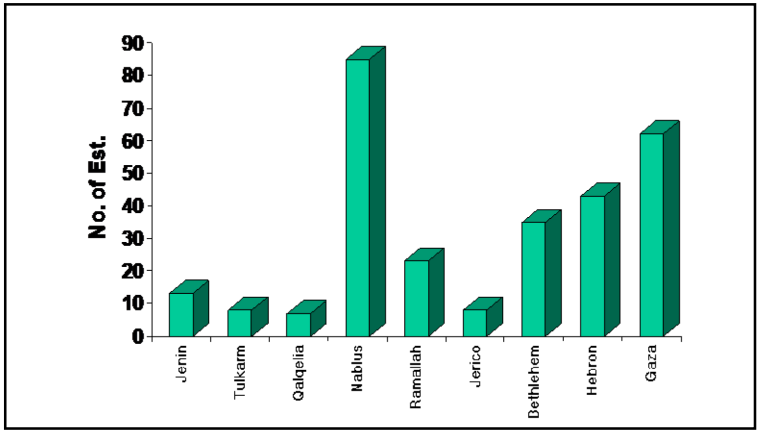
- Structure of wearing apparel industry is dominated by a large number of small establishments.
- Less than 7% of establishments employ 20 or more workers. Only 16 establishments employ 50 or more workers.
- Average size is around 8 persons per establishment in wearing apparel industry and less than 5 persons in textile industry.
- Barriers to entry are low.

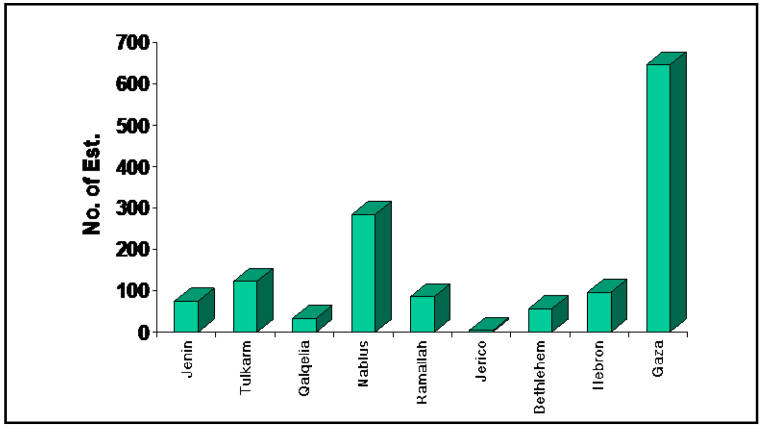


The threat of new entrants forces firms to compete on cost

Firm Strategy, Structure and Rivalry
Geographical Concentration

- Most textile establishments are concentrated in Nablus, Gaza, Hebron and Bethlehem.
- Most wearing apparel establishments are concentrated in Gaza, Nablus, and Tulkarm.





Source: PCBS, The Establishments Census, 1994, Final Report

Firm Strategy, Structure and Rivalry

Rivalry

- Despite large number of small producers, rivalry among local firms is, in general, weak. Competition is focused mainly on price. Quality of final product is generally low but may vary according to specifications.
- Palestinian manufacturers have been protected by the Israeli trade regime. This situation is changing as trade is being gradually liberalized and barriers to competition are falling.

Palestinian firms will find themselves in a position where they have to compete against foreign competitors who are lower cost, more differentiated, or have better delivery terms.

Firm Strategy, Structure and Rivalry

Strategy

- Wearing apparel production has five distinct stages: Design, cutting, sewing, finishing and marketing. **Few firms do all production stages**.
- Large firms usually subcontract with other small local workshops, especially during peak season, for one part of the process (usually sewing part).
- Most firms are run by owners who are often in charge of management, marketing, and technical aspects. Many of those owners developed technical experience from working in Israeli factories for a long time.

Firm Strategy, Structure and Rivalry
Strategy (continued)

- Many firms engage in imitation of foreign products (such as Levis jeans, etc.) as laws of property rights are weak and not enforced.
- In general, the ability of Palestinian firms to develop aggressive strategies is constrained by political and economic uncertainty. These firms usually focus on short-term goals, with minimal investment in machinery and equipment capabilities, supporting technologies, R&D, or training.

Most firms are currently pursuing strategies based on cheap labor and subcontracting to Israeli or foreign firms.

Firm Strategy, Structure and Rivalry
Subcontracting

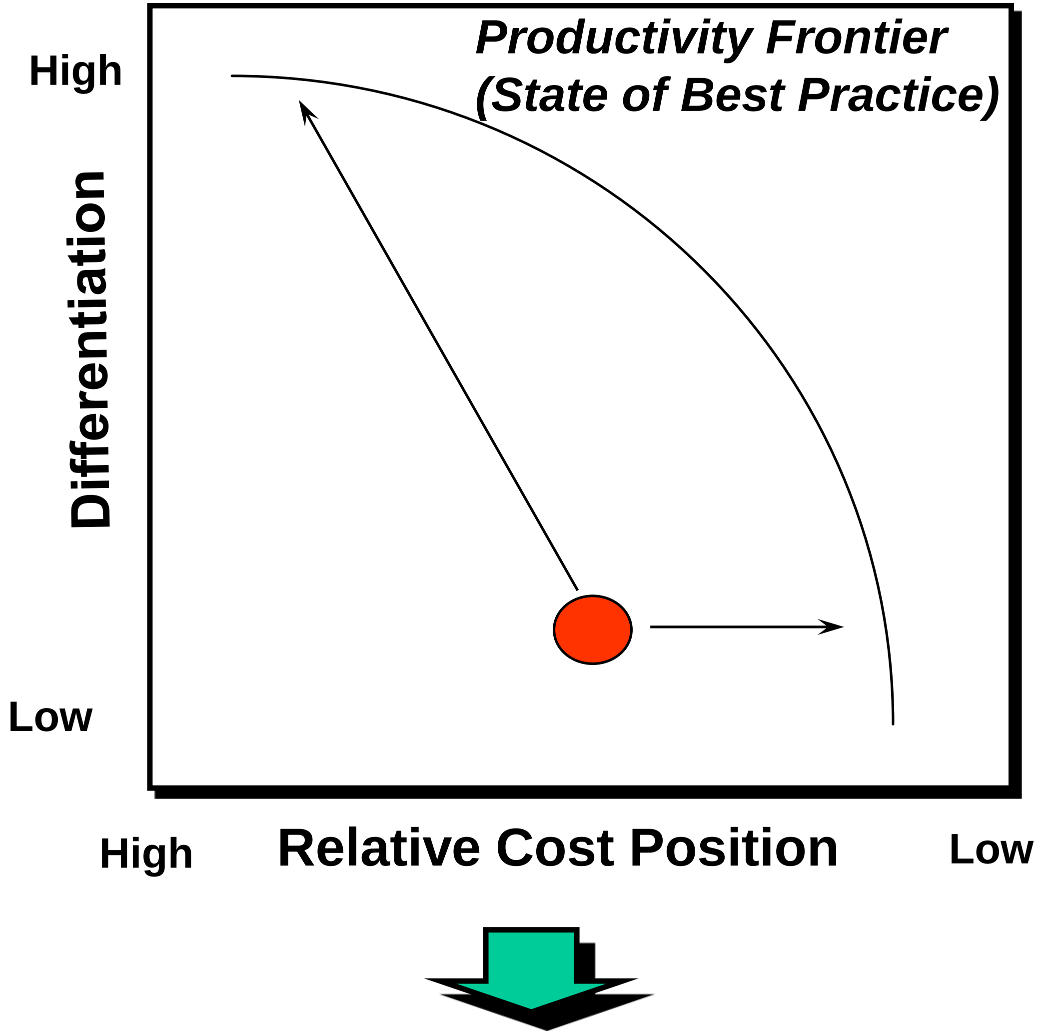
- Subcontracting to Israeli firms has been a strategy of many firms in the Palestinian wearing apparel industry. For example, subcontracting to Israeli firms represents 90% of the garments workshops in the Gaza Strip.
- The principal reasons for entering into subcontracting with Israeli firms are the lack of an access to markets and technology, and the need for a less working capital.
- Subcontracting takes one of the following forms:
  - sewing only (most common);
  - sewing and finishing; and
  - cutting, sewing and finishing

Firm Strategy, Structure and Rivalry
Strategy (continued)

- The Jordanian and Egyptian low-cost textile and wearing apparel industries will force Palestinian producers out of the low-cost markets. Subcontracting by Israeli firms will move to Jordan and Egypt.

Palestinian producers will have to move into differentiated markets where high quality standards, sophisticated designs, and high quality services are valued. Delivering greater value allows firms to charge higher prices for their products.

Operational Effectiveness and Strategic Positioning
The Palestinian Wearing Apparel Industry



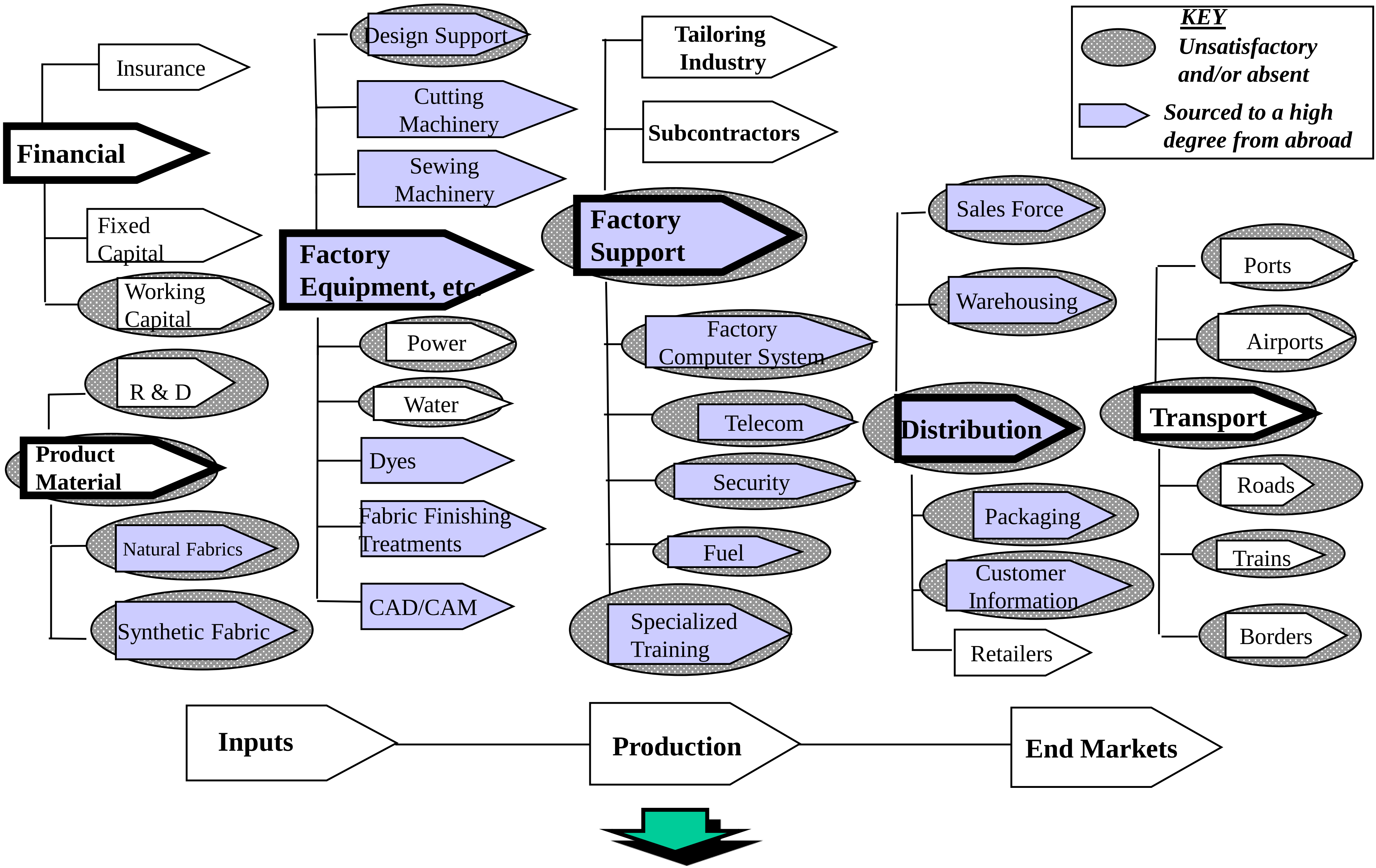
Palestinian firms can improve their operational effectiveness and move toward the productivity frontier through differentiating themselves

Supporting and Related Industries

- Weak cluster.
- Few competitive supporting and related industries.
- Most inputs are imported.
- Subcontractors never do design and marketing.
- In general there is lack of design centers, maintenance, training and marketing institutions.

Competitive Environment: The Cluster

Textile Case Study: Health of Related and Supporting Industries



Most elements of the cluster are sourced from abroad or are unsatisfactory

Problems and Issues

- The Textile and wearing apparel industry is facing strategic challenges due to the peace process and the liberalization of trade among parties in the Middle East. The industry will face growing competition as barriers to trade fall.
- Among the problems facing the industry are the poor infrastructure, lack of skilled resources, lack of institutions and regulation, and the low productivity of labor due to lack of training and capital.
- The industry, until now, focuses on low-cost, low-price products. This is not a sustainable strategy.
- Weak cluster is another problem facing the industry which limits its competitiveness.

What is Next?

- PNA and the private sector should work together to improve the competitive environment and to facilitate the creation of sustainable competitive advantage.
- To solve the issue of weak, uncompetitive cluster, foreign direct investment (FDI) should be encouraged to support merging local clusters and to bring in sophisticated technology and machinery.
- Firms should move from labor intensive to capital/knowledge intensive production.
- Firms should improve their operational effectiveness by offering lower cost and superior quality, at the same time, I.e. moving toward the productivity frontier.
- Industry should focus on differentiated, high quality, high valued products rather than on low-cost, low-priced products.
- Develop efficient distribution network and necessary institutions, especially training centers, R&D institutions, design centers, etc. Palestinian producers need to develop more competitive advantage in design, manufacturing skills, and market knowledge.