

# **Profile of Nicaragua's Textile & Apparel Industry**

**Source: New Cloth Market**

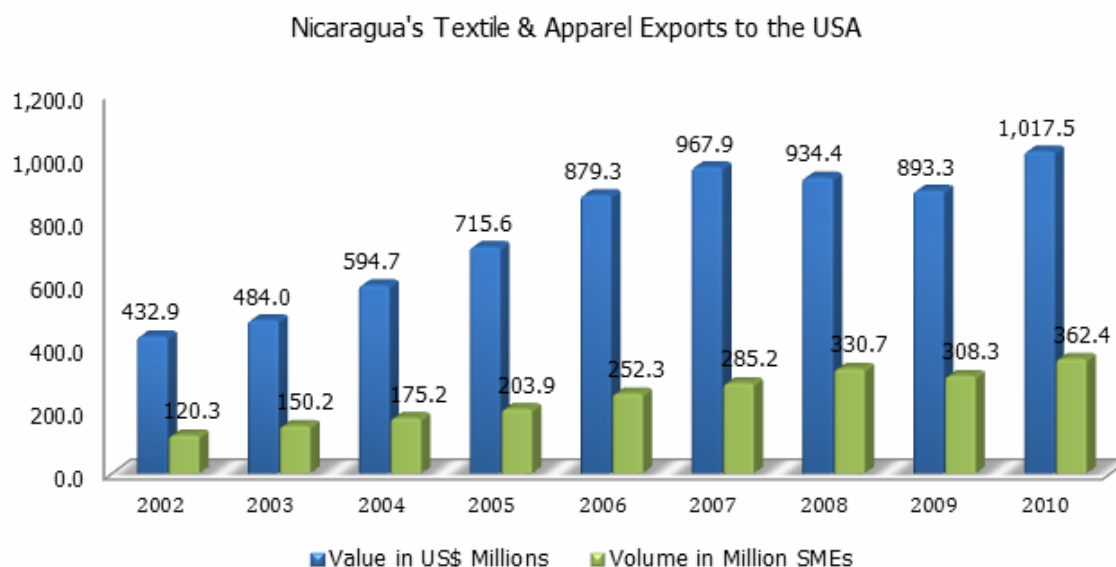
## Profile of Nicaragua's Textile & Apparel Industry

### Source: New Cloth Market

Given its strategic location, productive labor force, attractive investment opportunities, and generous fiscal incentives, Nicaragua has positioned itself as one of the most dynamic platforms in the Western Hemisphere's for manufacturing operations, whose exports reach the largest markets in the world.

Nicaragua's Textile & Apparel industry is an important development engine for the national economy, as it employed nearly 59,000 people by the end of 2010 and, during the same year, exported 362.4 million square meter equivalents (SMEs), valued at US\$1,017.5 million. This was indeed a record year in Nicaragua's apparel exports history, and it shows a strong recovery after the international crisis that affected the global apparel industry.

The following graph depicts Nicaragua's Textile & Apparel exports between the years 2000 and 2010.



**Note: Figures are in million US\$ and million SMEs.**

**Source: Office of Textiles and Apparel (OTEXA), U.S. Department of Commerce, April 2011**

As the previous graph depicts, in 2010 Nicaragua exported a record of US\$1,017.5 million in apparel to the United States, that is, a 14 percent increase compared to 2009.

During the past five years, Nicaragua's Textile and Apparel industry has experienced dynamic compound annual growth rates (CAGR) in terms of exports' value and volume:

- 7.3 percent growth in exports' value
- 12.2 percent growth in exports by volume

It is worth noting that, in light of the Free Trade Agreement between Central America, the United States and the Dominican Republic (DR-CAFTA), the U.S. represents the largest market for Nicaraguan apparel exports.

During 2010, Nicaragua ranked among the 12 largest apparel supplying countries to the United States in terms of volume. Its progress as one of the fastest growing garment exporting countries is reflected in its remarkable compound annual growth rate (CAGR), especially when compared with other countries in the DR-CAFTA region.

## Dynamic Growth in Apparel Exports

| Country            | CAGR 2003-2010 |             |
|--------------------|----------------|-------------|
|                    | By volume      | By value    |
| Average DR-CAFTA   | -3.3%          | -4.4%       |
| Honduras           | 0.1%           | -1.6%       |
| El Salvador        | -1.7%          | -1.7%       |
| <b>Nicaragua</b>   | <b>10.4%</b>   | <b>8.5%</b> |
| Guatemala          | -5.3%          | -6.1%       |
| Dominican Republic | -14.5%         | -15.0%      |
| Costa Rica         | -16.4%         | -15.4%      |

**Source: Office of Textiles and Apparel (OTEXA).  
U.S. Department of Commerce March, 2011.**

Investors find in Nicaragua key factors conducive to their companies' profitability. Among these factors:

1. High productivity rates, coupled with the most competitive labor costs in the region
2. Speed to market, leading to speed to profit
3. Significant improvements in the nation's infrastructure and business climate
4. The implementation of DR-CAFTA and its benefits
5. Generous investment incentives
6. High personal safety levels

World-renowned international brands have found in Nicaragua ideal elements to place garment production in the country; these brands include Under Armour, Liz Claiborne, Wilson, Wrangler, the GAP, the North Face, Lee Jeans, Cintas, Patagonia, Levi's, y Docker's and Dickies, among others.

Apparel manufacturers operating in Nicaragua also service major retail chains, such as: Target, JCPenney, Wal-Mart, GAP and Kohl's, all of which require a swift delivery of quality goods to the U.S. so as to reduce inventory costs.

### Industrial Clusters

In recent years, Nicaragua has become a major player in the global apparel industry and it has a leading position in the production of various types of garments directed to the United States. As international brands, retailers and apparel manufacturing companies come to recognize the advantages of producing in the Western Hemisphere, Nicaragua becomes the most attractive manufacturing platform for exports that reach the largest markets in North and South America, as well as Europe. Companies established in Nicaraguan manufacture different types of garments, including:

- Denim & Twill Bottoms
- Casual Knitwear & Activewear
- Organized sports uniforms
- Fleece Jackets
- Shapewear, girdles and ladies' undergarments
- Woven identity industrial uniform shirts
- Screen printing and embroidery

Besides apparel manufacturing operations, the Textile & Apparel value chain is complemented with twill fabric dyeing and finishing operations, industrial laundries, as

well as companies specialized in embroidery, labeling, screen printing and manufacturing of packaging materials.

The #1 supplier to the U.S. of Men's Knit Man-Made Fiber T-Shirts (HTS 6109.90.10.07).

The #1 supplier to the U.S. of Man-Made Fiber Girdles and Panty-Girdles, Whether or Not Knit (HTS 6212.20.00.20)

Third largest supplier to the U.S. of Women's Knit Cotton T-Shirts, Except Underwear (HTS 6109.10.00.60)

Fifth largest supplier to the U.S. of Men's & Boys' Knit Cotton Pullovers (HTS 6110.20.20.69)

Sixth largest supplier to the U.S. of Girls' Knit Cotton Trousers & Breeches, 5% elastomeric yarn (HTS 6104.62.20.06)

## Investment Opportunities

Nicaragua's market access and fiscal incentives, coupled with its productive and competitive labor, result in substantial cost savings for apparel exporters.

Nicaragua has evolved into a more experienced apparel producer, and there are ample, attractive investment opportunities both in garment manufacturing and in supporting industries, as shown below:

- Fabric production to complement the dynamic apparel manufacturing industry:
  1. Knit fabrics (cotton and man-made fiber)
  2. Twill and other cotton woven fabrics
- Attractive DR-CAFTA provisions for apparel production:
  1. Up to 1.5 million TPLs for all Men's & Boys' Wool Suit-Type Coats within OTEXA Category 433 (Chapters 61 & 62). Duty-free entry in the U.S. regardless of raw material origin. This DR-CAFTA benefit expires in 2014.
  2. Denim & twill garments.
  3. Organized team sports uniforms & activewear.
  4. Boxers, brassieres, jackets, woven pajamas, woven shirts, babywear, etc., all benefit from Single Transformation under DR-CAFTA.
  5. Medical apparel, uniforms, imagewear.
  6. Leather Footwear benefits from Single Transformation. Flexibility of sourcing raw materials from any country, assemble in Nicaragua and still enjoying duty-free status in the US
- Trims: buttons, zippers, pocket bags, elastic bands...

## Why Nicaragua?

### *Competitive Cost Structure*

Nicaragua has the most competitive labor costs in the region. The following graph shows a comparison of market wages in the region for manufacturing and assembly operations. These are fully-loaded market wages in the apparel manufacturing industry. Fringe benefits in Nicaragua include: social security, holidays and vacation leave, severance, thirteenth month and contribution to INATEC, the National Training Institute. These benefits amount to 46 percent of compensation.

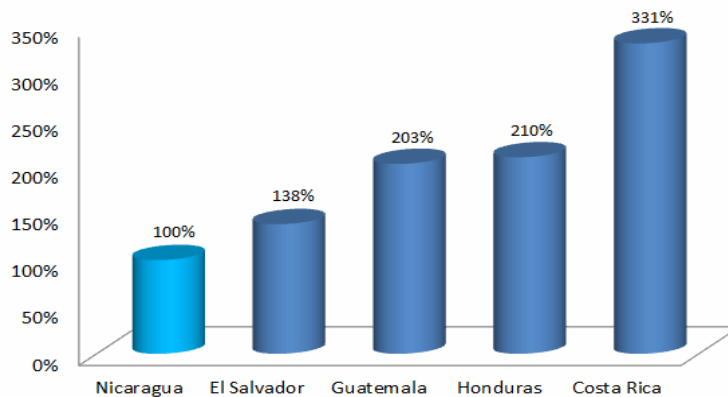
Companies find that cost-saving benefits along with qualified, productive human resources, make a difference in their businesses' competitiveness.

Moreover, the Tripartite Agreement signed in Nicaragua, a consensus between the Private Sector, the Government and Unions, provides certainty to investors as to specific minimum wages for manufacturing operations under the Free Trade Zone between 2010 and 2013.

- Year 2011: increase of 8% in Córdobas, or 2.86% in US\$\*
- Year 2012: increase of 9% in Córdobas, or 3.81% in US\$\*
- Year 2013: increase of 10% in Córdobas, or 4.76% in US\$\*

*\* Accounting for 5% annual fix devaluation rate of the Córdoba against the US Dollar (Crawling Peg System).*

### ***Regional Fully-Loaded Labor Cost Benchmark for the Manufacturing Industry***



**Source: PRONicaragua, July 2011, based on official information provided by Labor Ministries and National Banks of the Central American nations.**

A snapshot of the Free Zone Regime in Nicaragua by the end of 2010:

1. Total Exports: US\$1,574.2 million (46 percent of the country's total exports).
2. Number of employees: 84,898
3. Largest sectors within the Free Zone Regime: Apparel Industry, Automotive Wire Harness, Agribusiness.

This decision provides certainty for Free Zone companies as they are able to project labor costs for the period between 2011 through 2013. This is an unprecedented accomplishment in the whole region that shows Nicaragua's openness for investment and reflects the country's favorable business climate.

### **Attractive Fiscal Incentives**

Nicaragua's Free Trade Zone Law, compliant with the World Trade Organization's (WTO) guidelines for developing countries, grants generous fiscal incentives to export-oriented operations. The following tax holidays are effective for a period of 10 years:

- 100% Income Tax exemption. The normal Income Tax rate for companies outside the Free Zone Regime is 30 percent.

- 100% exemption on importing duties charged on machinery, equipment, raw material and intermediate goods, as well as means of transportation and support services.
- 100% Value Added Tax (VAT) exemption.
- 100% exemption on capital gains and Property Tax exemption.
- Unrestricted repatriation of capital.

### ***Preferential Access to Important Markets***

Speed to market —and duty-free benefits for products made in Nicaragua— make a significant difference in such a dynamic industry as Textiles & Apparel in terms of reduced inventory costs and increased ability to react to fashion trends and demands, which ultimately translate into higher profit margins.

Nicaragua's strategic location, combined with a productive labor force, allows companies to deliver production to the United States as fast as 50 days (average), since the day the program starts until it is shipped out of the Free Zone area. Short lead times satisfy customers' expectations, improving their inventory control and replenishment activities.

*Due to Nicaragua's proximity to the United States, ships reach Southern U.S. ports within three to five days. Additionally, it takes 2.5 hours of flying time to Miami and Houston and there are eight daily direct flights to main U.S. airports.*

Nicaragua enjoys free trade agreements with major trade partners around the world. The country's most relevant trade agreements include:

1. The United States, Dominican Republic and Central America Free Trade Agreement (DR-CAFTA)
2. Free Trade Agreements with Mexico and Taiwan
3. Preferential Access Agreements with Panama, Colombia and Venezuela
4. Generalized System of Preference with Canada, Japan, Norway and the European Union
5. Central American Common Market (CACM)

With the purpose of further increase its exports and expand its market access, Nicaragua negotiated a free trade agreement (Association Agreement) with the European Union, which will provide preferential access to one of the largest and most solid trade blocs in the world for a wider base of products made in Nicaragua. Because of the importance of this treaty, the goal is to have it effective by the first semester in 2012.

Furthermore, Nicaragua, as part of a regional effort, is also negotiating access to the Caribbean Community (CARICOM) and the Southern Common Market (MERCOSUR, *Mercado Común del Sur*) to strengthen its position as the ideal export platform for North and South America.

### ***Preferential Treatment for Garments under the DR-CAFTA Framework***

DR-CAFTA has contributed to eliminate duties for most of Central America's exports to the United States and helps to integrate the Central American economies into a single trading block.

DR-CAFTA's general rule of origin for apparel items is "Yarn-Forward," meaning duty-free benefits apply when cut and sew operations take place in Nicaragua, using regional yarn and fabric. Nonetheless, Nicaragua enjoys special rules of origin:

### ***Tariff Preference Levels (TPL) for Wool***

This benefit allows the Nicaraguan Textiles & Apparel industry to export garments made of cotton, man-made fibers or wool, free of duties to the United States, regardless of the fabric or yarn origin. The TPL benefit has been in effect since 2006 and will be valid until December 31, 2014.

Regarding wool, Nicaragua can export up to one million square meter equivalents (SMEs) of Men's Wool Coats free of duties to the United States, with fabric proceeding from any country in the world. These garments have higher value and complexity and their production will further diversify Nicaragua's ample apparel offer.

### ***Short Supply List***

DR-CAFTA's Textile and Apparel provisions include a list of specific yarns and fabrics deemed to be "not available in commercial quantities in a timely manner" in the Treaty's signatory countries, or in other words, in "short supply" from DR-CAFTA region mills. Provided the outer shell of a garment is cut and sewn in Nicaragua using these specific yarns and fabrics, it may enter the United States duty-free. There are no limits or quotas for exports applying the Short Supply rule and its duty-free benefit does not expire in time.

### ***Single Transformation***

This provision grants duty-free benefits in the United States for specific types of garments, with the flexibility for manufacturers to use fabric of any origin, as long as the products are cut (or knit to shape) and sewn in the DR-CAFTA region.

This represents a great opportunity for: woven boxer shorts, brassieres, woven pajamas and nightwear, babywear, women's cotton coats, among others. Single transformation trade is unlimited and the benefit does not expire in time.

### ***Cumulation with Mexico and the United States***

This mechanism allows the use of Mexican raw materials in the production of woven apparel in any DR-CAFTA country. The advantage consists in exporting these woven garments to the United States duty-free, qualifying as DR-CAFTA products.

The same occurs on the opposite way: raw materials originating in the United States may be used in the production of woven garments in the DR-CAFTA region, which may then be exported to Mexico duty-free.

Although the original agreement establishes a trade cap of 100 million SMEs per year to qualify for cumulation benefits, the agreement also includes terms to potentially double this cap over time.

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