

ADDIS ABABA UNIVERSITY

**College of Development Studies
Institute of Regional and Local Development Studies
(IRLDS)**

Value Chain Assessment in Ethiopian Leather Garment Industry The Case of Selected Garment Producers in Addis Ababa

**A THESIS SUBMITTED TO THE SCHOOL OF GRADUATE STUDIES OF
ADDIS ABABA UNIVERSITY**

**Advisor
Dr. Tegegne G/Egziabher**

**IN PARTIAL FULFILLMENT OF REQUIREMENTS FOR THE DEGREE
OF MASTER OF ART IN REGIONAL AND LOCAL DEVELOPMENT
STUDIES**

**By
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Addis Ababa**

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Approved by Board of Examiners

Signature

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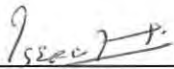
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ACRONYMS

| | |
|--------|---|
| DLI | Agriculture Development Led Industrialization |
| LIA | Ethiopian Leather Industries Association |
| ECBP | Engineering Capacity Development Program |
| ELICO | Ethio Leather Industries Private Limited Company |
| IBEF | Indian Brand Equity Foundation |
| LPTI | Leather and Leather Products Training Institute |
| MIDROC | Mohammed International Development Research and Organization Companies |
| MoTI | Ministry of Trade and Industry |
| PVCA | participatory value chain analysis |
| UNIDO | United Nations Industrial Development Organization |
| USAID | United States Agency for International Development |
| USD | United States Dollar |
| MEDaC | Ministry of Economic Development and Cooperation |

CHAPTER ONE

INTRODUCTION

1.1 Background of the Study

The leather sector is one of the fast growing and complex industrial sectors in the world economy. The total worth of the global leather market and its by products is several times greater than the market for fresh and canned meat despite the fact that hides and skins are by products of meat production. The master plan for leather and leather products industry of Ethiopia (UNIDO, 2005) compares the annual global trade in the leather sector in hides, skins, leather and leather products with other major tradable food items like meat, rice and coffee. It is shown that the size of leather and leather products trade volume was three fold the size of global meat production, four times the volume of coffee traded and more than eight times than the total volume of rice traded world wide in the year 2000. The global leather trade topped \$43.8 billion in 2004 (Master plan, 2005) and a spiraling \$70 billion in 2005 (Teshome, 2007).

China and Italy take the highest share of the 85 billion valued global leather industry as producing and exporting nations with \$19 billion and \$13 billion respectively. India ranks third with a \$2.4 billion industry that has also created 2.5 million jobs of which 30% are women (IBEF, 2006)

More than 60% of world leather production today is used for the manufacture of footwear and this makes it the most important application for tanning industry output. Asia, one of the most important footwear production centers of the world, has increased its share of production to 78.3 % of world total shoe production (UNIDO, 2005).

The leather industry in Africa is a potentially strategic sector for the industrial development and overall economic advancement of many African countries. Africa has a large population of cattle, sheep and goats that signify an abundant resource base to assume a leadership position in the global leather and leather products industry. The

sector is also labor-intensive with a potential to be a major employer along its production chain (Boehnke and Magariños, 2004).

Boehnke and Carlos (2004) claim that Africa has 20% of the world's cattle, sheep and goats but produce only 15% of world output of hides and skins. It also owns 10% of the world's cattle but produces only 4.5% of bovine hides. And export of hides and skins has fallen in recent years from 4% to 2% and that of tanning capacity from 9.2% to 6.8%. On the other hand, import penetration of African domestic leather footwear markets by other developing countries is estimated at 73.3%. African countries have in general shown a modest increase while countries in other developing continents have substantially increased their share of world footwear production (Boehnke and Magariños, 2004).

Availability of hides and skins for processing is determined by the rate of meat consumption since animals are primarily kept for their meat. Hence, collection and processing of its rich supply of hides and skins is heavily dependent on the rate of the meat consumption (Boehnke and Magariños, 2004). Problems that begin down the chain in breeding practices, consumption rate, collection, and processing are all suggestive of the fact that there are numerous hurdles to overcome in order to harness Africa's vast leather and leather product potential. The value chain approach to different sub sectors might help to get an in-depth understanding of the linkage and its problems in the leather industry. The value chain approach focuses on analyzing all stages of activities, pays attention to the intangibles, and helps to identify high-return and better competence areas in the global markets (Schmitz, 2005).

1.2 Statement of the Problem

The three major components that make up the leather and leather products industry in Ethiopia are the tanning sub-sector, the leather garment sub-sector and the leather goods sub sector. Economic importance of leather and leather products in the Ethiopian economy has become significant by earning foreign exchange for the country. Exports of the leather and leather products industry registered an increasing export revenue in the six

ABSTRACT

The major objective of this paper is to explore the strength and weakness of the value chain in the Ethiopian leather garment sub sector. In order to look into the strength and weakness of the leather garment value chain, nine garments and three tanneries were purposively selected as case studies. In order to see the linkage between the garments, the tanneries and their distributors in the garments value chain, qualitative method and simple quantitative methods of analysis like percentage are used.

Though Ethiopian finished leather is renowned for its fine sheep skin in glove making industries throughout the world, garment producers are making their products from reject quality leather unwanted by export standards. Owners of the garments in the study are found to be involved in all activities of the garments from the workshop to the office administration, sales, marketing, and planning issues. Their involvement from big purchasing, marketing and production monitoring responsibilities to small day to day office affairs and personnel management has resulted in very little time to carry out cooperation opportunities (with similar firms) and strengthening the leather garment supply chain.

The firms are small scale enterprises and linkage among them is characterized by mistrust and lack of cooperation to work together. The lack of coordination is a major reason for lack of bargaining power in leather purchase from their suppliers, lack of collective efficiency (greater production capacity) in the export activities, and learning from cooperation among themselves and from integration in the buyer driven global market. Major problems in the buying practice of the leather garments are the low (reject) quality of leather they purchase from the tanneries and very weak integration with their suppliers based largely on non market relationships. Due to scarcity and low quality of finished leather provided by the suppliers, nepotism, corruption and highly non transparent dealings have become common business practices between the garments and the tanneries.

The study recommends that the garments should have access to the purchase of higher quality leather to enhance their competitiveness in global garment trade. Effective management structure to undertake marketing research, reduce the slow decision making process in the purchasing of leather from the suppliers could be introduced. However, introduction of effective management practices at the firms should consider the small financial capacity of the firms. Skill building training for the workers should also be given due consideration in the upgrading process to enhance productivity of workers. Joint purchase programs should be organized by concerned authorities at the Ministry of Trade and Industry and multilateral developmental partners.

years from 1995-2000 and contributed 72% of earning from total manufacturing export in 1998-99 (MEDaC, 2000, cited in UNIDO, 2005).

However, it has lost ground not only to the biggest foreign currency earner coffee but also to oilseeds and *chat* (i.e. local stimulant herb) and was forced to slip into fourth place in the last four years (Haimanot, 2007). Latest figures from the Ministry of Trade and Industry indicate that the contribution of leather and leather products industry for the export trade stood fourth at 75,325 million USD in 2006 while coffee, oil seeds and pulses and chat registered 365,835 million USD, 255,442 million USD, and 88,505 million USD respectively (MOTI, 2007). Employment opportunities created were estimated at 7,278 or 7% in the formal sector and its gross value of production at 722 million birr in 2003, or 9% of total value of production. Value addition per employee per annum was 22,921 birr, which was below the national average of 23,555 birr in 2003 (Haimanot, 2007).

A World Bank study also argues that the sector is highly constrained by supply, quality, market, skilled manpower, and financial constraints. “All participants operate independently, all transactions are arms-length and cash-based. Prices fail to reflect premiums for superior quality inputs. No cross or joint investment exists and participants are having difficulty emerging from their low productivity trap. New technology introduction is minimal, capital equipment is dated, industry restructuring has not occurred and capacity utilization is low and declining” (World Bank, 2006).

Problems mentioned in the World Bank study also apply to the leather garment sub sector in Ethiopia. Strategic and operational problems have paralyzed the hopes of upgrading in the domestic value chain, diminished their chances to catch up with leading technologies in the sector, and hurt their comparative advantage in the global business (in renowned sheep skin, Teshome, 2008). These set backs in the value chain have combined to make the Ethiopian leather garment manufacturers left out of the lucrative global leather garment business.

Studies on the leather sector in Ethiopia reviewed by the researcher are sectoral in nature. Studies like Berhanu and Kibre (2001) and Worku (2003) have exclusively dealt with productivity and competitiveness of the leather industry (particularly tanning and footwear sub sectors) and the importance of footwear sector in the economy (Loop, 2003).

Accordingly, the studies done on the leather sector have not particularly dealt with assessment of value chain in the different sub sectors of the leather industry. The writer of this study has noticed that a research gap exists in this regard as studies on the value chain in the leather garment sub sector have not been undertaken. A closer look into the leather garment sub sector reveals that the existing horizontal linkages of leather garment producers (among themselves) and vertical linkage with tanneries and the market for their products has deep rooted problems.

This study, based on the observed gaps stated above, wishes to specifically assess the value chain of the leather garment sub sector with particular focus on selected leather garment producers and supplier tanneries in Addis Ababa.

1.3 Objective of the Study

The general objective of this paper is to explore the strength and weakness of the value chain in the Ethiopian leather garment industry. Specifically, the paper will try to:

- ↓ Look into leather procurement and buying practices, and production sourcing opportunities of selected leather garment producers;
- ↓ Look into export activities, marketing, and distribution of the garment producers.
- ↓ Look into coordination and integration problems among themselves and with tanneries and distributors; and
- ↓ Suggest measures to upgrade the existing value chain and enhance vertical and horizontal business linkage in the leather garment sub sector.

1.5 Significance of the Study

Upon completion, this study will hopefully initiate further detailed studies on the Ethiopian leather industry, particularly on specialization, clustering, and most importantly branding of Ethiopia's leather wear for more effective market penetration and sustainability.

The study might also opens better understanding of the value chain research in other sub sectors in the leather industry and other sectors of the economy as well.

Policy makers and regulating institutions like the Ministry of Trade and Industry may use parts of the study in playing their respective roles while formulating the development strategy of the country.

1.6 Scope of the Study

The study entirely deals with assessment of the existing value chain in the Ethiopian leather garment sub sector through selected garments and tanneries in Addis Ababa. It tries to see the business and strategic relationships in the leather garment value chain.

As discussed earlier, performance of the leather sector and its contribution to the Ethiopian economy has been dealt with in previous studies. This study wishes to specifically explore the garment sub sector value chain with the intent to assess the vertical and horizontal linkages among the different actors. Based on the findings, it also intends to forward intervention methods that are needed to upgrade the existing value chain.

The study examines the current business practice at selected garments and touches upon related issues that range from sourcing issues, buying and export practices to supplier selection, evaluation issues to cooperation and networking and upgrading problems in the leather garment value chain. Hence, the study strictly aims at value chain assessment of this sub sector and suggesting upgrading opportunities.

Issues related with competitiveness analysis, labor productivity in the sub sector and other areas of performance are completely out of the objective of this study.

1.7 Organization of the Study

The study is divided into five chapters. The first chapter deals with introduction and background of the study. In this chapter, statement of the problem, objectives, scope, significance and limitations of the study are stated. While chapter two deals with review of literature, chapter three provides the methodology of the study. Findings and discussion are presented in chapter four where findings are stated according to the outlined specific objectives. Chapter five, the last chapter presents summary of findings, conclusion and recommendation and winds up the study. Reference and annexes used in the study are provided following the last chapter.

1.8 Limitations of the Study

Numerous obstacles have been encountered in the process of this undertaking. The main one is probably selecting the garments and tanneries for the case study. Getting the consent of the garment and tannery officials was a very tiresome and at times frustrating experience. Unwillingness of the respondents to divulge financial details and their future plan was a big hurdle in the research duration. Simple financial information like annual turnover and sales from export earning were treated as classified information. However, such gaps were not significant to cause serious reservations of the findings.

As part of the study finding, the garments and some of the tanneries involved in the study have exhibited highly disorganized record keeping of their financial and marketing activities. Exact amount of purchased inputs and volume of sold garments were mostly not available or the officials were not willing to provide them. Such hurdles have made the data collection process extra difficult and resulted in delayed time to fill in missing information.

Lack of any material on the history of leather garments in the country was another problem. Highly fragmented and individualistic way of running the business has visibly devoid the sector of any referable material that can be used for literature review.

Materials on the sub-sector couldn't even be retrieved from the Ministry of Trade and Industry, which, at least theoretically, was supposed to be the right place to look for and find track records of any sub-sector in manufacturing.

Some of the respondents at the selected tanneries and garments were strongly unhappy to participate in the study and went as far as ridiculing the importance of studies including this one. It was assumed, from their remarks that such a sense of uneasiness to cooperate was due to "consultation and research fatigue". They have openly showed their discontent with "any projects" aimed at improving the sector and are quoted as saying they are "tired of questionnaires, consultations, and researches which have brought no result for the betterment of the sub sector."

Some gaps in the findings can be partly attributed to respondents' unwillingness to answer and elaborate on some questions and due to their demonstrated inability to understand the points under discussion despite repeated attempts to clarify.

1.9 METHODOLOGY

1.9.1 Study Design

The study is designed to asses the leather garment value chain of selected leather garments in Addis Ababa to investigate the weakness and strength of the leather garment value chain.

It is case study includes nine leather garment enterprises that are currently engaged in leather garment business some of which are currently engaged in different market expanding and upgrading in the process of expanding their capacity to export to foreign markets. Three tanneries who are currently supplying the leather garment producers with finished leather are also included in the study. Selection of cases is based on their business experience, market dominance, participation in professional associations, expert

opinion (based on their export activities and experience in the business), observation of the owners' experience, integration experience and ownership status.

1.9.2 Location of Cases (Garments and Tanneries)

The garments and tanneries selected as case studies are found in four sub cities in Addis Ababa. Two of the garments are located around the national stadium area where similar competing leather garment producers are also located. The other garments are located in Piassa (Arada sub-city), Bole (Bole sub-city), Saris (Akaki Kaliti sub-city), Hayahulet (Bole sub-city), and Sar Bet (Nefas Silk Lafto sub-city). The tanneries are located in Saris (Akaki Kaliti sub-city), Hana Maraim (Akaki Kaliti sub-city) and Koka, Oromia Regional State (Interview and checklist was handled in its Addis Ababa office located around Ambassador Theater).

1.9.3 Selection of Cases

Availability of leather garment producers in regional towns could not be verified by any organization including the Ministry of Trade and Industry. Data obtained from the Addis Ababa City Trade and Industry Bureau shows that there are 34 enterprises registered as leather and leather garment manufacturers in the city of Addis Ababa. Among these enterprises, the ones with bigger market share, experience, participation in professional associations, export activities and supported by expert opinion are all included in the study. Observation also reveals that the garments are champion brands in the city for leather garments and goods. At the same time, they are also front-runners in the sub sector who suffer different setbacks in their implementation of a variety of marketing and expansion activities.

The selected cases of garment producers are:

1. ELICO
2. Jonzo Leather Garments
3. Ethio-Sung bin Leather Garment
4. Joy Leather Garments
5. Kinaff Leather garments

6. Genuine Leather craft
7. Modern Zege Leather Garment
8. General Leather garment and
9. Abyssinia Leather garment

1.9.4 Selection Criteria of Garments

The garments found in Addis Ababa and which cover over 90% (ELICO 30%, Genuine 20%, and Kinaff 20%, Modern Zege, Joy and Jonzo 20%) of the total sale of leather garment in the city (all figure gathered from the garment owners) are included in the study.

The researcher of this paper has also visited three sub cities where many of the currently functioning leather garment producers are located namely Arada sub city (mostly Piassa), Bole sub-city (all shopping areas from 22 Matoria to Olympia and main Bole shopping centers) and Kirkos sub city (from Meskel Square to stadium area where many leather garment producers are densely found). Some 18 garments whose market outlets are found in the above mentioned sub cities have been visited. Addresses of the other leather producers registered at Addis Ababa Trade and Industry Bureau could not be found.

Requests submitted to the Trade and Industry Bureau of Addis Ababa to get addresses of all registered garments was not answered by the bureau. However, visits to many business centers in other sub cities revealed that there are no operating leather garment producers. Thus, the researcher concluded that all operating leather garment producers found to be currently in business have been visited and were considered in the selection process. The main selection criteria employed in the selection of the cases as opposed to their competitors in the sub sector are the following.

1.9.4.1 Dominance of Market

Thus, selection of these garments could be reflective of the weaknesses and strengths of the existing leather garment value chain. As leaders of the local market in leather garment

sub sector, the problems and opportunities of horizontal cooperation and vertical integration in the chain can be looked at based on the relationship that exists between these firms.

1.9.4.2 Experience

All the nine garments are the pioneers of the sub-sector in the country and have stayed in the sub sector between 12-25 years. Based on observation prior to the study, the researcher found that managers of these enterprises are veteran designers, businessmen, and individuals with the most viable experience in leather garment sub-sector in the country.

Information from the Ethiopian Leather Industries Association has also revealed that five of the nine garments are members are actively engaged in the efforts to promote Ethiopian leather products to foreign markets.

1.9.4.3 Expert opinion

Consulted authorities on the sub sector namely ECBP, TAYTU project (UNIDO assisted project to promote Ethiopian leather goods to European markets) Ministry of Trade and Industry Leather Division, Leather Industries Association recommended the cases for their long years in the businesses, notable failure and successes.

1.9.5 Selection Criteria for Tanneries

Ethiopia tannery, Walia tannery, and Awash tannery have been selected for the study to verify the questions provided for the garments to assess the linkage between themselves and the garments.

1.9.5.1 Market Dominance of Finished Leather Supply

Data from Ethiopia Tannery, the largest tannery in the country, revealed that it supplies 70% of the total finished leather consumed by the garments. Awash Tannery also sells finished leather to local garment producers but its relation is more vertically integrated with its sister garment company, ELICO which takes 90% of the finished leather it requires. Therefore, it was selected to take part in the study.

Walia tannery is also another supplier of finished leather among other tanneries but a planning shift to focus on the export of finished leather is forcing it to neglect the leather garment value chain. The inclusion of this tannery is believed to be important in analyzing the important issues of vertical integration in Ethiopian leather garment value chain.

1.9.5.2 Ownership

Ethiopia tannery is government owned tannery while Walia and Awash are under private and corporate ownership respectively. They are also small suppliers of finished leather to local garments but their ownership plays a big role in their business principles in the leather garment value chain. Awash is subsidiary of a corporation and its run in a different manner than the other tanneries and its management of finished leather sale to garments is based on different grounds.

Walia, a solely private tannery, operates with a different view for its role in the leather industry in Ethiopia and the leather garment value chain in particular. Awash tannery is highly focused on the export of finished leather.

Thus, the selection of these three tanneries with different ownership and strategies in the leather supply could help to see the implication in the domestic leather garment industry in the country. It will help to see how the domestic vertical integration in the value chain could be affected because of the different business strategies employed by the supplier tanneries.

1.9.6 Distributors

The study looks at the relationship between garments and their foreign distributors. However, the foreign distributors could not be located in the course of the data collection. Therefore, the researcher of this paper was forced to depend on the information given by the garments and key informants to analyze the vertical linkage between garments and their distributors.

1.9.7 Data Collection Method

A combination of methods which include checklist, in-depth interviews, observation, and review of secondary data are used to generate the required qualitative information for the research. Field data collection involved the use of checklist for the selected garments and tanneries to allow more probing and clarification. The cases were given the checklist to answer the question followed by in depth interviews conducted to get detailed answers to all the questions and fill any information gap that might result from lack of clarity. The checklist was specifically prepared with follow up questions to allow probing into each of the questions and cross check with the answers of the supplier tanneries.

The checklist was preferred to conduct this study to seek detailed and open ended responses to questions of finished leather supply (and vertical integration issues) and their opinion of the leather garment value chain, their role in strengthening the chain, and outlook of integration opportunities in the domestic value chain.

Key informant interviews from the Ministry of Trade and Industry, Ethiopian Leather Industries Association, UNIDO, ECBP, LLPTI, four leather technologists and consultants, three tannery managers and eight owners of garments were obtained along with direct observation to enhance the findings. Specific information collected from the key informants includes the business practice and management of the garments, main problems in the leather supply chain to the garments, problems of integration between garments and suppliers, export constraints and production capacity issues and upgrading and learning opportunities in the leather garment value chain.

1.9.8 Selection of Key Informants

A total of twenty one informants have been selected on the basis of their research experience in the leather sector in Ethiopia and their practical experience in the leather garment sub sector. Two experts from the leather sector division at Ministry of Trade and Industry, chairman of the Ethiopian Leather Industries Association, leather sector expert at UNIDO, leather expert at ECBP, a leather technologist at Taytu project (a UNIDO

assisted project to promote and sale Ethiopian leather products to European markets), leather technologist and garment expert at LLPTI, private garment consultant and entrepreneur, leather sales expert and leather technologist were included. Owners of nine garments and managers of three tanneries selected as case studies have also been interviewed.

1.9.9 Data analysis

The data is analyzed in terms of the designed study objectives. Data analysis for the study is qualitative and descriptive in manner. Qualitative analysis has been chosen because the cases are intended to explore the relationship, gaps, and chain constraints in the leather garment value chain. Simple statistics like average and percentages are employed in the course of the analysis.

1.9.9.1 Quantitative and qualitative methods

According to Trochim (2003), quantitative methods are exploratory and are used when the researcher wants to generate new theories or hypothesis or wants to achieve a deep understanding of the issue. Quantitative research is more confirmatory and deductive in nature.

Qualitative data is extremely varied in nature and includes virtually any information that can be captured that is not numerical in nature. Major categories of qualitative data are in-depth interviews, direct observation, and written documents. A variety of methods are common in qualitative measurement and these methods are largely limited by the imagination of the researcher. One of the methods in qualitative measurement is case study which is an intensive study of a specific individual or specific context. There is no single way to conduct a case study, and a combination of methods can be used (Trochim, 2003).

Quantitative methods are employed by when the sample is large and uses a standard questionnaire to ensure that all respondents are asked exactly the same set of questions in the same sequence. Qualitative analysis uses an outline of topics, or a set of general questions to serve as guide for the kind of information required instead of reading formal

questions from a structured interview schedule. Direct observation is also useful in this analysis for small scale exploratory studies than large scale quantitative studies (Research Methodology, 2000).

CHAPTER TWO

LITERATURE REVIEW

2.1 Definitions and Concepts

The global value chain approach has become the latest analytical approach that highlights new linkages in the global economy and brought new dimension about what it means to be involved in global trade and the global economy in recent years (Humphrey, 2004).

Kaplinsky and Morris (2000) describe the value chain as the full range of activities required to bring a product or service from conception through phases of production that involve a combination of physical transformation, inputs and services of other producers, and delivery to final consumers and disposal after use.

According to Sturgeon and Lester (2001), cited in Humphrey (2004), "...the traditional image of export activity for developing country firms would be an enterprise that designs, makes and exports a product. But now, the developing country exporter may work to a design supplied by an international buyer. Or the exporter may just produce a small part of the final product. Firms in developing countries may act as the organizers of geographically and organizationally fragmented supply systems".

Humphrey describes that the value chain view of global economic integration highlights the fact that the process of designing, making and marketing new products is not enough for many industries to gain access to international markets. Rather gaining entry into international design, production and marketing networks consisting of many different firms is more important.

"Understanding how these value chains operate is very important for developing country firms and policymakers because the way chains are structured have implications for newcomers. ...the development of these new forms of coordination in the global economy is widely seen as contributing to the rapid rise in manufactured exports from developing countries over the past two decades. These changes have created a new

environment with uncertain consequences for developing country firms (Humphrey, 2004).

An in-depth insight into these value chains and their dynamics of governance is imperative to determine the level of competence of developing countries in the world trade and identify potential areas of competitiveness. Humphrey asserts that there is an increasing recognition of this transformation across the world as the approach provides answers for questions like “How can economic actors gain access to the skills, competences and supporting services required to participate in global value chains? What potential is there for firms, industries, and societies from the developing world to “upgrade” by actively changing the way they are linked to global value chains? (Gereffi et al, 2001)

According to Gereffi, the value chain involves a series of components that begin with product design and the selection and purchase of raw materials and intermediate inputs and go through processing, marketing and distribution. The chain continues with the operation and sales of intermediate and end products. The last component of the chain is the consumption of final goods that is regulated by internal and external demands (Gereffi 1999, cited in De buckle, 2001). Gereffi describes this linkage as a series of activities that interact to bring about substantial transformation to a raw material so that it adds intrinsic value. “It is a comprehensive set of activities required to bring a product from a concept stage to marketing and consumption of end products” (Gereffi 1999, cited in De buckle, 2001).

The process of globalization has promoted two types of chains through which global production networks manage and operate: the producer-driven and the buyer-driven chains (Gereffi 1999, cited in De buckle, 2001). The first type is the characteristic of capital-intensive industries such as automobiles, aircraft, computers, and other advanced technology industrial activities. The buyer-driven commodity chains are organized around labor -intensive industries such as footwear and garments in which the marketing and manufacturing agents (retailers, branded marketing agencies and branded manufacturers) set up global production networks, principally in developing countries.

Enterprises in exporting, developing countries produce the finished goods under contract following the specifications, guidelines and technical advice provided by the purchasing agents. Successful examples of buyer driven commodity chains were Japanese in the 50's and 60's, Asian in the 70's and 80's and Chinese in the 90's (Geriffi and Korzeniewicz, 1994; Gereffi 1999, cited in De buckle, 2001).

2.2 Advantages of the value chain approach

A general understanding of these days is that broadly effective and thus poverty alleviating growth in developing countries that is also environmentally sustainable is not possible without access to the large and differentiated markets. Therefore, the question is not whether producers participate in local, regional, national and/or international trade, but how competitively and in a sustainable way they participate. The value chain approach presents possibilities to appropriately analyze the nature and determinants of competitiveness and used to identify resultant problems (Roduner, 2005).

The value chain reflects the existence of proactive sequence of activities where substantive changes in the value of a product take place. But commodity chain does not entail substantive change in terms of value creation but signified movement of commodities along its destination which may finally be consumption. A process in a value chain actually changes the product's status from being commodity (Geriffi and Korzeniewicz, 1994).

The analysis of commodity chain is centrally concerned with issues like division of labor, industrial organization, technological change, the production process, and global factors etc while emphasizing the geographical embeddedness of production systems. The crucial components of a well constructed value chain provide insight into determinant factors beyond particular production processes in a given time and place. Placing the various processes in their chains helps us evaluate the significance of the choice of property arrangement, labor control, and mode of linkage with chains upstream and downstream (Geriffi and Korzeniewicz, 1994).

According to Kaplinsky (2000) and Wood (2001), the value chain perspective is analytically useful for three main reasons.

- ↓ First, the focus moves from manufacturing only to the other stages of activity involved in supplying goods and services to consumers. Particularly, more attention is paid to the “intangibles” phases, such as distribution and marketing, whose cost often accounts for a larger share of the final price of a product than do manufacturing costs.
- ↓ Second, this type of analysis captures the flows of information as well as goods between the stages of activity in the chain, making clear that linkages between firms are often not at arm’s length and involve skills and knowledge that are scarce and command large financial rewards.
- ↓ Third, the key to understanding the global appropriation of the returns to production is the ability to identify high return activities along the value chain.

A deep value chain analysis is required to enhance the ability of local enterprises to compete in the global economy and improve the earning opportunities and working conditions of local people (Schmitz, 2005). Formulating sound economic policies that reflects the level of development in a specific industry and the country requires a basic understanding of how local enterprises fit into the global economy.

Mayoux (2003) says that participatory value chains analysis can be used as analytical tool for impact assessment tool to provide a framework for identifying the different levels of intervention involved, impacts of different types of intervention at different levels and other change processes affecting interventions.

As a planning and strategic learning tool, the value chain approach explores and identifies potential positive interlinkages between different ‘leverage points’, levels of intervention and collaboration between different agencies: government, donors, NGOs and local people.

Mayoux (2003) further explains that the value chains analysis has a number of key contributions to improving strategic learning in enterprise development and outlines four

types of intervention. The first one is that it conceptualizes enterprises as part of chains, networks and systems of different but linked production and exchange activities operating in different geographical areas: local, national and international. As a second intervention, it focuses on analyzing 'chain governance' and the complex interrelationships between markets imperatives, opportunities and constraints at the different levels and the different interests and power relations which influence how value is distributed at these different levels. Through an analysis of systems and power relations at different levels, the third intervention, enables a much more sophisticated modeling of the direct, indirect and unintended positive and negative effects of different types of intervention at different levels. This in turn enables a more complete exploration of different alternative strategies for poverty reduction following the findings of impact assessments.

Six different areas of enterprise development to which PVCA (participatory value chain analysis) may be adapted are further identified by Mayoux (2003):

1. **Homeworker and other grassroots organizations:** to increase knowledge of the opportunities and constraints on increasing incomes and benefits, to assess 'points of leverage' where change is possible, to assess levels at which networking and organisation might be able to increase the relative value reaching the bottom of the chain and identify the various opportunities and constraints at different levels of the chain which affect the effectiveness of any support.
2. **Impact Assessment of Fair Trade and Codes of Conduct:** to map the different levels which Fair Trade interventions and Codes of Conduct need to target, the different stakeholders involved, potential mutual and conflicting interests and areas for stakeholder cooperation in setting up ongoing structures for accountability.
3. **Microfinance Programmes:** PVCA can be used by programmes and microfinance groups to identify e.g. activities where financial services are

particularly appropriate or inappropriate, why this is so and the constraints at different levels of value chains which need to be addressed through non financial services.

4. **Business Development Services:** PVCA can be used here to identify the levels at which services might need to be integrated, the types of services which might be needed, in training itself for clients to analyze their situation and establishing why particular types of services might be most appropriate or inappropriate for different levels.
5. **Regulatory Frameworks:** PVCA can be used to clearly identify which activities and which stakeholders are likely to be directly affected or targeted by particular types of regulation, and the potential consequences for other stakeholders above or below those particular levels in the value chain.
6. **Environmental policy:** PVCA can be used to clearly identify the different levels and locations where environmental pollution is occurring and/or where environmental enhancement could be achieved, where stakeholder incomes might be sufficient to cover the costs of environmental policy and the levels at which pressures might be brought to bear for compliance and/or skills might exist for innovation.

2.3 Chain Links and Bottlenecks

In all countries, excellence can be found in some individual enterprises. However, discussion on improving competitiveness often concentrates on how to achieve more of such individual excellence. Schmitz (2005) explains that though this is very useful, it is not sufficient because “the competitiveness of the individual firm depends upon the competitiveness of the value chain to which it belongs. Competitive pressure to achieve efficiency gains forces companies to interact more closely with partners upstream and downstream in the value-adding process” (Altenburg, 2004 cited in Shmitz, 2005). Thus,

it is very important to give the linkages more attention for both local and global competence.

International competitiveness requires an effective domestic value chains as much as it requires an efficient supply chain in which suppliers are reliable and efficient, support institutions are equipped to test the quality of inputs and products to ensure international standards are maintained and relevant policy environments are created. Hence, higher qualities of domestic linkages and strong domestic support system have a central role in laying the basis for international competitiveness.

The value chain analysis can greatly help, compared to other approaches, to find out the weak point in the competition process. It is a great tool to answer questions like:-

- ↓ Which part of the chain holds up progress in the others?
- ↓ Which bottlenecks deserve priority attention of government?
- ↓ Which can be expected to be resolved by the private sector and which require public-private partnership?
- ↓ Where can the donor agencies help? (Schmitz, 2005)

The relevant value chain analysis helps to identify where the weak links are and devise a plan to increase competitiveness in the market compared to sectoral studies and priorities (Schmitz, 2005). In the value chain analysis, knock-on effects up and down the chain become more apparent and complex interdependencies can be visualized and communicated more easily. Thus, the approach provides a framework for sector-specific action. Moreover, it also ensures that this action plan does not stop with domestic linkages. The importance of facilitating linkages with the global economy is highlighted in the approach which could involve improvements in infrastructure, customs and others. The result could enable enterprises to move goods and people quickly in and out of the country.

Generally, the value chain approach helps to establish priorities for action by tracing the connections from the buyers to the producers. It can also be used for drawing national and foreign support agencies into a common strategy (Schmitz, 2005)

2.4 Coordination and Networking, Sourcing and Learning Opportunities in the Value Chain

2.4.1 Coordination and Networking

According to Prahalad and Hamel (1990) cited in Gereffi et al. (2005), coordination within value chains can take various forms. Coordination may occur through arm's-length market relations or non-market relationships. Coordination problems are reduced in the functional value chain not only because their ease of description makes contracts simple to write, but also because standard products can be produced for stock and supplied as needed. At the same time, because standard products are made by a variety of suppliers and bought by a variety of customers, problems arising from asset specificity are low.

Network actors in many instances control opportunism through the effects of repeat transactions, reputation, and social norms that are embedded in particular geographic locations or social groups. They explain that trust, reputation, and mutual dependence dampen opportunistic behavior, and in so doing make possible more complex inter-firm divisions of labor and interdependence than would be predicted by transaction costs theory (Prahalad and Hamel, 1990 cited in Gereffi, et al., 2005).

2.4.2 Sourcing

There are many advantages in outsourcing for already established manufacturing enterprises managing export markets (De Buckle, 2001). Increasing capacity and flexibility without investing, specialization, reduced production costs, reduced delivery times and provision of opportunities to experiment with new production lines and

suppliers without having to take financial risks are some of the advantages that can be mentioned.

Generally, costs involved in the production of new samples are absorbed by the producing company in the hope of receiving an order. Outsourcing has become very common in labor intensive industries such as apparel and footwear. Outsourcing fulfills the desire of multinational corporations to buy and market goods from developing countries and complies with the wishes of manufacturers in developing countries to do production-work and thus participate in the global business world (De Buckle, 2001).

As explained by Schmitz (2005), the outsourcing of manufacturing and service activities from the high wage to the low wage economies accelerates the recent trend of increasing functional integration between internationally dispersed activities. However, there are several constraints that are common in the manufacturing enterprises of developing countries that make it difficult to bring the parties together such as:

1. Lack of market information in developing countries new in the international markets
2. Lack of English speaking staff in manufacturers from developing countries
3. Poor communication infrastructure available to developing countries manufacturers
4. Poor physical infrastructure to reach factories located in marginal areas
5. Lack of experience in negotiating the contracts required by multinational corporations.

2.5 Value Chain Governance

The other important component in the analysis of the value chain is the concept of governance. Central to the global value chain analysis, governance can be defined as non market coordination of economic activity. We use the term to express that some firms in

the chain set and /or enforce the parameters under which others in the chain operate (Gereffi et al., 2001, Humphrey and Schmitz, 2001).

At any point in the chain, some degree of governance or coordination is required in order to make decisions regarding what will be produced (product design), how it will be produced (production process, technology, quality standards), and how much will be produced. The concept of governance involves the ability of one firm in the chain to influence or determine the activities of other firms in the chain. The governance perspective shows which organization defines who produces what, how much and when and at what price. These parameters can be set by a lead firm, by a group of actors or by parties external to the chain. The question of governance generally arises when some firms in the chain work according to parameters set by others (Roduner, 2005; Humphrey and Schmitz, 2001)

Schmitz explains that not all chains are governed by powerful lead firms. Some chains are merely strings of market-based relationships: there are market transactions but little exchange of other information or learning occurs. In others, there is intensive interaction between buyers and sellers along the chain, but the power dynamics between enterprises are unequal. According to Humphrey and Schmitz (2001, 2003), one can distinguish between four basic types of relationships more systematically.

1. **Arm's length market relations:** buyer and supplier do not need to develop close relationships because the product is standardized or easily customized. A range of firms can meet the buyer's requirements and the switching costs are low.
2. **Balanced networks:** firms develop information-intensive relationships, frequently dividing essential competences between them. The interaction is characterized by reciprocal dependence. The buyer may specify certain product performance standards or process standards to be attained, and is confident that the supplier can meet them.
3. **Captive networks:** in this case, the buyer exercises a high degree of control over other firms in the chain. The buyer specifies the characteristics of the product to

be made by the suppliers and the processes to be followed and monitors that their instructions have been carried out. This occurs when a buyer has doubts about the competence of firms in the supply chain.

4. **Hierarchy:** the lead firm takes direct ownership of some operations in the chain. The case of the intra-firm trade between a transnational company and its subsidiary falls into this category. However, we should never forget that since there are different kinds of value chains, just as many different responses are required from policy-makers and local firms. For example, local firms seeking to sell their own products in global markets need different kinds of support compared with firms that make sub-products to the specifications of big global buyers (Humphrey and Schmitz 2001, 2003).

Lusby and Panlibuton (2004) also classify chain governance into four:

1. **Market based:** where “Arm’s length” transactions take place between buyers & sellers. Little or no formal cooperation among participants.
2. **Balanced:** fairly equal decision making exists among participants. It is characterized by cooperation where no one side dominates.
3. **Directed:** controlled by firms who determine product, specifications, trade rules, etc in the chain.
4. **Hierarchy:** Vertically integrated enterprise that controls various functions along value chain.

The nature of governance in the value chain shows what kind of relationship exists between firms with regard to influence over decision making in the firms’ production activities in the market.

2.6 Importance of Value Chain Governance

Humphrey and Schmitz (2001) explain that the issue of governance in the value chain is important for the following reasons.

- ✦ Value chains shape market access: Even when developed countries dismantle trade barriers, developing country producers do not automatically gain access to

developed country markets because the chains which producers feed into are often controlled by a limited number of buyers. In order to participate in export manufacturing for North American and Western European markets, developing country producers need access to the lead firms of these chains.

- ✚ Fast track to acquisition of production capabilities: The lead firms are very demanding with regard to reducing cost, raising quality and increasing speed. But they also transmit best practices and provide hands on advice (and pressure) on how to improve layout and production flows and raise skills. It is this combination of high challenge and high support that is often found in the highly governed chains and that explains how relatively underdeveloped regions become major export producers in a short period of time.
- ✚ Leverage points for policy initiatives: Precisely because many value global chains are not just strings of market based relationships, they can undermine government policy but also offer new leverage points for government initiatives.
- ✚ Funnel for technical assistance: Multilateral and bilateral donor agencies have for decades sought to find ways of providing effective technical assistance to developing country producers. The central idea in this assistance is to combine technical assistance with connectivity. The lead firms in the chain became the entry point for reaching out to a multitude of distant small and medium sized suppliers.
- ✚ Understanding the governance of a chain helps to understand the distribution of gains along the chain (Kaplinsky, 2000, cited in Schimtz, 2005). Gains are distributed unevenly across value chains and () suggests that the ability to govern often rests in intangible competences (R&D, design, branding, marketing) characterized by high barriers to entry.

2.6.2 Value Chain Governance and Policy Makers

Schmitz (2005) explains that it is imperative that policy makers know whether local firms engage merely in transaction (buying or selling) or interaction (which also involves intensive exchange of information and transfer of ideas), if they expect these local firms to learn from participating in the global economy. They need to be aware of power and inequality in the chain because as much as working for powerful players can bring great benefits, it could also severely limit what the firms or government agencies can achieve. The value chain analysis provides policy makers with a pair of glasses through which they can see how local enterprises fit into the global economy and it provides all the actors with the tools to identify where improvements will be necessary to make these linkages.

2.6.3 Value Chain and the Issue of Core Competence

Value chain analysis can also be used to sensitize small and medium enterprises in a more fundamental sense (Schmitz, 2005). In many situations these small and medium enterprises do not see where they fit into the bigger picture. They may find it difficult to identify their core competence and may not realize the full impact that new open-trade regimes and global sourcing have upon their competitiveness, or even their survival. In order to compete in the global economy it is critical to find one's core competence. Identifying this core competence means being able to answer two questions:

1. What product or service can the enterprise offer that is of particular value to customers?
2. Would it be difficult for others to copy this product or service?

Global value chain analysis can help local enterprises and the institutions supporting them to engage in a process that helps them to participate in the global economy in an informed and gainful way. To illustrate the concept of core competence, Schmitz (2005) takes the garment industry as an example.

"...in the garment industry, standard market analysis will look at issues such as seasons, predicted fashions, consumer confidence, etc. in a given

export region or country. Value chain analysis will help local producers to pay attention to differences between global buyers and the specific demands of particular buyers who supply these export markets. Recognizing their specific needs will provide a way to focus on improving existing practices within local enterprises or on finding a new export niche (Schmitz, 2005).

2.7 Upgrading in Global Value Chain

The concept of upgrading refers to several kinds of shifts that firms or groups of firms might undertake to improve their competitive position in global value chains (Gereffi, Humphrey, et al, 2001). A thorough look into the chain governance is also imperative in the process of upgrading which is “a key capability to innovate and ensure continuous improvement (rate of which is compared to competitors) in product and process development. Innovation in itself may not be enough, and more important is the rate of innovation compared to competitors (Roduner, 2005).

Sturgeon (2006) divides the types of upgrading in the value chain into four main ones.

- 1. Process Upgrading:** Takes place when firms improve their existing systems to be more efficient, responsive, or quality-aware. Functions may be added or subtracted to achieve these goals, but the central value chain activity carried out the firm remains the same. An example is the introduction of better quality control systems (e.g., statistical process control) or new production equipment (e.g. injection molding equipment for outsoles) for the production of shoes.
- 2. Product Upgrading:** This type of upgrading takes place when firms shift to higher value added products within the same sector. Production processes may (or may not) stay the same, but the firm shifts to new, more profitable product segments of the same industry. An example is when a footwear producer shifts from mass-produced, low cost shoes to more fashion-intensive footwear produced in smaller lots and sold for high prices.

3. **Functional Upgrading:** Takes place when firms change their position in the chain of value-added activities by taking on a new activity, either as a substitute for existing activities, or as a compliment in a process that can be referred to as “bundling.” Unlike process upgrading, the central focus of the firm shift to a new value chain activity. An example is when a shoe manufacturer shifts its focus from the production of shoes to the sale of shoe production equipment (e.g., moulds sold to other footwear manufacturers).
4. **Chain or Inter-Sectoral Upgrading:** Takes place when firms move from one value chain to another. Processes and functions may also change, or they may not, but both immediate and final customers are in new sectors. The basic processes of the firm may stay the same, but inter-sectoral shifts come with new customers and requirements. An example is when a firm shifts from to the production of leather footwear to the production of interior parts for motor vehicles. Both may include fabrication in leather and plastic, but the end markets are clearly very different (Sturgeon, 2006)

2.8 Value Chain and Developed Leather Industry

The leather industry in general uses a by-product of slaughterhouses and transforms the raw materials into different types of leather and manufactured products. The leather production-consumption chain has three processing stages each requiring different combinations of material inputs, labor and capital. The first stage in value chain involves animal breeding and slaughtering practices to recover raw materials. Leather tanning and finishing is the second stage that involves relatively capital-intensive operations while the third stage, which is the production of leather products, is a more labor intensive (Boehnke and Magariños, 2004).

These three processing stages are linked to key commercial components of the leather industry value chain, the marketing of intermediate inputs, components and end products, trade and finally market or consumption. Inputs to the chain without which the chain cannot operate under competitive basis include qualified labor, design and art skills,

component production, technical and administrative support, institutions, research and policies etc (Boehnke and Magariños, 2004).

Leather sector report of India Brand Equity Foundation (2005) says that composition of exports has been changing with more and more value added products begin exported from leather products producing nations. "In 2004/2005, value added finished products constituted around 80% of total export from the industry; a far cry from 7% in the 1956/57. The value addition in the leather industry at present is estimated between 200-500%" (IBEF, 2005).

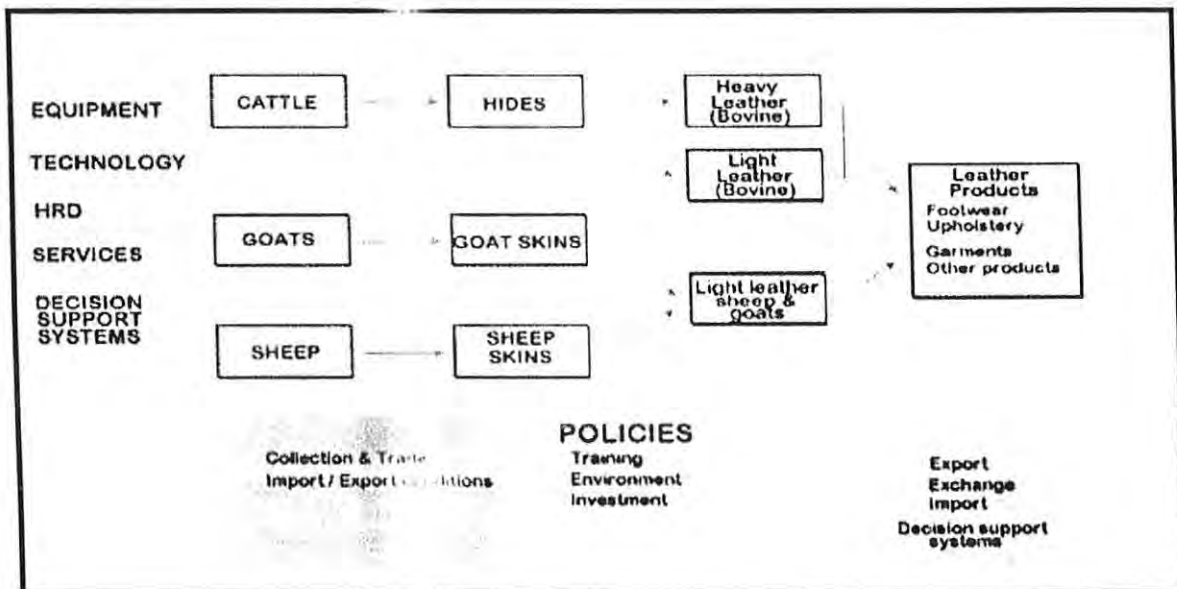
Skill, technology, and support facilities to produce and sell finished leather shoes, garments and leather products in the export and domestic market, Kidanu (2007) says, are what characterize a developed leather industry along with "the capacity in which it creates, expands and avails itself with raw materials". Poor practices in animal husbandry practices and slaughtering, inadequate collection networks, and the lack of a system of price differentiation by quality are main causes for under performance of Ethiopian leather industry (Kidanu, 2007). Lack of marketing and technological skills have further added to the problems to weaken the sectors competitive capacity both locally and internationally by decreasing the quality of the leather and manufactured leather goods.

Teshome (2007) also explains that despite the considerable quantity to its rank among the top ten in the world livestock resources, Ethiopia attains less than 1/10th of 1% of the \$70 Billion + global market; earning only \$75 million in 2005/06". Nevertheless, promising new developments are beginning to overcome these challenges and the leather and leather products industry now has some key opportunities to upgrade technologically and strengthen its marketing linkages. In order to maximize this potential and penetrate the global market for leather garments, goods and footwear, many constraints at all levels in the value chain must be carefully dealt with. Taking into consideration some of the constraints mentioned above, Kidanu (2007) argues that problems associated with

Ethiopia's leather industry and formulation of global competitiveness strategies cannot be fully answered without a careful understanding of the leather value chain.

The strategy proposed by the government of Ethiopia takes the policy mix, experimented with China and Italy for the footwear industry referred to as "Top-down (pull approach)". According to this approach, the leather products, mainly footwear selected as the priority sector and followed by leather garments and leather goods, should be developed in a way that it would "pull" the tanning sector to produce better quality and increased quantity of finished leather; subsequently raising the quantity and quality of raw materials as well (UNIDO, 2005)

Figure 2.1 The leather value chain



Source; Adapted from Blue print for the African leather industry, 2005

2.9 Ethiopian Livestock Resource and the History of Leather Sector in Ethiopia: An Empirical Review

2.9.1 Livestock Husbandry

Reasons for livestock keeping in Ethiopian society have much to do with firmly traditional values than the multiple economic rewards accrued from livestock. Haimanot (2008) explains, based on CSA figures, that one can see ‘drought resistance’ comprises the biggest (40%) of reason for engaging in animal husbandry followed by reproduction and milk production. Interestingly, a mere 1% of the total cattle herd is meant for beef generating purposes.

Table 2.1 Livestock husbandry in Ethiopia by specific purpose

| Purpose | Livestock | | |
|--------------|-----------|-------|------|
| | Cattle | Sheep | Goat |
| Milk | 24% | - | 7% |
| Drought | 40% | - | - |
| Beef/ mutton | 1% | 4% | 6% |
| Breeding | 30% | 95% | 86% |
| Wool | - | 0.5% | 1% |
| Others | 5% | 0.5% | 1% |
| Total | 100% | 100% | 100% |

Source: Haimanot Asmerew, ECBP, 2007 adopted from CSA, agricultural sample survey 2004/05

2.9.2 Livestock Resource

Ethiopia possesses considerable livestock resources which make it stand 1st in Africa and 10th in the world. To the surprise of any researcher in the field, however, figures about Ethiopia’s livestock resources have been found to contradict with each other. According

to Befekadu and Berhanu (2000, cited in Worku 2003), the country has an estimated livestock population ranging between 30-35 million measured in tropical livestock unit (TLU). Berhanu and Kibre 2002 (cited in Worku, 2003) also noted that Ethiopia held about 15.75% of the cattle and 9% of the sheep and goat herd of Africa in 1996, which confirms the claim that Ethiopia has the largest livestock population in the continent.

Nevertheless, another study by Tesfaye et al. (2004), said that the cattle population of Ethiopia is not yet ascertained by any relevant and credible institution as different estimates emerged at the time of their study in 2004. "...one common striking development reflected in these different sources of information is that Ethiopia has become second next to Sudan in its cattle population and is no more first in Africa (Teskaye et al., 2004).

The findings used for the formulation of the Ethiopian leather and leather Products Industry master plan in (2005) reveal that the country stands seventh in cattle, ninth for sheep and lambs and eighth for goat herds in the world. And within Africa, Ethiopia stands first in cattle resources while Sudan has more bovine cattle and considerably more sheep and lambs, but in goat population Ethiopia stands third after Sudan and Nigeria (UNIDO, 2005).

The first ever livestock census conducted in 2003 puts the livestock population of the country (also cited by Kidanu, 2007) at an estimated 41,000,000 heads of cattle 15,000,000 sheep and 14,000,000 goats. However, Tesfaye et al. (2004) claim that the figures given by the central statistics authority expose huge discrepancy with a FAO report of 2001 which put the livestock population at 35 million cattle, 24 million sheep, and 17 million goats.

The FAO figures have clearly shown a significantly lower heads of cattle compared with the findings of the national authority while sheep and goat populations are considerably higher than otherwise indicated by CSA. "...the discrepancy in the number of sheep and

goats could be justified as the census did not include the pastoral area of the country. The cattle population, however, is expected even to be higher if the pastoral areas were included” (Tesfaye et al., 2004). “Though Ethiopia possesses huge livestock resource endowed with large livestock stock that could be the basis for vibrant leather industry, livestock resources and off-take rates are not known for sure” (Haimanot, 2007).

Based on the findings from these different sources, Tesfaye et al. (2004) puts the livestock resources between 35 -41 million cattle, 15-24 million sheep and 14-18 million goats. Similarly, Kidanu (2007) appears to have indicated the same (41 million cattle, 24 million sheep, and 23 million goats) estimates of livestock that could comfortably support a sizable leather industry in Ethiopia. For reliability reasons, this study takes the figures put forth by Kidanu (2007) and Tesfaye et al. (2004) that estimate at 41, 24, and 18 million for cattle sheep and goat respectively.

Table 2.2: Livestock Resource of Ethiopia

| Country | Cattle in '000 | Sheep '000 | Goats in '000 | Total |
|-------------------------------|----------------|------------|---------------|--------|
| According to CSA Census, 2003 | 41,000 | 14,700 | 13,700 | 69,500 |
| According to FAO, 2001 | 35,000 | 24,000 | 18,000 | 77,000 |

Source: Adapted from Tesfaye et al., 2004, CSA, 2003 and FAO, 2001

With such an abundance of livestock resources, Ethiopia has got a comparative advantage in the leather and leather products sector to place itself among the top leather excellence and export hubs in the world. But poor animal husbandry, dismal physical and market infrastructure and in areas where cattle resources of the country are found, problems of quality and competitiveness and global marketing skills have combined to prevent the country from putting its large livestock resources to the benefit of its people and its economy at large. Despite the huge resource of livestock in Ethiopia, however, takeoff

rate has been extremely low taking into consideration the volume of supply. “The country provides about 2 million pieces of hides and 13.6 million skins annually. Had this amount been properly utilized, it could have been a great opportunity for those currently operating and potential investors in the sub-sector in particular and the country in general (Worku, 2003).

Estimates from the Ministry of Agriculture and Rural Development also show that the current skin removal rate is 7% for cattle, 33% for sheep, and 37% for goats. This could translate into an output of 2.4 million cow hides, 8.3 million sheepskins and 7 million goatskins in the year 2000. On average, Ethiopia has the capacity to supply 16 to 18 million pieces of hides and skins to local tanneries (Kidanu, 2007). However, the last few years have seen better utilization of the leather and leather products resources in the country. The leather sector has registered an encouraging contribution to the economy though a much bigger potential in both supply and demand sides of the market is yet to be harnessed. For instance, the leather and leather products industry has recorded a 29% growth in revenue in the current Ethiopian budget year and an average of 100 million Eth. birr worth of leather and leather products is gained by exporters and local consumers in this budget year alone (MoTI, 2008).

Despite some notable successes in jump-starting the sector and a reputation of excellence in the global market for its sheepskin used in the glove industry, many structural and technical problems continue to slow the growth of the sector from generating its optimum economic benefits employment opportunities.

Kidanu (2007) and Haimanot (2007) also argue that the value chain in the Ethiopian leather industry has interrelated problems beginning from the lowest point, which is animal husbandry, up to collection of hides and skins to tannery processing and manufacture of leather goods and all the way to finished products market locally and

2.9.3 Brief history of the Ethiopian Leather Industry

2.9.3.1 Pre 1974

History of the tanning industry in Ethiopia goes 70 years back and was started in response to the niche growing domestic market demand for leather shoes and other leather products. For this purpose the oldest two tanneries were vertically linked to two shoe factories Asco Tannery & Shoe Factory (the present Addis Tannery & Tikur Abay) and Darmar Tannery and Shoe Factory (Present Awash & Anbessa Shoe Factory). The two tanneries produced finished leather to be used in the making of shoes at their shoe factories while the semi processed skins were destined for export market (Tesfaye et al., 2004).

Dofan Ethiopia, presently Modjo Tannery was established to process crocodile skins for parent company Dofan Paris. Tesfaye et al. (2004) claim that the activities of this plant came to an end when the Ethiopian government banned crocodile hunting in 1973 and the tannery shifted its operation to skin processing. Ethiopian Pickling and Tanning (pickled sheep skin producer) started operation in 1972. Ethiopian Tannery, the biggest of such a facility both in production capacity and the sectors' foreign exchange earning to date, was set-up in 1972 as a project with the then Czechoslovakian credit and technical assistance (Tesfaye et al., 2004).

2.9.3.2 Between 1974 and 1993

The spate of nationalization process that that soon followed the regime change in 1974 hasn't spared the tanneries and shoe factories as they fell under state monopoly. "...they were put under the defunct National Leather and Shoe Corporation (NLSC) together with the Ethiopian Tannery which was already s parastatal. Combolcha Tannery was nationalized in 1977 and brought under the NLSC although it was then non-operational. At the time of nationalization the bulk of raw hides and skins were exported in raw form as the capacity of the tanneries was limited. Gradually, however, the capacity of the tanneries was increased and by the end of 1980's it reached to a level of absorbing all the

commercial supply albeit at low stages of process. This had triggered the NLSC to invest particularly on the two major tanneries namely Ethiopia and Awash to produce more value added items” (Tesfaye et al., 2004).

2.9.3.3 Post 1993

Tesfaye et al. (2004) in their final report for study on designing framework for the leather and leather products industry of Ethiopia, assert that economic liberalization that followed the down fall of the Derg and the of governance in the country, has disbanded the National Leather and Shoe Corporation and the factories were restructured and put under the auspices of a special board of management.

“...Dire was the only private tannery that existed since the early periods of the previous regime and Walia Tannery, another private tannery which started operation in 1991. A number of private tanneries and leather product factories were set up being encouraged with the existing policies. As a result presently there are about 16 private tanneries and 4 Public Tanneries. Similarly a number of footwear and other leather product factories were set up privately although there were several others before 1993 (Tesfaye et al., 2004).

2.9.3.4 Current situation

Currently there are twenty five tanneries operating in the country with job opportunities for over 4,000 people (Haimanot, 2007). Nine out of the twenty six tanneries are fully focused on the export of semi processed skins. Fourteen of them have acquired treatment facilities for effluents (UNIDO, 2005). Some studies suggest that current tanning capacity in the country stands at 33 million skins and 1.1 million cow hides. While 12 tanneries are only engaged in the production of semi-processed leather, 13 tanneries have crusting and finishing capacity. The majority of Ethiopia’s export is semi-processed leather which accounts 70-85% of total export of leather and leather products (Haimanot, 2007).

Table 2.3: Estimated current production of hides and skin

| Livestock | Population '000 heads | Off take rate % | Production of hides and skins |
|----------------|-----------------------|-----------------|-------------------------------|
| Cattle | 41,139 | 7.6 | 3,126,564 |
| Sheep | 23707 | 37 | 8,771,590 |
| Goat | 21669 | 44 | 9,534,360 |
| Sheep and goat | 45,376 | | 18,305,950 |
| Total | 86,515 | | 21,432,514 |

Source: Haimanot, 2007

2.9.4 Contribution to Export Trade

Figures from the Ministry of Trade and Industry (MOTI, 2007) show that the government planned to export a total of 11.4 million USD from leather and leather products sub sector but only 9.8 million USD which is 86% of the target was met. However, the performance from that month (June 2007) was by far the best performance from all the months registered in the 2006-2007 budget year (MOTI, 2007).

Among the 9.8 million USD export, 85% was generated from Ethiopia Tannery which collected almost 22% of the total revenue while 12% was covered by Dire Industries through Peacock Shoe Factory. Eleven percent came Colba Tannery, 8% from Hafede Tannery, 8% from Ethio Leather Industries, 7% from Sheba tannery, 5% from Walia tannery, 3% from Gelan tannery, 3% from Dessie tannery, 3% from Modjo tannery, 3% from Ramse shoe (MoTI, 2008).

The amount of revenue collected from the leather and leather products sub sector in June 2007, 9.8 million USD, has shown a 4% increase from the amount collected in May 2007, only one month earlier which was 9.4 million USD. When compared with that of the revenue collected in the same month one year before, a 9% increase has been registered. Out of the 9.8 million USD collected in the month of June 2007, 61.6% was secured from pickle and wet blue semi processed leather while 38.4% was collected from crust stage and finished leather and shoe exports (MoTI,2008). The June 2007 export

earnings from crust, finished leather and shoe exports and garment has amounted to 3.7 million USD out of which 956,006 USD was secured from shoe exports alone. This figure is shared by peacock shoe which has collected 291,500 USD, Ramse Shoe Factory with 259,400 USD, Blue Nile Shoe Factory with 208,900 USD, Anbessa Shoe Factory with 190,800 USD and only 6,000 USD from three small companies which were not included in the export planning prior to the start of the budget year (MoTI, 2008).

Generally it was planned to export 116.7 million dollars product to foreign markets in 2006-07 budget year but only 89.5 million dollars worth of produce was exported that amounted to 76.7% of the planned revenue. Companies which generated 85% of the above stated revenue include Ethiopia Tannery with 21%, Dire Industries through Peacock Shoe with 16%, Colba Tannery with 10%, Ethio Leather Industries with 8%, Hafede tannery with 8%, Walia tannery with 7%, Sheba tannery with 5%, Modjo tannery with 4%, Hora tannery with 4%, Dessie tannery with 3% and Kombolcha Tannery (MoTI, 2008).

This 89.5 million USD export of this sub sector harnessed in 2006-07 budget year has shown an 18.9% growth when compared to the same period in the previous budget year which only managed to register 75.3 million dollar. Out of the 89.5 million USD collected in the whole budget year of 2006-07, pickle and wet blue stage semi-processed leather constituted 64% while the remaining 36% was secured from crust stage, finished leather and shoe export. The performance of semi processed finished and shoe export in the previous year was only 24% of the total export earnings. Therefore, the performance of 2006-07 could be regarded as a period of better achievement (MoTI, 2008).

Out of the 3.7 million USD registered from the export of crust, finished leather and leather products in the 2006-07 budget year, finished leather picked the lion's share of 647,000 USD with Ethio Leather Industries contributing 58% ,Dire tannery 29% and Bahir Dar tannery 6% with the remaining divided among three other tanneries (MoTI, 2008). Likewise, out of the 2.1 million USD secured from the export of crust, Ethiopia

Tannery contributed 59% while Walia tannery took 23%, Dire 11%, ELICO 4.6%, and other two tanneries contributing the remaining (MoTI, 2008).

In the same budget year in 2006-07, 5.5 million worth of shoe was exported with peacock shoe taking 73% or 3.9 million USD, Ramse shoe amassed 602,100 or 11% Anbessa shoe 419,300 or 7.6, Blue Nile Shoe 338,900 or 6%, Ras Dashen 250,600 or 0.5 and others took the remaining (MoTI, 2008). Ministry of Trade and Agriculture has originally anticipated collecting 16.3 million USD worth of export In March 2008 from the leather and leather products sub sector. However, the plan fall short of target as only 56% or 7.4 million USD was collected. The ministry's plan to collect 100.4 million USD in the first nine months of the current budget year was only met with a 74% success that amassed 74.5 million USD (MoTI, 2008). The nine month performance has seen a total export worth of 27.8 million USD from crust, finished leather and leather products. The amount has registered 25.8 % increase compared from the same time period in the last budget year (which was 22.1 million USD).

Table 2.4: Summary of operation of the leather manufacturing sector

| Year | No of enterprises | No of employees/ From a total of manufacturing sector employees | | Fixed capital asses in Birr | Investment in fixed assets in Birr | Gross value of production in Birr |
|-----------|-------------------|--|---------|--------------------------------|---|---|
| 2003/2004 | 65 | 7,665 | 105,381 | 514,846,000 | 60,663,000 | 813,126,000 |
| 2004/2005 | 62 | 7,913 | 109,150 | 501,926,000 | 86,925,000 | 984,678,000 |
| 2005/2006 | 63 | 7,914 | 118,409 | 492,868,000 | 74,916,000 | 1,022,745,000 |

Source: CSA, 2007

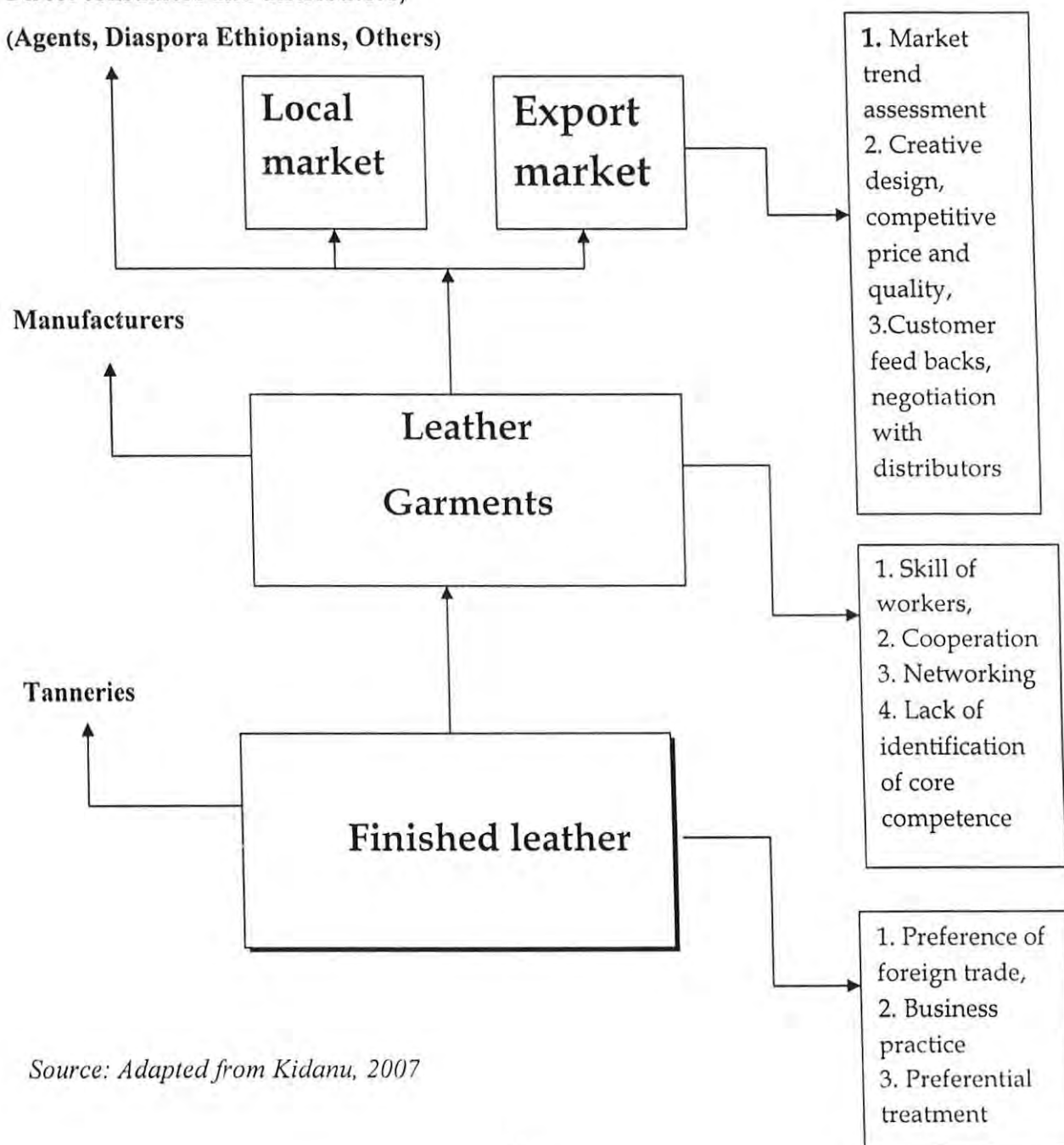
The above table illustrates the number of industries in the leather manufacturing sector, the share of employees from the total manufacturing sector, fixed capital, investment and gross value of production in birr. The figures show the significance of the leather manufacturing sector in the Ethiopian economy.

2.9.6 Conceptual Framework for Value Chain Assessment In leather Garment Industry in Ethiopia

ACTORS

KEY FACTORS

Direct consumers and distributors,
(Agents, Diaspora Ethiopians, Others)



Source: Adapted from Kidanu, 2007

CHAPTER THREE

Result and Discussion

This chapter deals with the findings of the research based on the objectives specified in chapter one. The first part gives a brief description of the selected garments and tanneries followed by a compiled data collected through interviews and the checklist on the current and maximum leather garment production capacity of the garments. It then explores the existing value chain in the Ethiopian leather garment industry based on variables pointed out as specific objectives of the study which are; input procurement and business practice, production sourcing opportunities and export activities of selected leather garment producers are discussed in the fourth part. Production, marketing, distribution, networking coordination and upgrading issues of leather garment producers are also discussed. Strength and weaknesses of leather garment value chain are discussed lastly in this chapter.

3.1 Brief Description of the Selected Leather Garment Manufacturers

In all the nine garments discussed in this study are established between 1983 and 1996. Size of workforce at the garments is found between 12 (Abyssinia) and 255 (ELICO). Main market target of the firms is the local market though eight of the nine garments are engaged in exporting their products through Diaspora Ethiopians and sales agents based in foreign countries. Destinations of the products of the garments are South Africa, Great Britain, United States and other European countries.

Seven of the garments have said that cheaper and high quality Chinese products have taken over their European markets. Genuine garment is the only garment currently involved in sourcing arrangement with Pittards Global Sourcing Agency, which had taken over the management of the company in 2007. Teshome kebede, owner of the firm, is one of the most qualified leather sector consultants in Ethiopia. Upgrading activities are not seen with many of the firms while only one, Modern Zege, has carried out an expansion project for 11,000 jackets per month production capacity. However, the factory

could not go operational for lack of raw material foreign market opportunities. None of the garments have been able to register export revenue in the last three years despite having submitted plan to Ministry of Trade and Industry to generate foreign currency (own survey, 2008, and MoTI, 2008).

Four of the garment manufacturers have based their marketing strategies on a vast pool of established personal contacts locally, US and European markets. Many of them are well reputed among the expatriate community in Addis Ababa.

There is lack of organized marketing, purchasing and administrative departments in seven of the nine garments visited. Compared to all others, ELICO has well organized marketing, production management, and purchasing departments. Strong family ties are found in many of the garments studied where decisions are made by a members rather than personnel who are directly responsible for different tasks.

Relation between the garment companies is not strong and many of them tend to operate separately. One garment owner has openly rejected any cooperation possibilities with similar garments “because no result has been seen in cooperation efforts in the last ten years”.

3.1.2 Products of the Leather Garments

The products at the studied garments include a variety of ladies and men’s garments. Jacket remains the main product but other items like vests, overcoats, ladies skirts, trousers, and leather goods like purses and handbags are also produced in smaller quantities. The study findings confirm the results of observation at the selected garments that jacket is the dominant product of the garment producers taking a share of 80% of all leather garment products. Interviews with industry experts revealed that the phenomenon is not unique to Ethiopia but elsewhere in the world as people tend to choose jackets than other forms of leather wear like trousers, skirts and other products.

Table 3.1 Range of product, production of jackets as total percentage of leather garments

| Name of garments | Product range | Jacket as % of total garment production |
|-------------------------------|--|---|
| 1. ELICO P.L.C | Ladies and gent's jackets, bags, briefcases, gloves, furniture, and other small articles | 80% |
| 2. General leather PLC | Ladies and gent's jackets, bags, overcoats | 90% |
| 3. Ethio-sung Bin PLC | Jackets, coats, vests, skirts, trousers, bags, purses others | 55% |
| 4. Joy leather PLC | Ladies and gent's jackets, bags | 87% |
| 5. Genuine leather PLC | jackets, leather goods and gloves | ** |
| 6. Modern Zege garment PLC | Ladies and Gent's jackets, belts, bags | 95% |
| 7. Abyssinia garment PLC | Ladies and gent's jackets, Bags, wallets, belts | 90% |
| 8. Jonzo leather garments PLC | Ladies and Gent's jackets and leather goods | 70% |
| 9. Kinaff leather PLC | Ladies and gent's jackets, handbags, vests. | 82% |
| | Average | 80% |

Source: Own Survey, 2008

** Not available

3.2 Brief Description of Tanneries

A. Ethiopia Tannery

The biggest tannery in the country has an annual turnover of 240,000,000 million birr, it has 700 employees and is engaged in the production of wet blue, crust and finished leather (own survey, 2008). Finished leather used for glove leather is major product of the tannery. The government-owned company is shifting its focus to finished leather production to increase its current share of 30% of the country's finished leather export (own survey, 2008 and MOTI, 2008). Data obtained from the tannery also shows that 70% of all finished leather used by leather garments is supplied by Ethiopia Tannery, making it the most powerful player in the leather garment value chain.

Currently under management contract with a British management firm, the tannery is accused by many garment companies for not providing the required quality of finished leather for garment production and ignoring the interests of local garment producers. The tannery, however, argues that low productivity coupled with disorganized and highly unpredictable purchasing management of the garment manufacturers has forced it to give minimal attention and exclude them from its priority marketing list.

B. Awash Tannery

Operating under the ownership of MIDROC Ethiopia, Awash Tannery has 800 employees and produces pickled, wet blue, crust and finished leather products. More than 90% of the finished leather (from sheep skin) and 10% of hides are exported to Asian (China) and European markets (own survey, 2008). The company is also involved in sourcing arrangement with two local tanneries which allowed it to buy semi processed leather in pickle stage to finish at its plant and export. Any decisions on joint venture and other partnerships are made outside of the tannery by corporate management. The main local buyer of its finished leather goes to ELICO; a sister garment company. Other garments are supplied with finished leather but the grade of the leather sold for all local clients is the 'reject' stock unwanted by the export market.

C. Walia Tannery

A private company established in 1995 G.C, Walia tannery has more than 300 employees. It is engaged in the production of pickled, wet blue, crust, and finished leather products. 80% of the finished leather is exported to China and Europe which are the main export destinations (Own survey, 2008). Policy incentive has encouraged the tannery to completely switch focus to finished leather production in the coming few years. Sourcing from local tanneries has resulted in increasing its finishing capacity.

The strategic plan of the tannery focuses on diversifying its foreign trade. Local sales and networking in the leather value chain are not included in the company's business activities. The tannery extends no consideration to local garments in its sale of finished leather. No incentive is also in place for garments because of the "difficult choice it has to make between export trade and engagement in the leather value chain" (Own survey, 2008).

3.3 Leather procurement and buying practice at the garment

Leather is the main component used in the making of leather garment products along with accessories like zippers, buttons, lining, pad, and strengthening materials. However, leather and lining (that covers the inside of the leather) make 90% of leather total material used in the production of leather garments (Own survey, 2008).

3.3.1 Leather purchasing

The study found that input procurement is the main problem area in their buying practices. Highly disorganized and traditional methods including high interference of owners in the leather purchasing process are observed in the garments. Study findings show that in seven of the nine garment companies, there is no purchasing department or focal person responsible for the purchase of leather from tanneries (see table 4.2).

The unstructured management has led to multiple job descriptions for the owners and a one man management system prevails at the companies. Specific responsibilities are not

delegated to professionals in specialized divisions to handle garment management tasks. The unstructured nature and lack of serious monitoring of management activities has reduced production and planning efficiency. It has also forced the owners to spend less time and resources to strengthen cooperation with garments on common issues like joint purchase of inputs, foreign market penetration and lobbying policy attention for more value additions in the domestic leather value chain. Further implications of owner managed buying practice are discussed below.

Table 3.2 Responsible Bodies for Purchasing at the Garments

| Responsible body for purchasing | Respondents |
|--|--------------------|
| Purchasing done by specially assigned department or focal person | 2 |
| Purchasing is handled with related management issues and with owners direction | 5 |
| There is no responsible person specifically assigned | 2 |
| Total | 9 |

Source: Own Survey, 2008

Table 3.3 Owners' Involvement in Finished Leather Purchasing

| Level of involvement | Number of firms |
|---|------------------------|
| Owner is directly involved in negotiation | 5 |
| Only responsible professionals are involved | 1 |
| Owners are partially involved in purchase process | 2 |
| Owners and other family members are involved in purchase decision | 1 |
| Total | 9 |

Source: Own Survey, 2008

The above table (table 4.3) indicates that owners are directly involved in the purchase of leather in five companies. In two other manufacturers, owners are partially involved (in monitoring) in the purchasing process. There is a professional purchasing person at only one company while the remaining one declined to answer the question. Owners at the seven manufacturers (full and partial involvement) handle the leather purchasing process and at the same time assume other administrative and technical responsibilities of the workshop and the office. Similarly, seven compnay owners out of nine said that they closely monitor the delivery and storing process after they have purchased the leather no matter how much time it might take.

3.3.1.2 Reasons of Owners' Interference

In five of the manufacturers, the owners have replied that they handle all the purchasing of leather by themselves because they can not trust anyone in quality selection and negotiation with the tanneries. They have also said that they have good knowledge of the complicated buying practice in the local finished leather trade.

Interviews further indicated that owners' direct involvement has proved to have affected negatively as owners are highly stretched in all managerial activities and devote less time

in strategic planning and studying integration and cooperation opportunities. Sense of responsibility of other managerial (purchasing, finance, marketing) staff is also diminished as only small sales and office activities are delegated to them.

The following are implications of owners' interference in the purchasing process:

1. Direct involvement of owners in purchasing process has caused strain in the owners' capacity to concentrate on bigger issues. It was revealed in the five companies whose owners directly handle purchasing process, owners spend many hours of their working days looking for finished leather, negotiating and executing deals with the tanneries. The cycle continues every two to three months and could go on more than two weeks before a deal is sealed for the required quality and quantity.
2. Owner's direct inference in leather purchasing, which is a painstaking activity for garment manufacturers (due to less consideration given to them by the tanneries), has led to small resources and less focus on important upgrading issues.
3. Freedom of decision making by other management members is very low. Hence, professionals in different managerial positions are not attracted to such organizations where the owner runs everything from designing to personnel, purchasing and marketing activities.
4. Lack of priorities in the owner's role in the management hurt all divisions of management. Continuous evaluation in production quality and workers' efficiency in the workshop is not properly monitored due to lack of time and allocation of resources by the owner.

3.3.1.3 Advantages of the Garments in the Leather Purchasing Process

Six of the nine garment companies said their advantage in the purchasing activity comes from the combination of experience in dealing with the tanneries and having insider information at the tanneries about product and processing quality. Only one said its strong side in the purchase of leather is knowledge of leather quality passed from the

family experience while two replied a combination of information from insiders (on price and quality) and their experience of identifying quality. One garment said its market trend assessment and price anticipation is the strong side in its purchasing process. Market information doesn't exist or it is unreliable. The findings imply that the majority of the garments heavily rely on insider information at their suppliers and traditional family knowledge to help them in their leather purchase from their supplier. These contacts are maintained through incentives for the information they provide to the garment producers. Such non market practices have arisen mainly from the scarcity and unreliability of sub standard quality of leather supply and detached them from transparent input purchasing mechanisms.

3.3.1.4 Planned Purchase

Planned purchase (here refers to annual plans prepared by the garments on the quantity, quality and time of finished leather purchase from their suppliers) program is not exercised at five of the nine garment companies. These companies replied that they have found it "very difficult" to implement any planned purchase program due to lack of demand forecasting for their products and highly unreliable tannery supplies. Other reasons given by the garments not to implement planned purchase program are:

1. Scarcity of finished leather supply and unpredictable market for their products
2. Fear of capital tie up (scarce working capital spent on raw material stock) in case both local and export markets slow down

Other three companies said buying period doesn't necessarily coincide with orders (from their distributors) and have disclosed that their purchase of leather could come following similar actions of competitor garments.

Concerning unpredictable orders, these producers said they fear that their small working capital might be tied up in stockpiled finished leather since sizable orders for jacket products usually come without prior notice. Hence, they are afraid that sudden orders that might not materialize and swings in the local market (strong sales in rainy summers and

weak in hotter months) could waste expensive and hard found leather and drive them into bankruptcy.

Probing questions in the in depth interviews have also revealed that apart from lack of planned purchase programs, three manufacturers replied that their purchase program might follow their competitors' action based on the assumption that "the competitor companies might have information (that others don't have) that either there is going to be a price hike of finished leather, scarcity of supply, or better quality finished up for sale at the suppliers."

Interviews concerning this question have found out that these three companies (which said their purchase might follow competitors) closely follow the purchase of leather by their competitors very closely and engage in the bid based on information from tanneries.

All the nine manufacturers said if they could cooperate with similar companies to implement planned purchase program, they could have a strong negotiating power to strengthen the supply chain of finished leather. Lack of demand forecast and planned purchase has made the garments lose their bargaining power with their suppliers for better quality and price.

3.3.1.5 Demand Projection

Six out of nine garment producers have replied that their purchasing procedures are not assisted by demand projection and marketing researches (see table 4.5). They have said that lack of big orders for their products and nepotism and corruption at supplier tanneries make any demand projection efforts meaningless. Therefore, they have decided it isn't necessary to put in place demand projection of leather supply.

While two companies has said they don't have any demand projection because previous demand projection efforts turned out to be wrong, only one replied that it has found the demand projection of its purchasing department efficient and correct.

The following are implications for lack of demand projection in the purchasing process:

Inability of the garment manufacturers to have demand forecast in their purchasing process to determine the quality and quantity of leather input is a disadvantage for the following reasons.

1. They are not able to estimate their yearly budget for procurement of leather and adjust their financial status to cover expenses. This has caused a big planning gap in both their annual operational plans and future strategic plans.
2. There is considerable wastage of time and resources in the search for leather when orders for jackets are received from foreign distributors. And owing to the scarcity of supply and longer negotiation period with tanneries, it significantly affects delivery time and weakens relationships with product distributors.
3. It could make the garment manufacturers unable to adjust their financial status for any price eventualities in input procurement.

Lack of demand forecast in their purchasing process, also makes the companies more vulnerable to price hikes and results in financial constraints in light of the steadily increasing price of finished leather. This assertion could be validated by the spike in the price of finished leather in the last three years. The price of finished leather has climbed by more than a 100% in the last three years (from 9 Birr/Sq. feet to 19 Birr/Sq. feet) and has hurt the competitiveness of Ethiopian jackets in European markets.

The high cost of leather has made the products of the garments more expensive in European leather trade fairs they have participated in, where they were unable to compete with Chinese, Turkish and Indian products (Survey result, 2008).

3.3.1.6 Performance Evaluation of the Purchasing Process at the Garments

Study findings show that six of the nine companies have assessed their performance of leather purchasing activity as 'not efficient' while two have said their purchasing process does a satisfactory job of securing good quality leather with a competitive price. Only one said it can't say whether the purchasing process is good or bad.

The six garment producers which assessed their purchasing process as “inefficient” attribute their inefficient activity to the following reasons.

1. Fatigue from lengthy negotiations with tanneries leading to purchase of high priced but low quality leather.
2. Longer time and money spent on securing leather supply (it includes “commission and incentive” paid for information, selection and loading procedures at suppliers.)

Strong family ties have been seen in the management of seven of the garments thus, the connection between family involvement in the purchasing activity and its impact on the process has been analyzed.

The findings of the study indicate that collective and slow decision making process by stakeholder family members at two companies adds more bottleneck to an already slow purchasing process. Five companies said family involvement in the purchasing has had a little impact on the process. Only one said that no family interference takes place due to corporate nature of the company. One producer didn't respond to the question.

The following statement is given by two expert informants on the traditional practice of the garment manufacturers in their leather purchasing process.

“Such a slow and corruption-vulnerable purchasing process is one reason why foreign market penetration is so difficult for our garment industries. Efficient production and timely delivery are important in the export market and any foreign company that wants to engage in partnership with these garments would be concerned of traditional approaches in their buying practice.” (Source: compiled from interviews with two leather experts, 2008)

Lack of modern management practices in the purchasing process could have a negative impact in the entire production and distribution and timely delivery and hurt

competitiveness of their products. Slow, bureaucratic and multi member purchasing process make part of the entry barriers into foreign markets.

3.3.2 Selection of Suppliers

Selection of supplier was one of the main areas of the exploration. The following table presents the garment companies' criteria to select their suppliers.

Table 4.4 Supplier Selection Criteria of the Garments

| Respondents | Selection criteria in order of importance |
|-------------------------|--|
| 5 garment manufacturers | <ol style="list-style-type: none"> 1. Business relation with the tannery 2. Better quality of leather 3. Business practice of the tannery 4. Administrative efficiency of the supplier |
| 4 garment manufacturers | <ol style="list-style-type: none"> 1. Better quality of leather 2. Credit facility 3. Business partnership 4. Reputation of the tannery |

Source: Own Survey, 2008

* Responses are placed from high to low significance in the decision

Table 4.6 shows that selection criteria of the garments are quite varied. For five of the companies, business relation with the tannery and quality of leather are very important in their selection of suppliers while better quality of leather and credit facility are the most

important criteria for the remaining four respondents. Interviews with leather consultants have revealed that scarcity of leather is the main reason for the garment producers to prioritize good relationship with tanneries over strict quality standards. The relationship is an arm's length at all the nine garment producers where the needs of the leather garment producers are totally not considered in the production and marketing plan of the tanneries.

Since switching costs from one supplier to the other are very low due to mostly similar quality of leather and services (only reject quality is up for local sale at all tanneries and no attractive services), no long term relationship, learning and networking opportunities are present.

However, the companies prefer to maintain personal relationship with insider informants at the tanneries and management staff for preferential treatment during leather purchase. However, interviews with industry experts and consultants confirmed that making quality of leather top selection criteria is not practical in the current situation. This is due to the fact that the garments do not usually provide big and early orders (or provide them in very smaller quantities) and the suppliers do not strive to ensure that the specifications are met due to small orders and export oriented strategy.

In this arm's length relationship between the buyer and the supplier, the garment producers suffer from non-price vulnerabilities like quality and reliability of delivery which mostly arise from poor performance of the suppliers. Scarcity of leather has forced the garments to buy leather without proper inspection of the stock at the supplier's warehouse to deal with assessment of quality once the stock is secured.

Such practices that arise from scarcity of leather have highly compromised the quality of leather used in garment production and made the garment companies incur financial loss. Apart from deteriorating leather quality, color quality and thickness inconsistency problems are also noticed in the purchase of leather.

Generally, supplier selection criteria is dictated by the supplier and less emphasis is given for better quality of leather and timely delivery issues and more focus to maintain good

relationship with suppliers. Since the suppliers fully govern the supply market, the garment manufacturers have no choice but to settle for the quality, quantity and delivery time set by the suppliers. Hence, the scarcity and low quality of leather has forced the garment companies to prefer maintaining good relations with suppliers than prioritizing quality, quantity, delivery and sustainability of the leather supply.

Maintenance of good relations with the tanneries has come as a result of the tanneries' growing tendency to reject purchase orders from garment producers they consider "unfriendly" while they maintain "better relations" with others and give them preferential treatment.

The above stated observation entails a strong negative implication in the vertical integration prospects (in the domestic leather garment chain) as relations in the supply chain are not aimed at strengthening the domestic supply chain and compete in the global garment trade with better quality products.

3.3.3 Evaluation of Suppliers

Seven of the nine respondents have rated the performance of their finished leather suppliers from bad to very bad and extremely unprofessional. Interview with owners of seven garment companies found that their suppliers extend "no special treatment and services in their business dealing while only two said their suppliers "sometimes" give them credit services.

Only two respondents enjoy transport delivery services but not on constant basis while seven confirmed there are no transportation services provided. Two companies replied that they get both credit and transportation facilities but the service doesn't materialize on a constant basis.

Five garment companies have replied that their constant requests for better services have always gone unanswered. Seven manufacturers have said that lack of credit, transportation and other administrative problems at their tanneries have totally eroded their hope of getting a dependable finished leather supply.