

Flying Geese in Ethiopia's Leather Industry? Understanding Asian/Chinese Impact on the Leather Value Chain in Ethiopia

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Preliminary Findings Not For Circulation

Understanding China's Impact on Ethiopia's Leather Sector

Motivation | Questions | Method | Results | Next Steps

The Team at Chinese Tannery in Ethiopia



It' seems so important. I bet somebody would give us money to figure out what is happening!

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Please Remember

- Preliminary Evidence
- CEPR/DFID Exploratory Grant
- Goal Today
 - Background
 - What we know and don't know
 - Directions for future work
 - Perfect timing for feedback

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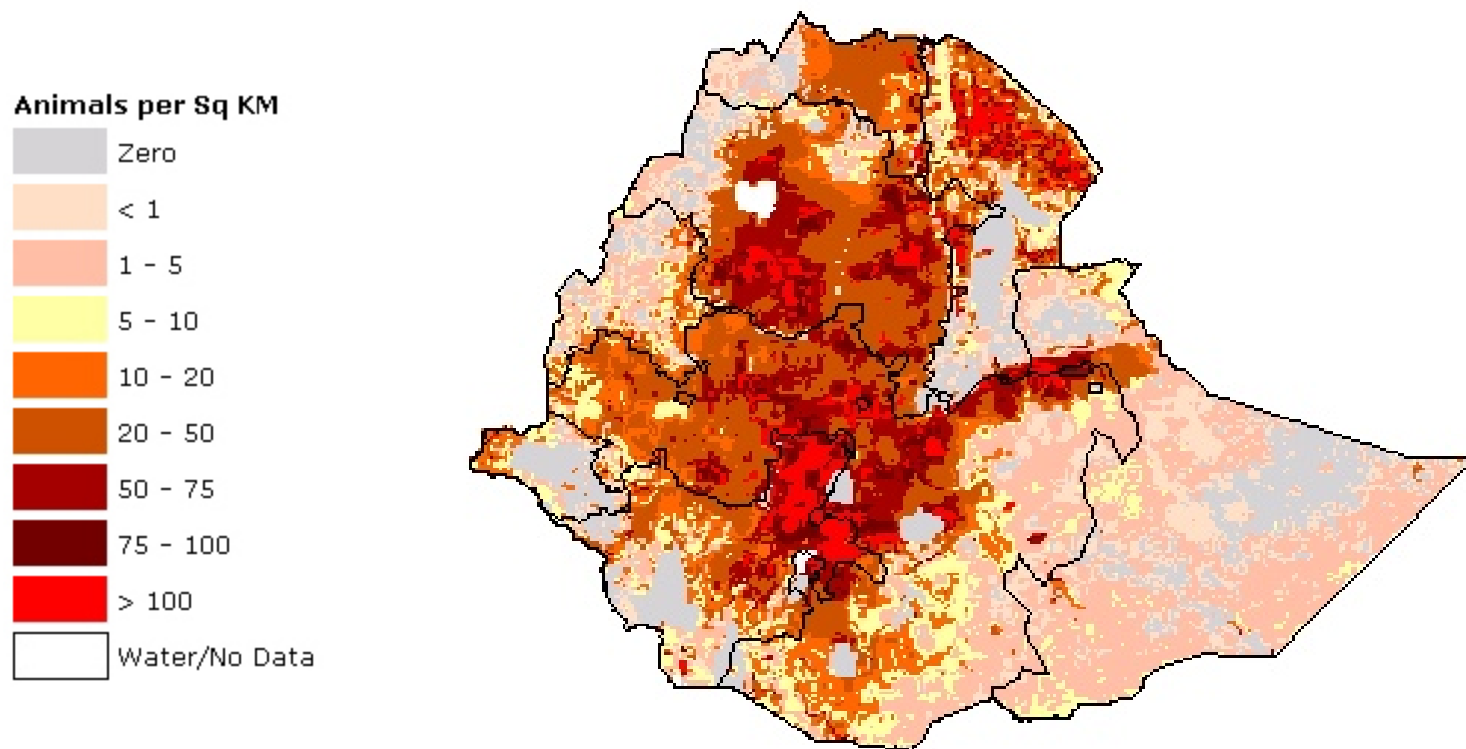
Key Facts

- Leather/Livestock Sector Tremendously Important
- Livestock/Leather Enormous Untapped Potential
- Nature of China's Involvement Complex
 - Imports thought to be a disaster but many domestic firms recover
 - Concerns that Foreign Investors Squeeze Out Locals
 - Foreign Investment Could Help Upgrade Industry
 - Investment in Manufacturing Marks a Shift
- Timing of Foreign Investment Lends Itself to Evaluation
 - Important for Ethiopia
 - Also Relevant for Other Recipients of Chinese FDI

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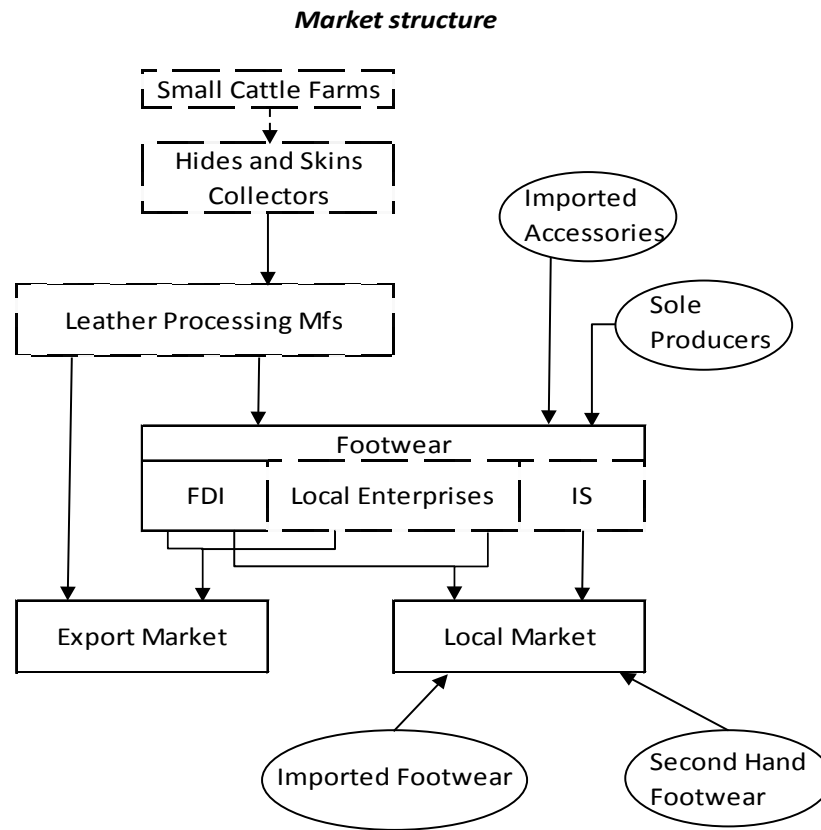
Livestock Population of Ethiopia One of Largest in World



Disease, Demography and Institutional Development

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Leather Value Chain's Enormous Potential



Small Farms: 65.5 million ha/
90,000,000 heads

Hide & Skins Collectors: about
1,500

Leather Processing Mfs: 24
FDI: 9/24

Formal Footwear Mfs: 15
FDI: 6/15

SMEs: 1,000 +

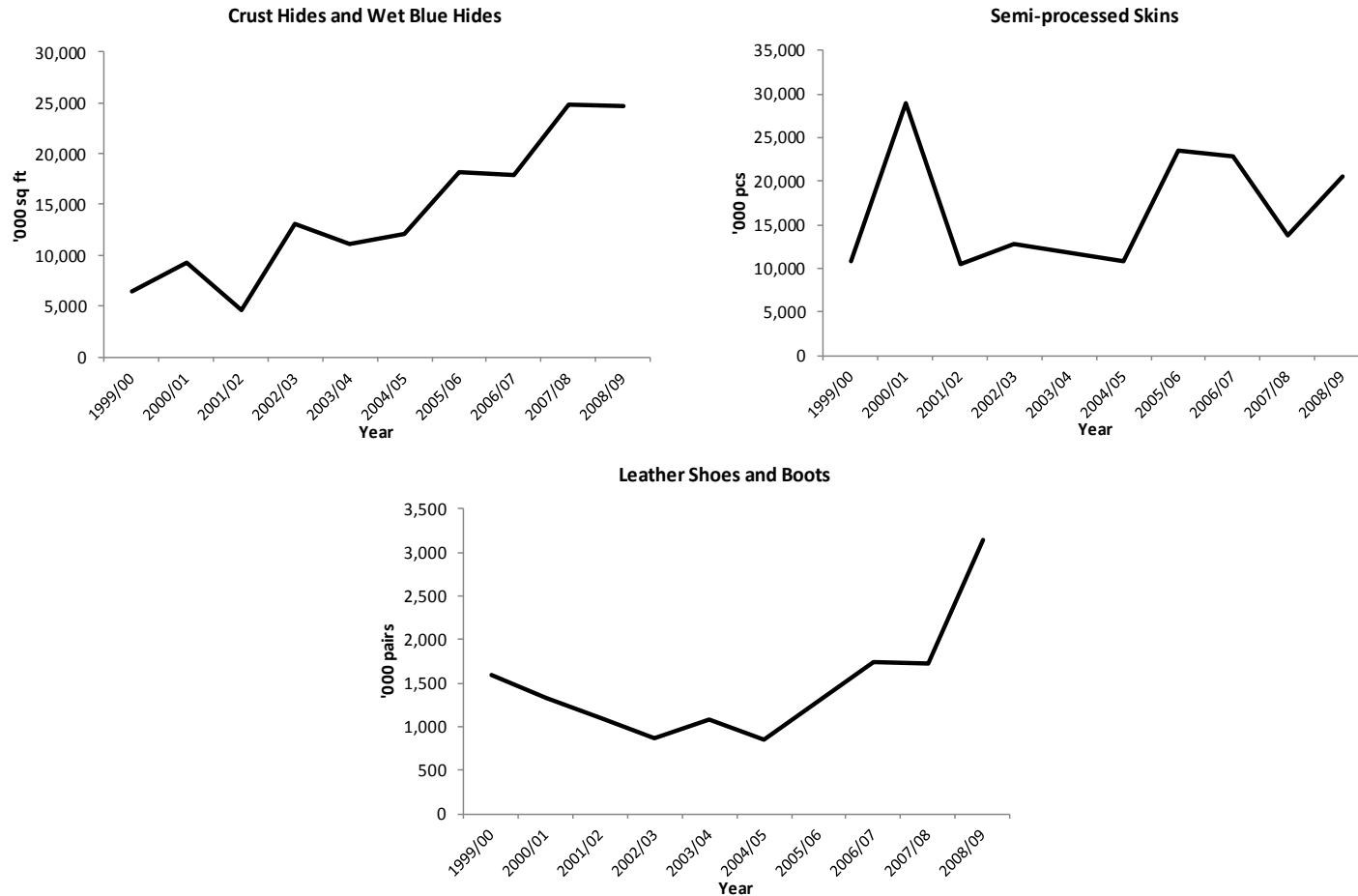
Notes:

- i) FDI – Foreign Direct Investment Enterprises; IS – Informal Sector
- ii) Dash line (- - -) indicates a weak linkage, lack of organization, and areas where technical support is required to help strengthen linkages along the supply chain

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Output of Raw Hides, Processed Leather and Shoes

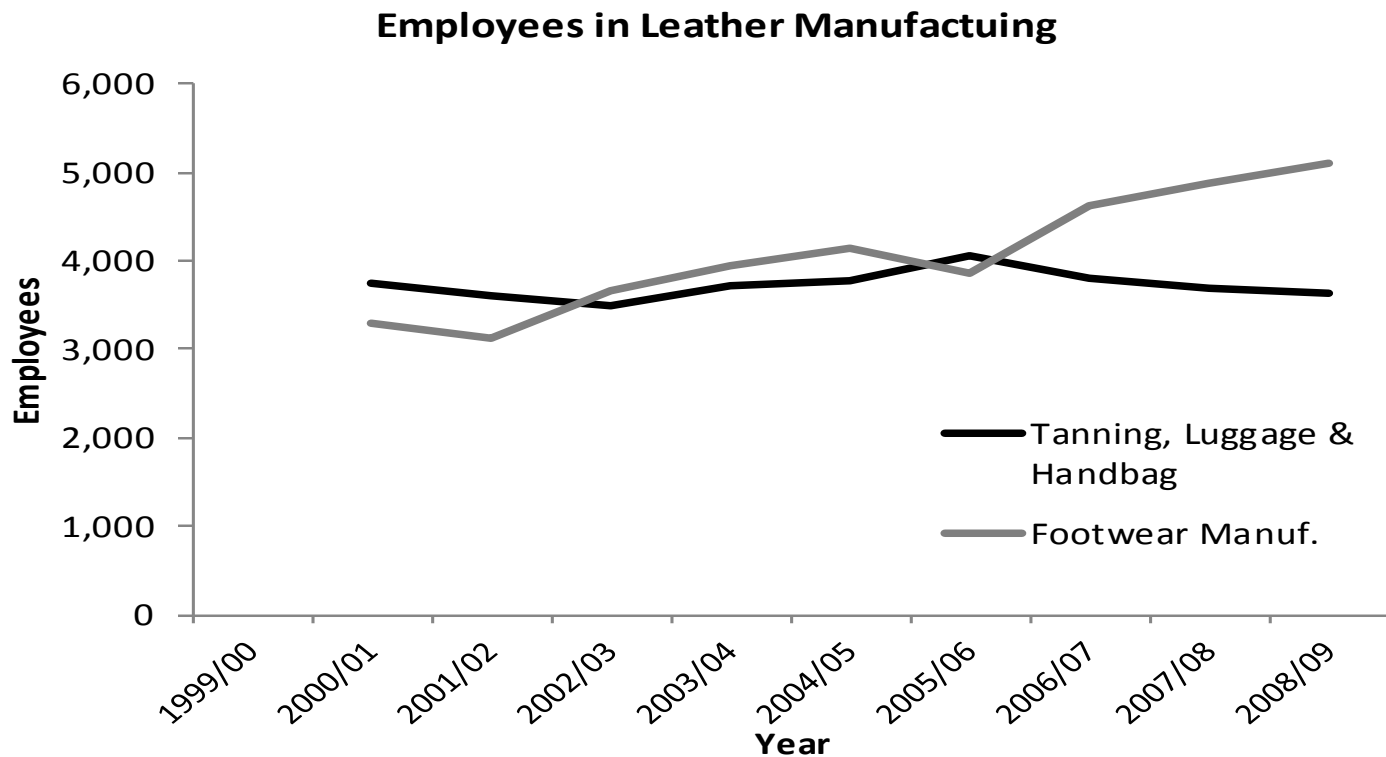


Source: Central Statistical Agency of Ethiopia, Ethiopia MoFED Annual Report, National Bank of Ethiopia Annual Report (various years)

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Formal Sector Employment

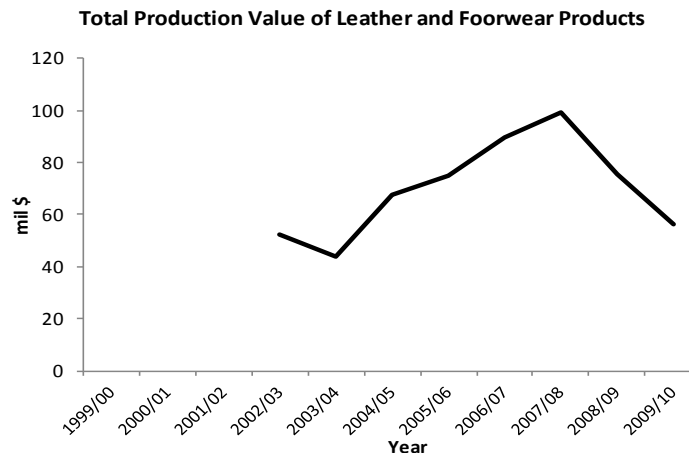
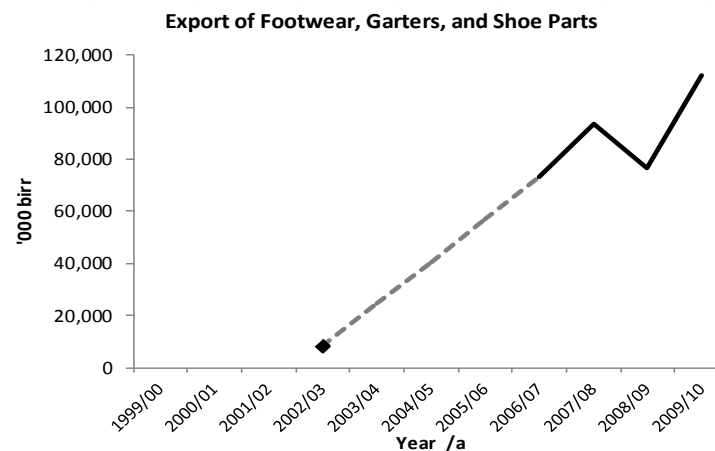
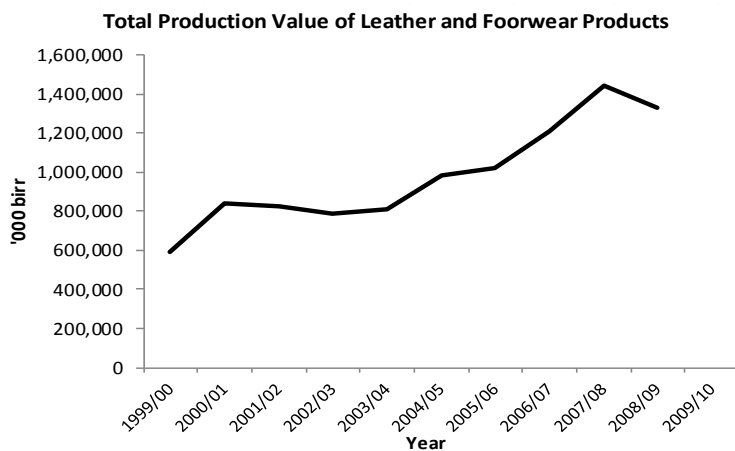


Source: Central Statistical Agency of Ethiopia, Ethiopia MoFED Annual Report, National Bank of Ethiopia Annual Report (various years)

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Production and Exports



Note: /a Based on calendar year

Source: Central Statistical Agency of Ethiopia, Ethiopia MoFED Annual Report, National Bank of Ethiopia Annual Report (various years).

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Market & Employment Potential

Table 57: Snapshot of Leather Sectors in China, Vietnam and Ethiopia, Tanzania and Zambia

Key Comparative Indicators	China	Vietnam	Ethiopia	Tanzania**	Zambia
Total Imports (Value - US\$1,000)	\$ 429,529	\$ 6,474	\$ 620	\$ 1,199	\$ 13,304
Total Exports (Value - US\$1,000)	\$8,305,873	\$2,322,047	\$ 3,701	\$ 941	\$ 2,363
Companies Operating in the Sector (by size)					
Small	40.0%	47.4%	98.6%	55%	50%
Medium	27.0%	24.3%	0.8%	18%	30%
Large	33.0%	28.3%	0.6%	27%	20%
Estimated Number of Workers*	2,702,142	632,266	7,600	1,000	600
Male	55.0%	18.0%	56%	58%	75%
Female	45.0%	82.0%	44%	42%	25%

* Trade data refers to leather upper footwear only

** Year 2008 figures in the case of Tanzania. Does not include micro and small firms with less than 10 employees.

Global Development Solutions, LLC from interviews and national statistics. Trade data from Comtrade.

Many Government Policies Targeted at Industrialization of Leather Sector: Changing Over Time

- Derg Period: Ban of Export of Raw Hides
- 150% export tax on semi-processed leather (wet blue) – 2008
- 150% export tax on unfinished leather (crust) -- 2011
- Leather Export Products Made a Priority Sector
 - Income Tax Breaks (2 to 8 yrs holiday) for Investors
 - Land at reduced lease rate
 - Cost sharing scheme for foreign experts
 - Building for small shoemakers + technical assistance
- General incentives: duty drawback scheme

Ethiopia Competitive but Inefficient

- No commercial livestock sector
- Relative to China and Vietnam
 - Absenteeism high
 - Wastage high
 - Unused capacity
- Unit cost in Ethiopia still lower than in China!
- Higher than Vietnam but Vietnam does not have raw inputs

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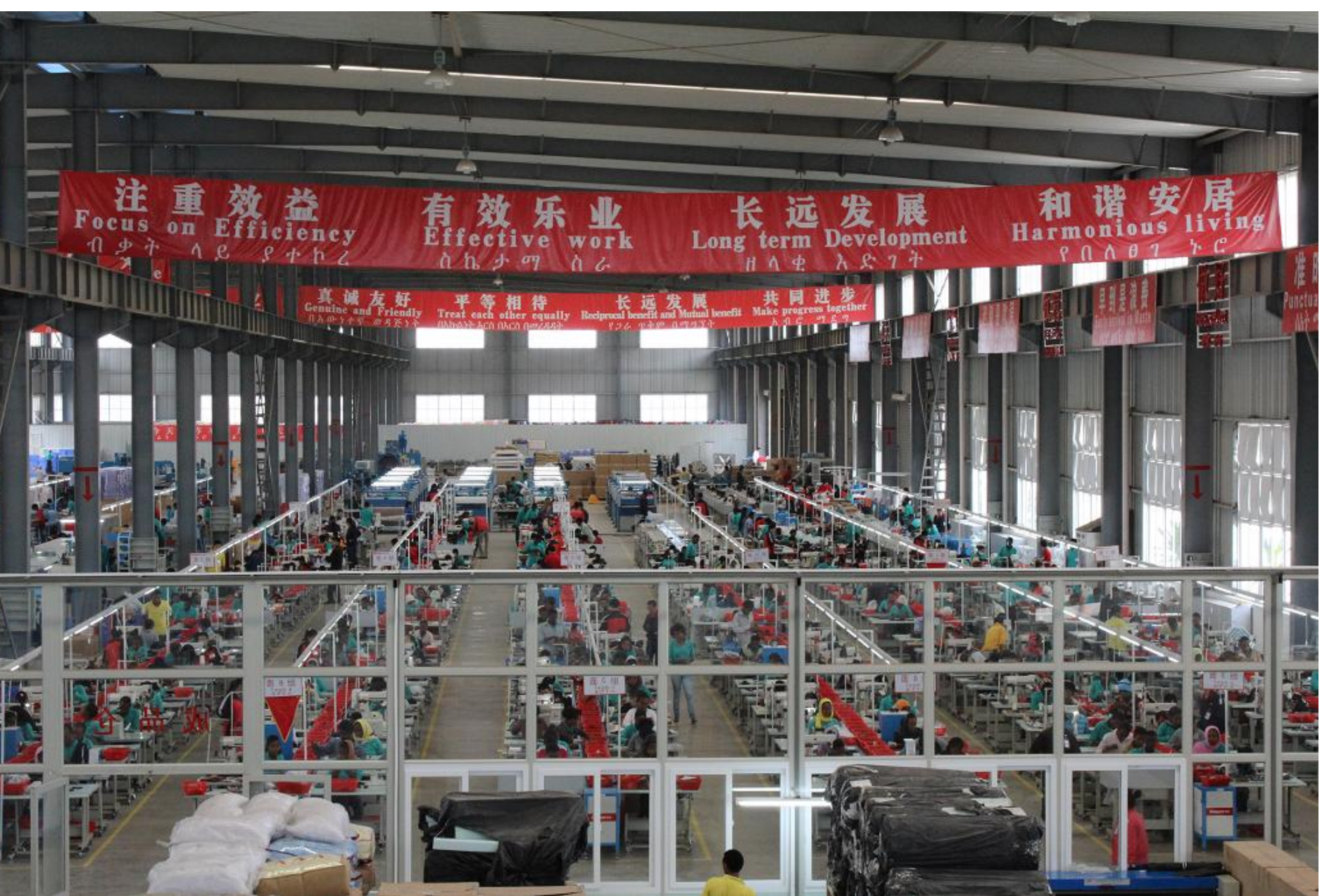
Increased Foreign Investment in Ethiopia

2004	2005	2006	2007	2008	2009	2010
0.43	4.93	23.95	13.28	9.71	74.29	58.53

Source: Ministry of Commerce, "Statistical Bulletin on China's Outward FDI 2010."

Note! Planned investment by one Chinese factory alone is upward of 2 billion USD.

But we all know numbers can be misleading ...



Huajian Shoe Factory : Shoe Assembly Line



Huajian Shoe Factory Assembly Line: Close Up



China Africa Overseas Tannery

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Summarizing

- Leather Industry in Ethiopia Has Significant Potential
- Leather Industry is Inefficient and Technology Outdated
- Foreign Investment Seems to be Taking Off
- Foreign Investors Could
 - Improve Technology All Along Value Chain
 - Train Workers
 - Employ Workers
- Foreign Investors Could Also
 - Operate in Isolation
 - Destroy Small Businesses
 - Grab the Hides and Run

Two Broad Questions

- How active are the Chinese in the leather value chain in Ethiopia?
- Are Chinese (foreign) firms operating in isolation or are they integrating with Ethiopian firms and people?
 - Is there any evidence that trade has led to investment ?
 - What has been the role of government policy so far ?

Semi-Structured Interviews : Goals

- Snowball Technique
- Determine Extent and Nature of FDI
- Get a Better Sense for Interactions between Foreign Investors and Locals
- Determine Whether Follow On Project Worthwhile

Semi-Structured Interviews : Timing

- Exploratory Grant Funded April 2012
- Ethiopia Fieldwork June - July 2012
- China Fieldwork August – September 2012
- Deborah Brautigam
- Tang Xiaoyang

Semi-Structured Interviews : Sample

- Interviewed Formal Sector Leather Processing Firms
 - Tanneries
 - Foreign and Local
 - Members of
- Did not Interview
 - Owners of Livestock
 - Small Shoemakers (around 1,000)

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Census: Ethiopian Leather Industries Association Members

	Members/ Interviewed	Ethiopian Firms Interviewed	Indian & Chinese Firms Interviewed*	Other Foreign Firms Interviewed*
Tanneries	24/21	13	6	2
Leather Products & Shoes	15/12	7	2	3
TOTAL	39/33	20	8	5

* Includes firms that have applied for membership. Chinese & Indian firms include joint ventures

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Initial Census/Survey of Asian Linkages										
	N	% with current Asian empl.	Business trips to China % **	Business trips to India %	Import supplies from China %	Import supplies from India %	Buy machinery from China %	Buy machinery from India %	Use Chinese TA %	Use Indian TA*** %
Ethiopian Firms	20	15%	85%	50%	65%	20%	20%	10%	5%	100%
Foreign Firms (non Asian)	5	60%	80%	20%	60%	20%	40%	20%	60%	0%
Asian Firms*	8	100%	100%	0%	63%	0%	63%	0%	63%	0%
TOTAL	33									

*Includes joint ventures with non-Asian partners

** % of firms answering yes

*** Includes TA provided by Ethiopian government program twinned with Indian institutions, and TA purchased from other firms.

[These statistics may be underreporting linkages. Not all firms may have been asked this question. Firms still under construction may not be importing supplies yet.]

Leather Processing: Linkages

- Increased exports and imports and some evidence that trade has led to technical assistance from India.
- ALL of the Chinese and Indian investors in tanneries had previously purchased output from local tanneries
- Reported that purchases by these tanneries was driving up the price of raw hides – good for farmers/bad for local tanneries
- Personnel movement is modest
- Complaints that government policy aimed at upgrading the industry has favored foreigners who have access to capital and better technology

Leather Processing : Technology Transfer

- Ethiopia's Leather Industry Development Institute (LIDI) partnered with two Indian government institutions, to improve its' technological knowledge of the leather industry in 2011.
- Indian experts were sent to 11 tanneries in Ethiopia for benchmarking studies. Each factory got 3-4 experts for 1 year. Results are mixed.

Leather Processing: Future

- Friendship Tannery (Chinese)
 - Plans to develop regional processing center
 - Leather from Mali, Sudan, Cote d'Ivoire, Somaliland etc.
- Three Chinese tanneries and two Indian tanneries have promised to build glove or shoe factories in Ethiopia
 - Not yet realized
 - Concerns about investment environment
 - Concerns about ability to meet international quality standards

Leather Processing : Summary

- Significant investment in tanneries by foreigners
- Foreign investment in leather processing appears to have squeezed out some locals (problems are credit, technology, quality)
- Some evidence of training
- Significant complaints about foreign competition in leather industry (not so in shoe industry)
- Government policy reducing firms ability to export unprocessed leather is partially responsible

Manufacturing of Leather Products: Linkages

- For a few years, there was competition in output market between local shoemakers and Chinese imports
- Currently the market appears to be segmented:
 - Foreign firms export ladies shoes
 - Local firms produce men's shoes for export and local market
- None of the local shoe companies we interviewed hired foreign experts in the recent past.
- One company (Walia) sent 5 technicians to their main client Indian TATA group for training.

Manufacturing of Leather Products: Linkages

- Hong Kong company New Wing, which has two production bases in mainland China, bought a factory in May 2011 and began operation in Sept 2011.
 - Previously NW was outsourcing to Anbessa.
 - Employed 300 local workers in July 2012.
- NW and Huajian are working on OEM orders from USA and Europe [Guess, Tommy Hilfiger & others].
 - Products 100% for export
 - Both are producing exclusively lady's shoes,
 - Both source leather supply locally.
 - New Wing depends more on local supply and wants to establish its own tannery for refined processing.

Manufacturing of Leather Products: Training

- Huajian , located 35 km away from Addis, trained its own staff, most of whom are newly graduated college and high school students.
- The company is planning to send 300 workers to China for further training .
- The company is teaching shoe-making skills to 200-300 local individuals outside of the company as part of a Corporate Social Responsibility Program.

Manufacturing of Leather Products: Training

- The British tannery has established a glove-making factory and brought their agent in China to train the Ethiopians in production skills.
- The Chinese agent also intends to shift his own glove factories in China to Ethiopia through this cooperation in order to take advantage of the low labor cost.
- A German glove maker as well brought technicians from its branch in China to train Ethiopians in their experimental factory in Gondar.

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Manufacturing of Leather Products: Future

- China's Huajian Group has signed an MOU with the China-Africa Development Fund to invest 2 bn usd in building a shoe production base in Addis during the next five years
 - Note that Huajian Group built a factory in the Sino-Ethiopia Economic Cooperation Zone and began operation only 4 months after its' president visited Ethiopia for the first time in September 2011.
- Cheap labor and access to raw materials are the main reason for this investment.
 - The company has 24,000 workers in China, average monthly wage is 2000-3000 RMB (300-450 usd),
 - In Ethiopia they pay local workers only 600 Birr (35 usd) per month.

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Manufacturing of Leather Products: Summary

- Chinese have started to invest along with Indians, British and Germans – these are large firms.
- Most foreign firms still in nascent stage.
- Training by Chinese takes place within foreign firms
- Domestic firms getting some TA from Indians
- However some smaller shoe factories losing out as foreigners set up their own firms and competition for hides increases
- Policy has played a role in bringing small firms together but impact is unclear
- Potential for significant future investment , technology transfer and jobs

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Finishing Up and Future Work

- Write up results to complete commitment to CEPR/DFID for funding exploratory grant
- Clearly significant scope for additional research:
 - Big picture welfare analysis a la McMillan/Rodrik Cashew Industry Analysis – Include Owners of Livestock
 - More substantial baseline survey that includes small firms
 - Timing is right since industry is just starting to change (note in Ethiopia, 98% of firms still small while in China much wider dispersion in firm size)
 - But if baseline survey, need to sharpen the questions
 - Technology transfer?
 - Impact of government policy?
 - Impact on employment? Market access?