Challenges for the Indian Leather Industry in the next decade

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Indian Leather Industry

1. Average growth over the last 12 years is 6%
2. L&LP average growth over the last 10 years is 4.6%
3. If we factor in inflation, growth is negligible
4. Growth of China, Vietnam & Indonesia has been more than 10% per year

India’s Leather Exports

Animal	Percentage
• Goat	60
• Cow	20
• Buffalo	15
• Sheep	3
• Others	2
Total	100

Average price per sq.ft is $1.60

Structure of the Industry

1. Economy of Scope / Economy of Scale
2. Hardly any listed companies. Mostly Family owned
3. Raw material availability is inelastic
4. Moderately Capital intensive

Structure of the Industry

Economy of Scope / Economy of Scale

1. Most Indian companies operate on economy of scope in niche products, with low capacity < 200000 ft per month
2. Problem arises when they want to grow
3. No studies reg. issues of shifting from economies of scope to economies of scale
4. Factories doing well collapse when they shift to economies of scale

Structure of the Industry

Economy of Scope / Economy of Scale

5. Margins are not linear
6. Value addition is not the same in all segments
7. Break-even-point shifts up

Solution:

1. Prepare a detailed project report
2. Outsource extra production to test model
3. Shift to in-house only if results achieved

Structure of the Industry

Family Owned Companies

1. Growth very slow since internal cash generation is the only avenue for growth
2. Listing co's can bring in cash for quick expansion eg. Textile Industries
3. Can also consider Private Equity
4. 3 year planning required for becoming a listed company
5. Performance of few listed co's has been very poor. Focus was only to unlock value and not for growth. Minimum size 100 Cr

Structure of the Industry

Raw Materials Available

1. Availability is inelastic worldwide
2. Industry has complicated matters by having too many variants
3. Origins /size/animals/products
4. Strategy of buying pack but selling wet blue is not used effectively
5. European tanneries plan on fixed and consistent source of raw material from slaughter houses

Structure of the Industry

Raw Materials Available

Solution:

- Reduce RM variants to 2/3 only
- Ensure all variants add value
- Fixed price contracts
- Holding cost must not erode margins by more than 50%

Structure of the Industry

Capital Costs

1. Machines can
   a) Improve quality
   b) Increase production / productivity

2. In most co's – Capital Expenditure is much below depreciation. This results in low technology & inability to keep up-to-date

Environment

1. Tanning is a Core red Industry (one of 14)
2. Not desirable in most countries, since they can import
3. Industry is not proactive to environmental issues, only reactive. Eg. Coke announced that they will not use groundwater from 2009
4. Need to fund research for solid sludge and recycling 70% water
5. Need to reduce water usage by 50%. India is a tanning hub. We must therefore lead the world on environment issues

Technology

1. Production in the industry has declined. Therefore new technologies in last 5 years are negligible
2. Focus on technology is reducing manpower
3. Issues like yield increases process time and quality. Chemistry not addressed adequately
4. Far East manufacturers focus only on copying and making low cost machines
5. Critical areas are
   1. Machinery
   2. Chemicals
   3. Water
   4. Process time

Our industries must focus on how to use heterogeneous raw material & make it homogenous before bulk operations

Threats from Synthetics

1. If leather prices are >0.50 – 0.75 $/ sqft compared to synthetics, then we are okay
2. Industry does not track Synthetics and its prices
3. This could cause sudden problems in Prices especially in low end products
4. Marketing strategy does not address how to beat Synthetics – more colours, textures, things that machines cannot do easily
5. We can predict …. Cow – Suede – Sheep – Goat –synthetics cycle

Value Addition

1. While we add value in high end products upto 25% we are devaluing many low end products
2. Need to calculate value add in each product segment. Get rid of segments that do not add value
3. Options available are to sell wet blue and offer extra capacity for job work
4. Focus marketing efforts on low value adding products to atleast cover full overhead costs

New Markets

1. Our leather industry today focuses on China and Europe
2. As an industry they should be atleast four key markets for leather with a minimum of 10% share from India
3. Clear marketing plan and focus by all companies to get this market share
4. Greater focus on leather for women shoes
5. New segments like upholstery to be targeted
6. Important to have a mix of Dollar / Euro markets. Eg. Pittards failed because they did not do this well

New Products

Economy of Scope

1. For companies working on economies of scope need for innovative high-end products every season
2. Important to target 30% sales from new products otherwise PD is not effective
3. New Products must be able to fetch 0.25 – 0.50 $ higher price. Product life cycles are short and one should be able to get the advantage at the beginning

New Products

Economy of Scale

1. Focus should be on producing leather below $2 / sqft for upper leather and $0.90 - $1 for lining
2. Build capability to sample large quantities and scale up quickly
3. Raw materials stock essential for this
4. New products should target the commodity products in the Cow range
5. Increase new products when cow prices are high to tempt customers with substitutes. This is important for Goat and Sheep

Conclusion

1. Industry will not grow more than 5% unless the structure of the industry changes
2. Environmental issues could have major impact and a fall back plan for each type of problem should be prepared (what if?)
3. Industry must focus on uniformity in commodity type products so that many companies can sell the same product
4. Unless value addition increases by 3-4% yearly they will not be able to survive
5. Growth can be mainly in new markets rather than in China and Europe
6. If business from new products < 30% industry will not grow

Thank You