

# A STUDY OF CHALLENGES FACED BY INDIAN LEATHER INDUSTRY IN DOMESTIC AND INTERNATIONAL MARKET (2017-18)

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## ABSTRACT

**Leather Industry is one of the export oriented industries in India having an annual turnover of US \$12 billion (approx.). The Industry occupies a prominent place in Indian Economy due to its substantial export earnings. Like any other Industry there are certain internal and external factors influencing the domestic and export performance of Indian Leather Industry. Through this paper an attempt has been made to examine the impact of major variables/factors affecting the export performance of leather and leather goods, using secondary data sources. This paper also tries to examine the strengths and weaknesses of Indian Leather Industry through SWOC Analysis and PORTERS FIVE FORCE Model covering two major cities famous for leather manufacturing and exports, i.e. Kanpur and Unnao districts of Uttar Pradesh, India.**

## INTRODUCTION

Leather is one of the most widely traded commodities in Global Market. The growth and demand for leather is driven by fashion industry specially textile, footwear, furniture and interior design industries.

India is the fifth largest exporter of leather goods and accessories in the world. India is one of the largest leather footwear manufacturers exporting around 10-15 percent of the output. Almost 65 percent of the shipments are to Europe. According to Council of Leather Exports only 50 percent business is in exports, while the rest is served in domestic market. Council also said that the industry is expected to touch around \$27 billion by 2020, and the domestic business would be around \$15 billion<sup>1</sup>.

India is the third largest global supplier of Leather Garments which is only possible through easy availability of quality raw material coupled with skilled craftsmanship. Major brands like Zegna, Marco Polo, Armani, Abercrombie & Fitch, Mango, Andrew Maarc and Guess source Leather Garments from India<sup>1</sup>.

The major markets for Indian Leather Garments are Germany with a share of 23.23%, France with a share of 11.55%, Spain with 12.17%, Italy with 10.07%, USA with 9.45%, UK with 6.68% , Netherland with 3.77, Denmark 4.49% and Canada 2.19%.

## EXPORT HIGHLIGHTS<sup>2</sup>

- In 2016-17, total exports from leather manufacturers were recorded at export value of US \$5325.85 million comprising of Raw Hides and Skins, Finished Leather, Leather goods, Leather garments, Leather Footwear and its components, Saddlery and Harness.
- During April 2016-January 2017, the major markets for Indian leather products were US (15.69%), Germany (11.82%), UK (10.85%), Italy (6.61%), Spain (5.27%), France (5.02%), Honk kong (4.71%), UAE (3.69%), China (3.16%), Netherland (3.01%), Belgium (1078%) and Australia (1.44%).

## **METHODOLOGY**

This study is based on secondary data which has been collected through SWOC Analysis and Porter's five force model of Indian Leather industry.

In this paper, we are analyzing the major weaknesses and challenges which leather industry is facing and their impact on the leather export performance, through SWOC Analysis and applying Porter's five force model.

Through SWOC Analysis we are finding the major challenges and weaknesses which industry is facing and due to which there is a downstream industry's performance. Whereas, through Porter's five force model, we will get the intensity of the external forces on the industry like- the buyers, the suppliers, the competitors and the substitutes.

Through SWOC Analysis and Porter's five force models in this paper we will study the major challenges which the industry is facing and their consequence on the domestic and export performance of the Indian leather industry.

## **OBJECTIVES**

- To study the major challenges and weaknesses of Indian leather industry
- To find out the intensity of the external forces on the industry so as to check the favorable and unfavorable factors for leather industry.
- To find out the ways to convert the weaknesses into strengths and the challenges into opportunities so as to improve the leather export performance.

## **SWOC ANALYSIS OF LAETHER INDUSTRY**

### **STRENGTHS**

1. Existence of more than sufficient productive capacity.
2. Easy availability of low cost labor.
3. Large raw material base.
4. Exporter friendly government policies.
5. Exposure to export market with well established linkages with buyers in developed countries like EU & USA.
6. Continuous emphasis on product development and design up gradation.

### **WEAKNESSES**

1. Low level of modernization and up gradation and integration of developed technology is very slow.
2. Low level of labor productivity due to inadequate training and unskilled labor.
3. Horizontal growth of tanneries with less number of organized product manufacturers.
4. Little brand image.
5. Unawareness of international standards by many players as many of these are SMEs.
6. Highly unhygienic environment.
7. Weak support infrastructures for exports.

**OPPORTUNITIES**

1. Abundant scope to supply finished leather to multinationals setting up shop in India.
2. Product diversification- There is lot of scope for diversification into other products.
3. Growth of international and domestic markets.
4. Exporter friendly government policies for promotion of leather sector.
5. Increasing international and domestic markets for garment and fashion accessories.
6. High growth potential on exports, the ready availability of leather, the abundance of essential raw materials and rapid strides in the areas of

**CHALLENGES**

1. Production in the industry has declined due to unfavorable government policies and environmental issues.
2. There is stiff competition from other countries like China, Indonesia, Thailand, Vietnam and Brazil which are more competitive than India; So as an industry India should have atleast four key markets for leather with a minimum of 10% share.
3. Indian leather industry is also facing a lot of problems in adapting fast changing fashion trends.
4. Challenges from synthetics.
5. Perpetual dependence on western markets.
6. Inelastic supply of raw materials.

**PORTER'S FIVE FORCE MODEL**

As we apply Porter's five force model for Indian Leather Industry, we will get the following results-

1. Competitive Rivalry: Is very high, as the structure of industry is Oligopoly and there are number of equally balanced competitors in the market who are producing the same luxury leather products.

There are already many good brands; especially some famous big companies have their brand equity and impressive brand stories with which they have already captured a greater market share. E.g. Louis, Gucci, Chanel etc.

Leather and leather goods are niche market products, so the goods need to be distinguished enough which influence the customer's view towards the brand.

2. Bargaining power of buyers: The buyers of this industry have low concentration and the bargaining power of buyer is weak. The bargaining power is weak when the target customers have high brand loyalty and they tend to have high emotional switching costs which decide their consuming behavior towards one brand.

As leather products are basically niche market products and are uniquely designed and customized and buyers have lesser knowledge about the market price and the demand thus, bargaining power of buyers is poor and weak.

3. Bargaining power of suppliers: The leather and leather products are highly expensive and are specifically designed for niche class so the bargaining power of the suppliers is very strong.

4. Threat of substitute: There are many substitutes of leather and leather products present in the market at lesser prices like-

- Faux Leather: Unlike earlier substitutes like rexine, many of these modern materials have luxurious look and feel. These materials are made of fabric and plastic.
- Cork Leather: The material is made from the bark of cork oak tree.
- Microfiber: Some companies create this material using industrial scrap polyesters and so on. Vegetan is one of the trade names for microfiber that is made to resemble leather.
- Ocean Leather: This is another substitute that look and feel like leather and is called as ocean leather because it is made from kelp, which is large seaweed.
- Canvas or Textile: When some fabrics or type of canvas can be made to resemble leather, they are great looking stylish and cruelty free choices even when they don't resemble leather.
- Vinyl or PVC: Polyvinyl chloride is widely used in alternative, punk or Goth fashion segments because of its closer resemblance to leather.
- Other natural materials

5. Threat of new entrant: As there are many companies with a brand name in this industry already having a huge market share, it makes very tough for the new entrants to enter into the market and capture the market share.

It also requires a huge capital to enter the industry and to make up the brand equity.

So, from Porter's five force model we can conclude that

Porter's five forces	Intensity
Threat of new entrant	Medium
Threat of substitute	High
Bargaining power of buyer	High
Bargaining power of supplier	Low
Competitive Rivalry	High

## **RESULTS AND CONCLUSION**

From the above analysis, we can say that following are the challenges and weaknesses of leather industry-

### **Weaknesses of leather industry and their consequences**

1. Low level of modernization and slow up gradation of technology: Slow growth and the use of inefficient technology is largely responsible for wasteful use of water and chemicals, high load of effluent pollutants and low productivity of the tanning industry.
2. Low level of labor productivity due to inadequate training and unskilled labor: A large part of labor in leather industry is illiterate and this is the reason they are unaware of technology, the technical knowhow as well as the pros and cons of the methods they are using. Due to lack of adequate knowledge and skills the productivity is also hampered as the workers are not properly trained and educated.
3. Horizontal growth of tanneries with less number of organized product manufacturers: Horizontal growth here means extension of assets and companies of the leather industry at same level without any modification and innovation. Most of the tanneries and leather are Small Medium Enterprises (SMEs) and are unorganized due to which productivity is low and not as per international standards.
4. Little Brand Image: The brand image of Indian leather products is comparatively low than those of its competitors like China, Bangladesh etc. This is one of the reasons of lesser demand of Indian leather products in export market.
5. Unawareness of international standards by many players as many of these is SMEs: This is the main factor which is responsible for the sluggish export performance of leather and leather products as compared to China –
  - Fragmented production base with limited resources for modernization and marketing.
  - Comparatively lower productivity and poor quality consistency, system deficiencies resulting in longer turnaround time for making samples (India- 2,3 weeks whereas china 1/2 days) and longer duration for transport (by sea routes) as compared to china makes the Indian leather industry unfit as per the international standards.
6. Weak Infrastructure: The dominance of household sector and small scale enterprises with very small expansion of production base in the medium and large sectors particularly in tanning and footwear sectors; leather garments and goods sector have all along been in the small scale sectors. Consequently, supporting infrastructure for making production aids and components, particularly for footwear has not grown adequately.
7. Highly unhygienic environment: According to the data of Council of Leather Exports, India has more than 2000 tanneries that produce more than 2 billion sq feet of leather annually making the nation one of the largest exporters of processed leather. But, working conditions inside these tanneries are more toxic than anywhere else. Workers inside these tanneries are exposed to toxic and caustic chemicals and minerals and often suffer

from skin and lung irritation. It is also found that the tanneries do not inform or educate their workers about the chemicals they are using and how to safeguard themselves.

Now, let's discuss about the challenges, their impact and how leather industry can overcome from these situations,

## **CHALLENGES**

**I. Unfavorable government policies and environmental issues:** Even though Leather entrepreneurs are one of the largest foreign exchange earners of the country, they are facing innumerable problems due to banning of slaughter houses, inadequate funds to construct water effluent treatment plants, delay in payment by the buyers, slow process in sanctioning funds by the bankers, unauthorized labor absenteeism, poor quality of equipments and government restrictions.

The new policies framed by the government of India directly affect the functional areas of leather industry. In the name holiness, some powers are trying to implement ban on slaughtering of animals and stringent pollution norms are being adopted by the state and central governments, which are directly affecting the growth. This reflects in the closure of some units and creating unemployment problems especially for semiliterate, illiterate and downtrodden communities.

The new goods and service tax (GST) rates favor multinational sports shoe brands, while it has hit domestic leather product manufacturers who want to grow up in the value chain.

According to Rafeeq Ahmad, former chairman of Council of Leather Exports GST has a negative impact on all leather product categories, as the burden of all indirect taxes will go up under GST. He also concluded that the Leather and leather products are already hit by the restriction on cattle trading and transport of cattle and hide, Exports are expected to fall by around 15% in the financial year (FY) 2017-18 as availability of cattle hide is expected to shrink this year. In FY17 the country exported leather and leather products worth \$6 billion.

Not only government policies there are other environmental issues related to leather industry which has become a major challenge for the industry.

The conventional leather tanning technology is highly polluting as it produces large amount of organic and chemical waste. Most of the tanneries in India cannot afford proper pollution control so they discharge their waste directly into dump sites. For e.g. the city of Kanpur is hub of 350 tanneries and many of this discharge their waste directly into river Ganga. Under some conditions, the trivalent chromium these waste contains may become oxidized to hexavalent chromium, which is highly hazardous to both human and animal health.

Due to significant amount and specific properties, tannery waste is a serious environmental burden. The proper utilization of this waste does not only eliminate the negative environmental impact but also brings benefits such as energy and material recovery.

**II. Competitive rivalries such china, Thailand, Indonesia, Vietnam and brazil:** Indian leather has an strong competitive rivalries due to which Indian leather exporters find it difficult to survive in international market because of its weaknesses.

Other Asian countries like China, Vietnam, Indonesia and Thailand are the major competitors of Indian Leather exporters in global market and seem to give a tough competition just because unlike India, they have a good export manufacturing policy in place which facilitates.

From above information it is proved that the Indian leather exporters have strong rivals in the international market and thus they have to work hard for their survival and growth in western markets (countries).

**III. Fast changing fashion trends are difficult to adapt (Bargaining power of buyers):** In India there are so many barriers that an exporter faces in leather industry within country itself like government policies, lack of funds

and technology etc and with these problems it is very difficult for an exporter to survive or compete in the global market and adapt this fast changing fashion trend.

For e.g. as we all know leather products are niche class products and comes in luxurious goods and the softest, most luxurious leather comes from the skin of new born or even unborn calves, sourcing this leather is unethical and is already banned in Indian market thus Indian exporters fail here in competition with other exporting countries like China, Bangladesh, Vietnam etc. Secondly, Efforts undertaken by manufacturers in terms of innovation and new product design is least or negligible due to insufficient funds and technical knowhow.

Thus, the bargaining power of buyers is high in leather industry because they have other options available in the market at cheaper rates.

IV. Threat of substitutes (synthetic leather): Leather industry is not an eco friendly industry and also the chemicals used for tanning gives out toxic gases and effluent which makes it dangerous place for workers as well. The modern tanning processes not only use loads of energy, water and chemicals but also pollute the land to such an extent that the old tanneries land cannot be used for cultivation as well. Thus, the facts highlight that leather is a significant drain on country's resources.

But on the other hand there is synthetic leather which is eco friendly in nature and cheaper in compare to leather products. For e.g. Faux leather which is made up of artificial materials (PU, PVC), Vegan leather which is a typical bonding of plastic coating with a fabric backing.

So, this substitute is giving a tough competition to leather industry in international market as the synthetic leather is a man made fabric treated and dyed so that it resembles real leather. They are much cheaper and environment friendly than natural leather.

V. Perpetual dependence on western markets: As we already know that leather industry is one of the largest foreign exchange earners of the country and its major markets are Germany, Italy, UK, Spain, France Hong Kong, UAE, etc but being the largest foreign exchange earners of the country this perpetual dependence of leather exporters on western countries has become a challenge for leather exporters because export products are subject to quality, standards, importing country's government regulations, financial risks and product adaptation. For e.g. recently there is news in BUSINESS LINE (THE HINDU) that WTO is planning to introduce restrictions on leather goods imported into the EU due to chromium tanning in leather products which is harmful for humans as well as environment. In addition to this M.Rafeeq Ahmad, chairman of Council for Leather Exports also had a word with 'THE HINDU' in which he said "India's global market share stands in the leather and a leather product is 3%. We are suffering on two counts namely high tariffs and weak Euro currency. In European market we have to compete with Portugal, Romania and Slovakia on cost and logistics factor while we have to adjust the cost price according to prevailing currency European exporters have an advantage over us. In the export market we compete with Indonesia, Bangladesh, Vietnam and Thailand on tariff".

Thus, from the above scenario we can say that exporting leather to western countries on one side brings foreign currency but on other side exporters are paying a lot for their survival in the market.

VI. Inelastic supply of raw materials (bargaining power of suppliers): The basic raw materials needed for the leather industry are hides and skins. At present, the industry foresees a nationwide shortage of hides and skins. In the days to come this would lead to scarcity of basic raw material i.e. leather for the product sector of the industry. The supply of hides and skins being dependent on the livestock population, its birthrate, demand for red meat, mortality rate and recovery from carcasses, is highly inelastic in nature. One of the major reasons is the banning of slaughter houses in the country. Secondly, the natural calamities and marginal growth/decline of

livestock in some states. Further an estimate shows that the raw materials are lost due to unhygienic practices of gathering skins and processing. Lastly, large quantities of raw hides and skins around 35% to 40% are smuggled out to neighboring countries and making the problem more acute.

So, inelastic supply of raw materials to manufacturers and exporters makes it difficult for them to perform and compete in the international market and hampers their productivity and thus it is a serious concern for the Indian leather industry and thus the bargaining power of suppliers is weak because of inelastic supply of raw materials.

VII. Most of the units are at declining phase: Since Modi government came in scenario the declination of leather industry started. As per the information the Modi government's crackdown on Muslim dominated abattoirs and the trade of cattle dragged down India's export of leather shoes by more than 13% in June.

India the world's second largest supplier of shoes and leather garments, exports nearly half of leather goods with overseas sales estimated at \$5.7 billion in the 2016/17 financial year to march, down 3.2% from a year later. Footwear exports fell more than 4% in April-June (2017) to \$674 million.

Due to banning of slaughter houses by the yogi government in Uttar Pradesh which is a hub of leather and leather products the exporters are unable to meet the requirements of the buyers and thus most of the buyers are moving towards the rivals in Asia and South East Asia.

Lastly, the industry is also grappling with a Goods and Service Tax, introduced in July 2017 which has pushed the production costs by 6-7 percent.

Therefore, these challenges are pushing the Indian leather industry towards declining phase.

## CONCLUSION

In this paper we have discussed the major weaknesses of leather industry and challenges faced by the Indian leather exporters and from the above results we can say that the situation of Indian leather industry and the exporters need to be improved by the government and the other organizations. They should make the situations favorable for the exporters and the industry so that they can compete in the international market and adapt the fast changing trends by providing the required funds, technology and knowledge so as to improve the condition of Indian leather industry as this industry is one of the largest earners of foreign exchange.

Here are some points which can make the situations better for Indian Leather Industry:

- According to the Council for Leather Exports GST rates on leather products should be decreased for the sake of leather exporters.
- Water and waste treatment plants should be provided to all the SMEs by the government in order to protect the environment.
- Government should promote research and development in this field so that the exporters can innovate new things in this industry and make themselves compatible buyers in other countries.
- Government policies should be designed for the betterment for the industries and the exporters but banning of illegal slaughter houses has affected a lot to the productivity of the leather export market which is not at favorable for the exporters.

There are other areas also which needs to be worked upon to save the Indian leather and leather industry from declining.



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