

# BRIEF: TRANSFORMING the NIGERIAN LEATHER INDUSTRY



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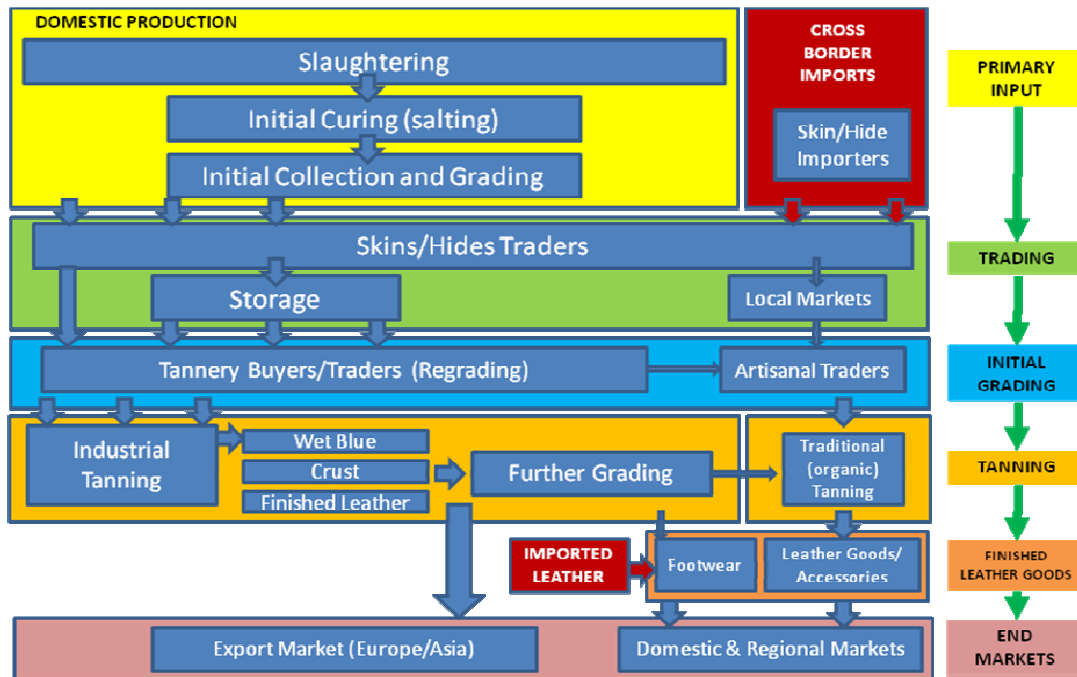
The Growth and Employment in States (GEMS) programme is a five-year programme jointly funded by the World Bank and DFID. Its aim is to increase growth and employment, especially for poor men and women, by improving competitiveness in strategically important Nigerian industry clusters in selected states and nationally, as well as through business environment reform. Wholly funded by DFID, the target market for the GEMS1 component is the meat and leather industry.

As in other target markets, GEMS1 uses the Making Markets Work Better for the Poor (M4P) approach targeting sustainable improvements in market outcomes by altering the incentives that the market as a system provides to participants. It addresses major government and market failures in the system thus bringing about systemic change. Improving the incomes of the poor, especially women and the young, is an explicit goal of M4P programmes.



## HOW the INDUSTRY WORKS...

### Leather Value Chain Structure:



**Production and Trading of Hides and Skins:** The sector starts as a by-product of the meat sector when hides and skins are stripped off a slaughtered carcass to get to the other parts of the animal. Despite the slaughter of nearly 7 million cattle annually, the majority of Nigerian hides are used to produce ‘pomo’ (the local term for edible hide). Therefore most leather produced in Nigeria is from sheep and goat skins. Most slaughter of sheep and goats is informally done by local butchers at village level and otherwise at formal slaughterhouses and abattoirs dispersed across various cities and states. Slaughtering peaks during the *Sallah* religious festivals.

The skins trading stage involves a large elaborate network of around 30 skin traders and 250 medium and small sub-traders. This network manages to gather skins for tanneries from across the country as well as other parts of Africa and: an important network characteristic is the common practice for industrial tanneries to advance funds to appointed dealers which in turn finance small collectors and traders thus alleviating credit constraints in this cash business. Prices paid by major traders to butchers and market dealers are currently N600 for Grade 1 sheepskin and N400 for Grade 1 goatskin (representing a drop of about 50% on prices paid in 2010: major traders presently make a profit of about N100 per sheepskin and N50 per goat from the tanneries. The average value of a reject skin is N100. Skins are still the main cost driver throughout the chain accounting for 64% of costs in tanning and 73% in finishing. Salting is the method used for curing and preserving skins. The formal tanneries complete grading checks at tannery gate with standards varying from tannery-to-tannery depending on the requirements of its end customers. Grades 1, 2 and 3 skins are generally determined by a combination of quality issues. Rejects are sold to traditional/artisanal tanneries.

**Tanning:** Following acceptance at tannery gate, the skin passes through the warehouse system of the tanneries and later through various machine tanning processes after which it is called leather. There are three main stages during the tanning process: (1) wet blue, (2) crust and (3) finished leather. The Leather Industry in northern Nigeria (mainly centred in Kano) has two subsectors – formal tanning and traditional/artisanal tanning.

The **formal tanning subsector** has 3 large and 5 medium size active industrial tanneries based in Kano that account for 90% of all exports (according to ComTrade in 2010, around 40 million tanned hides over \$3 billion representing just under 3% of the global market) to international re-tanners mostly in Europe but increasingly the Far East reflecting the geographical shift in production for end markets of the past decade or so. Around 18 formal tanning enterprises have closed or become inactive over the past 12 years. Three smaller formal tanneries service the domestic market.

**Finished Leather Goods (FLGs):** The Nigerian FLG value chain includes the producer group of actors of which there are two types – industrial and artisanal producers.

The **industrial producer group** has two main production groups – large and small industrial producers which accounts for over 60% of all the actors in the sector. The **large industrial production group** is characterized by complete and fully-integrated automated production systems with less labour involvement. The small industrial producers import and locally assemble component parts of various FLGs. The **artisanal producers** have two distinct operational groups based on the nature and scope of the operation: these are ‘artisan complete’ and ‘artisan specialist’.

The main three inputs for FLGs are leather (the primary input), components and accessories. The two main types of leather used by producers are natural and synthetic leather. Synthetic leather is used mostly for footwear and some fashion accessories such as upholstery, ladies’ bags and purses, shoes and slippers, and forth. Skins are generally used more in footwear production and hides for footwear and other leather goods.

The Nigerian domestic FLG sector competes with imported Chinese products which have a 90% share of the market! Not surprisingly, there is substantive informal exporting of Nigerian FLGs to neighbouring west African countries though poor product quality threatens this market. The annual market for Nigeria FLGs is an estimated \$200 million.

The formal subsector essentially captures all the better quality skins that are available in the market. There is no uniform standard for tanned leather: each tannery has different chemical formulas using imported chemicals from major European suppliers, techniques, and technologies to produce various types of leather articles. Following wet blue transformation, the tanneries will regrade and select the wet blues for further processing into crust and finished leather for client requirements. Imports of wet blue will also be considered at this stage

**Traditional/artisanal tanneries** use traditional methods to convert lower grade raw skins into reasonable quality finished leather (currently around 2 million pieces per year) for the domestic finished leather goods market. Traditional tanners typically work with raw skin and wet blue rejects, which are obtained at favourable prices through various channels. However the number of skin rejects has fallen in recent years as larger tanneries are keeping even the lowest grades of skin and wet blue. Small-scale tanners, dyers and leather product manufacturers have increasingly been forced to source their skins and leather in neighbouring countries.

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Accessories and components consist of leather, sole, glue, thread, metal accessories and foam. The most popular FLG products are footwear (around 85% of all FLGs), house-ware, and fashion accessories and ornaments. Slippers and sandals comprise around 80% of footwear production.

The main FLG production areas are Kano, Onitsha, Aba and Lagos. Covered shoes dominate production in Aba (daily production of 20,000 shoes), Lagos and Onitsha and are significant in Kano and Kaduna, while slippers and sandals are dominant in Kano and Kaduna and significant in Aba, Lagos and Onitsha. House-wares and ornaments are significant in Kano and Sokoto while fashion accessories are significant in Aba, Lagos, Onitsha and Kaduna.

## INDUSTRY DYNAMICS...

**Growth Drivers:** ComTrade estimates the **global market for finished leather goods** at around USD 1 trillion. Demand for leather worldwide increase 3-4% annually during 2005-08 but fell in 2009 due to the global economic and financial crisis: 90% of the global trade in leather are goods, products and accessories.

According to TradeMap data, China dominates the export market with around one-third share: other leading producers include Italy, Brazil, India, Pakistan, France and Hong Kong. Footwear has been a major driver of growth for both China and Italy. Ibid estimates the global market for skins at around USD 29 billion. The global leather **market is fuelled by three main drivers:** new products, new fashion trends and the creation/introduction of new applications for leather.

Nigeria has one of Africa's largest livestock sectors and leather is the second major earner of foreign exchange after Oil. The major drivers of recent change and growth in the Nigerian leather sector have been government interventions: the most recent being the banning of wet blue exports and a minimum requirement of crust exports in 1999. In both cases many tanneries closed and only the foreign-owned tanneries had the financial resources and technological know-how to invest in new equipment, machinery, and technology.

Nigerian exports rose considerably in 2010 (over \$3 billion) compared with 2008 (\$680 billion) due to investment by the major tanneries in higher value products (i.e. from crust to more finished leather) which also enabled them to increase the usage of Grade 3 skins hitherto rejected for domestic craft leather production. The government's Export Expansion Grant (EEG) scheme has been another important driver of recent leather exports growth. As demand for skins by tanneries exceeds domestic supply, 48% of the 52 million pieces procured in 2010 were salted skins/hides imported from neighbouring countries as well as eastern and northern Africa (58% of all skins processed are goat). Many of these imported skins are of lower quality and trade at a substantial discount compared to prices paid to skins originating from Kano, Katsina and Sokoto. It is estimated by industry that Nigeria imports around USD 300-500 million annually of leather products informally, as the import of leather is officially banned. The estimated value of the Nigerian FLG sector for domestic and regional markets is USD 200 million.

**Global Industry Production, Power and Responsiveness Trends:** Unable to meet the demand of fashion for a wider variety of colours, smaller orders, and faster service, many European tanneries closed down around the turn of the millennium and **production has shifted to low-cost Asian centres** such as China, India and Vietnam as well as Brazil. Today, Asia is the hub of leather shoe production accounting for 85% of global leather shoe production.

**Power in the value chain has shifted from industrialists to brands:** over time, this shifted first from skin suppliers and warehouses (from 1960-1975), to the tanneries (1975-1990) to manufacturers (1990-2000), and then to retailers such as Zara, Tommy Hilfiger, and Timberland, which control distribution of the product and sub-contract production (2000-2010). Today, the power is shifting into the hands of the consumer.

*"We have too many suppliers. Our goal is to a long-term relationship with fewer suppliers. It's very important to have good, reliable suppliers who want to make money, and we want them to comply with corporate social responsibility regulations."*

Yves Carcelle, CEO of Louis Vuitton Group of Companies

As power has shifted gradually further and further away from the tanneries and suppliers, the imperative to become rapidly responsive to demand, lean and efficient to ensure survival has become increasingly intense. **Consolidation is occurring at the retail and brand level, tightening supply chain management.**

**Employment Creation:** The meat and leather industry provides the market for millions of Nigerian primary producers and many more in neighbouring countries. The formal leather subsector in Kano creates around 9,000 full time and 5,000 seasonal jobs: the 5 traditional tanning clusters in Kano create over 8,000 full time jobs while a further 40,000 are employed in artisanal tanning in the area. The FLGs sector provides direct employment for around 100,000 in Lagos, 300,000 in Aba, 150,000 in Onitsha, 60,000 in Kano, 10,000 in Kaduna and a further 200,000 in other areas. Women comprise about 30% of the FLG workforce but much less in tanning. If various classes of indirect employees of finished leather, transport and others are considered, the number engaged by the sector may tend towards a 2.5-3 million.

**Competitiveness:** Overall, skins only represent a small percentage (less than 3%) of the value of an animal, which means that the availability of skins for leather depends on the attractiveness of keeping sheep and goat for meat. Thus, the fortune of the leather sector depends on the fortune of the meat and livestock sector.

In order to remain competitive in future years the formal tanning sector will need to adapt from being sellers of large packages of commodity crust leather by improving their ability to produce smaller volumes of specific leather products (re-tanned, finished leather and finished leather goods) to meet changing customer specifications. In these circumstances there is a need to upgrade the full range of leather products produced and to improve the interaction of the Nigerian skin leather sector with international and regional customers.

Kano's leather cluster participates almost exclusively at the lower end of the value chain rather than the higher value-added, export-oriented finished leather goods segment. This translates into low value and low margins for manufac-



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turers. A basic crust or semi-finished skin, for example, is exported for only about USD6 to USD9 on average, depending upon quality, finish, grade, size, etc. Products made for the domestic market are no more sophisticated than the material for export.

FLG producers specialize in low-end products of poor quality with poor finish, made with technologies and tools that have been largely abandoned in the rest of the world. Nigeria manufactures and sells only low-end shoes and slippers of poor quality, while more than 120 million pairs of basic, medium-quality leather shoes are imported from Asia.

### POPULAR LEATHER INDUSTRY MYTHS and REALITIES...

**Myth: Red Sokoto goat skins command a premium price!**

**Reality:** Tanneries do not pay a premium for Red Sokoto skins and base their payments for all skins on quality issues centred on the area (i.e. size) of the skin and the level of grain damage (usually caused by one or a combination of skin parasites, poor flaying by less-skilled slaughterers and poor preservation). The small-stock source is also irrelevant as larger Nigerian tanneries use modern equipment and chemicals to transform skins into finished leather satisfying a range of client finishing requirements.

**Myth: Nigerian finished leather goods are made from Nigerian leather!**

**Reality:** Nigerian finished leather goods are mainly produced from imported leather since Nigerian tanneries export most of their finished leather to take advantage of the EEG scheme

**Myth: Nigerian finished leather goods are not exported!**

**Reality:** A significant volume of Nigerian finished leather goods is exported to regional markets, especially ladies' and gents' shoes made in Aba and Onitsha, and sandals and slippers from Kano

**Myth: Nigeria would be better-off if 'Pomo' production and consumption was discouraged in favour of leather production!**

**Reality:** The raw skin value to the farmer for 'Pomo' is 1.5-2 times that of leather while employment generated in modern tanneries is less than that in Pomo production and retailing

### GEMS1 RESPONSIVE SUPPORT...

The **target impact** of GEMS 1 is "to increase growth, income and employment, especially for poor men and women, in meat and leather markets in selected states and nationally". The **expected outcome** is to "improve the performance and inclusiveness of meat and leather sector market systems that are important for poor people". Complimenting target outputs of the Nigerian Leather Industry Transformation Agenda while ensuring high local ownership by the private sector, and responsive to resolving major industry competitiveness constraints while exploiting major growth and employment opportunities, the core leather industry strategy for GEMS1 is supporting markets and linkages for the following:

- **Finished Leather Goods (FLGs) for Domestic and Export Markets:** Working with partners both in the local leather goods manufacturing sector and those that supply services to the sector to improve marketing, develop access to improved materials and implement improved production techniques, especially to increase competitiveness vs. Chinese imports.
- **Skin Supply to Tanneries:** Working with partners both in the skin trading value chain and those that supply goods and services to create linkages and develop and implement improved techniques for reducing skin damage and improving skin preservation and sorting and increase skin value.
- **Production of Finished Leather for Export:** Working with partners in the tanning sector (those that manufacture crust and finished leather) and those that supply services to the sector to develop improved manufacturing processes and market access for finished leather including manufacturing process and market access improvement.

Other important areas of potential intervention under consideration include: (1) supporting markets and linkages for the export of quality finished leather goods; and, (2) strengthening support functions to improve sector coordination and information management.

Prepared by GEMS1, the DFID-funded programme supporting the Nigerian Meat and Leather Industry implemented by GRM International Limited

