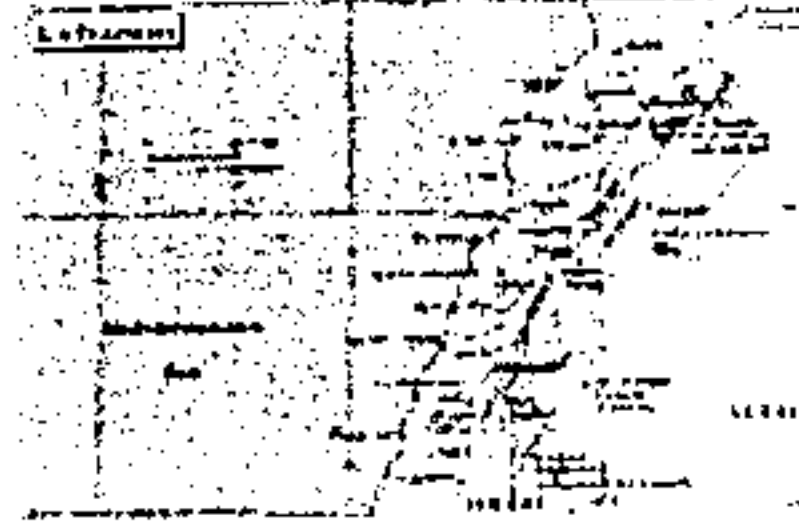


الجمهورية اللبنانية
المكتب وزير الدولة لشؤون التنمية الإدارية
مركز مشاريع ودراسات القطاع العام



PROJECT MANAGEMENT UNIT
INDUSTRIAL MODERNISATION PROGRAMME
LEBANON



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SECTORAL ANALYSIS ON
THE MODERNIZATION OF THE SHOE INDUSTRY

Chet du Service Technique

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SAMI ASSY

الجمهورية اللبنانية
مكتب وزير الدولة لشؤون التنمية الإدارية
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Republic of Lebanon
Office of the Minister of State for Administrative Reform
Center for Public Sector Projects and Studies
(C.P.S.P.S.)

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I. INTRODUCTION

The precise number of shoe factories operating in Lebanon is not known due to the damages of the Lebanese civil war, which drove many factories out of business and many others to operate only on a part-time basis. This instability in the industry continues today and prevents us from ascertaining the exact number of factories.

Pre-war figures put the number of operating factories between 600 and 800. Today however, we estimate that the number is closer to 500, according to the Lebanese Workers' Syndicate of the Shoe Industry. Of the 500, approximately 70% are small shops scattered all over the country, many in remote villages:

- All produce classical and house shoes for men, women and children.
- Four factories specialize in army shoes.
- Practically none has the sophisticated machinery to produce specialty shoes, i.e., beachwear, outdoor-sports, safety shoes etc.

The shoe industry prospered before the war and was supplying 80% to 90% of the needs of the local market while exporting to Arab countries. The quality produced ranged from low to high. The industry was protected by customs duty and import licenses delivered on the basis of small quotas to various importers.

During the war, at least 60% of the factories were displaced and their protection became merely symbolic. This situation continues today.

In addition to the weakening of customs protection, the shoe industry suffered fatal damage caused by dumping from Far-Eastern countries and the fall of purchasing power in the Lebanese market. Many factories were unprepared to face these problems and were subsequently forced to either shutdown or continue working with extreme difficulty

and with meager profit. Nevertheless many factories continued to operate with modest success.

We have selected 81 factories as representatives of the Lebanese shoe industry in part based on visits and the expertise of people in the field. Any measures taken to aid the sample, can also be applied to the entire industry. The sample will be analyzed based on the factories' ability to develop into healthy firms, facing the current competition and diversifying in fields such as boots, sportswear, beachwear, etc.

The elements necessary for the survival of the factories are: production of high quality shoes, the use of advanced machinery, the skills of trained employees and the possession of their own stores for direct distribution to consumers.

II. STATISTICS

(table 1 attached)

The breakdown of the selected factories is as follows:

- a) 28 factories employing 787 workers produce first-rate shoes.
- b) 31 factories employing 891 workers produce second-rate shoes.
- c) 22 factories employing 437 workers produce third-rate shoes.
- d) 1 factory producing exclusively army shoes

80% of first-rate shoes are sold locally

50% of second-rate shoes are sold locally

70% of third-rate shoes are exported

III. COMMENTARY

This data shows that the Lebanese shoe industry protects itself in the local market by selling high quality shoes. The factories not inventoried in the sample produce mainly low quality shoes and count on export—this is why export can represent around 35% to 40% of all Lebanese production of shoes.

Quality shoes are those answering fashionable designs, manufactured with top quality material mainly from natural origin and made so as to meet customer demands for durability, flexibility and comfort.

➤ High quality

Of the factories in group a) only 13 employ 20 or more workers which proves that a large number of high quality shoe producers still rely on artisanship and are therefore subject to elimination if they don't automate. The 13 factories in

question, account for 1,200,000 pairs of shoes produced while the 15 others account for approximately 300,000 pairs.

➤ **Medium quality**

Of the factories in group b) 18 employ 20 workers or more and produce 1,400,000 pairs of shoes while the other 11 account for 250,000. We observe that in general, factories producing second-rate shoes have more employees than those producing first-rate shoes. They usually have a more important segment of export where dumping competition is less severe.

The database presented suggests also that the great majority of the factories, i.e., those lacking machinery and training are vulnerable due to severe competition in Lebanon and abroad. It also demonstrates that in order to survive they have to modernize, mechanize, and train their employees to be in a position to export especially to European markets. Only 13 of the 81 factories are equipped with adequate machinery, four have trained personnel on new equipment, but all factories need assistance in exporting to Europe.

The Lebanese shoe industry needs assistance in four areas:

- New equipment
- Training
- Export to Europe
- Diversification

a- New Equipment

To be able to compete price wise, factories need new equipment reducing working hours specially when producing high quality goods.

Factories producing high quality shoes and lacking the proper equipment defend themselves better than those producing low quality but are still vulnerable to international competition.

The majority of these factories don't have the necessary funds to invest in new machinery. To save them, it will be necessary to provide them with long-term loans at low interest rates.

b- Training

Many factories have trained personnel and are producing high quality shoes but this training becomes obsolete in the face of new technology. It will become necessary for the majority of factories to train their employees on newly acquired machinery and to hire designers and experts.

Training is a perpetual process requiring factories that produce high quality products to continuously perfect the skills of their employees. This is especially true when new machinery is acquired. Furthermore, shoe manufacturers must ensure that their workforce is up-to-date on technical, commercial and administrative tasks. Employees must be trained as to new ways of doing business as well as new technology. By investing in human resources, the shoe manufacturer ensures efficiency and modernization.

c- Export

The shoe industry in Lebanon is compelled to produce high quality since otherwise it would have to compete with low-priced products, often low-grade dumped in the market by the Far-Eastern countries.

Fortunately, some of the shoe factories in Lebanon produce quality similar to the best quality produced in Europe. But the majority of the factories produces low to medium

quality shoes and don't have what they need to enter the export market of Europe. Their export potential lies mainly in the Arab countries.

The statistics above show that many factories are actually exporting to Arab countries where they have sometimes their own stores in which they sell their products. Their quality while not superior, is accepted, either because of the low-priced product competing with lower quality or because special ties and self-owned stores. Furthermore, the local factories show the flexibility needed for the market in number, color and specification that the foreign dumping producers are not meeting. Currently they have more flexibility than the Far Eastern countries but they have to lower their prices sometimes to the cost.

Since selling in Lebanon has become difficult because of the semi-recession and the advantage that big firms with their distribution system have over the majority of the producers, the latter are forced to try their best to export.

Financing remains a problem to deal with, especially because the majority of the factories can't find the necessary funds to import machinery to organize themselves for export, buy raw materials and pay better wages.

Some of the big companies as shown in the statistics ahead can increase their capacity in order to export.

The fact that Lebanon has signed with Europe opens great opportunities for the Lebanese shoe industry.

The ability to produce high quality products with comparatively low wages is supposed to boost this industry tremendously provided we can enhance the product quality and the capacities of the existing factories. The hope for the future exports lie in the European markets.

Exporting shoes from Lebanon has never been difficult. Arab markets have been importing Lebanese-made shoes since long before the war. Approximately 35% of the total production is still exported to Arab countries but year after year we see these figures dwindling and there is grave danger that they will soon stop altogether due to fierce international competition. It is therefore of utmost importance that we open new markets in Europe. However, exporting to Europe requires a restructuring of the Lebanese shoe industry with the help of new equipment and training. It will be impossible to export the same quality shoes to Europe as those exported to the Arab world.

Besides equipment and training, the Lebanese exporter must also be acquainted with the customs and conditions of International markets. An infrastructure must be built to accommodate various trade methods and determine the appropriate marketing strategies and distribution channels.

In order to keep ahead of the competition, the shoe manufacturer will need to determine the niches and types of products in demand abroad and to ensure that they can be readily modified to meet the changing needs of the consumer. Once the pricing strategy has been determined, the product must be promoted in the country of destination via advertising, fashion fairs and other promotional venues. To place the product, the shoe manufacturer must determine the most appropriate channel of distribution: direct sales to consumers, selling to wholesalers or selling to retailers. When selling to retailers, shoe manufacturers will need to ensure that the following criteria is met:

- **Reactivity:** Shoe manufacturers must be responsive to retailers and to accommodate their needs.
- **Delivery time:** Shoe manufacturers must be able to deliver merchandise within the retailers' specified time.
- **Specifications:** Shoe manufacturers must maintain the specifications required by retailers.

d- Diversification

Diversification is one of the most important components of a significant increase in the volume of shoe production in Lebanon. Diversification in the industry entails the production of sports shoes, climbing shoes, beachwear and other specialty shoes that are produced in Lebanon. There are two main reasons these shoes are not being produced in Lebanon. Before the Lebanese war, the Arab world, preferred to import what they needed of the specialty market from Europe and not from Lebanon. And for their part, local manufacturers were satisfied to sell mainly classical shoes because in the absence of real competition because of government protection in Lebanon, they did not equip their factories with modern machinery. Following the war, the situation remained the same.

Since the Lebanese shoe industry can no longer count on protection and competition is becoming increasingly severe, the best solution to survive is to diversify and export to Europe.

Equipping the shoe industry with new machinery, hiring designers and experts and training the personnel will open the door to diversification if access to the European markets becomes easier. At this point, help from ELCIM and the new agreement between Lebanon and Europe becomes timely.

The shoe industry, based only on classical shoes could nevertheless live and prosper because shoemakers in Lebanon have the creative flair and are inventive. Before the war, some factories ventured in the production of sports shoes but could not continue because the sports industry is a mass production business and it is not easy to compete with international companies. Currently, the only types of shoes that still relatively evade dumping competition from abroad are high quality classical shoes.

Producing new kinds of shoes necessitate a study of the market to see if there is stability in the demand, ability of the local industry to meet specifications, quantity and prices comparable to the existing competition.

Thorough studies of the markets will provide guidance as to the kinds of shoes in demand on the international markets especially in Europe.

IV. POSSIBLE APPLICANTS

Of the above-mentioned group, 27 factories are likely to benefit from our intervention. The selected group does not include names, only specifications showing the criteria on which we based our conclusions. The data for the selection was collected in part during visits to the factories and confirmed by experts working in the field but also taking into consideration volume and quality in the chosen factories.

Table of likely candidates :

(table 2 attached)

There are 12 factories of 20 employees and above producing first-rate shoes, eight factories of which produce women's shoes, two produce children's shoes and four produce men's shoes.

There are 15 factories of 20 employees and over producing second-rate shoes, of which five produce women's shoes, one produces children's shoes and nine produce men's shoes.

There are certainly other factories than those designated in the table above that could also be successful applicants, while some of those mentioned may not.

We will now designate and analyze the criteria and conditions of their success.

a- Minimum Economic Scale

The shoe industry is in principle labor-intensive, lending itself to various sizes, depending on the region, the clients etc.

Trying to define the minimum economic scale in Lebanon depends on various elements: labor wages, competitors inside and outside, kind of clients targeted, etc.

According to these elements and taking into consideration, machinery, training and export needs as well as the current dumping from Far East countries, especially China, we believe that the minimum economic scale of a shoe factory should be as follows:

- Value of machinery: \$200,000.00
- Number of workers: 20
- Personnel: 10 trained workers, one designer, six understudies, one doorman, one shopkeeper.
- Quality of production: First and second rate quality, in every way superior to the quality dumping the market. Sold for \$25 and up from the factory.

Such a factory is able to protect itself in the market but it will have a much better chance of making profit if it has direct access to the consumer.

b- Quality Standards

Due to low-cost shoes flooding the Lebanese market from Far East countries, the shoe industry has to target the markets requiring medium and high quality shoes. This is one of the reasons why more than 60% of the units existing in Lebanon are facing difficulty, some have closed completely, others work at 50% or less of their productive capacity.

When considering quality, one must certainly take into consideration the complex and labor-intensive process of making shoes, which varies according to the materials used,

- Acquiring modern machinery with training on these new machines
- Restructuring of the firm in order to have a sales and technical department.
- Better synchronization and full use of the machinery in order to maximize production and reduce cost.

The variety of shoes that can be produced is very large: classic shoes, boots, sandals, slippers, house shoes, children's shoes, sport shoes, leisure shoes, women's shoes for women, men and children.

Diversification according to the fashion and the desire to cut costs becomes a must for whoever wants to develop his business. This entails a restructuring to include technical and business expertise and new machinery to accommodate the fashions and the volume.

In the current situation we can expect growth as shown in the statistics above. ELCIM could provide advice, expertise and training as well as provide experts while the factory should find the capital to buy machinery and pay extra wages.

Few are able to provide the financing needed unless they can be loaned credit with low interest for an extended period of time to be used not only for investment in machinery and other equipment but also partly used as working capital.

Factories making profits or at least not in the red are the ones expected to grow. The industry as a whole will not grow unless it modernizes and turns to export especially to Europe.

VI. KEY SUCCESS FACTORS AND WAYS AND MEANS

As this study shows, the shoe industry needs a complete restructuring with the help of the Lebanese government and ELCIM in which the key success factors are:

1) The production of high quality shoes

Research and development is the first step in raising the quality of shoes manufactured in Lebanon. ELCIM can provide information on the latest technologies as well as the means to develop the industry from a business perspective. This can happen with the aid of in-depth diagnoses of each successful applicant. Other ways in which ELCIM could help is:

- i) To conduct on-site focus groups
- ii) Identify trade fairs abroad for attendance by Lebanese manufacturers
- iii) Identify European designers interested in working with Lebanese manufacturers
- iv) Eventually help create schools for state-of-the-art shoe design
- v) Provide expertise on new business methods
- vi) Help provide machinery that can produce high quality shoes at low cost.

2) Export to Europe

- i) Create seminars for all shoe manufacturers to explore the best export practices to Europe; understanding customs and conditions of the targeted markets as well as export regulations; and ensuring that they can be responsive to retailers' demands, specifications and are able to deliver on time.
- ii) Propose ways for the Lebanese government to create an organization of export guarantees—such as, Coface or Hermes
- iii) Identify venture capitalists
- iv) Identify the importers and retailers who might be interested in entering into business with Lebanese shoe manufacturers.
- v) Help to organize export houses
- vi) Provide contacts

3) Diversification

- i) Help in identifying niches and determining the types of products in demand in targeted markets. Including specialty items such as sports shoes, party shoes, snowboarding shoes, boot styles, illusive footwear (hard to find, specialty

shoes), period shoes (previous era shoes), ethnic shoes (such as Native American moccasins), cultural styles (bohemian and cowboy), safety shoes, “cyber chic” shoes (futuristic shoes, especially popular with men nowadays, compliment today’s cyber fascination), and inventive dress shoes. Shoe types range from clogs, moccasins, ankle boots, and slippers to sandals. Shoe styles now often focus on ethnic or cultural themes such as: folksy; patchwork quilting; Moroccan beading; Scandinavian embroidery; Nordic trims to name a few.

- ii) Seminars to provide guidance to factories in new areas of production and to provide experts.
- iii) Providing studies of the markets to determine if there is stability in demand.
- iv) Advising the industry on ways to meet specifications of foreign retailers and importers as well as prices, quantity and ability to easily modify.
- v) Provide information on joint ventures to help manufacturers diversify

4) Joint Venture

A shortcut to the success factors is the use of joint ventures between well-known European labels and Lebanese manufacturers as a means of improving the shoe industry. The Europeans will profit from low-waged, skilled labor. The Lebanese will benefit from their association with the label, the European markets and distribution systems, the know-how and the most advanced machinery.

The joint venture could be a participation in the local factory; a contract by which the Europeans give the Lebanese manufacturers the know-how and right to use the label against a fee; and the possibility of purchasing the advanced machinery from Europe.

These options can expand in Lebanon thanks to the country’s liberal economy, the tradition of high quality products and the new era of commercial relations initiated by the agreement between Lebanon and Europe.

The success factors listed in this study and the ways and means proposed will certainly help some if not all the applicants to develop into dynamic, modern and profitable firms with the proper financing.

Very few firms if any have the ability to obtain credits from banks or to generate the necessary funds to modernize and grow. With the help of ELCIM, we should be able to facilitate access to long term financing. The ELCIM Financial Unit would offer a number of services including advice and information to applicants as to the credits available to them from the Lebanese Banks or the EIB as well as to provide guidance on the necessary forms and follow through with applicants to final implementation. Since the private banker in any case supports the credit risk, the Financial Unit can help establish feasibility studies to convince bankers of the soundness of the demand.

Anti-dumping law

According to the General Agreement on Tariffs and Trade (GATT), dumping occurs in one of the following three cases: 1) when the price on imported goods is lower than the cost of production plus a reasonable margin of profit 2) less than the price established by the country suspected of dumping in a third country 3) less than the price at which the company or government sells inside its borders.

The Lebanese Decree Law #31 of August 5, 1967 provides measures to fight dumping when it endangers a Lebanese industry, by adding to the custom duty an extra tax equal to the subsidies accorded to the foreign exporter by his government. We propose that this law be implemented every time dumping is confirmed.

Location			Kind Produced			Quality Rating			Markets		Machinery Needs	Training Needs	Export Needs
	Co. #	# of Empl.	Men	Woman	Child	I	II	III	Local	Export			
Beirut	1	40		100%		A			100%				E
Beirut	2	10		100%		A			100%		M	T	E
Beirut	3	6	100%				B		100%		M	T	E
Beirut	4	15	50%	50%		A			100%			T	E
Baabda	5	270	75%	10%	15%	A			75%	25%			E
Baabda	6	15	75%		25%	A			100%		M	T	E
Baabda	7	15		75%	25%			C		100%	M	T	E
Baabda	8	25	100%				B			100%	M	T	E
Baabda	9	10		100%				C		100%	M	T	E
Baabda	10	25	100%				B			100%	M	T	E
Baabda	11	30		50%	50%			C		100%	M	T	E
Baabda	12	75	100%				B		40%	60%		T	E
Baabda	13	20	100%					C	50%	50%	M	T	E
Baabda	14	10		100%			B		100%		M	T	E
Baabda	15	10	100%			A			100%		M	T	E
Baabda	16	20	35%	35%	35%	A			70%	30%	M	T	E
Baabda	17	25	100%						100% (*)		M	T	E
Baabda	18	40	100%				B			100%	M	T	E

Location			Kind Produced			Quality Rating			Markets		Machinery Needs	Training Needs	Export Needs
	Co. #	# of Empl.	Men	Woman	Child	I	II	III	Local	Export			
Baabda	19	40	100%				B			100%	M	T	E
Baabda	20	70	100%				B			100%	M	T	E
Baabda	21	30	100%				B			100%	M	T	E
Baabda	22	20	100%					C		100%	M	T	E
Baabda	23	15		100%				C		100%	M	T	E
Baabda	24	25		100%				C		100%	M	T	E
Baabda	25	40	100%				B			100%	M	T	E
Baabda	26	15		100%				C		100%	M	T	E
Baabda	27	15	100%					C	40%	50%	M	T	E
Baabda	28	15		100%				C		100%	M	T	E
Baabda	29	10		100%				C	50%	50%	M	T	E
Baabda	30	10		100%				C	50%	50%	M	T	E
Baabda	31	12		100%				C	50%	50%	M	T	E
Baabda	32	25		100%			B		40%	60%	M	T	E
Baabda	33	8		100%				C	60%	40%	M	T	E
Baabda	34	15	100%					C	50%	50%	M	T	E
Baabda	35	12		100%				C	50%	50%	M	T	E
Baabda	36	15	100%				B			100%	M	T	E

Kind Produced			Quality Rating			Markets							
Location	Co. #	# of Empl.	Men	Woman	Child	I	II	III	Local	Export	Machinery Needs	Training Needs	Export Needs
Baabda	37	15	100%				B			100%	M	T	E
Baabda	38	15		100%				C	50%	50%	M	T	E
Baabda	39	25		100%				C		100%	M	T	E
Baabda	40	50	100%				B		40%	60%	M	T	E
Baabda	41	40					B		100%				
Baabda	42	25	100%			A			100%		M	T	E
Baabda	43	15		100%			B		50%	50%	M	T	E
Baabda	44	20		100%			B			100%	M	T	E
Baabda	45	15		100%				C	60%	40%	M	T	E
Baabda	46	10		100%			B		60%	40%	M	T	E
Baabda	47	30	100%			A			100%		M	T	E
Metn	48	15	70%		30%		B		100%		M	T	E
Metn	49	15			100%		B		100%		M	T	E
Metn	50	25			100%		B		100%		M	T	E
Metn	51	30		100%			B		100%		M	T	E
Metn	52	25		100%				C	100%		M	T	E
Metn	53	15		100%		A			100%		M	T	E
Metn	54	15		100%		A			70%	30%	M	T	E

Location			Kind Produced			Quality Rating			Markets		Machinery Needs	Training Needs	Export Needs
	Co. #	# of Empl.	Men	Woman	Child	I	II	III	Local	Export			
Metn	55	15		100%			B		30%	70%	M	T	E
Metn	56	20		100%		A			50%	50%	M	T	E
Metn	57	15		100%			B		30%	70%	M	T	E
Metn	58	30		100%		A			100%			T	E
Metn	59	25		100%		A			100%			T	E
Metn	60	15		100%		A			100%		M	T	E
Metn	61	15		100%		A			100%			T	E
Metn	62	12		100%		A			70%	30%	M	T	E
Metn	63	15		100%			B		50%	50%	M	T	E
Metn	64	25		100%		A			100%			T	E
Metn	65	15		100%		A			60%	40%		T	E
Metn	66	25			100%	A			100%			T	E
Metn	67	15			100%	A			100%		M	T	E
Metn	68	15			100%		B		100%		M	T	E
Metn	69	15		100%		A			30%	70%	M	T	E
Metn	70	20		100%		A			60%	40%	M	T	E
Metn	71	10		100%		A			100%		M	T	E
Metn	72	10		100%		A			100%		M	T	E

[illegible]

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مركز مشاريع ودراسات القطاع العام

Co. #	# of Empl.	Kind Produced			Quality Ratings		Markets	
		Men	Woman	Child	I	II	Local	Export
1	40		100%		A		100%	
2	270	75%	10%	15%	A		75%	25%
3	75	100%				B	40%	60%
4	40	100%				B		100%
5	40	100%				B		100%
6	70	100%				B		100%
7	30	100%				B		100%
8	40	100%				B		100%
9	25		100%			B	40%	60%
10	50	100%				B	40%	60%
11	25	100%			A		100%	
12	30	100%			A		100%	
13	25			100%		B	100%	
14	30		100%			B	100%	
15	20		100%		A		50%	50%
16	30		100%		A		100%	
17	25		100%		A		100%	
18	25		100%		A		100%	
19	25			100%	A		100%	
20	20		100%		A		60%	40%
21	30		100%			B	40%	60%
22	60		100%			B	100%	
23	20		100%			B	50%	50%
24	30		100%		A		100%	
25	25	100%			A		100%	
26	25	100%				B	100%	
27	60	100%				B	100%	