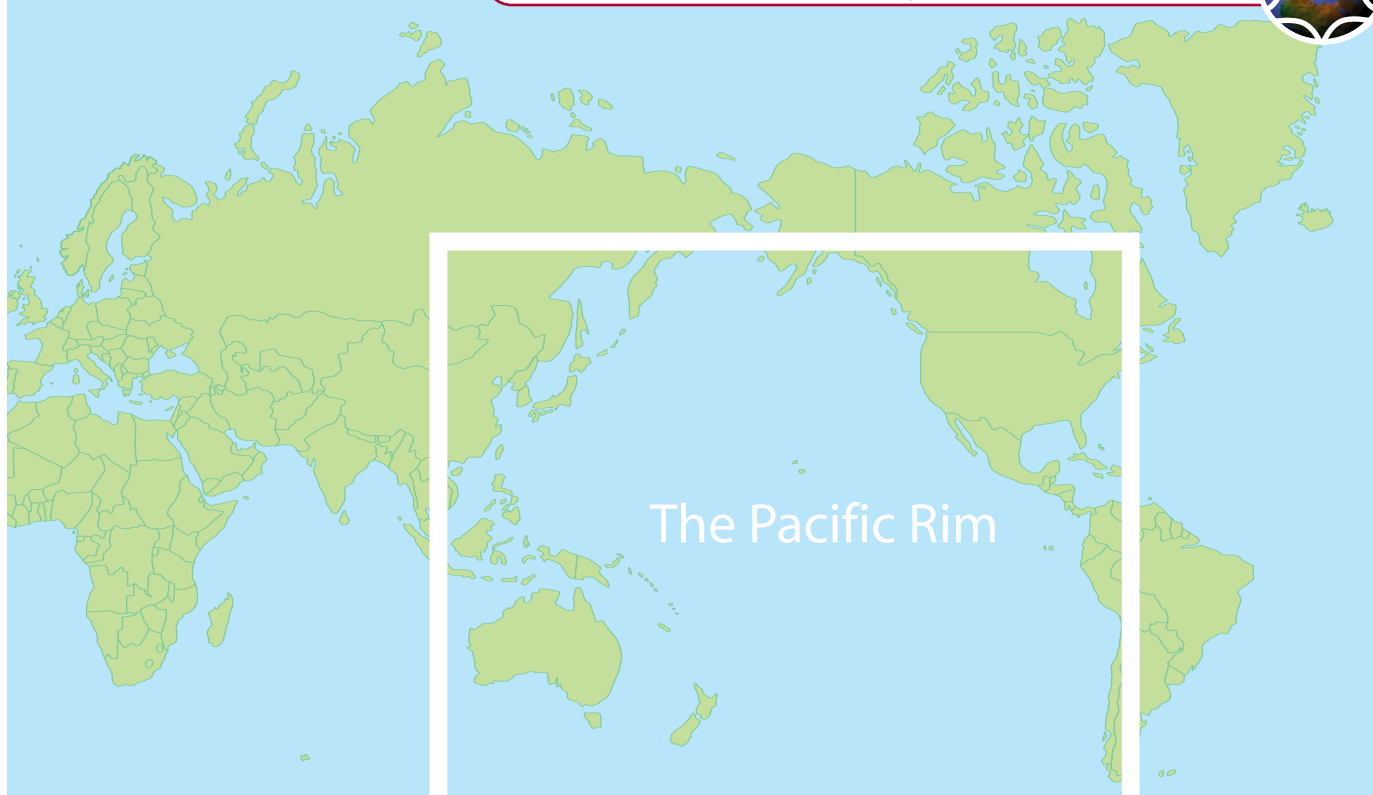


Regional Commentary: The Pacific Rim



During the 1990s industrialists were frequently warned that the 21st Century was to be the 'Pacific Century' and how the growth of China would lead to a realignment in trade routes and a new balance of importance of trade for the many countries bordering the Pacific.

But the unexpected political events of the 21st Century has taken the focus off what has been happening in this region and, of course, China's immense growth which has dominated everything else. Yet many new trade routes have been set up as other Pacific countries have established new business with China, whilst others have sought alternate partners to balance the risks of China monopolising the industry.

The Pacific Rim—edging towards success or demise?

China's dominance in the leather and footwear industries is indisputable but, as discussed in the last issue of *World Leather*, things are changing in China—labour costs are now lower in both India and Vietnam and China is now less certain about the role of low added-value manufacturing such as shoemaking, certainly in the rich south-east. Furthermore, the Chinese government has real concerns about the environmental impact of the early stages of the tanning process, especially where rapid urbanisation has trapped isolated plants within the new conurbations. Even environmentally conscious tanners, such as Ecco, have had to work hard to gain

permission to establish new tanneries and other high quality well-established tanneries are now threatened in both greater Beijing and Guangzhou. This uncertainty in no way means that the dominance of China will diminish, but it does indicate that companies are more likely to seek out alternate or parallel partners. For example, Japan's leather trade is now doing business in places such as Cambodia, Myanmar and Bangladesh, which was not foreseen, even a few years ago. Korea is also successfully trading with both Vietnam and Indonesia and both South Korea and Taiwan now have much higher exports to China than to the USA.

Tradition versus technology in Japan

Japan has always been a country of contrasts and contradictions. On the one hand it is one of the most urbanised societies in the world, while on the other it still clings to many ancient traditions and social customs. It has also been the most powerful economy in the region for the past 50 years. Whilst it has a history of aggressive exporting across the world it has also adopted many protectionist measures with regard to its domestic industry, including the leather and leather-related industries. For many centuries tanners in Japan, unless large-scale industrial operations, have been viewed as 'low caste'. As a result they have been given special ►



Regional Commentary: The Pacific Rim



Himeji's traditional white leather used for a souvenir card holder

protection and tax benefits by the government. During the '90s the worldwide leather industry, and especially the European Leather Association, Cotance, fought hard to persuade the Japanese to open the market to imported leather, but with only limited success. In reality it took the Kobe earthquake to change the market when much of the shoe production capacity that was lost was replaced in China and elsewhere, offering Japanese shoemakers and brands a choice of world supply for the first time.

Japan is a major consumer of leather and leather products as a result of its high consumer purchasing power, albeit the difficulties caused over the last decade due to domestic stagnation. Japanese leather products are known for their world-class quality, technology, workmanship and styling. However, leather sector investments in other regional countries and high labour costs mean that imports have captured a significant slice of the country's consumption. Imports now account for around 75% of total consumption of leather and leather products in Japan, making it the world's seventh largest importer of leather and leather products. However, the tanners that do remain in Japan have proved tenacious and none more so than the group from Wakayama. With some 20 members in this area south of Osaka and the famous tanning centre of Himeji, the Wakayama tanners have exhibited at the Hong Kong Fair for some years. They added Shanghai ACLE in September 2006

and the seven members who attended reported a good outcome. Their leathers included bovine, horse and sheepskin.

Japan's imports of leather and leather products increased from ¥375,780 million in 2001 to ¥401,628 million (\$3.45 billion) in 2005 and exports rose from ¥26,760 million to ¥29,939 million (\$257 million in the same period. Japan imports most of its leather from China, followed by Italy, South Korea, the USA, Thailand, Pakistan, Cambodia, France and Indonesia. Imports of footwear, leather garments, leather goods and other products are still subject to a tariff quota system and legally required labelling under the law for the promotion of effective utilisation of resources and footwear outside of the quota generally attracts an average customs duty of 60%. Over and above the quota system, Japan has a number of very individual aspects. In particular it has a definitive sizing system whereby sizes are expressed in centimetres. Japanese feet are also generally broader than European or American, so the girth measurement also needs to be proportionally different. This has made it harder to move production overseas and Japanese importers with specific knowledge of Asian sources, which could produce footwear to meet Japanese specifications, were especially sought out. A number of new plants making just uppers were established, although nearly all have now been converted to full shoe production.

Despite these heavy duties and

individual requirements, leather footwear imports have been increasing for a number of years on a volume basis as production has steadily moved overseas. In addition to China, some Japanese shoemakers have relocated production to Cambodia and Bangladesh in recent years, where costs are even lower than in China. The breakdown of imports of shoes shows that flagship products continue to be women's and men's shoes with composition leather outer soles and although only a small volume is involved, upmarket men's footwear with leather soles has been steadily growing year-on-year. Italy was the main exporter of footwear to Japan up until the mid-1990s, but by 2003 China accounted for 6.21 million pairs or 31.2% of imports. In 2005, the country imported just over 36.5 million pairs of leather shoes. Cambodia has moved into second place in the ratings. Bangladesh has also done well, but the surprise is Myanmar, which has actually overtaken Cambodia for some lines of men's shoes. Meanwhile, Italy and other EU exporters have suffered due to the high value of the euro over the past few years and the average value of Italian footwear is now four times that of Chinese.

Against this background, domestic production of leather footwear has naturally also fallen substantially and declined from around 55 million pairs in 1998 to about 35.37 million in 2002 and it must be assumed that it has fallen much further since. However, top quality Italian women's shoes still have a cachet, as have the best British made men's welted shoes and, of course, the leading international sports and brown shoe brands.

Hide consumption (million pieces)

	1980	1995	2000	2004	2005
Imports	8.59	5.07	2.71	1.92	1.39
Domestic	1.19	1.46	1.25	1.25	1.22
Total	9.78	6.53	3.96	3.17	2.61

Source: Japan Leather Industry

Principal sources of footwear imports (million pairs)

	2000	2001	2002	2003
China	4.34	3.68	4.75	6.21
Cambodia	2.45	3.50	4.38	4.74
Italy	2.79	3.19	3.18	2.87
Bangladesh	0.79	1.36	1.30	1.64
Myanmar	0.73	0.82	0.93	1.46
Others	4.37	3.77	3.35	3.01
Total	15.47	16.32	17.89	19.94

Source: Japan Exports and Imports ➤

Regional Commentary: The Pacific Rim



Fur and leatherwear

The seasonal demand for leather and fur garments has always been strong in Japan and good design has meant that fashion has required frequent replacement rather than keeping a leather jacket as a commodity item for many years. Yet over recent years fur and fur product imports have continued to tumble in terms of both volume and value. Subsequently, the economic recession, the global animal protection movement, abnormally warm winters, and other negative factors came into play. The most common imported fur materials are relatively inexpensive sheepskin, sheep, goat and rabbit. These materials accounted for 75.1% of all imports on a volume basis in 2003. Recent advances in printing technology have led to the emergence of casual rabbit fur coats with leopard-print patterns. Furthermore,

recent improvements in the economy and birth of a male in the line of succession for the Emperor will likely see consumption in both the fur and garment and the luxury bag sector grow, and is also thought likely to lead to a welcome spurt in population growth.

A downturn in production down under

Australia's sheepskin tanning, bovine tanning and footwear industries are under threat of being swamped by the continued expansion of the giant Chinese economy.

Australia's place in the current global leather industry has evolved into one of a supplier of raw material. Although the country's wet blue production expanded rapidly in the '70s and '80s it has now contracted with four of the 11 wet blue

plants having now closed (although one imports wet blue to take to crust), and even one of these is now run at low production levels. The five plants that are owned by meat companies have had significant capital expenditure invested in them and equipment upgraded. Italy has dropped to second place behind China as the major consumer of Australian hides and skins. Several Chinese companies have found it economic to set up offices in Australia purely to source hides and skins direct from the abattoirs or from dealers for their tanneries in China.

China continues to have a voracious appetite for Australian raw material, with the majority of cattle hide exported salted, although a significant number are also taken as wet blue. China's demand is for higher quality wet blue for shoe leather, while Italy still takes the lower grades and 'ticky' Queensland material for its upholstery leather business. China finds low grades from Brazil more attractive than Australian material, but Australian traders believe that this is because they cannot be doing the right calculation on the Brazilian drop splits. Korea and Japan are also still active in the Australian wet blue market.

Something to celebrate

In spite of the problems faced by the Australian industry there are some positive developments in the industry. Australian meat company Teys Bros celebrated its 60th birthday by announcing new directions into value adding of beef and hides. Teys purchased Murgon Leather in 2004, to follow other Australian and USA meat companies which own their own wet blue plants. Teys has spent around A\$4 million since the purchase, setting up the Murgon Leather plant with improved effluent treatment facilities and a new brine curing raceway. At the moment hides



from Teys' Lakes Creek, Innisfail and Biloela meatworks are going to Murgon, with hides from Beenleigh and Naracoorte (in South Australia, its only operating works outside Queensland) being brine cured elsewhere. Teys plans to expand Murgon Leather's capacity from the current 1,700 hides per day to take all of the output of Teys five works. Teys Bros amalgamated with Consolidated Meats in 2003, and now employs 2,300 people, has a joint venture interest in a 28,000 head feedlot at Condamine, on the Darling Downs area of Queensland, and offices in Chicago and Tokyo.

Efforts to increase the value of cattle hides in Australia have also been boosted by the testing of an integrated supply chain between three producer alliances, an abattoir and a tannery. The six-week trial covered 371 hides from three sources, Gipps Beef, Castricum Brothers and Polkinghorne's, in south-east Victoria. The cattle were processed at Radford and Sons in Warragul and the hides tanned to the wet blue stage by Geelong Leather. The aim was to demonstrate the commercial feasibility and benefits of such a supply chain and demonstrate its operation with regard to absolute integrity of hide identification from producer to tannery; information collection and the transfer from tannery back to producer; and the use of an objective hide grading system. A cost-benefit analysis will assess the return on investment and where added-value is generated, particularly in terms of tracing hides and providing meaningful feedback to producers.

Traditional selections collapse

A major change in the Australian industry has seen the collapse of the traditional markets for Victorian, New South Wales, straight run and ticky selections. With the advent of the feedlot industry, and cattle transported from all parts of the country to feedlots in the grain belts, these terms have lost any meaning. Most wet blue operators are now offering graded lines, and the salted merchants are offering hides from nominated abattoirs or companies, in an effort to give the purchaser some form of quality assurance in their purchasing. With this in mind, further research on fighting the devastating effects of the cattle tick is planned, with the Queensland government giving A\$1.4 million (\$1.057 million) to the Beef Cooperative Research Centre, Australia's largest integrated beef research centre, to discover and commercialise a vaccine to control cattle ticks. The aim is to develop a once-a-year vaccine, to replace the previous one that required three to four booster shots, which is not practical for the large northern free range beef production systems.

The cattle kill is also on the decline from over eight million in 2002/2003 to 7.5 million in 2005/2006. The drought in 2003 brought excess cattle onto the market, falsely inflating the kill, and the national herd is now rebuilding. Female ►



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cattle slaughterings for example are down from over 50% to 44% and falling. The feedlot industry is also booming, with over 920,000 cattle on feed, a record number. The extra numbers going on feed have exacerbated the lower kill numbers. Some of the bigger export abattoirs are operating on a four-day week as a result of the lack of cattle coming onto the market. Commentators state that despite this the Australian hide price has come back into line with world parity, a change from the over-priced situation of 2005 and early 2006 brought about by fierce domestic competition for hides.

Despite the Australian prices moving back into line with global market levels, companies are still struggling to compete. Schaffer Corporation, the parent company of Howe Leather and Gosh Leather, has recently announced that Howe Leather experienced difficult trading conditions for the 2005/2006 financial year, with sales falling A\$7 million from A\$98 million to A\$91 million. One of the major causes of this decline is that Howe has lost

its BMW business to South Africa and has experienced reduced demand from USA, where local car makers have lost ground to Japanese and Korean manufacturers. In response, Howe has now opened cutting operations in Slovakia, and within six months all of its cutting plants will be off-shore, in order to ensure that it remains globally competitive. The difficult situation has also led to the company's decision to close due to the demise of the leather furniture manufacturing industry.

The Australian sheepskin tanning sector, which had some serious players such as Myalls, Jacksons and Bowrons, has also been in decline, with these and others having also ceased their operations in Australia. The Australian markets for skins have shifted from the traditional ones of Spain, Italy, France, Korea and Türkiye to the major customers of today, China and Russia. Climatic conditions have brought about a decline in the kill and in the weights of skins, and has kept prices firm, with good interest in better quality materials. The coming season holds

promise for markets in Russia, with China expected to stay firm and Türkiye expected to come back into the market.

	2004 exports (A\$ million)	2004 imports (A\$ million)
Hides & skins	504.789	1.529
Processed leathers	326.589	81.579
Leather clothing	26.161	240.686
Footwear	32.355	706.678

Australian Shoe Industry

The footwear industry has contracted steadily over the past 20 years and is now quite small. With one or two exceptions, almost all manufacturers are small producers of specialised footwear that utilises specific Australian raw materials such as sheepskin for Ugg boots and kangaroo for specialist sports shoes. Only, around 3% of women's and up to 10% of men's footwear purchased in Australia is locally made, with about 65% coming from China. The local men's industry ➤

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has a solid base of industrial/safety footwear, while the women's industry is still dominated by the Ritchie Group, who manufacture around 60% of the women's fashion footwear made in Australia. Their competitive advantage—investment in technology, systems and people and short lead times through a tight supply chain made possible by using locally made leathers—has enabled them to compete with China.

The country is probably best known internationally today for its production of industrial and safety footwear and this is the mainstay for companies such as Bata,

Steel Blue Australia, Blundstone and Comfortwear. The latter two are both old established businesses, Blundstone having started in 1870 and Comfortwear in 1907. Blundstone is also something of an exception in having its own tannery. Probably the best known Australian manufacturer is RM Williams which produces the eponymous 'stockman's' boot. More than 70 years ago, Reginald Murray Williams began to make bush saddlery and boots while camped in South Australia's remote gammon ranges. Here, he met 'Dollar Mick' Smith an itinerant saddler and, after much trial and error, made his

first pair of stockman's riding boots. The company now makes a range of boots using a variety of Australian sourced leathers to suit each application. The traditional oil-impregnated and elastic-sided riding boot however, remains the core product. The leathers used include Willow—chrome tanned ox-hide for unlined work boots; Greasy kip—similar but impregnated with oils for water resistance; yearling—from young cattle for dress or lighter weight work boots; kangaroo—fine grain and high strength for light weight boots; Vesta—matt-finished cowhide containing water repellent chemicals permanently bonded to each fibre; and Sandstorm—a high tech oiled leather for extreme conditions.

The pause in the country's import tariff reduction on footwear, which has levelled out at 10% from 2005 to 2010 will drop to 5% in 2010, has caused further restructuring. It has been in a controlled fall for over 10 years, but the industry has been able to adapt through a mixture of controlled exits, manufacturing offshore, and productivity improvements for those who choose to remain.

The Australian government has recognised the importance of the textile clothing and footwear (TCF) sector to the economy and also the threat that China's accession to the World Trade Organization (WTO) is likely to pose. It also believes that the WTO Agreement on Textiles and Clothing, and other potential Free Trade Agreements, will continue to present both opportunities. It has therefore taken steps to improve the competitiveness of the industry by encouraging new investment in capital equipment and innovation through the \$575 million TCF Post-2005 Strategic Investment Programme Scheme. This non-competitive grant scheme came into effect on July 1, 2005, when the existing TCF (SIP) Scheme finished. It will run until June 30, 2015. Combined with a staged programme of reduced tariffs, it is intended to provide the industry with the support and time to adjust to a lower tariff environment.

In addition to these two schemes, the government has also introduced a \$50 million 10-year TCF Structural Adjustment Programme, to support further industry consolidation and labour market adjustment, a \$50 million 10-year TCF Product Diversification Scheme (PDS), to assist clothing and finished textile manufacturers to globalise their sources of supply and a \$25 million 10-year Small Business Programme to encourage improvements in the business culture of small TCF firms in Australia.

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Schedule
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*Heidemann Lecture,
John Arthur Wilson Memorial Lecture
Technical Sessions, Visual Displays, Fun Run*

Friday, June 22
*Technical Sessions, Visual Displays,
Golf Tournament, Explore Washington*

Saturday, June 23
*Technical Sessions, Sports/Social Activities Luncheon,
Reception, Banquet, Closing Ceremony*

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South Korea loses out to China

Since the early 1960s, South Korea has achieved an incredible record of growth and integration into the high-tech modern world economy. Four decades ago Gross Domestic Product (GDP) per capita was comparable with levels in the poorer countries of Africa and Asia. In 2004, it joined the trillion dollar club of world economies. Today its GDP per capita is 14 times North Korea's and equal to the lesser economies of the European Union. This success through the late 1980s was achieved by a system of close government/business ties, including directed credit, import restrictions, sponsorship of specific industries, and a strong labour effort. The government promoted the import of raw materials and technology at the expense of consumer goods and encouraged savings and investment over consumption.

Exports growing

During the period of January-June 2006, Korea exported goods worth \$155.53 billion compared with \$136.51 billion in same period last year—showing a growth of 13.9%. In June 2006 alone, Korea exports recorded \$28.27 billion, marking a high growth rate of 19.2%. By export category (estimated, Ministry of Commerce, Industry and Energy), automobile (up 9.8%), petroleum goods (up 40.4%), and ships (up 48.7%) all made sizeable gains. The leather & footwear industry in South Korea developed strongly in the sixties and seventies. Indeed it was the main industry to support Korea's phenomenal growth along with textiles, iron & the electronic industries until the late '80s. At that time rising wage costs pushed the leather consuming industry into moving to seek out cheaper labour, and the industry was also badly affected by the Asian financial crisis of 1997-99 and labour reforms, which again increased labour cost. Chinese companies to day argue that Korean and Taiwanese shoemakers failed to develop their own brands and so lost much of the business to China. Consequently several Korean tanneries and footwear units were closed down and many footwear manufactures have shifted their production base to neighbouring countries like China, Taiwan and Thailand. However, some of those Korean tanneries that are still operating have huge capacities, specialising in upholstery leathers and other specialty leathers.

Similarly, footwear units which are now in operation in Korea have a very

sophisticated and substantial production base, producing high quality and better designed shoes/boots, especially ski-boots, hiking boots, mountain boots, sports shoes, outdoor footwear etc. These units cater to both domestic as well as the export market.

South Korea imported leather and leather products worth \$ 1.187 billion in 2004 compared with \$1.148 billion in 2003 and \$1.096 billion in 2002—translating into a steady growth in imports. Meanwhile, exported leather dropped to \$1.587 billion during 2004 against \$1.627 billion in previous years—showing negative growth.

West Coast USA

In 1857, an article in the Pacific Sentinel listed four tanners in Santa Cruz California: the Kirby and Jones tannery, located then on Mission Hill, the Porter Brothers in Soquel, C. Brown and Company on Laurel and the Grove Tannery operated by William Warren and James Duncan on what was to become the Salz Tannery on River Street. These four, according to the article, were able to tan and dress 10,000 hides a year. In addition, the Santa Cruz County manufacturers had established outlets in San Francisco for leather goods that included skirting, harness, belting, bridle and sole leather. In the latter part of the twentieth century Salz built up an excellent reputation for innovative leathers and marketing and produced a number of fine products that were often to be sold out such as their calf like Becerro, Laramie and Latigo. With the rise of the Pacific region it appeared that Salz was in the right place but, however, at the start of 21st century the management decided that the fight to compete was too tough and it was time to bow out, and this effectively ended the leather industry presence on that side of North America.

The power of Portland

As a result the West Coast of the USA is no longer home to major tanners or footwear manufacturers but it nevertheless has enormous influence over the fortunes of the global leather and footwear industries. In reality the USA having lost a footwear manufacturing capital in Brockton, Massachusetts, has gained a footwear knowledge management capital in Portland, Oregon. Beaverton, one of Portland's suburbs, is home to Nike. Portland is also home to adidas USA, as well as Columbia Sportswear. The Portland Development Commission has picked out the sports apparel, equipment and

footwear sector as one of five key industries that will help grow the economy where employment and growth industries have not had an easy time. Employment in the footwear and apparel sectors grew 16% in the metro area between 2001 and 2004, to upwards of 9,500 workers.

It is not so much the big names that give Portland its significance but the small companies and design studios which flourish there and are owned and staffed by ex Nike and adidas staff. These include companies such as AQX Sports, which makes aquatic training shoes, Esatto which makes hiking-boots, Velocity, which is run by Nathan Crary, the grandson of the founder of Danner, to make footwear which moves activity from the heel to the forefoot, and Q Branch, which makes customised footwear.

Nike shines

The star of all this remains, of course, Nike, the largest footwear brand in the world. Its total revenues for the fiscal year ending May 31, 2006, were \$15 billion of which 60% was from sales of footwear. It directly employs about 26,000 people and approximately a further 650,000 indirectly through Nike contracted factories around the globe. And it has been the inspiration for the advance of globalisation within the footwear industry. The Pacific Rim has played an important part in Nike's history ever since the company's inception when the company's co-founder Phil Knight first began importing shoes from Japan in 1963. Nike Asia Pacific has been in operation since 1977, when it began to sell footwear in the region and subcontract the production to factories in Taiwan and Korea. Nike Japan was established in 1981. The next few years saw China become both a major production source as well as a vital long-term market.

The Asia Pacific region is now Nike's third largest in terms of revenue and by far the biggest in terms of manufacturing. It employs approximately 3,282 people in the region directly and has 252 contract factories in North Asia and 238 in South, employing between then over 550,000 workers. It has 13 branch offices and subsidiaries all over the region, including Australia, China, Hong Kong, India, Indonesia, Japan, Korea, New Zealand, Singapore, Malaysia, the Philippines, Thailand, Sri Lanka, Taiwan and Vietnam. The phenomenon that is Nike just keeps on going and its importance to the region cannot be overstressed, nor of course, can the importance of the region to Nike, nor to the leather industry as a whole. ☺