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Reality check

First, a necessary vent. If the intention of the ACLE was to portray an industry weakened by a slowdown in footwear sales and desperate to constrain expenses, then Shanghai 2016 was a success. Economical would be a polite expression to describe the forum and layout of the facilities and in addition the supporting services were not consistent with the various attractions offered by this global city. Disappointment was a common thread associated with discussions, participation and quality of the various stands. While there were most likely some exceptions, the organisers did a second-rate job of showcasing an industry that today is challenged to compete with synthetics. Why is this concept so hard? With more than 50% of the global hide supply destined for China, the Shanghai show should be the centre of the leather universe and not a farmers' market, where artisans come and pitch their products from hastily assembled tents.

Now back to more pressing issues. Let's not hide from the news, which frankly is not positive or even optimistic. No, I am not referring to machinations of the US political spectacle, but more specifically narrowing the focus to the leather business. There is a strong case to be made for "easing, followed by adjustments, thereafter realignment". Yes, it's becoming clearer that the demand for auto-leather is beginning to abate. After a sustained drive these past six years, light vehicle sales are losing traction and the long and winding road is now causing manufacturers to decelerate. North American volumes have peaked with their 2015 highs and while the proportion both of SUV and luxury cars has grown, overall the numbers are slowing. In China we will no doubt see similar patterns of congestion and as the market contracts we will indubitably see the brakes applied to leather seating. Please do not be alarmed or rush for the off ramp: the auto-leather business, which had been operating in the fast lane is now simply slowing down. Tanners that function in the luxury segment will continue to enjoy moderate volume while the commodity parts suppliers will battle for price-related victories, which naturally will squeeze margins.

In its simplest form, shoe leather business is not changing for the better. On September 21, adidas launched the Futurecraft M.F.G, which represents the future of localised footwear manufacturing. It is a great application of technology combined with shortened delivery timeframes, but leather, the one key ingredient that's near and dear to all our hearts, is missing. This

apparently seems to be the diagnosis many wish to ignore. Not believing there is a lack of leather usage in footwear is akin to ignoring the cognitive distortions that lead to emotional insecurity and depression, all of which are clearly apparent in today's market. Sellers remain optimistic in stating the rally is just around the corner while buyers, who are actually standing on the corner, solicit customers to sample their wares. There is no stand-off, no face-down and clearly no bluff. New leather orders from the shoe sector are deficient and clearly not encouraging. The trend for alternative substrates and retail margin opportunities are the number-one priority, and therefore it is true to observe that leather not only has lost its sole but also its upper place on top.

So what's happening to raw material prices? The hide market is attempting to recover from one giant hangover. The excesses of the great bull market, in which producers and sellers alike became intoxicated from the exuberance of high prices, are now faced with morning-after syndrome, which neither the "hair of the dog" nor a special pill will resolve. "Fess up", "accept responsibility" and "take the punishment" are all apt phrases that apply to all participants. As the cure is more drawn out compared to the symptom, we are collectively trying to find every reason why the market will stay trapped within its current trading range, but from the demand side it sure don't look peachy.

On the supply side of the equation, beef margins have improved dramatically enhancing the belief that irrespective of demand, you build it and they will come. It's been a long time since beef producers have enjoyed the returns currently being



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experienced and this relegates by-product values to the sidelines and pressures the purveyors of spin to cling to bullish beliefs. Corn is the currency whose value has been pummelled to levels not seen in a few years, the consequence of which is a more viable ration for feed and a better economic proposition. Tantamount to releasing the Kraken, producers are killing with abandon and 2016 will bear witness to a turnaround in the beef business. So much for the clarion call for lower cattle inventories and overpriced beef products when beef was being positioned more for the luxury market compared to chicken and pork. Wow, what a turnaround and market change.

US export volume increased by 8% in July from a year earlier according to statistics released by USDA and compiled by the US Meat Export Federation (USMEF). Beef export value for July was 5% less at \$526.7 million. For January through July, export volume was up 4% to 640,888 tonnes, while value fell 10% to \$3.44 billion. On the surface all positive indicators for increased hide supply.

This year's ample supply of beef is primarily driven by year-on-year increases in commercial cattle slaughter (4% more) and heavy dressed weights (seven pounds

heavier). Forward projections show a continued gain in beef production into 2017 as the increased availability of slaughter-ready cattle and generally heavier carcasses result in more beef, USDA analysts say. They add: "Annual beef production is forecast to reach 25 billion pounds in 2016, up 5.3% from last year. Total commercial beef production in 2017 is forecast 3.4% higher at nearly 26 billion pounds." So we are going to see more and heavier hides, which based on the above mentioned numbers equates to over 1.2 million more hides; this is in the face of reduced leather for footwear and translates into lower hide prices.

From an international perspective the US dollar is not helping matters as the greenback remains very strong and is a reason for price pressure. With more than 94% of all US hides being exported the currency influence is a factor. We can expect at least a 3%-5% "scratch" or "greenback" effect as global buyers look to offset their banking conversion costs with adjusted raw hide levels.

Putting all the above together in one tidy package we come to the conclusion that Newton's Law of Gravity is once again proved correct. Prices will continue to adjust as the gravity of supply and the

lack of broad shoe leather demand will bring the hide market into a more reasonable and economic range.

So what's the solution to ACLE? The organisers need to think in broader and more sophisticated terms. While it's a given that the number of attendees will be assured, it's the quality and type of person who will be encouraged or attracted to participate. This year we witnessed an increase in street-sellers hawking their fake watches and pens while gobbling up any free swag that was positioned on welcome tables. Most of the exhibitors spent more time swatting away these people compared to welcoming global buyers. The fair should nurture and encourage exhibitors with published resumes and adhere to the precepts of the ACLE being a leather fair and not a forum for synthetics. The event in 2016 could be described as a bait-and-switch event where the draw was leather and the ensemble was faux, fake and fictitious. Providing a first-class environment, with a more concerted and thoughtful approach to promoting this incredible raw material is essential in making Shanghai the epicentre of global leather manufacturing. Having the air-conditioning switched on would also be a plus. ☺



The popularity of SUVs has led Audi to update its Q3 model. SUVs' share of the car market has grown, although overall growth is now beginning to slow down. CREDIT: AUDI AG