



CLUSTER DEVELOPMENT INITIATIVE



The CDI is jointly implemented by PSIC & UNIDO



DIAGNOSTIC STUDY REPORT ON LEATHER FOOTWEAR



40, T Block Gulberg-II, Lahore. PAKISTAN

Phone: 042 35714083-86

www.cdi.psic.gov.pk

ACKNOWLEDGEMENT

Diagnostic Study Report

This diagnostic study has been carried out as part of the Cluster Development Initiative Project (CDI), conceived, funded and executed by Punjab Small Industries Corporation (PSIC). The Government of Punjab, under a Trust Fund Agreement, engaged United Nations Industrial Development Organization (UNIDO) as the implementing partner for capacity building of the cluster teams, planning and executing Competitive Reinforcement Initiatives (CRIs).

The completion of the diagnostic study is an important milestone achieved so far and is a result of the combined efforts and support of various individuals and institutions. We would like to thank the international experts on Cluster Development, Mr. Vedat Kunt and Mr. Nima Bahramalian, engaged by UNIDO, for training of the cluster teams and supervision of the Diagnostic Study Report. We are also thankful to Mr. Badar ul Islam, National Project Coordinator and Mr. Qasar Wasique Ahmad, National Technical Expert, UNIDO for their support and assistance.

The Cluster team is grateful to Dr. Muhammad Mujtaba Piracha, Secretary Industries, Commerce & Investment Department, Government of Punjab and Mr. Khalid Saleem, Managing Director, PSIC for their continued support and guidance in the execution of the project. We are also obliged to the CDI Project Director, Mr. Fazal ur Rehman and Additional Project Director, Mr. Hamid Mahmood Malhi, along with the support staff, for facilitating the cluster teams in every possible way.

The Leather Footwear & Products Cluster team would also like to thank the Pakistan Footwear Manufacturers Association (PFMA), Principle manufacturing firms, Business Development Service Providers, Training Service Providers, companies operating in backward and forward channels and sector experts for their timely response and kind support towards the CDI project.

*Farazia Majid, Cluster Manager
Qasim Ali, Deputy Cluster Manager
Faizan Shoukat, Cluster Facilitator*

Table of

Contents



Executive Summary	1	3.6 Marketing & Market Analysis	45
1. Introduction		3.7 Business Resources	47
1.1.1 Objectives of the Diagnostic Study	4	3.8 Human Resource	48
1.1.2 J&C Programme and the Cluster Development Initiative	5	3.9 Infrastructure & Superstructure	50
1.1.3 Cluster Development	6	3.10 Compliance & Certifications	51
1.2 Limitations of the Study	6	3.11 Competitors & Competition	52
1.3 Approach towards Diagnostic Study	7	3.12 Cluster Governance	53
1.3.1 Development of Questionnaire	7	3.13 Operations Management	54
1.3.2 Data Collection	7		
1.3.3 Analytical Tools Applied	7	4. Analytical Tools Applied	
1.4 Industry Scenario	8	4.1 PESTEL Analysis	55
1.4.1 History of the Industry	8	4.1.1 PESTEL At National Level	55
1.4.2 Overview of Pakistan's Footwear Sector	8	4.1.2 PESTEL at Cluster Level	57
1.4.3 Global Scenario of the Footwear Industry	11	4.2 Five Forces	60
1.4.4 Snapshot of Pakistan Footwear Industry	18	4.3 SWOT Analysis	63
1.4.5 Geographical Concentration	21	4.4 Diamond Model	67
1.4.6 Socio Economic Indicators	22	4.5 Value Chain Analysis	69
1.4.7 Major Actors	24	4.5.1 Formal Shoe-Value Addition & Water Fall Diagram	72
		4.5.2 Casual Shoe-Value Addition & Water Fall Diagram	73
2. Institutional Setup & Framework		4.6 Cooperation Matrix	76
2.1 Government Sector	27	4.7 Cluster Map	78
2.2 Autonomous Bodies	29		
2.3 International Agencies	30	Key Constraints, Explanations & Recommendations	
2.4 Other Support Institutions	31	5. Snapshot of Field Visits	86
2.5 Financial Institutions	32	6. List of abbreviations	88
		7. References	89
3. Footwear Industry Assessment			
3.1 Trends	34		
3.2 Raw Materials	37		
3.3 Production Processes Flow Chart	39		
3.3.1 Production Details	40		
3.4 Technology	42		
3.5 Innovation & R-D	44		



Executive Summary

The cluster concept has gained prominence as an economic policy tool aimed to foster innovation and the growth of a competitive private sector in developing as well as developed countries. Clusters play a critical role in generating employment, income, increasing exports, fostering innovation, and developing opportunities for the local community to become drivers of broad-based local economic development.



The Government of Punjab has recently adopted the “Punjab Growth Strategy”, which incorporates a target of annual 8% annual GDP growth within the Province. As a step towards enhancing the development of private sector, the Government of Punjab has developed an Industrial Sector Development Plan, oriented towards increasing private sector investment, thereby enhancing job creation and exports. As a part of this, the Government introduced a Cluster Development Initiative (CDI) program to support the growth and competitiveness of key manufacturing clusters, based on international best practices. The Cluster Development Initiative (CDI) is a project under World Bank’s Jobs & Competitiveness Program. The key objectives of the CDI include driving productivity and competitiveness through established SME manufacturing clusters in Punjab.



In the framework of the Punjab Jobs and Competitiveness Programme, the Government of Punjab has signed a cooperation agreement with United Nations Industrial Development Organization (UNIDO) to provide technical assistance for the development of industrial clusters in Punjab province and to support their further integration into global value chains.

The objectives of this study are to identify the problems and advantages of the cluster eco system, prepare a roadmap and policy guideline for future interventions in the sector to facilitate growth through cluster based industrial



development. Under UNIDO’s guidance, a questionnaire was developed by the CDI team, covering critical areas of information. Thereafter, an in depth diagnosis was carried out which included meetings with principle firms, support institutions, financial institutions, business development service providers, suppliers, and customers of the sector as well as through desk research.

As a country, Pakistan is the 6th largest producer of footwear in the world; however, since major production is domestically utilized, the exports currently stand at 3.3% of the annual production of 366 million pairs (2015). The overall share of the Pakistani footwear in the global market is less than 0.1%. According to the Trade Map, Pakistan shows a positive trend in exports of HS-code 6403, which is footwear with outer soles of leather or leather composition (uppers of leather).

The footwear sector of Pakistan is mainly concentrated in & around Lahore, which contributes 70% of the total footwear production. The export needs are fulfilled by the organized / mechanized sector almost exclusively. In addition to the formal mechanized sector, the cottage industry also supplies the bulk of the domestic needs according to changing designs and tastes around the year. Entire families are working to produce low priced and low quality shoes for the local market. These are traditionally made through manual methods.

This diagnostic study used various analytical tools and models including Value Chain Analysis, Porter’s Five Forces, Cooperation Matrix & Cluster Map to highlight gaps & relationships among the major stakeholders of this sector. A comparative analysis of footwear produced & sold in Pakistan with standard pricing techniques has been carried out to highlight the value capturing points vis a vis deviations in pricing patterns between Pakistan & Europe.

The key constraints of the cluster may be summarized as follows:

- Weak Product Development & Design: Weak R&D in the industry as well as weak linkages with the academia has resulted in lack of innovation and design capabilities, especially in sole making. In exports, the Pakistani manufacturers produce on behalf of international brands and customers, whereby the design is given to them by the customer itself. Designs are also emulated through the internet or by buying samples.



1. INTRODUCTION

- **Lack of Expertise in Markets & Marketing:** Manufacturers are not dynamic in experimenting with new business models and marketing to consumers directly. Consultancy services related to marketing and branding are weak.
- **Insufficient Skilled Labour:** A large proportion of the labour, owing to the seasonality factor, is hired on piece rate/contractual basis, leading to higher turnover. Female employment remains low due to social, cultural and working environments. Training institutes like GILT do not have adequate running funds to cover practical costs.
- **Limited Presence of Support Industry & Technology:** Negligent investment in the support industry in footwear sector has resulted in the industry importing ancillary items, increasing both lead time and cost. The import lowers profit margins as well as efficiency.
- **Lack of Third Party Compliance Support:** Some laboratories have been built by the public sector including PCSIR and CPC. However, these lack international accreditation. Private companies including TTI, SGS and Intertek offer limited testing services.
- **Rules & Regulations:** There is a lack of a dedicated policy/ strategy regarding the footwear sector. The industry is either not part of the policy making process or is not given the whole picture. This results in formulation of policies, which are not beneficial to the industry.

This report contains a set of recommendations in areas including but not limited to Product Design & Finishing, Marketing, Support Industry, Compliance & Certifications, Policy Formulation, etc in order to generate collaborations amongst various value chain actors, support institutions and BDSPs for the growth of the Lahore footwear cluster.

1.1.1 Objective of the Diagnostic Study

The objective of this study is to assess the competitiveness of the footwear sector, understand the dynamics of supply and demand factors, support mechanisms as well as linkages between backward and forward industries and cluster actors. Principal firms of the cluster, suppliers, support institutions and business development service providers were met and interviewed. Data and information gathered from secondary sources was analyzed in order to understand common problems, advantages and disadvantages of the cluster.

This study addresses factors that have contributed to the development of the cluster and the barriers that hinder its growth. It also helps understand the comparative socio-economic environment of the cluster, identify effective leverage points for intervention, provide a baseline for future monitoring and evaluation, and help build initial trust with and among the stakeholders. The study also entails potential intervention areas to overcome the prevailing issues vis-à-vis possibilities of joint actions on the part of cluster actors.

1.1.2 Jobs and Competitiveness Programme and the Cluster Development Initiative

Keeping in view the stagnant growth of the manufacturing clusters in Punjab, the Government of Punjab has recently adopted the “Punjab Growth Strategy”, which incorporates a target of 8% annual GDP growth within the province. The Industrial Sector Development Plan, an element of the Growth Strategy, is oriented towards increasing private sector investment, thereby increasing job creation and exports. As part of the development plan, the Government has introduced Cluster Development Initiative (CDI) to support the growth and competitiveness of key manufacturing clusters, in particular through interventions of the Punjab Small Industries Cooperation (PSIC). This initiative is part of a larger cooperation on “Jobs and Competitiveness” programme with the World Bank.

In the framework of the Punjab Jobs and Competitiveness Programme, the Government of Punjab has signed a cooperation agreement with UNIDO (United Nations Industrial Development Organisation) to provide technical assistance for the development of industrial clusters in Punjab province and to support their further integration into global value chains.

The purpose of CDI is to create an enabling environment for growth and prosperity of industries, to create better quality of life through economic uplift in Punjab and to upgrade technology and enhance productivity, quality and profitability of local industries. The lead on the implementation of the CDI for the Government of Punjab is with the Punjab Small Industries Cooperation (PSIC).

In consultation with UNIDO, clusters with high potential for growth in Punjab were identified and the following four pilot clusters have been selected;

- Readymade Garments
- Auto parts
- Leather Footwear
- Surgical Instruments



1.1.3 Cluster Development

The cluster concept has gained prominence as an economic policy tool aimed to foster innovation and growth of a competitive private sector in developing as well as developed countries.

Clusters play a critical role in generating employment, income, increasing exports, fostering innovation, and opportunities for the local community and become drivers of broad-based local economic development.



As a starting point for Cluster Development, it is imperative that a thorough diagnostic study needs to be carried out; then a strategy and action plan built upon the main findings of the study, in consultation and most importantly in consensus with the cluster stakeholders.

1.2 LIMITATIONS OF THE STUDY

It is important to stress that, in a complex socio-economic environment and in a micro and small enterprise cluster environment, no one-off study can be expected to identify all relevant issues and their remedies. The diagnostic study provides an entry framework, a snapshot of the existing business environment with current possible opportunities, threats and the cluster’s advantages and disadvantages. These need to be regularly fine-tuned and revised with the stakeholders and supplemented with specialized studies, on a need basis, at later stages.

1.3 APPROACH TOWARDS THE DIAGNOSTIC STUDY

1.3.1 Development of Questionnaire

A comprehensive questionnaire was developed in joint consultation with UNIDO for various actors in the cluster. These included the principle manufacturers, the training institutions and the support industry. A detailed study of the secondary sources, comprehensive training sessions by UNIDO and adaptation of the questionnaire to the needs of the relevant stakeholders, as and when needed, resulted in the development of the final questionnaire.

The main areas covered in the questionnaire include Social, Economic and Value Chain Dynamics of the Cluster, Production, Cluster Connection & Supply Chain, Certifications, Operation Management, Technology, Raw Materials, Business Resources, Human Resource Development, Institutional Support, Marketing, Infrastructure, etc

1.3.2 Data Collection

The 'Leather Footwear and Products' cluster for Lahore manufacturers can be categorized in Large, Medium, Small Firms and Cottage sector. The Pakistan Footwear Manufacturers Association (PFMA) is the representative body of footwear manufacturers. This provides a platform to members for various activities including seminars, trainings, identifying problems being faced by the stakeholders and submission of findings to the Government, among others. Out of 203 principle firms, in and around Lahore, 70 were contacted, out of which 28 responded. In addition to these surveyed firms, training institutions, international donor agencies and members of the support industry were also interviewed.

1.3.3 Analytical Tools used

SWOT Analysis:

SWOT analysis is a tool used to identify not only the strategic position of the manufacturers, but that of all major actors in the supply chain. This helps in recognizing the current situation of the business environment and preparing for future possibilities. SWOT is a combination of four factors - Strengths, Weaknesses, Opportunities and Threats. It covers all factors (positive and negative) that can affect the cluster's success. In this study, the CDI team did a SWOT analysis for all the major actors in the supply chain.

Other Models:

This Diagnostic study also includes other models including Porter's Five Forces, Waterfall Diagram, Diamond Model, Pestle Analysis, etc.



1.4 INDUSTRY SCENARIO

1.4.1 History of the Industry

Pakistan has inherited century's old craftsman-ship of shoe making. With the passage of time, efficient skills were blended with modern technology, and the sector began producing a wide range of highly attractive styles and designs to cater to the needs of customers.

During the 1950s well-equipped tanneries were set up at Karachi and Lahore. During the 60s and 70s more units were established at Hyderabad, Kasur, Sialkot, Multan, Sahiwal and Gujranwala. Well-developed tanneries and an abundant supply of quality leather gave rise to the establishment of related industries including leather garments, footwear, gloves and products. Rising costs of manufacturing units in various industries including footwear in the developed countries resulted in shifting these units to low cost regions like Asia. More than 70% of the world footwear production is made in Asia. Footwear is the sub-sector that has the maximum potential for value addition in finished leather, with improvement in quality and innovation. Leather industry, including leather products, is one of the major export-earning sectors in Pakistan.

1.4.2 Overview of Pakistan's Footwear

The footwear sector is a labor intensive industry which enjoys growth in both domestic and international markets. The overall employment generated by the footwear sector, including both direct and indirect is estimated to be around 500,000. At present, some of the renowned manufacturing firms in footwear are Bata Pakistan Ltd., Servis Shoe industries Ltd., Footlib Pvt Ltd, Firhaj Footwear, Urban Sole, Starlet Shoes etc.

Pakistan's footwear industry presently produces almost all the varieties of shoes and sandals for men, women and children which include the following: leather footwear for men, women & children, artificial leather shoes, heavy duty boots for army and police, sports shoes, joggers, safety footwear & rubber shoes.

Visual Products Mapping

(Major Products of Footwear Cluster)

Men's Shoes



Women's Shoes



Kids Shoes



Sports & Athletics



Army, Police & Safety Shoes



Rising costs of manufacturing units in the developed countries have resulted in a shift towards low cost regions like Asia. Despite being the major raw material producer, Pakistan is unable to tap the world market as its share is below 0.1% in world exports of footwear. The industry has the capability and resources to take a lead in the world market, which may be achieved by better utilization of resources, skill building and promoting allied industry.

1.4.3 Global Scenario of the Footwear Industry

According to APICCAPS', the worldwide production of footwear in 2015 reached 23.0 billion pairs, 0.4% down from the revised estimate from the previous year.

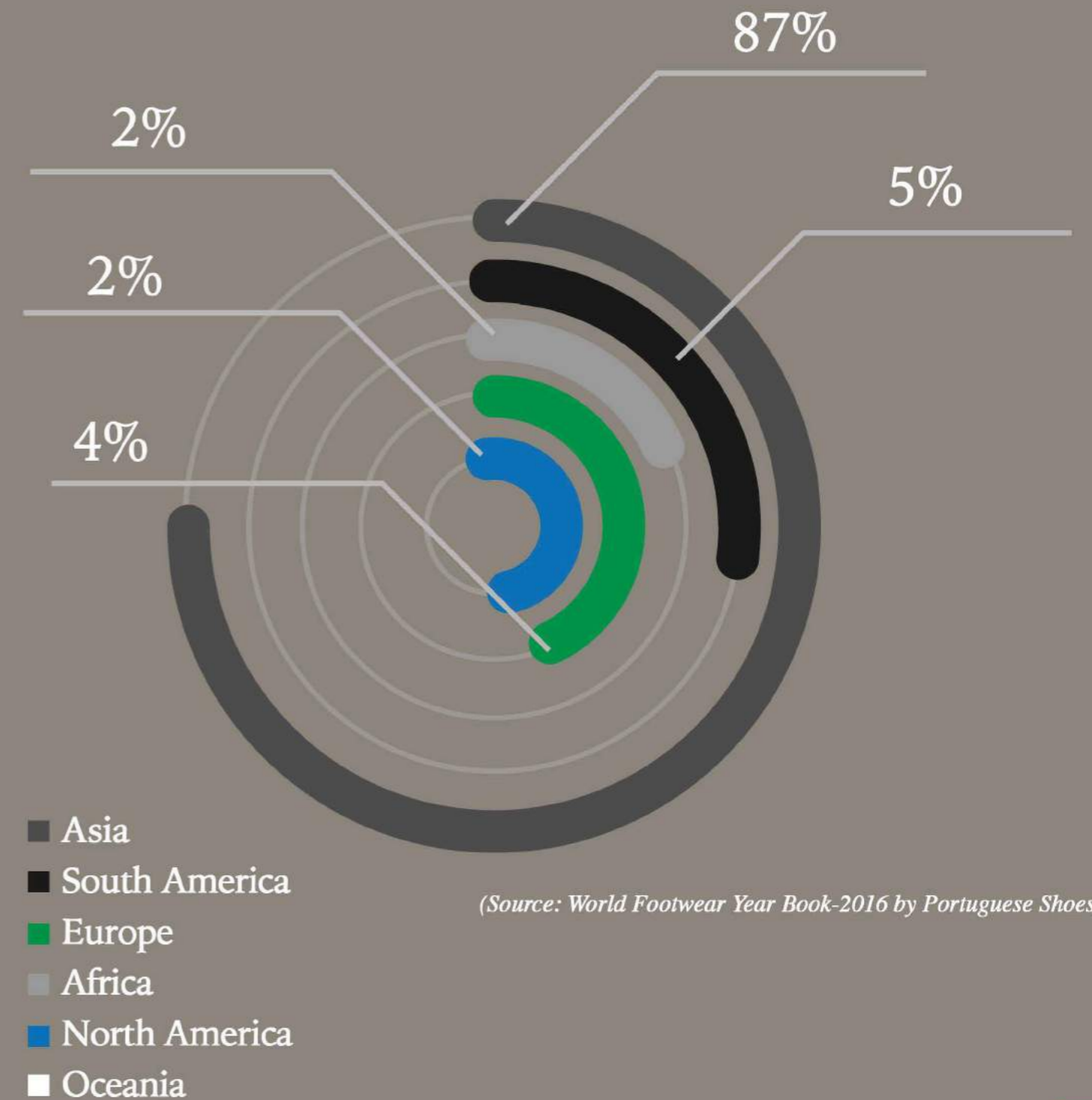
Although there have been slight disparities in the yearly market share, the general trend at the continental level has remained fundamentally unchanged since 2011. 86.8% of world production remains in Asia, with China being the undisputed leader. The year 2015 noted a decline in Chinese production by 5%, dropping its market share to 59.1%. However, India, Vietnam and Indonesia strengthened their positions. Thailand replaced Italy at the bottom of this table. Brazil and Mexico are the only non-Asian countries here:

Top 10 Footwear Producing Countries

Rank	Country	Pairs (In Millions)	World Share
1	China	13581	59.1%
2	India	2200	9.6%
3	Vietnam	1140	5.0%
4	Indonesia	1000	4.4%
5	Brazil	877	3.8%
6	Pakistan	366	1.6%
7	Bangladesh	353	1.5%
8	Turkey	350	1.5%
9	Mexico	251	1.1%
10	Thailand	200	0.9%

(Source: World Footwear Year Book-2016 by Portuguese Shoes)

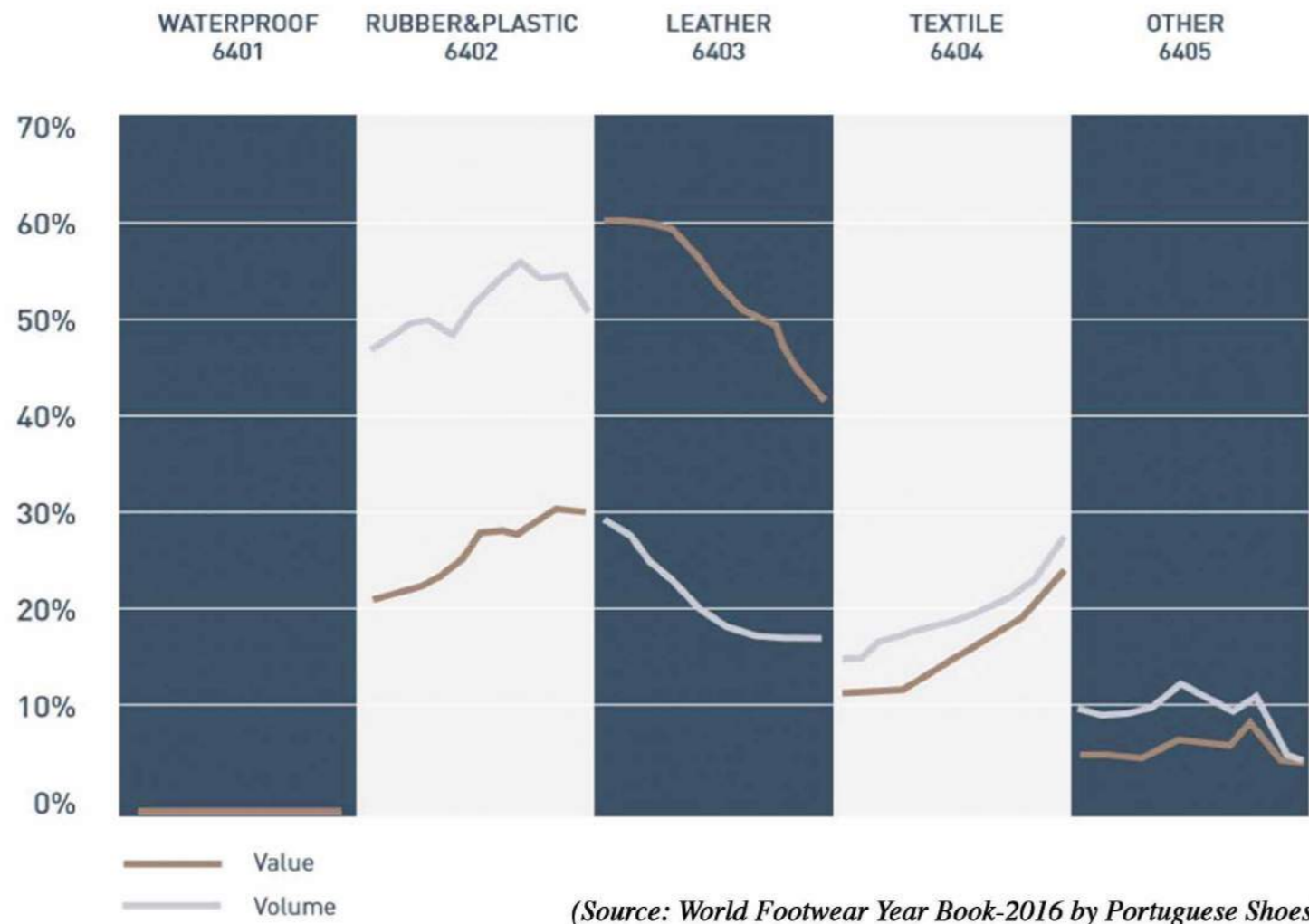
Distribution of Footwear by Continent (Quantity) 2015



(Source: World Footwear Year Book-2016 by Portuguese Shoes)



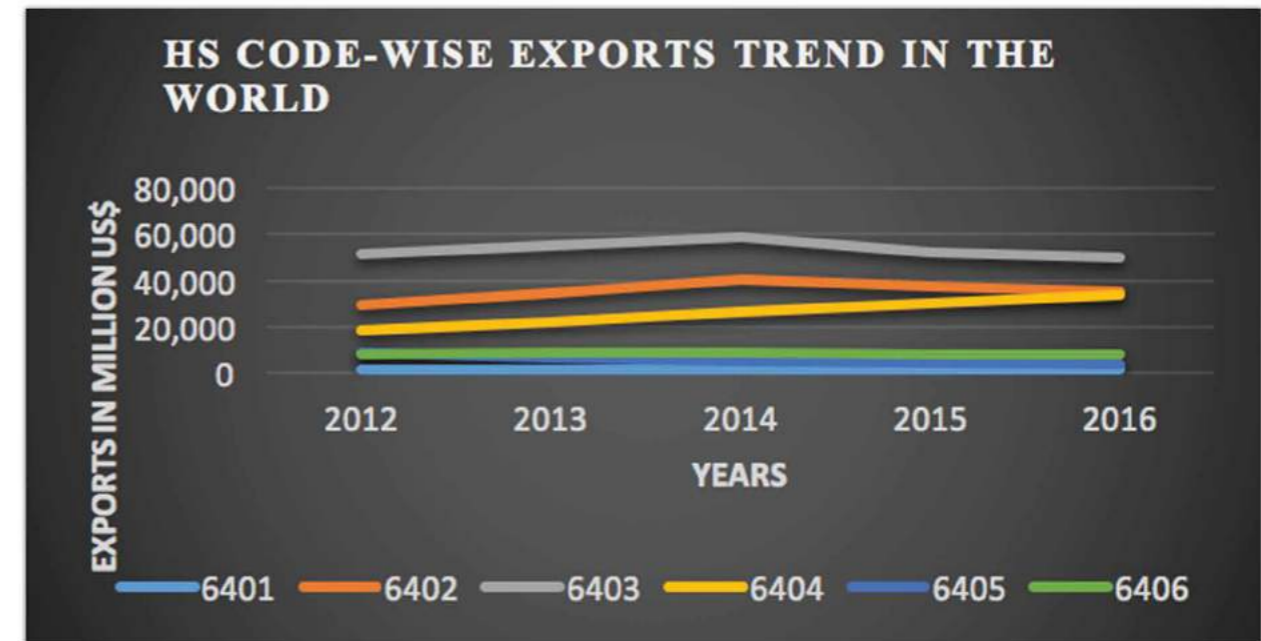
Statistics reveal that textile footwear has grown significantly in terms of both value and volume. Additionally, the percentage of leather footwear in overall exports is declining and is currently at 42% in terms of value and 15% in terms of volume. Rubber and plastic footwear represent 30% of the traded value.



Relationship between Trends in International Export Market & Local Industry's Approach:

Pakistan is also producing for popular brands including Caterpillar, Pierre Cardin, Kurt Geiger and Caprice among others. The ITC Trade Map time series data of the last 5 years reveals that there is an upward trend in exports of footwear under HS Code-6404 (having outer soles of rubber, plastics, leather or composition leather and uppers of textile materials) whereas exports of footwear under HS Code-6402 (footwear with outer soles and uppers of rubber or plastic) and under HS Code-6403 (footwear with outer soles of rubber, plastic, leather or composition leather and uppers of leather) is declining. Other types of footwear are almost stagnant.

In contrast, Pakistan's main focus is still under HS Code-6403 where there is a continuous decline. The world market is increasing under HS Code-6404 even though less focus is in exporting such products.



(Source: ITC Trade Map)

Decline in Leather Footwear

Manufacturers in the International Market

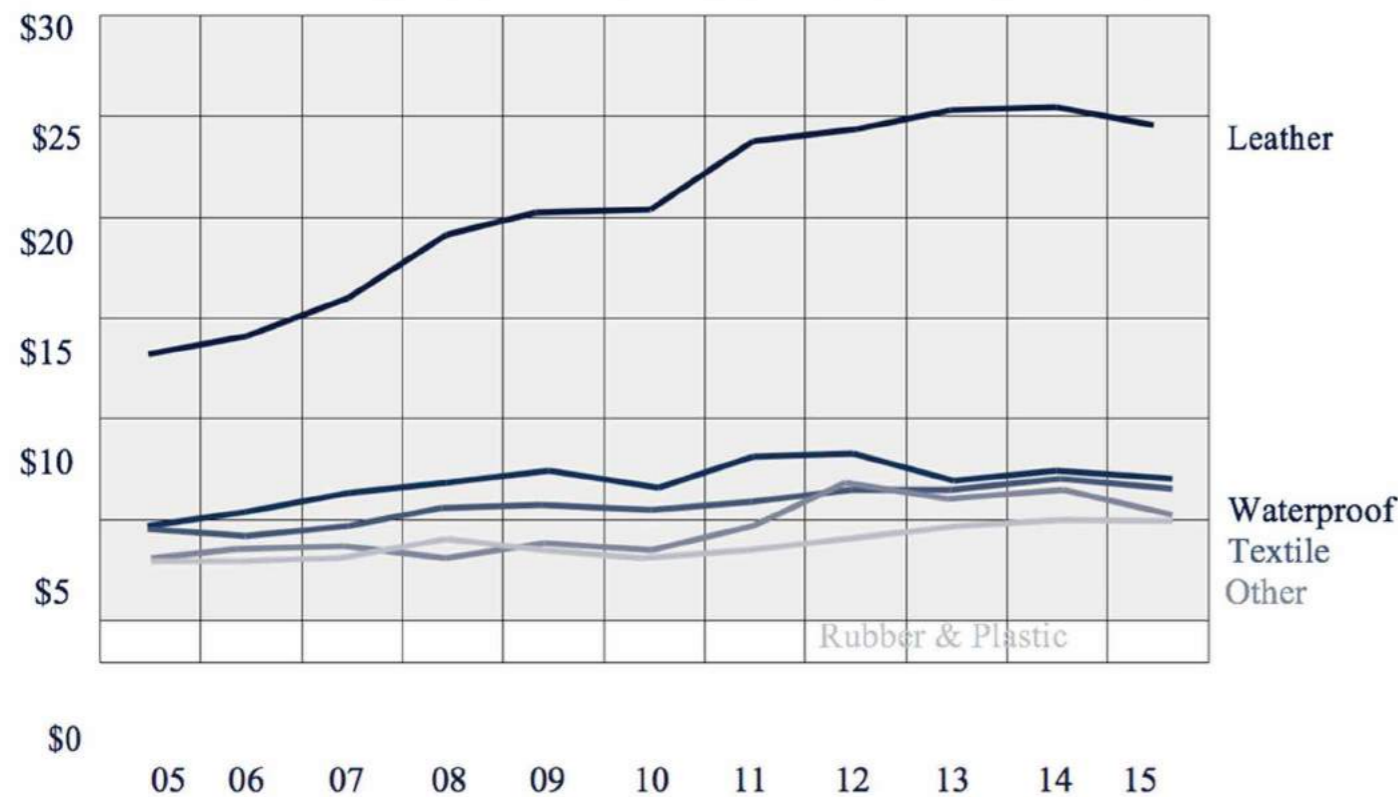
There has been an overall decline in leather footwear across the world (mainly Asia and Europe) but this is especially apparent in South America. Currently, it is 14% of the whole, down from 52% ten years ago. All three continents maintained their share in leather in 2015. However, trends were less apparent in other parts of the world, owing in part to issues in data collecting for some countries.

The average export price of leather shoes reported in 2015 was US \$24.39. This was much higher than that of the others, almost 4-5 times higher. Asia exhibits the minimum average price of leather footwear at US \$17.80 and Europe reports the maximum at US \$38.90. There is more disparity between continents in non-leather footwear. Footwear that showed an upward trend in 2015 included rubber & plastic, and textile footwear. Last year prices decreased by 4% for leather footwear, 1% for waterproof footwear and 10% for 'other' footwear.

There is a significant difference in how the footwear manufacturers around the world deal in international markets. China exports 73% of the pairs of footwear it produces which makes it the largest footwear producer in the world. Turkey (52%), Thailand (62%) and Cambodia (83%) are other major exporters. However, India (9%), Indonesia (19%), Brazil (14%), Pakistan (3%), Bangladesh (14%) and Mexico (11%) cater mainly to their local markets. Portugal exports everything it produces (101%), while Italy (109%) and Spain (150%) export more than they manufacture.

The average prices of the big manufacturers also differ: Italy is (46.21 dollars), Portugal (26.08 dollars) and Japan (25.62 dollars). Iran and Turkey charge less than 5 dollars per pair, the average price charged by Thailand and China.

Average Price by Type of Product 2005-2015



(Source: World Footwear Year Book-2016 by Portuguese Shoes)

Top 10 Footwear Producers of the World in 2015

Rank	Country	2011		2015		Export
		Pairs (Millions)	World Share	Pairs (Millions)	World Share	
1	China	12887	60.5%	13581	59.1%	72.7%
2	India	2209	10.4%	2200	9.6%	9.4%
3	Vietnam	804	3.8%	1140	5.0%	91.3%
4	Indonesia	700	3.3%	1000	4.4%	19.2%
5	Brazil	819	3.8%	877	3.8%	14.1%
6	Pakistan	298	1.4%	366	1.6%	3.3%
7	Bangladesh	276	1.3%	353	1.5%	15.5%
8	Turkey	188	0.9%	350	1.5%	51.6%
9	Mexico	253	1.2%	251	1.1%	11%
10	Thailand	244	1.2%	200	0.9%	62.4%

(Source: World Footwear Year Book 2012 & 2016 by Portuguese Shoes)

Vietnam was the only one of the top 5 exporters of Asia to increase its exports in 2015, and in terms of value, is approaching one-fifth of the continent's total exports. However, China's top position remains unparalleled, owing to a much lower average price than that of its regional partners.

Top 5 Exporters of Asia (2015)

Rank	Country	US\$ (Millions)	Continent Share	Pairs (Million)	Continent Share	Average Price
1	China	51194	63.2%	9878	81.7%	\$ 5.18
2	Vietnam	15041	18.6%	1041	8.6%	\$ 14.45
3	Indonesia	3972	4.9%	192	1.6%	\$ 20.65
4	Hong Kong	3578	4.4%	208	1.7%	\$ 17.19
5	India	2465	3.0%	207	1.7%	\$ 11.92

(Source: World Footwear Year Book-2016 by Portuguese Shoes)

Top Exporters of Leather Footwear

Leather footwear exports declined overall by 11% in 2015. With the exception of Portugal changing places with India, the top 10 exporters of leather footwear in 2015 remained the same and in the same order. China retains its top most position in the producer category despite losing market share in comparison to 2014. The market share for Vietnam increased considerably and moved to third place, next to Italy which is in second position.

Top 10 Exporters of Leather Footwear (HS Code 6403)

Rank	Country	US\$ (Millions)	World Share	Pairs (Millions)	World Share	Average Price
1	China	10922	20.5%	725	33.1%	\$ 15.07
2	Italy	7695	14.4%	125	5.7%	\$ 61.50
3	Vietnam	5965	11.2%	293	13.4%	\$ 20.37
4	Hong Kong	2455	4.6%	90	4.1%	\$ 27.34
5	Germany	2392	4.5%	69	3.1%	\$ 34.74
6	Indonesia	2233	4.2%	95	4.3%	\$ 23.48
7	Spain	2132	4.0%	57	2.6%	\$ 37.46
8	Belgium	1968	3.7%	71	3.2%	\$ 27.86
9	India	1923	3.6%	115	5.3%	\$ 16.72
10	Portugal	1840	3.4%	59	2.7%	\$ 31.00

(Source: World Footwear Year Book-2016 by Portuguese Shoes)

1.4.4 Snapshot of Pakistan Footwear Industry



The Pakistan footwear industry caters primarily to the local market and is among the world's top ten footwear manufacturers at 6th position.

Pakistan's exports in 2015 fell by some 11% while imports increased by almost the same percentage. Pakistan exports mainly to Europe and imports almost exclusively from China.

Pakistan showed exports worth US\$ 116 m in 2015, ranking it 45th in the world in terms of value and 40th in the world in terms of quantity with 12 million pairs. Average price of a Pakistani shoe is almost \$10.

The Imports were displayed at US\$ 89m, making it 87th in the world in terms of value and 79th in terms of quantity with an import of 18 million pairs at an average price of almost \$5.

Footwear Industry of Pakistan (2015)

	Value		Quantity		Price
	Millions USD	World Rank	Million Pairs	World Rank	USD
Exports	\$116	45	12	40	\$9.58
Imports	\$89	87	18	79	\$4.96
Production			366	6	
Consumption			372	12	

(Source: World Footwear Year Book-2016 by Portuguese Shoes)

According to the Trade Map, Pakistan shows a positive trend in exports of HS-code 6403, which is footwear with outer soles of leather or leather composition (uppers of leather). Balance of Trade (BOT) under this HS-Code is favorable i-e \$72.825 million as in 2016 Pakistan's exports were \$86.823 million & imports remained \$13.998 million. In contrast Pakistan has unfavorable BOT under HS-Code 6404 (footwear with uppers of textile materials) where Pakistan imported goods valuing \$54.102 million whereas exports were only \$3.766 leaving BOT at -\$50.336 million. Codes 6401, 6402 and 6406 have negligible transactions

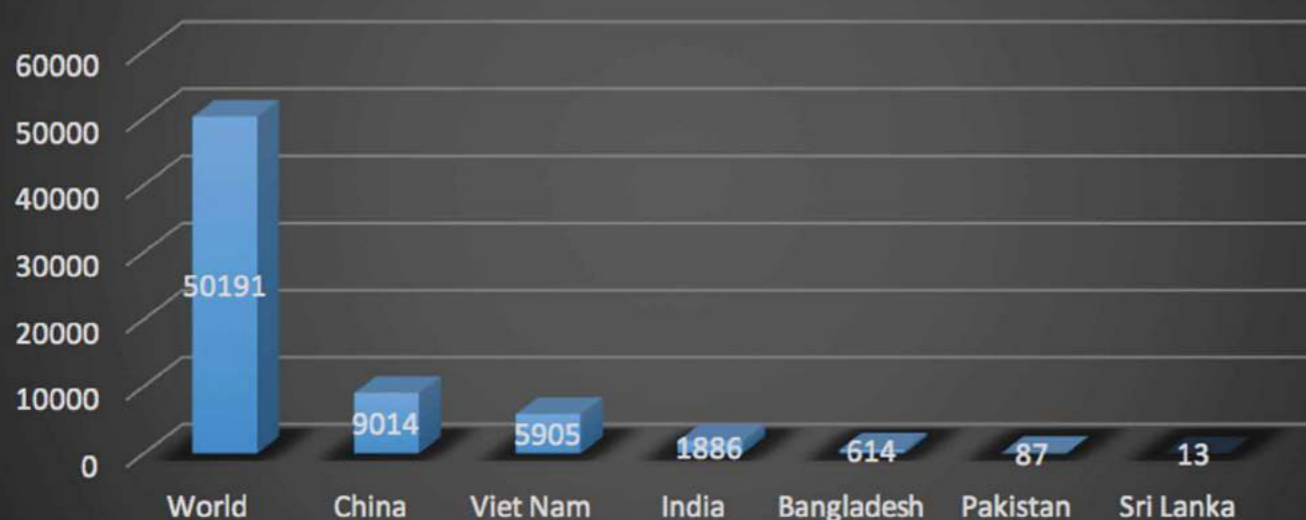
HS Code-Wise Balance of Trade

H.S Code	Product label	BOT 2012	BOT 2013	BOT 2014	BOT 2015	BOT 2016	Exports 2016	Imports 2016
'6403	Footwear with outer soles of rubber, plastics, leather or composition leather (excluding orthopedic footwear, skating boots)	55.454	66.462	89.139	72.942	72.825	86.823	13.998
'6401	Waterproof footwear with outer soles and uppers of rubber or of plastics	-0.007	0.78	0.019	-0.004	0.007	0.046	0.039
'6406	Parts of footwear, incl. uppers whether or not attached to soles other than outer soles	0.012	-0.628	-1.835	-2.485	-1.529	1.713	3.242
'6402	Footwear with outer soles and uppers of rubber or plastics (excluding waterproof footwear)	-10.488	-1.177	2.281	-0.664	-7.15	3.25	10.4
'6405	Footwear with outer soles of rubber or plastics, with uppers other than rubber, plastics, leather	-4.282	-8.336	-18.472	-13.615	-8.606	12.688	21.294
'6404	Footwear with outer soles of rubber, plastics, leather or composition leather and uppers of textile materials	-18.101	-14.842	-22.719	-31.738	-50.336	3.766	54.102

(Source: ITC Trade Map)

Position of Pakistan with respect to its Regional Partners in Exports (HS Code 6403)

HS Code 6403 Exports (Footweares with Uppers of Leather)



(Source: ITC Trade Map)

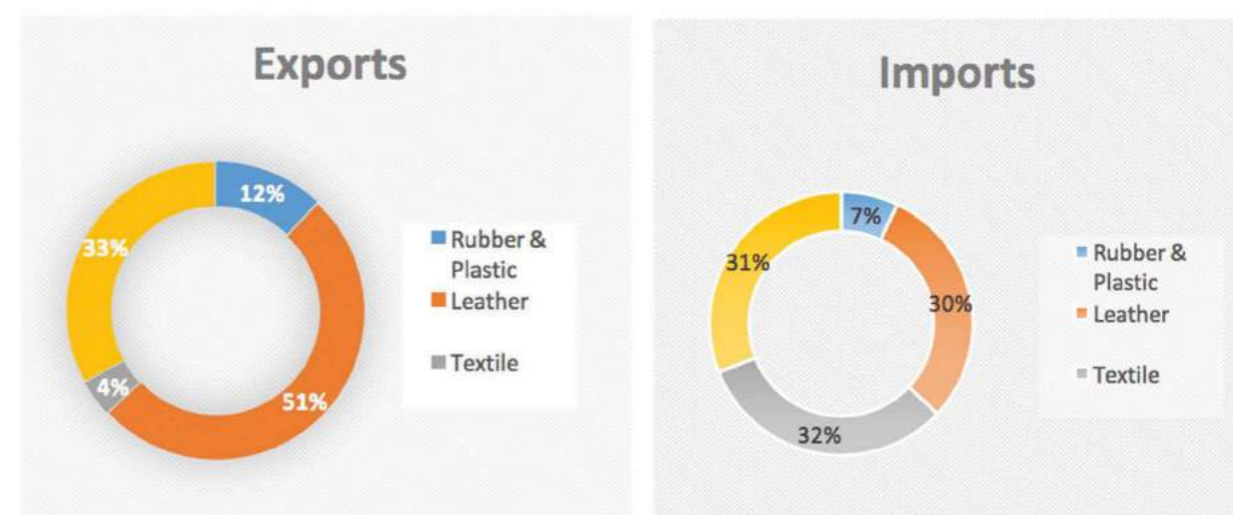


The above graph displays Pakistan's position in exports of HS code 6403, in comparison to its regional competitors. As can be seen, Pakistan is lagging behind both India and Bangladesh. Bangladesh has been awarded the Least Developed Country (LDC) status that allows it to enjoy special privileges in terms of both lower import duty by the importing countries and increased quota, making its product more competitive.

India has grown significantly both in terms of local market and exports to the world. This is partly due to favorable policies implemented by the government for establishment of their support/ auxiliary industry as well as a more proactive role by the manufacturers in terms of quality and finishing. The Indian government also announced an 8% export rebate to counter GSP Plus status that was awarded to Pakistan.

Pakistan faces stiff competition due to several factors including increased lead time, higher input cost and lower export rebates.

Types of Footwear Traded (Pakistan)



As can be seen above, the maximum exports in footwear by Pakistan remains in leather i.e at 51%, while imports are highest in textile footwear. Reasons, among others, include lower purchasing power of the local market. Pakistan imports almost exclusively from China, which has the lowest price in the region.

EXPORT TRENDS

EXPORT MARKETS	Million US\$	Value Share	Million Pairs	Quantity Share	LAST 5 YEARS VARIATIONS	Million US\$
Germany	25	21%	2	13%	Germany	53%
Italy	16	14%	1	11%	Italy	35%
UAE	13	11%	3	27%	UAE	-
UK	10	8%	1	6%	Netherlands	305%
Spain	8	7%	1	4%	Saudi Arabia	-54%

(Source: World Footwear Year Book-2016 by Portuguese Shoes)

Pakistan exports mainly to Europe, with Germany being at the front end of the export market. In the last 5 years, exports to Germany have increased by 53%. In 2015, Pakistan exported footwear worth US\$ 25m, which is 21% in terms of value and 13% in terms of quantity.

IMPORT TRENDS

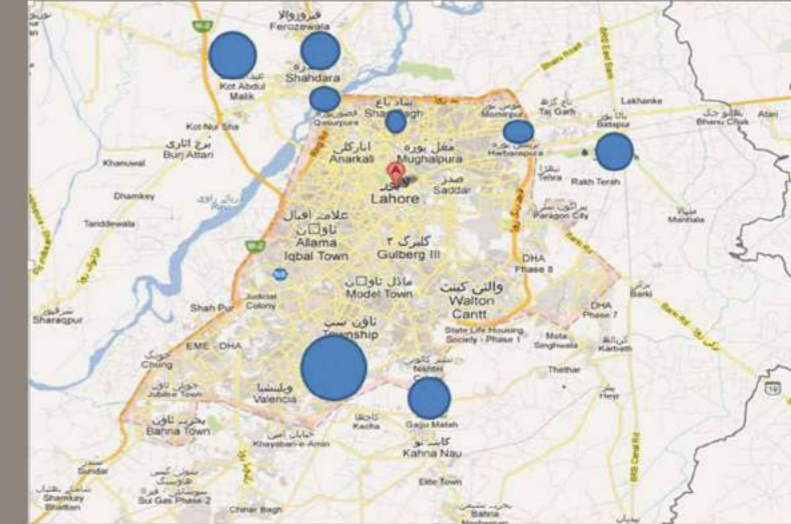
IMPORT MARKETS	Million US\$	Value Share	Million Pairs	Quantity Share	LAST 5 YEARS VARIATIONS	Million US\$
China	81	91%	16.5	92%	China	61%
Thailand	2	3%	0.6	3%	Thailand	-54%
Vietnam	2	2%	0.3	2%	Vietnam	151%
Indonesia	1	1%	0.1	1%	Indonesia	386%
Malaysia	1	1%	0.1	1%	Japan	-98%

(Source: World Footwear Year Book-2016 by Portuguese Shoes)

The import statistics signify China as almost exclusively the main import market of Pakistan, with a value share of 91% and quantity share of 92%. As can be seen above, over the last 5 years, imports from China have increased by 61%.

The following map shows the industry concentration in Lahore.

Industry Concentration (in & around Lahore)



1.4.5 Geographic Concentration

Major industrial setup

The major industrial setup in the footwear industry in Pakistan is in & around Lahore. The main clusters are located at Kot Lakhpat, Ferozpur Road (Gajjumata), Ravi Road, G.T Road (Muridke), Sheikhpura Road (Kot Abdul Malik) & Harbanspura.

CATEGORIZATION OF FOOTWEAR MANUFACTURERS

Category	Punjab Province	Footwear Cluster (in & around Lahore)	Interviewed Firms	Members of PFMA among Interviewed Firms
Large	18	16	10	10
Medium	41	38	7	6
Small	179	149	8	3
Micro	No Data Available		3	0

(Source: Directory of Directorate General IPW&M-Punjab & PFMA)

1.4.6 Socio Economic Indicators of the Lahore city

The city of Lahore is bound on the north and west by Sheikhpura district, on the east by India and on the south by Kasur district. The Ravi River flows on the northern side of Lahore. Lahore district covers a total land area of 1772 Sq. km (Bureau of Statistics, Punjab). The city is growing at a considerable rate. The city lies between 31°15' and 31°45' North latitude and 74°01' and 74°39' East longitude.

The population of Lahore is more than 11.1 million. Male and Female population ratio is approximately 53 and 47 percent respectively. (Bureau of Statistics, Punjab).

Lahore district comprises of 2 tehsils and 9 towns. There are approximately 1,352 educational institutions including degree and post graduate colleges.

Literacy rate of the city is 73 %. (Bureau of Statistics, Punjab)

Lahore has 318 health institutions which include hospitals, dispensaries, basic health units, etc (Bureau of Statistics, Punjab).

Lahore is the provincial capital of Punjab. It is the 2nd largest city of Pakistan and a hub of economic activity. Major industries situated in the district include foundries, textile units, automotive, footwear and food and beverages. The city is the largest software producing and exporting city in the country.



Footwear Sector (Estimated Table)

Description	Indicator
Average price per pair	<10 \$ (Exports) <4.96 \$ (Imports)
Total Productive Assets	457 Billion PKR (Estimated)
Output	2-3 Pairs/Per worker a day (Leather & high end Products) 12-18 Pairs/Per Worker a day (Synthetic & other low end products)
Total Production	366 Million Pairs (2015)
Direct Employment	350,000 (Estimated)
Male : Female Workforce Ratio	95% : 5%
Office : Production Staff Ratio	15% : 85%

Footwear is a labor intensive industry. While the overall footwear sector caters to the domestic market, the leather footwear is mainly export oriented. Production in this cluster is done both in-house and through outsourcing. Due to this nature of business, the number of permanent employees is less as compared to contractual employment.

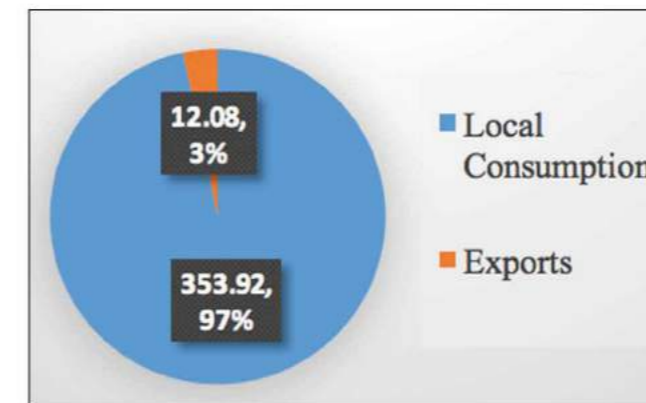
70% of the footwear industry is in the cottage sector, which operates in an informal setup. Entire families are working to produce low priced and low quality shoes for the local market. These are traditionally made through manual methods.

These micro units neither have the business resources nor the inclination to upgrade their small-scale manufacturing and mostly sell directly to the consumer. Sometimes, a group of them join resources to set up a small scale manufacturing unit, employing simple but effective solutions, and become vendors for the bigger companies.

The total employment in such units is less than 10. The credit constraints, lack of will of the producer/worker, limited access to foreign markets, lack of awareness and lack of capacity etc. are the main problems faced by these small and medium scale producers in this cluster.

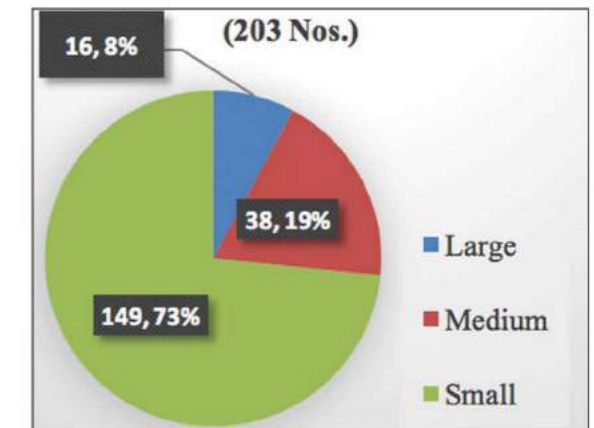
Turnover in this industry is quite high. It is easy for the workers to switch their jobs due to the contractual labor, while the younger lot is choosing not to enter the footwear sector. Job insecurity, availability of alternate employment opportunities, low wages, slow career progression and a feeling of being under-valued are the key factors for this.

Annual Production (366 Million Pairs)



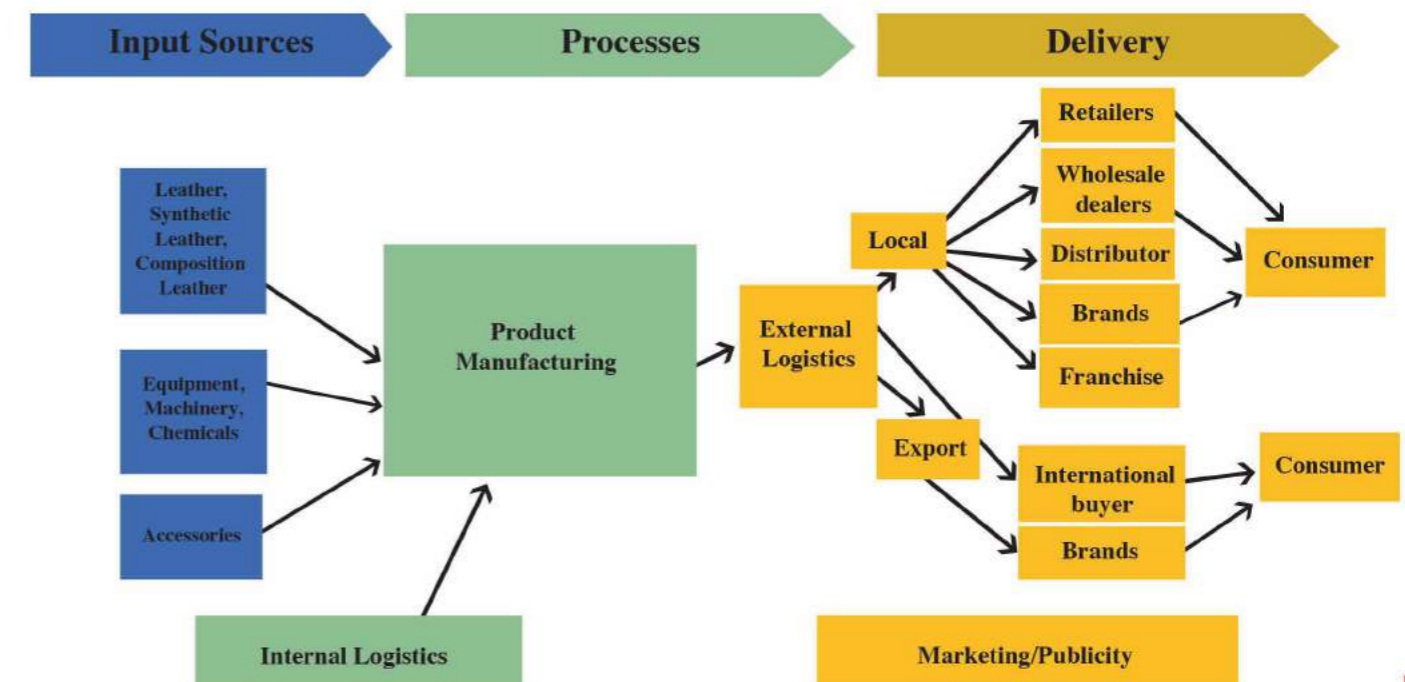
(Source: World Footwear Year Book-2016 by Portuguese Shoes)

Identified Units in Cluster (203 Nos.)



(Source: Industrial Directory: Directorate General Industries, Prices, Weights & Measures)

1.4.7 Major Cluster Actors





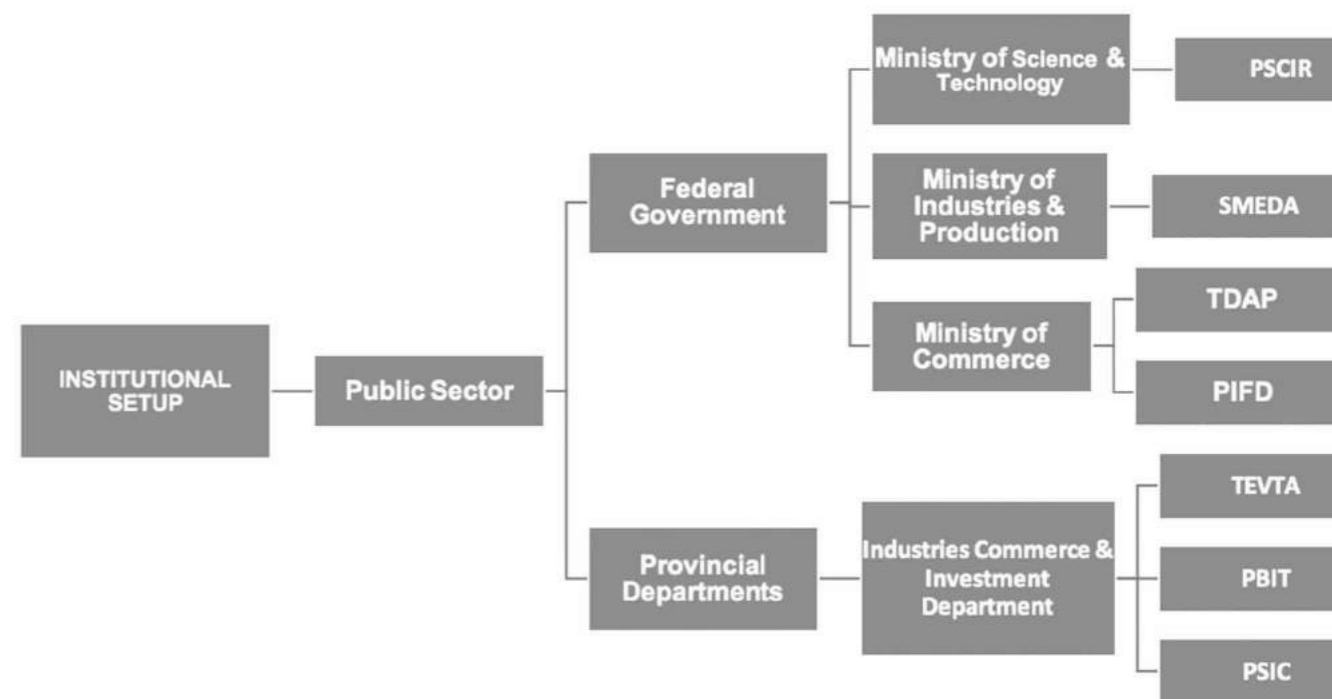
2. INSTITUTIONAL SETUP & FRAMEWORK

The main institutional setup comprises various government ministries, departments, support institutions including training institutions, financial institutions, international donor agencies, sectoral associations and chambers as well as universities that are closely related to the development of any industrial sector including the footwear industry. There are also developmental networks within the cluster that provide a useful platform for activities such as joint marketing in the cluster development.

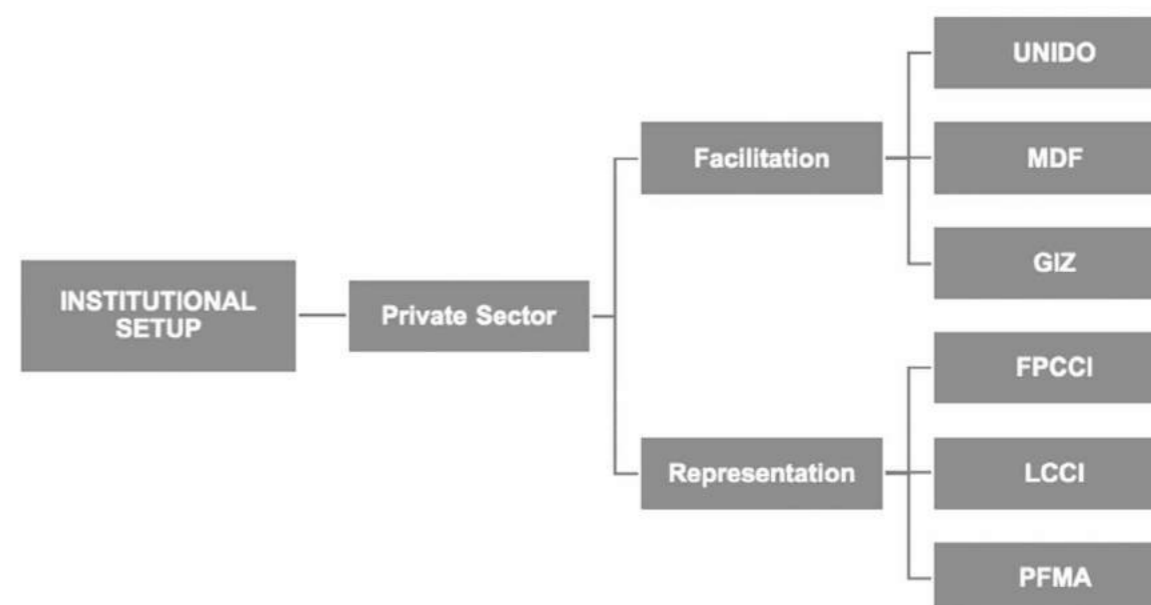
The following chart gives an overview of the institutional setup at the public and private level. Some of these institutions work directly with the industry, while others have an indirect role. These linkages will further be discussed in the cooperation matrix (page 80)



Public Sector



Private Sector



2.1 Government Sector

The Government plays a crucial role in providing a business conducive environment to the industrialists of any sector. While ministries at both the federal and provincial level play a role, only the most relevant departments, with a direct and proactive interaction with the cluster will be discussed in this section.

• Ministry of Science & Technology (MoST)

The Ministry of Science & Technology (MoST) is working to develop and launch scientific and technological programs in Pakistan. MoST is currently implementing “Certification Incentive Programme for SMEs under Productivity, Quality and Invention (PQI) Initiative 2025” to promote certification & compliances culture among the industrial organization; the interested organization can seek its required certification from the relevant forum and later be reimbursed for the cost.

However, upon discussion with the industry, it was noted that although the industrialists were interested, majority of them were unaware of this scheme.

• Environment Protection Department (EPD)

In order to implement environment protection measures, the Environment Protection Department, Punjab was established. EPD further established the Environment Protection Agency (EPA) for the protection and improvement of the environment.

EPA is mandated to prevent and control pollution and for promoting sustainable development in the province. EPA is enforcing effective regulations for protection of the environment. It has made qualitative and quantitative standards for the discharge of effluents like water treatment at tanneries, industrial wastes and air emissions etc. for general applicability.

• Technical Education & Vocational Training

TEVTA was formed in 1999 and aims towards enhancing competitiveness in Punjab to bring it at par with international standards.

Key objectives include promoting and providing demand driven technical education and vocational training in skill development in various sectors including the footwear industry. Consolidating the existing technical education and vocational training system under one management structure and regulate and develop standards including internationally recognized trainings.

Tevta offers short terms courses, diplomas, 3 years Diploma in Associate Engineering and also B-Tech programs. Tevta is currently supporting all major industrial sectors including automotive, textile & readymade garments, surgical instruments, light engineering, civil & mechanical engineering, telecommunications, etc. It also has a state of the art institute for leather footwear & leather technology at Gujranwala namely Government Institute of Leather Technology (GILT).

• Training & Educational Institutes

Various institutions including Gujranwala Institute for Leather Technology (GILT), Pakistan Training Vocational Council (PVTC), Punjab Skills Development Fund, Pakistan Institute of Fashion Design are providing technical and management skills for the leather sector, including footwear.

• Punjab Vocational Training Council (PVTC)

Punjab Vocational Training Council (PVTC) was established in 1998 on the basis of Public Private Partnership by the Government of Punjab. PVTC in collaboration with GIZ, PSDF, UNICEF, JICA, British Council, and other national and international development agencies is extensively contributing towards poverty alleviation through skills training.

Keeping in view the latest trends and based on market demand through Training Needs Assessment (TNA), PVTC has developed curricula for 100+ various trades to cater to the growing demands of industrial, agriculture, health and service sectors.

The training of these trades is being imparted through its 326 Vocational Training Institutes (VTIs) established in vacant /underutilized Government buildings throughout the Punjab with an annual training capacity of 160,000 trainees per annum.

PVTC is currently developing curriculum for a dedicated course on footwear namely “Cut-to-Pack” that will enable the trainees to get training in all processes of footwear manufacturing; the trainees will serve the industry as Supervisors. This course is scheduled to be started from January, 2018.

• Gujranwala Institute of Leather & Technology (GILT)

GILT was established in 1949, making it one of the oldest institutes for the leather sector in Pakistan. While it was primarily founded for R&D and quality control, GILT later started to cater to the footwear industry also. The institute now provides a Diploma in Associate Engineering which is a 3 year course in Footwear Technology as well as relevant courses of varying duration in Shoe Designing and Modeling, Grading of Shoe components, Pattern Engineering of Shoe components, Shoe Upper Stitcher, Leather Garments Stitcher and other Special Short Courses. These courses are offered at an affordable cost.

While the institute is providing both short term and long term courses in footwear, it is struggling with enrollments, especially in the short term courses. Some of the reasons cited are non-conducive working environment, lack of benefits, job insecurity owing to contractual labour and availability of more attractive alternate job opportunities.

While GILT remains the most relevant training institution with a fully equipped lab for production processes, the training focuses more on the theoretical parts as compared to the practical training. The reason mentioned for this was insufficient funds required for practical training. This as well as the need for more qualified trainers and up to date curricula has resulted in inadequate training skills being imparted to the labour. This observation was also echoed by the industry, which felt that even the trained labour lacks necessary skills because of which the employers again have to spend months training them.





• Pakistan Institute of Fashion Design (PIFD)

The PIFD was established in 1994 in joint collaboration with TDAP and Olivier Lapidus. Pakistan Institute of Fashion Design was initially established to fill the gap of trained professionals in the Textile sector. However, it now has a fully functional leather footwear department with fully equipped labs and the latest machinery including laser cutters, CAD/CAM facility, EU funded Shoe Master, etc.

The department of leather accessories and footwear received positive response and is running at full capacity. The students graduate to junior level / middle level management roles, majorly in the creativity and design departments. The board also consists of industrialists from the footwear sector.

A meeting with the management revealed that while the institute provides facilities for practical training, the students are required to bring the raw material (i.e leather) themselves. In addition, it is also expensive and unaffordable for the general public. Due to this reason, only a limited number of people can avail this facility.

The industry expressed satisfaction with the skill level of employees graduating from PFID. However, the school lacks training in shoe finishing as well as latest developments. With assistance, this school could contribute considerably towards addressing such shortcomings. Both the management of PFID and industry expressed willingness to work in joint collaboration to design courses that would work towards filling this gap.

• Al-Khawrazmi Institute of Computer Sciences, UET Lahore (KICS)

KICS is an institute established at the University of Engineering & Technology Lahore (UET), KICS conducts research & development in Computer Science and Information Technology. KICSs mandate is to create innovative products and technology for the industrial sectors. Currently KICS is working on energy efficiency and offering energy efficiency advisory courses for management level positions on a weekly basis. It also plans to introduce short courses for middle management so that industrialists can better train their HR for optimal energy utilization.

2.2 Semi-Government/Autonomous Bodies

The semi Government/ Autonomous bodies include:

• Small & Medium Enterprise Development Authority (SMEDA)

Small and Medium Enterprises Development Authority (SMEDA) is working under the Ministry of Industries & Production, Government of Pakistan. SMEDA was established in the year 1998 with the vision to develop and promote a strong SME base in the country. SMEDA is working to broaden SMEs in the country by provision of an enabling environment and business development services to SMEs. SMEDA is an active player in the implementation of the Prime Minister Youth Business Loan Scheme (PMYBLS), which is an initiative of the Government to promote entrepreneurship in the country.

SMEDA has established its offices in all provinces; it extends support to prospective entrepreneurs through provision of sector/industry specific feasibility studies. SMEDA also publishes sector studies and in the past it has

jointly worked with UNIDO & PSIC in publishing a Diagnostic Study on Leather Goods Cluster-Sialkot in 2006 under “Cluster Development Program for SME’s in Punjab”.

• Trade Development Authority of Pakistan (TDAP)

Trade Development Authority of Pakistan (TDAP) works under Ministry of Commerce, Government of Pakistan. TDAP is mandated to promote global trade development and encourage participation of local industrialists in international exhibitions. It also organizes expos in Pakistan to attract foreign buyers and create awareness. TDAP is managing Expo centers at Lahore and Karachi where local businessmen are supported to exhibit their products. TDAP also organizes trade delegations, implements trade policy initiatives and various sector-development projects. The role of TDAP is further discussed under section

2.3 International Donor / Development Agencies

• Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ)

GIZ is a provider of international cooperation services for sustainable development and international education work. It has over 50 years of experience in a wide variety of areas, including economic development and employment, energy and the environment, and peace and security.

In the footwear sector in Pakistan, GIZ has worked for the development of skilled workforce in footwear related trades (like Shoe Lasters) in collaboration with PFMA & member companies for on the job training on the factory floor. (2011-2016)

The second phase of the TVET Sector Support Programme commenced from January 2017 for another five years. The Programme is supported by the European Union, Government of Germany and Norway. The overall objective is to improve governance and private sector participation (like PFMA) in the TVET sector to increase quality skill development that meets the demand of the labour market.

• Market Development Facility (MDF)

Market Development Facility (MDF), is a multi-country private sector development program funded by the Australian Government. It is currently operating in Fiji, Timor-Leste, Pakistan, Sri Lanka and Papua New Guinea. MDF supports businesses with innovative ideas, investment and regulatory reform that will increase business performance, stimulate economic growth and ultimately provide benefits for the poor.

In Pakistan, MDF has collaborated with the PFMA and assisted in establishing the local ancillary industry, which is negligent in the footwear sector. MDF has assisted Intra Systek in procuring shoe-last manufacturing machinery to set up the first shoe-last production unit in Pakistan. The company is, in limited percentage, supplying

plastic last to mechanized manufacturers including the leading exporters more quickly and cost effectively than the imported lasts, reducing the input cost and lead time.

Tabraiz Mold Engineering (TME), is a bottle mould making company that has been supplying to the packaging industry for the last 20 years. They expanded their operations by developing shoe making moulds, which were approved by the footwear manufacturers. MDF provided financial assistance to TME in setting up local industry by purchasing mould-making machinery in the shoe industry.

Similarly, Footlib – a leading shoe manufacturer, set up an all women stitching unit with the help of MDF.

• United Nations Industrial Development Organization (UNIDO)

UNIDO is the specialized agency of the United Nations that promotes industrial development for poverty reduction, inclusive globalization and environmental sustainability.

UNIDO is currently the implementing partner for setting up a water treatment plant for tanneries in Sialkot. This project is funded by Global Environment Fund. Previously, UNIDO worked for the leather gloves sector in CE marking and production & quality through the TRTA-II program.

Additionally, UNIDO is also the implementing partner for Cluster Development Initiative (CDI), in collaboration with Punjab Small Industries Corporation (PSIC) for the uplift of export oriented sectors in Punjab, including leather footwear & products through interventions in potential areas of, among others, marketing, productivity enhancement and skill development.

2.4 Other Support Institutes

• Pakistan Footwear Manufacturers Association (PFMA)

PFMA was established in 1985. The association works to provide a platform to member firms for joint activities like holding workshops, seminars and training sessions to assist companies understand trends and critical updates on the footwear business. It also updates on customs rulings, product recalls, and general footwear duty and import trends, taxation and budget. PFMA in collaboration with PTA has also taken the initiative to start a leather expo in Pakistan in recent years. The association also conveys concerns of the industry to the Government.

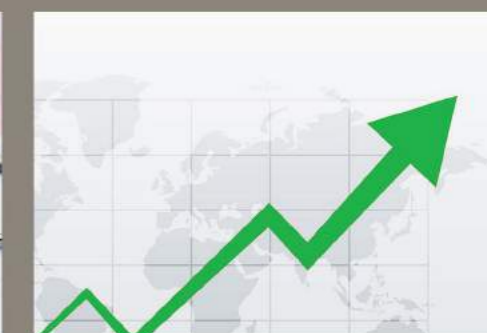
The association is also aiming towards developing a service footwear center for the footwear industry, based on the model of FDDI, Footwear Design & Development Institute of India. The main beneficiaries will be the footwear companies of Punjab. The association is already in talks with Italian companies for joint collaboration and is also seeking Government support, though there has been no development at the Government level yet.

Additionally, the association is also developing a common facility center (CFC). This is also a joint project between Assomac and PFMA. The CFC will include machinery for material and quality testing as well as CAD/CAM for design purposes. This lab is expected to be operational in the first half of 2018.

2.5 Financial Institutions

Banks, leasing companies, insurance companies and mutual funds are the common forms of financial institutions in Pakistan's economy.

In order to serve the micro/cottage sector, micro financing banks are also operating, which provide customized loan facility to small entrepreneurs. Currently as per SBPs prudential regulations a Small Enterprise (SE) can avail financing up to 25 Million, whereas a Medium Enterprise (ME) can be provided financing up to 200 Million Rupees. Interviews with the industry revealed that majority of the companies prefer not to take loans due to high interest rates as well as cumbersome procedures. Previously, specialized institutions like Industrial Development Bank of Pakistan (IDBP) served the industrial sector through liberalized financing policy.





The big industries, while catering to the local demands, are also striving to remain competitive in the international market. Despite availability of good quality leather, the footwear industry of Pakistan has been unable to sustain its position in export markets due to the changing needs of the European customer and emergence of new players like Vietnam, Sri Lanka and India. Additionally, the global market is now showing more inclination towards synthetic and non-leather shoes, in which Pakistan, at present, does not have any particular advantage.



3. PAKISTAN FOOTWEAR INDUSTRY ASSESSMENT

Footwear is a labour intensive industry, employing nearly half a million people both directly and indirectly. Among the subsectors of leather, it has maximum value addition and earns valuable foreign exchange from exports.

In addition to the formal mechanized sector, the cottage industry also supplies the bulk of the domestic needs according to changing designs and tastes around the year, whereas export needs are fulfilled by the organized / mechanized sector almost exclusively. In the Lahore cluster, many factories have a production capacity of 2,500 pairs per day, while the larger units may produce as much as 10,000 pairs per day. It includes leather, textile and synthetic shoes.

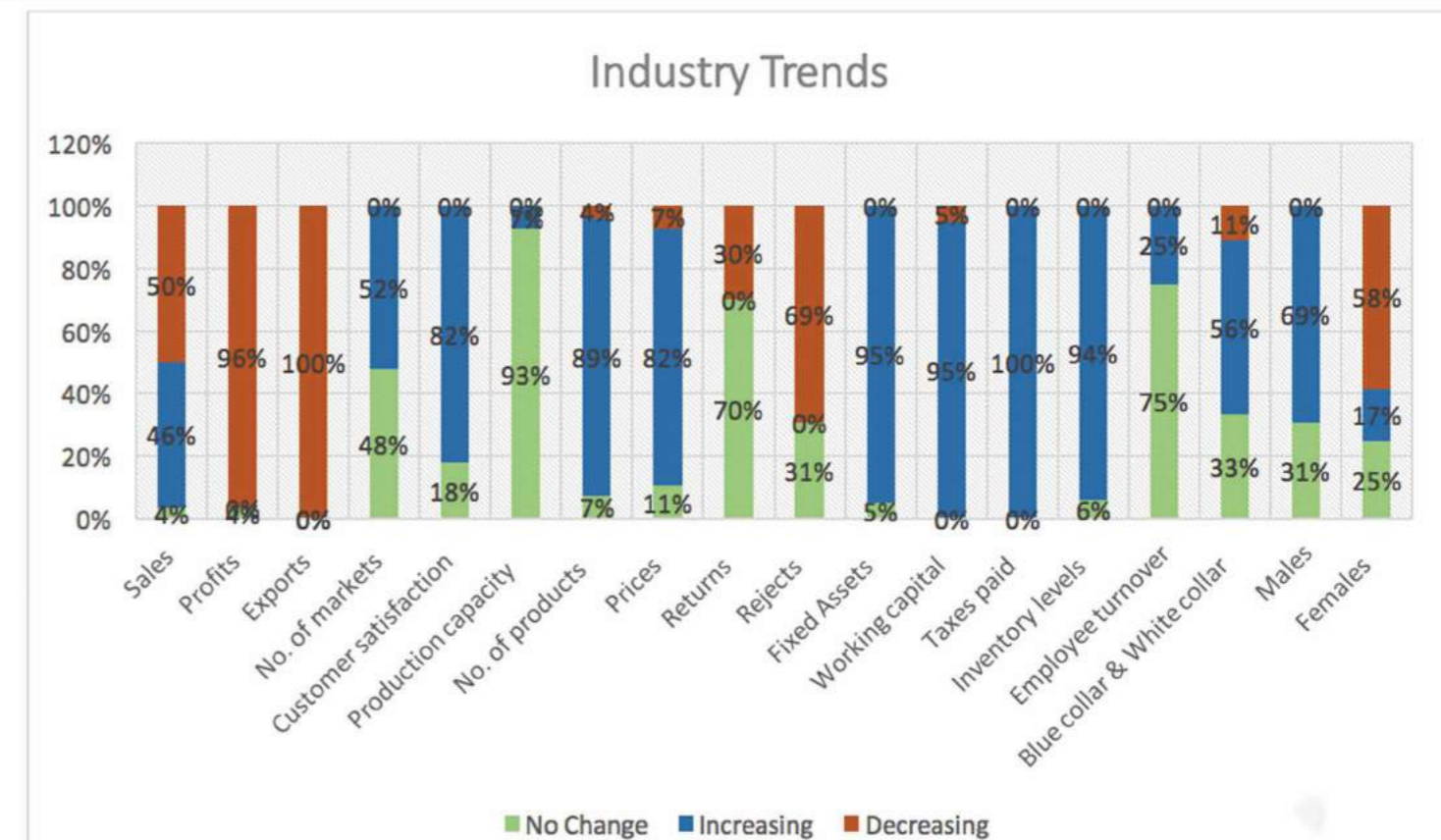
Presently, the footwear industry is facing tough competition in exports due to prices of the products. Countries giving financial benefits to their manufacturers by way of duty drawbacks, research and development support, subsidized support industry, cheaper power tariff, etc. offer cheaper products to the international buyers than Pakistan.

Pakistan has an opportunity to excel in this sector as there is a shift towards low cost regions like Asia where roughly more than 80% of world footwear production is made. There is a potential to multiply the volume of exports with the improvement in quality and innovation. At present approximately 25% of the local market share is captured by a couple of companies.



3.1 Industry Trends

The footwear sector of Pakistan is mainly concentrated in and around Lahore. As per the Pakistan Footwear Manufacturing Association, the footwear manufacturing units of Lahore (in & around) contribute 70% towards the annual footwear production. A detailed data collection process was initiated to collect industry information through the questionnaire developed by CDI & UNIDO's team during field visits.





According to the survey, which represented about 14 % of the formal Lahore footwear cluster, the sales in the local market have generally remained the same with 50% of the respondent firms stating a decrease and 46% stating an increase; 4% were of the view that the sales have been stagnant.

However, all of the respondent firms claimed a decline in export of leather footwear over the last 3 years.

Growing competition in the international market as well as emergence of countries including Vietnam in production of footwear, higher input costs and reduction of export rebate by the Government combined with non-availability of support industry have made the Pakistani shoe non-competitive as compared to the regional partners including India and China. Limited presence of allied industry increases the input cost as well as the lead time. Pakistan footwear industry relies heavily on imported materials and accessories including lasts, moulds, trims, heels, adhesives, buckles etc. This negative trend is also reflected in the value chain analysis of formal and casual leather shoes, amounting to 28% of the input cost.

Bangladesh, due to the Least Developed Country (LDC) status gets an added advantage as countries importing from Bangladesh have to pay significantly lesser import duties as compared to when importing from Pakistan. Similarly, the Government of India has also played a proactive role in negotiating lesser duties on Indian leather products with some countries including Japan.

Another reason for a decline in exports is that Europe, which is the main export market of Pakistan, is switching towards low cost artificial leather / synthetic footwear, whereas the strength of the Pakistani footwear manufacturers remains in leather, due to availability of abundant and good quality leather.

Almost all the interviewed firms (96%) reveal that profit margins are currently very low. This is due to stiff competition in the local market. Similar products are offered by all manufacturers, making it easy for the price conscious buyer to switch. This along with a high influx of low cost imported shoes, has resulted in a price war within the industry. Additionally, due to multiplicity of taxes at each stage of business, the overall taxes have increased. Industrialists are paying import duties while purchasing raw material and accessories from abroad, taxes in utilities, sales tax and income tax which adds to their cost of production. Firms also have to keep a certain level of inventory at all times to cater to customers who want quick deliveries. No major investment seems to be made in this sector in recent years.

While the competition is lowering the profit margins for the industrialists, it is resulting in better quality and growing customer satisfaction, with very few sales being returned by the customers. 69% of the respondents informed that rejection rates are very low and usually remain below 2%.

Owing to seasonality and decline in exports as well as demand of high-end products in the local market, most of the (93%) footwear manufacturers are not enhancing their production capacity. The utilization of the installed capacity is 40-60% due to low orders. However, a small percentage admitted to gradually increasing it.

Since footwear is an integral part of the fashion industry, there exists a rapid change in style, design and customer choices. Thanks to advancements in technology and the culture of online marketing and sales, the world has now become one global market. Both the consumer and the producer are well aware of the latest fashions and popular trends. With more and more brands selling their products online, it is not only easy to buy but also emulate the same designs. While on one side, this discourages R&D advancements due to availability of thousands of designs online, on the other side it facilitates manufacturers in producing newer and more popular styles easily and frequently.

Keeping in view the latest customer choices, majority of the footwear manufacturers are introducing new products to remain competitive. An overwhelming majority of the respondent firms (89%) informed that the number of products are increasing with a small percentage (7%) stating no change and decrease (4%). These 4% may be targeting product lines with higher production volumes rather than more products with low volumes.

In the cottage sector, the sample is provided by the customer which is then replicated. This will be lower in quality and price.

Employee turnover is high within the footwear industry. Generally the lower income group including unskilled, skilled and line supervisors switch to other companies and also for other sectors more frequently for higher pay and perks as compared to the middle management. Average annual turnover in stitching can reach as high as 30%. The lasting department also witnesses high turnover on average, however, this is comparatively lower than the stitching department (up to 15% annually). A majority of the line and floor supervisors lack competence and technical knowledge in key areas such as optimal production work flow, workers management and motivation, machine maintenance, health and safety, inventory and storage, cleanliness etc. There is a dearth of supervisors with these competencies, despite high demand. This leads to frequent switch overs, monopolistic attitude of such staff and unhealthy competition between enterprises.

The switch over by skilled and supervisory staff is to other companies within the same sector, while the unskilled and semi-skilled labour may also switch to other sectors like Textile. Although, a higher salary is the most frequent reason for changing jobs, other factors like non conducive working environment, job insecurity, permanent job as compared to contractual, slow upward mobility and a general feeling of being undervalued also contribute to this. Most of the respondent firms (75%) informed that the employee turnover in their companies is as per the prevailing trend in the industry, while 25% stated that the turnover is higher in their companies, i.e. employees leave more frequently than in their counterpart companies. This may be due to lack of financial resources required to retain employees. New entrants attract the existing workers of small factories by offering higher salaries.

In the cottage sector, the turnover is very low. The reason is that mostly families and relatives are working together in an informal environment. Additionally, there is more freedom in working style as compared to strict rules in the bigger companies. Sometimes, owners also give loans to the families of the unskilled laborers, thereby ensuring that the workers are unable to leave until the loan is paid off.

In large factories, female workforce is provided with better and segregated work environment including additional facilities like transportation. In general, the ratio of female workers is decreasing and this remains within 2 to 5%. More than half of the respondents were of the view that their female workforce has reduced, while 17% stated it has increased. Factories that are inclined towards hiring females informed that the female workforce have better focus, concentration and higher productivity. Reasons for low ratio of female workforce are discussed in more detail in section 3.8.

In the cottage sector, the ratio of women is greater, at 20%. This is because women are not required to leave their homes. In case of the head of family being a shoe maker, the women in the family work alongside him; in cases of outsourced work, the company gets the raw materials dropped at and finished products picked from the houses. Quality checks are also made at the house. In such cases, the women get 60% of what their male counterparts receive.



3.2 Raw Materials & Ancillary Items

Pakistan has a well-established tanning industry; hides are easily available in large quantities. The tanning sector is majorly exporting processed leather to the world. Approximately, 80 percent of the total leather produced is exported, both in finished form as well as wet blue. The export of wet blue leather has been declared illegal. Finished leather represents 44 percent of the value of total exported leather, while leather goods including garments, footwear, gloves and accessories represent 56 percent of the value exported.

Despite the availability of quality leather, some processed leather is still imported, in limited quantity for high end products. The proportion of imported leather remains low. While earlier it was estimated to be 25%, this has now decreased owing to a decline in exports of leather garment & product industry, which was importing the main chunk for high end garments and products. Some leather footwear companies are also importing a small percentage of high quality leather like deer leather, for high end shoes. The leather is being imported from countries like Brazil, Italy, Africa, the Middle East and Australasia to supplement local supply.

Despite being a major raw material producer, Pakistan is unable to tap the world market. Its share in the global market for footwear exports is below 0.1%.

The footwear sector is facing issues in relation to the absence of allied industry; with the exception of the chemical industry, which has grown significantly. New factories for PU (Poly Urethane) are being established and most of the chemical is being produced and bought by the footwear industry locally.

There is high import dependency for ancillary items (e.g. lasts and moulds) and consumable accessories (e.g. trims, buckles, heels etc.). The majority of large companies import directly while the medium and small companies buy from the local importers.

Reliance on imports for ancillaries and inputs leads to increased lead times, higher costs and delays in providing samples and orders for international customers. This is one of the reasons that make the Pakistani footwear less competitive as compared to the other regional players.

61% of the footwear manufacturers are using mainly local and some imported raw material followed by 29% who are using only local raw materials; whereas 4% of the interviewed firms are using either only imported raw materials or mostly imported or both in equal amount.

This 4% is export oriented and catering to international customers. As such, they have to adhere to superior quality standards. In the domestic market, also they produce high end footwear. In order to give their footwear an edge over the local, low cost shoes, these companies prefer to buy imported materials. These percentages include leather, soles & adhesives. In contrast, majority of the footwear manufacturers rely on imported auxiliary items due to non-existence of allied industry in Pakistan.

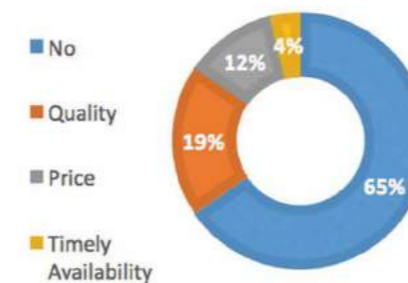
In the cottage sector, all kinds of raw material are bought locally. The focus is to get cheap prices. As the products are sold in the domestic market where the general consumer is more price conscious than quality conscious, they rely on lower quality standards.

The footwear sector relies heavily on import from China and to a lesser extent on other countries namely India, Italy, and Turkey.

The footwear manufacturer's main source of information for purchase of raw materials includes exhibitions, foreign buyers, developed linkages with suppliers and self-research. A majority apply a mix of all strategies to explore raw material availability & selection. Those who are mainly working with bigger brands and international buyers usually follow their suggestions and instructions.

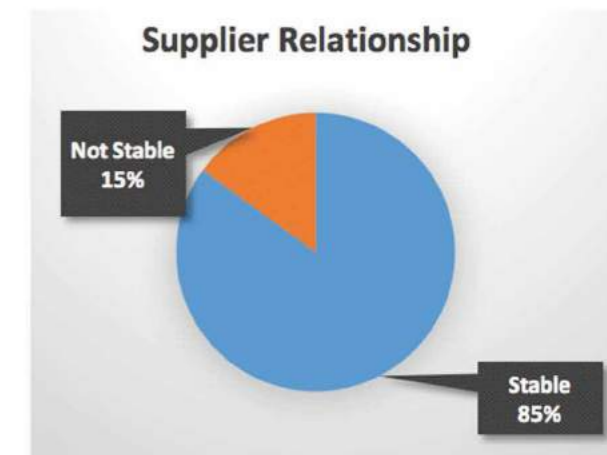
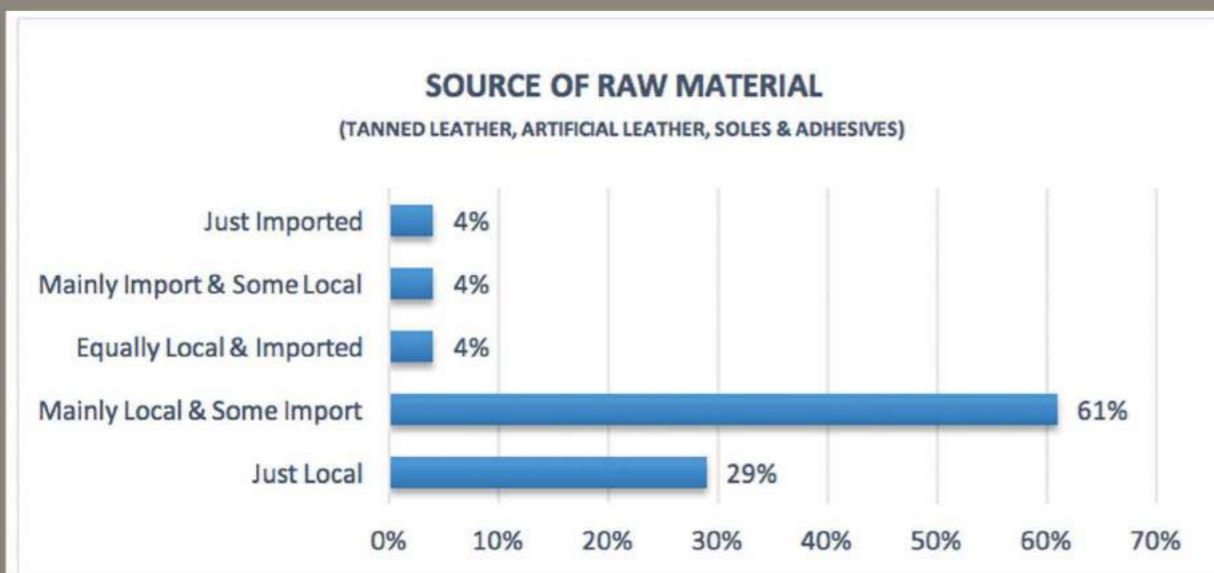


SUBSTANTIAL PROBLEMS WITH RAW MATERIAL SUPPLIERS



65% of respondents do not have any substantial problem with suppliers, whether they are importing directly or through importers. This depicts existence of strong linkages that have developed over time, followed by 19% of the respondents who claim that quality is a major issue with raw material suppliers. Price and timely delivery are other factors.

As can be depicted from the graph (left), there is a stable manufacturer-supplier relationship that exists within the Lahore footwear cluster. 85% of the sampled enterprises reported to be satisfied with their backward linkages with 15% of the respondents claiming otherwise.



3.3.1 Production Details

3.3 PRODUCTION PROCESS FLOW CHART

The following chart depicts the production processes involved in producing footwear, along with the methods used, both manual and semi-automated. As mentioned earlier, leather footwear is a labour intensive sector. As such all firms employ manual methods, with the medium and large companies also using semi-automated processes. In large footwear manufacturing units, employees specialize in one particular production stage. In smaller companies (mostly with less than 10 employees) one person can be involved in multiple processes. The smaller companies as well as the cottage sector only operate manually. This is due to limited financial resources and low income customers.

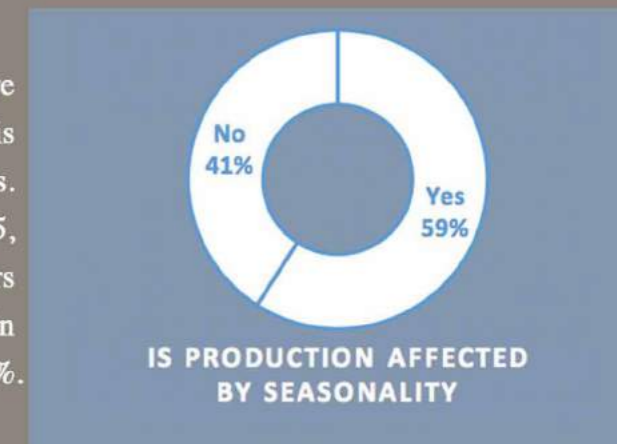


In order for Pakistan to market domestically produced footwear in the global market at international benchmark prices, it is imperative that production is also globally competitive and at par with the best international practices. In 2015, Pakistan produced around 366 million pairs of footwear annually, of which approximately 12 million pairs were exported. In comparison, India produced 2200 million pairs and China 13,581 million pairs (refer chapter 1, table Top producers of the world 2015)

It is important to recognize that modern production of footwear, accessories, etc. involves a wide variety of leather, fabric and composite components.

While the large firms operating in footwear industry have semi-automated production processes, majority of the SME are still using manual and obsolete techniques. These smaller companies are vendors to bigger companies which may be manufacturers or branded exporters. Most of these vendors produce the whole shoe, although in some cases certain operations (upper stitching) are outsourced only. As they do not directly export themselves, they neither have the business resources nor the inclination to modernize their production. The bigger companies have their own vendor support programs including technical support.

Most of the export oriented firms and other SMEs as well, are currently operating at 41%-60% of their installed capacity. This is due to a continuous decline in the overall leather exports. According to the Yearbook by Portuguese Shoes, Pakistan in 2015, was the 6th largest producer of shoes. However, the industry caters to the local market and focuses on internal sales, estimated to be in the region of 50 percent of demand. Its global share is less than 1%.



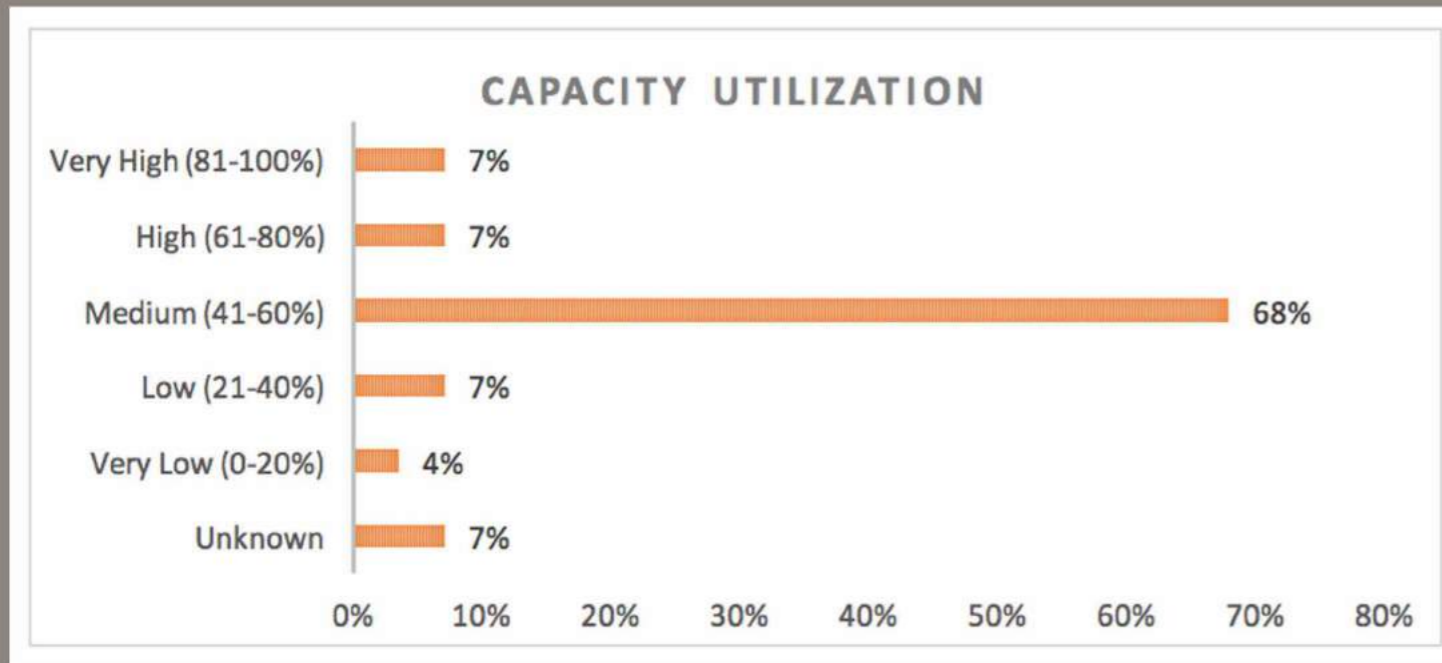
In the domestic footwear sector, manufacturers mainly focus on men's wear while importing most of the women footwear. Changing fashions, proficient designing skill coupled with fast manufacturing processes are the main reasons behind this. Some of the gap in ladies shoes manufacturing is covered by the domestic cottage industry producing leather, fabric and polyurethane shoes. 86% of the responding firms have developed their production plans whereas the rest of the manufacturers do not have any formal production planning. Since the majority of footwear manufacturers work for big brands as their vendors, instead of making annual plans, they make separate production plans for each customers/order.



3.4 Technology



The production of footwear is highly affected by seasonality. More than half (59%) of the respondents informed that during special occasions, like Eid and start of the new academic year at schools, they work at maximum level. However, during the rest of the year, production is slow. Very few of the footwear companies produce other products like wallets and belts during the low season. However, production of these products is outsourced. The low season is normally used for producing samples, participation in fairs and marketing.



Consequently, the overall production capacity utilization remains within 41-60% of the installed capacity. The cottage industry operates in an informal manner and produce in small quantities as and when they receive the order.

In Pakistan, the major focus has been on the tanning and support for the manufacturing component of the leather footwear and goods industry has been weak. Use of technology is very limited, most of the large firms are using CAD/CAM facility; very few companies are using laser cutting machines and direct injection technology. However, most of the firms are still working on manual operations. Reasons include low number of orders as well as lack of education in the labor class. The cost and maintenance of the new machines as well as training of the staff remain the major factors behind non adaption of latest technologies. The workers lack an understanding of the correct machine settings, maintenance and use of corresponding components for optimal production. They also lack relevant theoretical and technical knowledge which results in use of hacks/tricks to resolve any issues. This solves the problem temporarily but proves detrimental to the production in the long run. Access to latest technology and equipment is important for expanding the production of leather footwear and goods. The Pakistan Machine Tool Factory (PMFT) in Karachi provides customized services for machinery and equipment for different sectors. Also, there is limited presence of foreign brands with their Sales Representatives.

In general, the footwear machinery is either imported directly as in the case of large manufacturers (10%) or imported through an importer (90%). These importers are not dedicated footwear equipment importers only, but provide machinery for different sectors. As such, they are not trained to provide follow up or training services, except in the case of mechanical failure which is covered in warranty. The manufacturers, therefore, have to invest time and resources to get their staff trained to operate it.

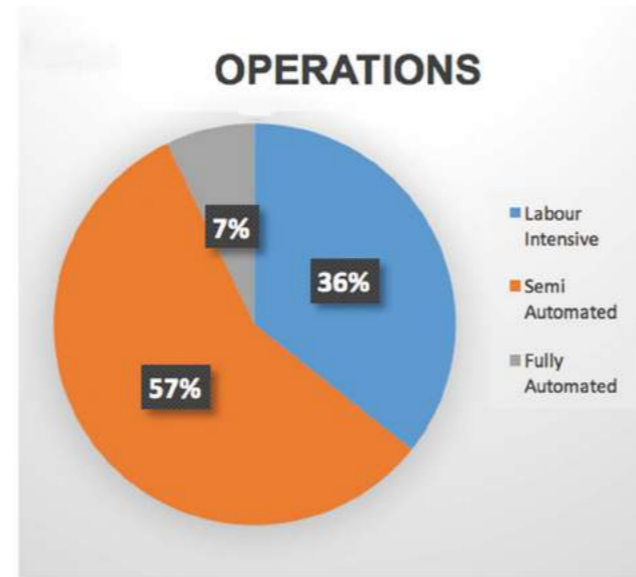
The production process is also linked with the target market. Competing at top level for high end footwear requires the same level of skill and technology. In the case of the Lahore footwear cluster the scenario is different. While there is an edge in the skill level of stitchers, there is an overall dearth of skilled labour. This factor, combined with old technology results in production of an average product for high value market. Additionally, as the industry is majorly catering to the local market, which is more price conscious and less quality conscious, the focus is on producing low cost, low value shoes.

The cost, information and capacity to adopt latest technology are an issue with the small and medium producers.

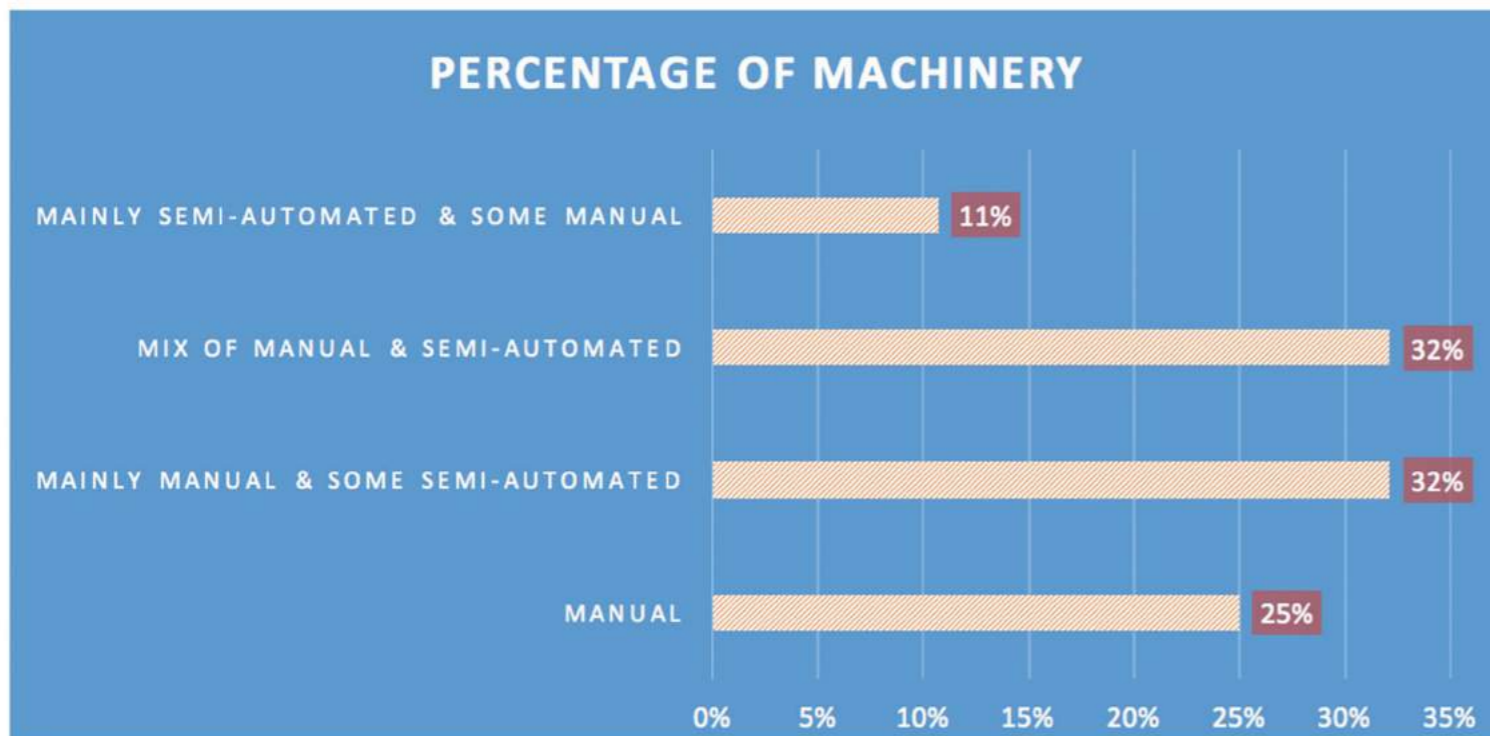


3.5 Innovation & R&D

57% of the sampled enterprises are using a mix of labor and technology and can be categorized as semi-automated followed by 36% respondents whose operations are labor intensive and who are not using any sort of technology. 7% of the respondents claim to be using fully automated operations; this percentage of firms has outsourced some of their production to vendors while keeping in-house the production of that footwear which is fully machine made



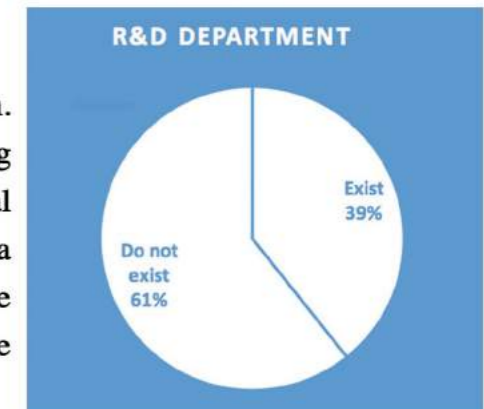
The majority of the interviewed firms use a mix of manual operations and semi-automated machines, followed by small firms who only have access to manual production. Some large exporters are using latest machines.



Innovation and R&D is weak in this sector. While the large firms have R&D departments, majority of the shoe manufacturers are working as vendors for large firms; these firms refer to themselves as Order Enterprise Manufacturers, which are basically full supply packages; they get the orders and manufacture them. Innovation in both products as well as processes is limited. Process innovation refers to modifying a production process for cost-cutting, labour-curtalement, and efficiency gains benefits. These benefits ultimately translate into rapid productivity output. In this also, the Lahore cluster remains weak.

Reverse engineering is widely practiced, whereby firms either produce the design given by the customer or emulate the ones already available online. Company owners/ directors themselves travel abroad to buy designs which they then manufacture.

The data collected through the questionnaire also reveals the same pattern. 39% of the respondents have established R&D departments for developing new & innovative products; These departments consist of an industrial engineer, designer, designing software or CAD/CAM and in a few cases a small mock production process line. However, 61% of the firms do not have any R&D section. The respondents were of the opinion that to curtail the additional cost of shoe designers, the firms are developing new designs by



themselves by obtaining information through foreign exhibitions. There is a significant gap prevalent between the industry & academia. The majority of the footwear industry has almost no R&D collaboration with any institute.

Innovation and R&D play a crucial role in the economic uplift of any sector. Leading international companies in the world offer their own designers facilities for making footwear in shoe making workshops or to model it in 3D with a software package to increase innovation as well as improve the current product.

Engineering advancements are having a huge effect on the product innovations in footwear, especially the sole. Leading international companies including Nike, Timberland, Adidas, Clarks as well as others are investing heavily in developing latest techniques in sole making to provide additional comfort and benefits. From installing sensors to identify pressure points to making entire soles of air technology, sky is the limit when it comes to leveraging innovation for profits.

A strong R&D cannot only improve the process and product but also help in creating substitute materials. Microfiber leather is being developed by China. This is a breathable form of synthetic leather and offers the same durability and strength as leather.



3.6 Marketing & Market Analysis



Traditional leather goods manufacturers in Pakistan are not dynamic in experimenting with newer business models and direct marketing, both of which would provide opportunities to expand production.

Very few firms have formal marketing plans or established marketing departments to effectively plan future business. These plans are approved by the board management and all other processes are then carried out as per the approved plan. 72% of the interviewed cluster firms have developed their marketing plans to launch their products, 12% of the firms do not have any marketing plan, whereas 16% of the firms have informal plans for marketing their products.



The main market of the footwear industrialists is local. As Pakistan's population is exceeding 200 million, the potential exists in catering to the local consumers. The Pakistan Footwear Manufacturing Association (PFMA) in collaboration with the Pakistan Tanners Association (PTA) recently took the initiative of organizing the Mega Leather Show in Lahore that is held in January. While this exhibition started taking place only two years ago, it has already started to bring in foreign customers.

Major export markets of leather footwear and products is primarily Europe and within that Germany, Italy and UK. The business in this cluster is generally through self- help basis. Companies participate in leading international exhibitions like Garda for networking and to create awareness as well as arrange meetings with international buyers through middlemen / agents.

While this is an effective way of meeting potential customers, it has its own drawbacks. Firstly, it is a costly process and requires not just additional resources but also grooming, confidence and exposure to be able to participate in and negotiate at these forums. The small and in some cases even medium sized firms are unable to avail such opportunities. Additionally, as the competition is stiff and rivalry is high, companies do not have the trust to collaborate with other companies for joint marketing. As a result, individual efforts to get business prove to be a roadblock in the overall growth of the industry.

Trade Development Authority of Pakistan (TDAP) works towards providing subsidized access to some of these international exhibitions. However, the needs of the industry may be incorporated during the planning process by TDAP to ensure maximum mileage from participation. This includes prominent placement of the Pakistani booth, along with attention arresting branding and visual representation of a specific interest as well as B2B rooms for private negotiations. Alternately, the industrialists may be given the responsibility to plan these.

Furthermore, the Pakistani missions abroad also do not create awareness about the Pakistani footwear industry or engage the potential customers for B2B sessions

The marketing of a product is essential for sales. The main marketing channel used by the firms is exhibitions (both international & local) as well as local agents. Additionally, electronic & social media are also becoming popular tools for creating awareness for both international and local customers.

For sales in the local market, retail outlets, wholesalers, franchises and distributors remain popular. The smaller firms are vendors to the medium and larger firms. They also produce and sell to the wholesalers directly. Sometimes, the medium and larger firms also produce for each other. The large firms, in addition to exports, also have retail outlets and factory outlets, where they display footwear produced for the domestic market. Both medium and large firms have stable linkages with the local wholesalers and distributors. In some cases, large firms also give franchises of their brand outlets. For example, one of the leading companies is serving its customers locally through a retail network comprising more than 400 retail outlets, 467 registered wholesale dealers, 13 wholesale depots, 28 wholesale distributors and 41 wholesale franchises across the country.

The cottage sector sells directly to the wholesalers as well as the final consumer. This includes low cost, low quality footwear for men, women and children.

Industry sources and interaction with the manufacturers reveals that only 11% of the companies of the Lahore cluster are directly involved in exports. However, these companies also cater to the local market.

The USA remains the biggest importer of shoes. Approximately, 70% of the shoes produced worldwide are imported by the US. The Pakistani footwear manufacturers, with the exception of a couple of companies, have been unable to tap the US market. The main reason for this is that the US market deals in huge orders in bulk. The Pakistani manufacturers have yet to achieve that level. Furthermore, tapping into a new market requires time and resources to invest in market research, hiring of agents and customer interactions, all of which the companies (at this point in time) do not have. As the local companies have smaller scale setups, they prefer to continue with their regular customers and known markets for quick orders and quick returns.

50% of the surveyed cluster firms are selling their products in the local market. 18% of the cluster

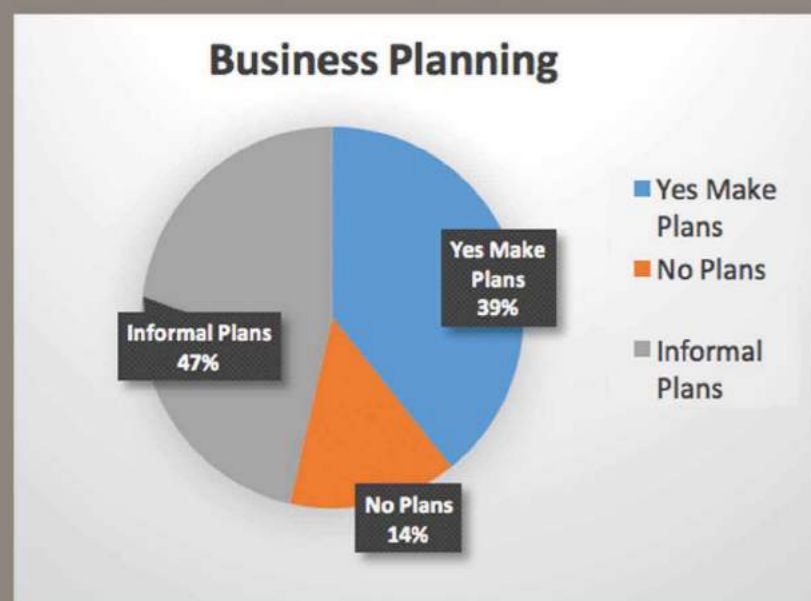
firms are focusing mainly on exports. These are the major players of the cluster which are producing leather shoes for high-end consumers. 32% of the firms are mainly selling their products locally but also exporting some of the products.



The companies which are mainly in exports believe that in the local market, a severe price-cut competition is prevalent which is increasing with time. Consequently, such companies are now focusing on break-even rather than generating profits. However, companies which are mainly catering to the local market are of the view that cumbersome export procedures make exporting a daunting task, while the same amount of profits can be made by selling to the local market.

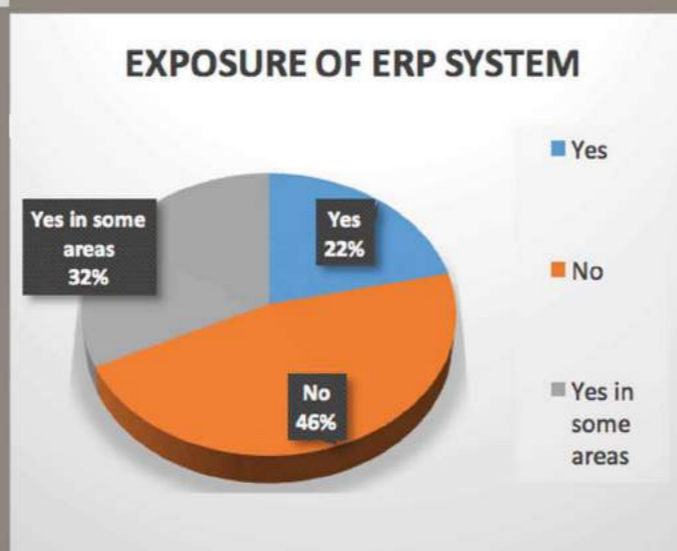
3.7 Business Resources

The footwear sector of Pakistan is a classic example of family owned businesses. Most of the businesses commenced with personal resources. Reinvesting part of their profits helps them in expanding their business. While the larger firms use banking facility, the smaller to medium companies find access to finance, a roadblock to further expansion. Higher interest rates and cumbersome banking procedures make stakeholders hesitant to take loans. The footwear retailers pay for the products once the merchandise is sold.



However, the bigger firms and new entrants are inclined towards business planning for increased efficiency. 47% of the sampled cluster firms make informal plans, 39% of the firms do proper planning and the remaining 14% do not have any inclination towards business planning. The overall footwear sector represents less tendency towards getting financing with majority of the entrepreneurs having established their businesses with personal resources.

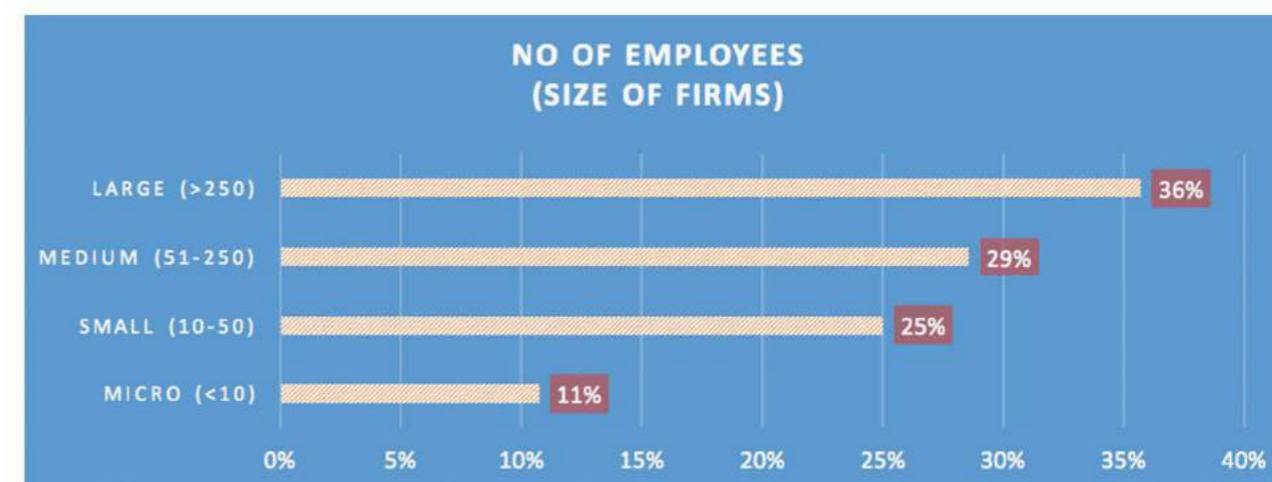
The footwear industry is highly subjective to fluctuations in demands, operating costs, seasonal trends, etc. ERP software helps to make the critical business processes more streamlined and integrate them for better management & resource planning. However, only 21% of the interviewed cluster firms are using any ERP system. 47% are not using ERP whereas 32% of respondents are using ERP system in some areas mainly accountancy. This less inclination towards ERP is due to lack of interest by industrialists to invest in software systems as they are faced with lack of financial resources and orders.



Within Pakistan's footwear sector, over 80% is cottage based. This sector mostly operates informally. One of the challenges they face in entering the formal economy is the extra resources required to conform to various regulations including safety, health, human, quality, etc. They do not have the understanding to comply with banking requirements or the personal resources to expand. They do however, have an in-depth understanding of the business environment. This enables them to bypass the system to produce at lesser cost and sell at a lower price. There is no association to represent the informal cottage sector.

3.8 Human Resource

On average, large firms have over 250 employees while medium sized firms have 51-250 employees and small companies have around 50 employees. The micro/cottage sector typically employs less than 10 workers, in most cases the workers are family members



36% of the interviewed cluster firms employ more than 250 employees and therefore fall under the category of large firms. The medium & small sized firms consist of 29% & 25% respectively, whereas 11% of visited firms employ less than 10 workers and can be categorized as informal micro firms.

The female workforce is limited to stitching units. Servis and Footlib are examples of companies that have set up stitching units exclusively for women.

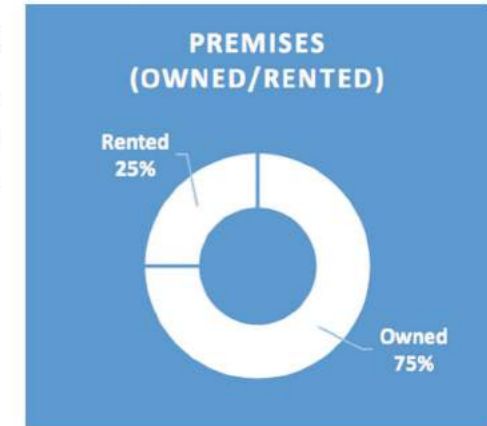
In general, this sector (in Lahore cluster) prefers to hire men, even though women are reported to have better focus and give more detail to attention. Reasons for this include unavailability of segregated work space for women leading to socio-cultural issues. Secondly, lack of transportation also contributes to hindering women seeking work in factories, which are usually placed outside the central areas of the city. Additionally, on the training side also, women prefer to enroll in courses where classes are either segregated or in women majority. As a result, training institutes offer limited courses for women and only if sufficient numbers are enrolled.

Some women also work in design and quality control, but the ratio of female to male workers continues to be low. Businesses also hire women to comply with certification requirements, which in turn help secure more orders from foreign buyers.

As per the industry resources, there is a lack of skilled labour in the footwear industry in Pakistan. Footwear manufacturers find it difficult to hire and retain skilled workers. This constraint is further intensified as the manufacturers generally do not offer a premium to skilled workers. Additionally, the impact of seasonality on labour demand leads to outsourcing. Slow upward mobility and seasonality increases labour insecurity which makes retention a problem.

3.9 Infrastructure & Superstructure

75% of the sampled enterprises own the factory land while 25% have rented premises. Most of the large firms own the land that they are established on. These are formal industrial establishments, whereas SMEs and cottage industry are mostly undocumented and operate in an informal setup, mostly in their own homes. Small companies have rented premises.



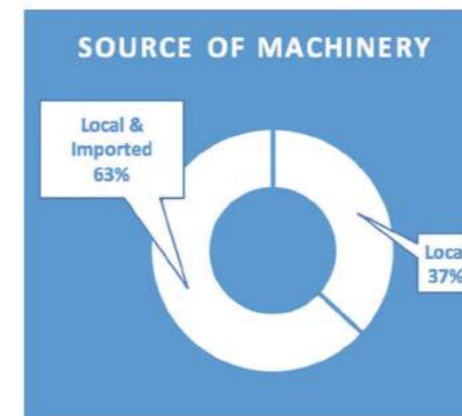
This insecurity has become apparent in low enrollments by the training institutions. This was reflected during interaction with the GILT. People prefer alternate employment opportunities to working in factories, including footwear.

Large companies have formal trainings for their middle and senior management, both locally and internationally. In the shoe lasters' course, jointly organized by GIZ, PFMA and TEVTA at the Gujranwala Institute of Leather Technology (GILT), companies provided labor to be trained at their own expense. This course was successful. In general, the labor force gets on the job training. Medium to small companies do not have any formal training for their staff. The owners of the companies themselves participate in training sessions, mostly conducted locally.

An analysis of the current situation reveals that the manufacturers lack confidence in the training institutions and are dissatisfied with the standards of services provided. They, therefore prefer to train their labour in the factory. Usually 2-3 workers are trained from outside and then those workers further explain the learned art to the rest of the employees.

On the other hand, the training institutions are reporting a constant decline in enrollment, despite unemployment in the country. Reasons include slow career progression, low wages and a general feeling of being under-valued.

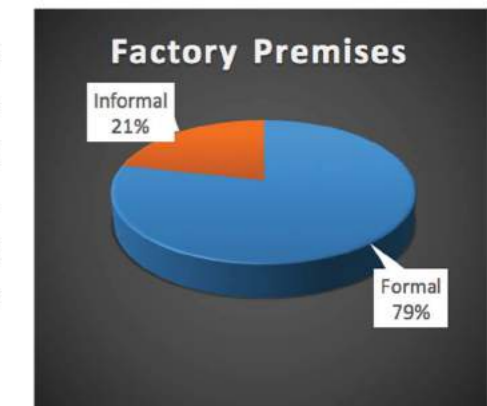
Most of the firms do not have any capacity building plans for the labour but would welcome on job training programs where workers can get training at their own premises. Additionally, as highlighted by majority of the sampled firms, stitching and finishing are key areas that require training and development.



A large proportion of the firms are using old machinery which is imported from China and Italy. Few firms have the latest machinery & tools. The micro & cottage industry is a far cry from adopting modern methods, upgrading their machinery or improving the working conditions and environment for their labor.

63% of the cluster firms are using a mix of local & imported machinery whereas 37% of the respondents are only using local machinery. The large & medium sized firms usually directly import from major markets including Italy & China, whereas the small firms usually rely on refurbished or locally assembled machines.

Within the sampled enterprises, 79% have formal factory premises while 21% have informal setups. The majority of the formal factory premises are within industrial areas. The informal setups are either established within houses or in plain rented halls without any proper structure or designated process areas. Furthermore, these companies are reluctant to formalize their operations to avoid taxation. Such setups enable them to produce at lesser costs than their formal counterparts.



3.10 Compliance and Certifications

Compliance & certifications, while mandatory for the Tanneries, seem to have less significance in the footwear sector. Two thirds of the sampled enterprises are ISO 9001 certified while one third do not have any certification. Out of the certified firms, few have ISO 14000 and BSCI certifications also.



A major proportion of the shoe manufacturers are working as vendors for bigger firms in the domestic market, who do not require any certification or social & environmental compliance. However, the companies have the product checked for quality as per the customer's requirements. This includes random checking of the finished product by teams of the client. Sometimes, the customers require international quality checks, in which case, the products are sent to EU notified labs. The importers also have their own procedures and quality checks/audits.

Nevertheless, the global trend is inclined towards tighter regulatory environments (with more countries requiring certification for imports) and increasing customer demands to comply with social responsible business requirements. This has led to a need for increased visibility across the supply chain associated with the manufacture of all retail-ready items, including leather footwear.

The Leather Working Group (LWG) is a multi-stakeholder group that was initially created in 2005 by the leading footwear manufacturers of the world including Nike, Adidas and Timberland to promote sustainable and appropriate environmental business practices within the leather industry. This is now becoming a very important certification internationally, the compliance of which will be mandatory by 2020. Leather manufacturers can join the group by having an LWG audit conducted by an approved auditor. The audit generally takes 2 days on-site and is a comprehensive evaluation of a leather manufacturer's environmental credentials. The audit is conducted against the LWG's protocol.

This means that the tanneries must essentially be LWG certified in order to be able to export. Likewise, the leather footwear and products' manufacturers will also be affected, although to a lesser degree, depending on the demands of the customer. The high cost of this certification coupled with the unwillingness of the relevant consultants to travel to Pakistan poses a significant threat to the country's leather industry.

Taking advantage of market opportunities requires compliance with increasingly stringent market and customer requirements. This is particularly important for the EU market as Pakistan was granted GSP+ status, effective as of January 2013. There is also a lack of testing facilities in Pakistan, capable of certifying compliance with requirements.

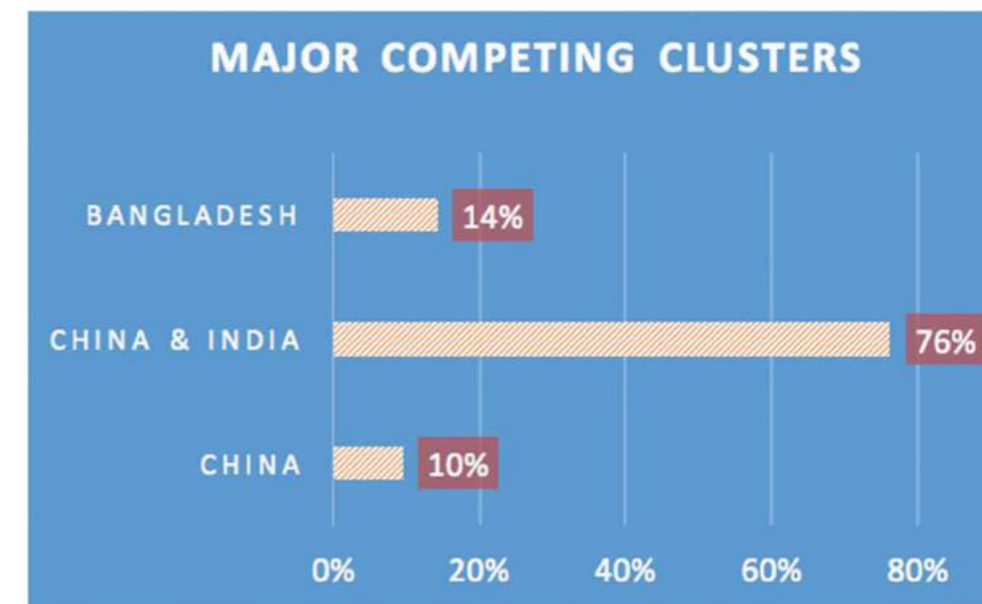


3.11 Competitors & Competition

The footwear industry is changing rapidly. Locally, the industry is moving towards cut throat competition because of overcapacity in terms of supply. One reason for this is the import of low cost footwear from China. This coupled with the local production, has led to a price war within the manufacturers, resulting in reduced profit margins. Companies are offering similar kinds of products to the same target market. This means that the switching cost for the customer is low. Companies are using diverse strategies on distribution and retail.

In Pakistan, the Lahore footwear cluster is leading in comparison to other clusters in Punjab and even Pakistan. Reasons include better infrastructure, higher productivity of the labour, good governance and better training institutions.

In export markets, the largest share is occupied by China & Vietnam, whereas India & Bangladesh are showing an upward trend in capturing more market. This is due to lower input costs, superior quality & better product finishing. The majority of cluster firms regard China & India as their major competitors.





3.12 Cluster Governance

Pakistan Footwear Manufacturers Association (PFMA) is the only body representing approximately one-third of the footwear sector in Pakistan. A review of the member list of PFMA reveals that it has around 115 members from all over Pakistan including 80+ members from Lahore & surrounding areas. However, a major proportion of its members are not shoe manufacturers. Very limited number of cluster firms have PFMA membership, therefore no strong cluster connection & relationships can be seen in this sector. The remaining firms, which are not members, are in thousands of number and not represented by any association.



64% of the cluster firms interviewed for the study are members of PFMA and satisfied by the role of the association; These firms were of the view that although more work is required, PFMA is providing the right platform and facilities for the member companies. 7% of the interviewed firms have membership of LCCI while rest of the firms are not associated with any forum.

The above percentages do not represent the whole footwear sector as PFMA only enlists the formal tax paying sector. The larger proportion of firms fall under the informal economy. The association has collaborated with MDF & GIZ and has worked to synergize this sector by skill development and introduction of allied industry (Shoe Last & Molds). The beneficial firms are interested in retaking such support.

3.13 Operation Management

56% of the interviewed firms are of the view that defect rates remain within 1-2% of the total production. Moreover, the rejected products are also sold as category B or low priced articles. 24% of the firms informed that their reject rates are very low and usually remain within 1%. 20% of the respondents were of the view that in production losses remain around 2-3%.

Industry sources are of the view that the 2% production loss does not represent the true picture. Since majority of firms do not have any mechanized system to document production losses, the actual percentage may be higher. This is because the footwear manufacturers do not consider wastages accrued during each phase of production, which if accounted, may push the actual wastage percentage to 5-8%.

Some of the firms are aware of production monitoring systems. They are implementing lean manufacturing techniques and also working for development of KPIs.





4. ANALYTICAL TOOLS APPLIED

4.1 PESTEL Analysis at National Level

In order to comprehend the macro environment factors, Political, Economic, Social, Technology, Environmental and Legal, PESTEL analysis is a helpful tool. The analysis carried out using the PESTEL tool can be used by the organizations to understand the existing external marketing/business environment vis-à-vis formulate strategies. In addition, PESTEL analysis provides key inputs to perform the SWOT analysis.

Following table shows some critical macroeconomic indicators for Pakistan:

Indicator	Figure	Ranking
GDP	USD283,659.9807 million (2016)	26 th
PPP	USD1,014,180.70 million (2016)	25 th
Population	193,203,476(2016)	6 th
GDP per capita	USD1468.19 (2016)	176 th
Industrial growth rate	5% (2017)	
GDP contribution by Industry	20% (2017)	
Labour participation rate	53% (2014)	
Human development index	0.55 (2015)	147 th
Expected years of schooling	8.1 years (2015)	
Primary school dropout rate	20.4% (2015)	
Employment rate	51% (2015)	179 th
Gender inequality index	0.54 (2015)	130 th
Environmental performance index	34.58 (2014)	148 th
Ease of Doing Business	147 out of 190 (2017)	147 th
Global Competitiveness Index	115 out of 137 (2017)	115 th

Key Tax Incentives Provided in FY17

Several tax incentives were provided to support exporting industries and the agriculture sector. The government also incentivized investment and employment generation by allowing firms tax credits. The important incentives are summarized below:

Exporting industries

- Five major export-oriented sectors (textiles, leather, sports goods, surgical goods and carpets) exempted from sales tax (zero-rating) on purchase of raw material;
- Off peak electricity tariff rates were reduced to Rs 5.35 per unit from Rs 8.85 per unit;

Industrial raw material

- Customs tariff slabs for import of industrial raw material were reduced from 5 to 4, by merging 2.0 and 5.0 percent slab to a new 3.0 percent slab, 10.0 and 15.0 percent slabs were substituted with 11.0 percent and 16.0 percent slabs and the 20.0 percent slab was kept unchanged;

Investment and employment generation

- Facility of 1.0 percent tax credit for every industrial undertaking employing 50 persons was increased to 2.0 percent, and the setting up period was extended till June 30, 2019;
- Tax credit facility for investment in Balancing Modernization and Replacement was revised upward to 20.0 percent from the existing 10.0 percent and period to avail this facility was extended till June 30, 2019;
- The condition of 100.0 percent of fresh equity raised through shares to avail 100.0 percent tax credit was relaxed up to 70 percent fresh equity raised with proportionate tax credit facility and the time period for this measure was extended till June 30, 2019;



4.1.2 PESTEL Analysis at Cluster Level

Factors

Government stability and likely changes
Bureaucracy
Corruption
Tax Policies
Trade control
Import restrictions and tariffs
Government involvement in trade unions and agreements



Political Factors

Growth rates
Inflation rate
Interest rate
Exchange rate
Unemployment trends
Labor Cost
Credit Availability
Trade flows & patterns
Levels of Consumers' disposable income
Price Fluctuations



Economic Factors

Education level
Attitude towards imported goods and services
Attitude towards product quality and customer service
Buying habits
Attitude toward "green" or ecological products
Population growth rate
Sex distribution



Socio-Cultural Factors

Basic Infrastructure Level
Rate of technological change
Spending on R&D
Technology Incentives
Technology level in your industry
Communication infrastructure
Access to Latest Technology



Technological Factors

Weather
Climate Change
Laws regulating environment pollution



Environmental Factors

Copyright, patents/Intellectual property law
Health and Safety Law



Legal Factors

Political Factors:

- ✓ Government stability remains a mandatory factor for proper policy formulation & implementation.
- ✓ Any instability makes the stakeholders risk averse which may impact their decisions negatively. Incompetent administrative setup hinders industrial sector development; prevalence of malpractices is on higher side.
- ✓ Currently, bureaucratic setup impedes the growth of the cluster due to cumbersome and ineffective procedures, which poses a threat
- ✓ Government has introduced several tax policies in the form of incentives and rebates, which serve as an opportunity for the cluster.
- ✓ Poor implementation poses a threat for the cluster and new entrants consequently.
- ✓ Low government involvement in trade unions and low involvement of industrialists in the decision making process/ agreements that are made at the government level is a serious threat for the current scenario. This also depicts weak public-private linkages

Economic Factors:

- ✓ Recently, the interest rate has witnessed a decrease. This implies increased credit opportunities for businessmen.
- ✓ Moreover, falling interest rates also mean people will no longer put their money in banks for saving purposes, investing it instead.
- ✓ Cumbersome process of acquiring credit along with collateral demands of financial institutions poses a threat for the cluster and due to the procedural issues industrialists generally do not prefer to take loans.
- ✓ Higher cost of production is a result of increased labour cost as compared to India & Bangladesh;
- ✓ Industry is not competitive with regard to labor productivity.
- ✓ High trade flows of regional competitors e.g. India, China, etc. pose a threat for the cluster.
- ✓ Low income leads to low business. High price fluctuations lead to unstable pricing of the products which poses a threat to the industry.

Socio-Cultural Factors:

- ✓ Currently existing workforce is uneducated which results in high cost of business due to low productivity and inability to apply modern production techniques & best practices.
- ✓ Preference of imported goods is a threat to the cluster. This is because of superior quality and low price of the imported footwear.
- ✓ Since our proportion of youth is increasing-more hands to work is an opportunity.
- ✓ Under-utilized female workforce is an opportunity for the cluster particularly in designing, stitching & packing.



Technological Factors:

- ✓ Investing more in technology provides better growth opportunity.
- ✓ Lack of R&D activities due to weak industry academia linkages and lack of resources results in low end products, thereby making the industry unable to compete with the regional partners.
- ✓ Moderate technology level poses a threat to the cluster as it results in low production and quality.
- ✓ Good communication infrastructure provides an opportunity for the industry to communicate swiftly.
- ✓ Access to latest technology in cluster is low as compared to regional competitors.

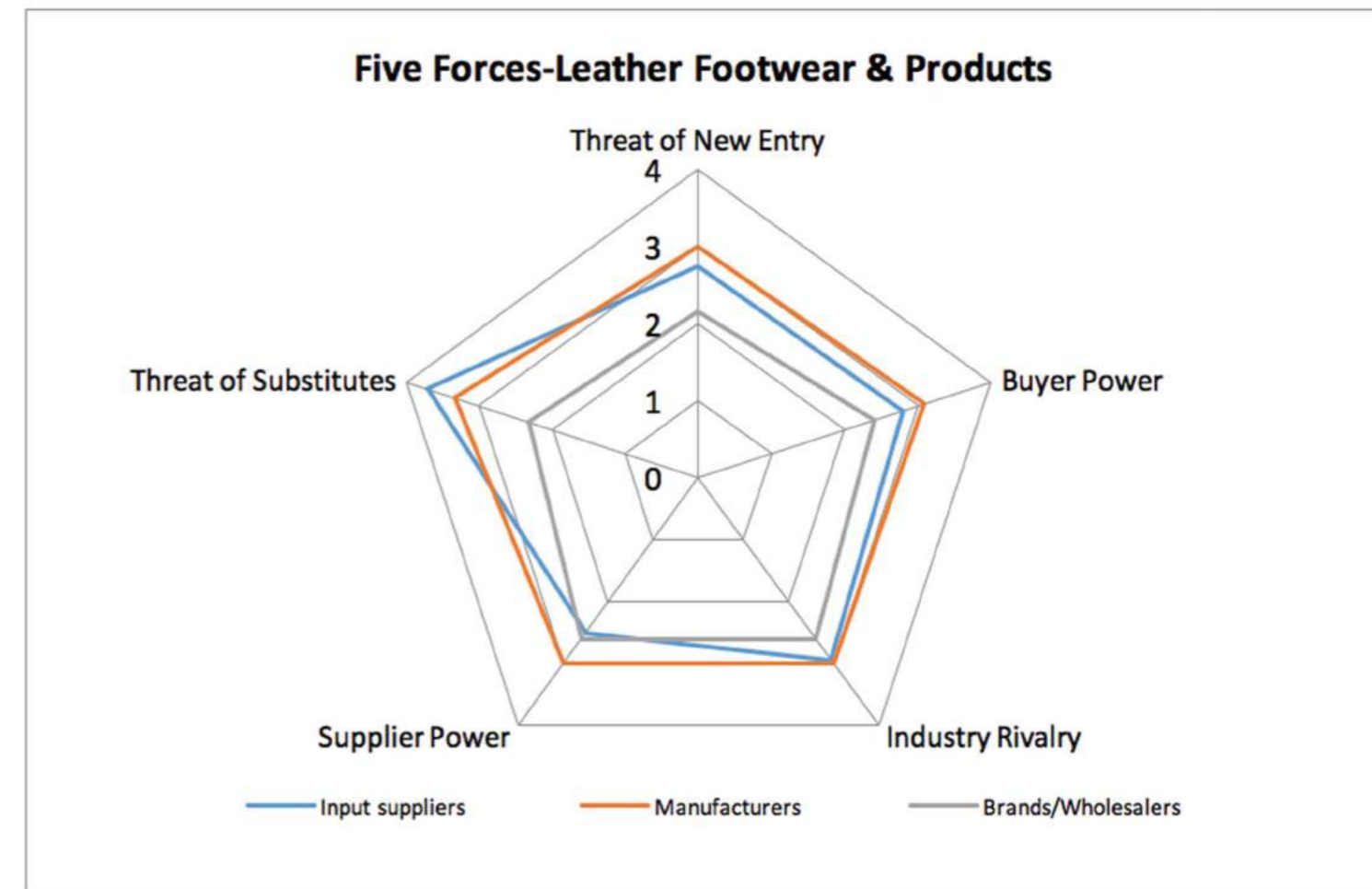
Environmental Factors:

- ✓ Environment affects production levels - in summers there is low production while winters result in high production rates.
- ✓ Environment affects products and machinery (rusting, precision errors).
- ✓ Cluster firms are least interested in infrastructural improvements, therefore environmental factors result as a threat for the cluster.
- ✓ Availability/quality of raw materials may get affected due to climatic changes; in the past we have witnessed floods that affected livestock quantity as well as quality of hides.
- ✓ Environmental laws are framed to save the natural environment from industrial waste & pollution. However, weak enforcement of these laws is currently proving to be an opportunity for the industry as it results in low cost of doing business. In case this changes with strict enforcement, then it will be a threat for the cluster.

Socio-Cultural Factors:

- ✓ Weak enforcement of Intellectual Property Law provides an opportunity for the cluster to copy and replicate other products. On the other hand, it hinders development in the cluster as the industry is not designing its own products.
- ✓ Health and Safety laws also force owners to provide a better working environment to the workers. Enforcement of laws is weak. However, with respect to the cluster it increases the cost of doing business. Generally footwear has a negative impression abroad because of the same. In the long-term it will be a threat, if not already.

4.2 Porters Five Forces Analysis for Leather Footwear





Analysis of Footwear Manufacturers

Threat of New Entry

This element of the Five Forces Analysis identifies the extent of new entrants' influence on existing firms in the leather footwear cluster. The threat of new entry for the footwear manufacturers is moderate to high. The factors contributing to moderate the entry threat in the cluster are low legal barriers & Government regulations, lower product differentiation and easy access to suppliers and distributors. On the other hand, increasing brand consciousness among the end customers, capital requirements to establish leather shoe manufacturing units, economies of scale and higher sunk costs are raising the bar to enter into the footwear cluster.

Bargaining Power of Buyers

The analysis indicates that the bargaining power of the buyers (wholesalers/retailers/end customers) is low to moderate. While the number of buyers are high and price conscious, the size of buyers and each order is relatively low keeping in view the dynamics of fashion trends in the footwear. Switching cost for the buyer is also low as options are endless, except in cases where brand loyalty is high. Buyers have easy access for importing cheap footwear as well. However, the wholesalers and retailers also have to strike a balance between the design/quality and price as these factors play an important role in the final sales.

The threat of backward integration from the end customers is very low, however, this threat is low in case of wholesalers and retailers.

Competitive Rivalry

Industry rivalry in case of the principle firms or the footwear manufacturers is moderate to high. A large number of shoe producers are competing to capture a higher share in the existing market (mainly local) with similar range of products, thereby generating a high level of rivalry among the cluster firms. The level of rivalry is further exacerbated with the increasing accessibility of cheaper imported footwear attracting customers with low brand loyalties.

In view of the above, to counter the high rivalry level the footwear producers are investing substantially in product marketing trying to create product differentiation. This in turn leads to higher marketing expenses and ultimately higher product prices. The industry growth is moderate due to moderate population growth, fashion trends and seasonal requirements.

Bargaining Power of Suppliers

The analysis of Porters five factors reveals that the bargaining power of the supplier is moderate to high. We are considering here the tanneries as the major supplier for the leather footwear cluster companies. Since the tanneries producing high quality leather are export oriented having low preference to provide quality leather to local footwear cluster companies, therefore the footwear companies are left with the choice to either use lower quality leather or procure good quality leather at export market prices. The local footwear cluster companies having their own tanneries are enjoying competitive advantage in terms of accessibility to high quality leather at lower prices.

However, there are more than 200 small tanneries supplying leather of acceptable quality to the footwear cluster manufacturers moderating the bargaining power of the suppliers. A number of substitute materials have already penetrated into the market affecting market share of leather footwear adversely. These materials include rubber, textile, plastic, synthetic, microfiber, etc.

Moreover, the Leather Working Group, which will be a mandatory certification by 2020, will change the dynamics as the number of suppliers who are LWG certified will be less. This may lead to those suppliers monopolizing the market and increase their bargaining power with respect to the leather manufacturers. This is especially true for those players that are more into exporting.

Threat of Substitution

This force indicates that there is a moderate to high threat of substitutes present. The market is flooded with footwear products made of rubber, textile, plastic, synthetic and microfiber. The number and the performance of substitutes is comparable to leather footwear, while the cost of switching to these substitutes is low for the medium income level end customer.



4.3 SWOT Analysis

Strength	Weakness	Opportunity	Threat
Markets			
<ul style="list-style-type: none"> ✓ Presence in local market ✓ Size of the local market is big, better understanding of the local demand. ✓ Fast growing domestic market ✓ Price competitive (globally) ✓ GSP Plus status ✓ Well organized sales channels 	<ul style="list-style-type: none"> ✓ Market share is decreasing in international market ✓ Lack of brand recognition ✓ Diminishing rate of profits ✓ Weak shoe finish techniques results in limited market-ability of the products ✓ Lacking product and market diversification ✓ Strong price competition among the cluster companies ✓ Poor marketing strategies in the export market. ✓ Lower market and product diversifications 	<ul style="list-style-type: none"> ✓ Un-tapped markets like USA ✓ Emergence of low end markets like Africa ✓ Low end products can be exported to Africa. ✓ JVs to meet requirements of USA & Australian Market ✓ Establishment of allied industry ✓ Greater market access through CPEC, especially to Central Asia and Africa ✓ Opportunity for higher value addition through targeted marketing or designing. 	<ul style="list-style-type: none"> ✓ Least developed status of regional competitor (Bangladesh) reducing exports of Pakistan ✓ Local market share being captured by low cost Chinese imported shoes ✓ Emerging exporters like Vietnam & India ✓ Shift from leather to non-leather shoes by European customers due to decrease in income level ✓ Negative country image. ✓ Increasing stringent legislation and compliance requirements in the existing and potential export destinations (LWG).

Strength	Weakness	Opportunity	Threat
Technology			
<ul style="list-style-type: none"> ✓ Presence of international brands ✓ Awareness about latest technology in Footwear ✓ Availability of imported new/re-refurbished machinery & equipment ✓ Increasing awareness related to CAD/CAM designing ✓ Local availability of sewing machines ✓ Availability of ICT technology ✓ Availability of latest machinery at affordable prices from nearby countries like China 	<ul style="list-style-type: none"> ✓ Old production techniques. ✓ Reliance on the conventional manufacturing methods and technologies ✓ Limited adoption of best operations and quality practices resulting in low productivity ✓ Use of outdated & refurbished machines ✓ Weak R&D linkages ✓ Less tendency towards technological development ✓ Lacking indigenous production of capital goods (machinery and equipment) ✓ Due to usage of obsolete technology, high in line rejection rates and defects ✓ Lacking awareness and access to new technologies among the SMEs ✓ No technology acquisition company ✓ Access to finance for technology acquisition ✓ Lack in adoption of latest technology. ✓ Low level of indigenous technological development 	<ul style="list-style-type: none"> ✓ Technological spillover ✓ Establishment of Common Facility Center (CFC) to promote technology in the footwear cluster ✓ Center of excellence for footwear sector planned ✓ Existing infrastructure available for reverse engineering of machinery like Pakistan ✓ Machine Tool Factory, Karachi, etc. ✓ Duty rebates on purchase of technology 	<ul style="list-style-type: none"> ✓ Emerging regional competitors with latest technological adoption ✓ Weak government policies implementation regarding refunding of rebate claims





Raw Material			
Strength	Weakness	Opportunity	Threat
<ul style="list-style-type: none"> ✓ Quality leather is available locally Amongst the top ranked quality leather producer after Italy (industry sources) ✓ Strong agricultural base provides abundant hides ✓ Presence of large number of suppliers 	<ul style="list-style-type: none"> ✓ Limited support industry increases the input cost and lead time ✓ Quality raw materials (other than leather) are not manufactured locally ✓ Accessories are mainly imported ✓ High duties on import ✓ Cumbersome import procedures Proper material quality testing facility is not available ✓ Inadequate supply and high energy costs for the industry (PKR 16/KW at peak hours) 	<ul style="list-style-type: none"> ✓ Promotion of PU sole making locally ✓ Rebates in duties for import of machinery (not available locally) for companies operating in SEZs ✓ Development of support industry through interventions by international agencies ✓ Lasts & Mold industry is emerging ✓ Substitute materials and development/acquisition of technology to diversify products 	<ul style="list-style-type: none"> ✓ Overall decline in demand for leather footwear ✓ Footwear made of substitute materials are replacing leather footwear market. ✓ High price of good quality leather ✓ Comparative advantage in terms of cheaper and high quality substitute material of regional competitors, can suppress the leather footwear cluster growth

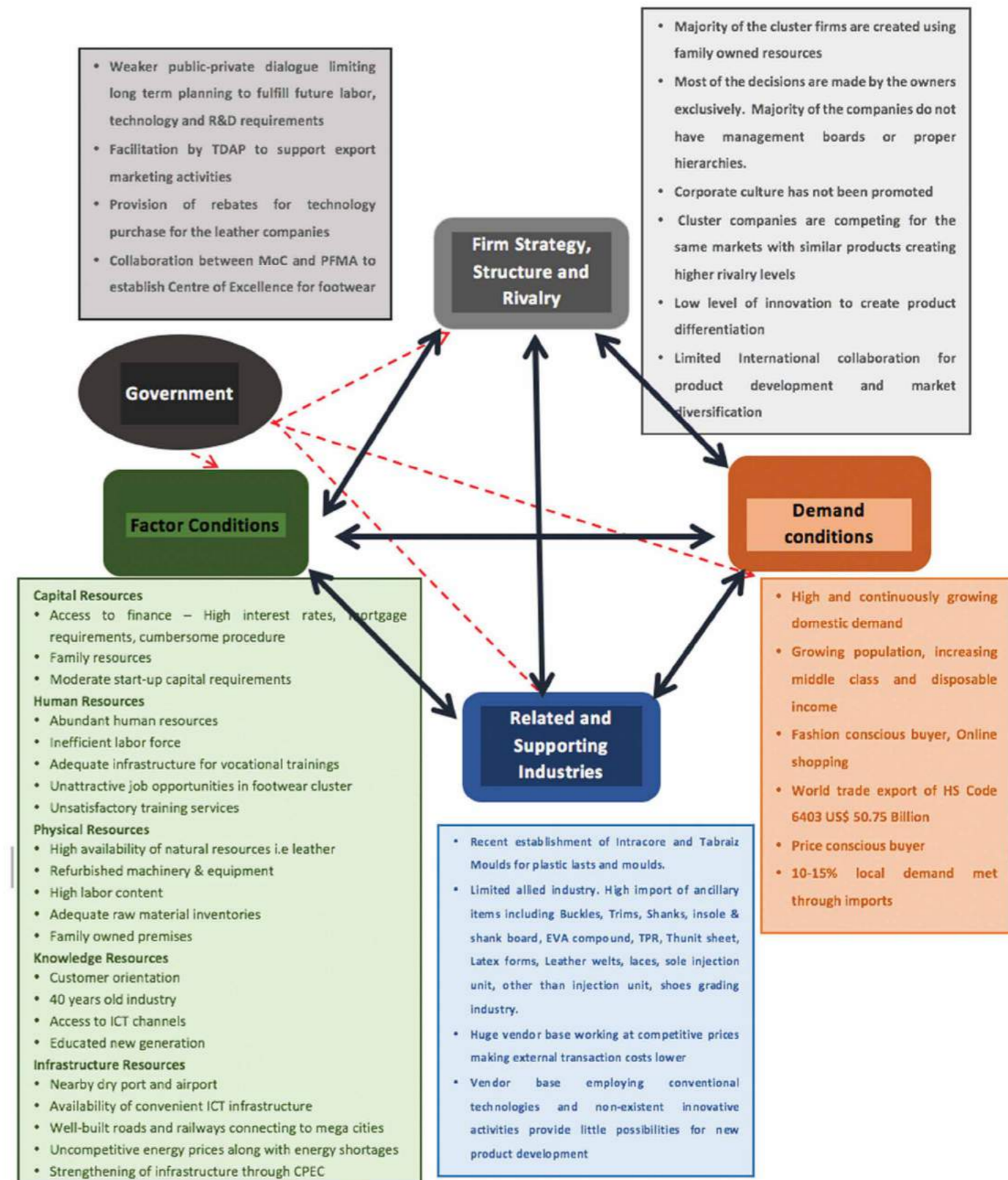
Human Resource			
Strength	Weakness	Opportunity	Threat
<ul style="list-style-type: none"> ✓ Availability of semi-skilled workers trained by government institutions ✓ Availability of workforce at lower/competitive wages with respect to China, Turkey ✓ Availability of vocational training infrastructure to develop semi-skilled workforce ✓ International Donors like GIZ, MDF and public organizations like TEVTA, PVTC, PSDF have collaborated for enhancement and promotion of courses in support industry i.e shoes lasters course, Technical Education & Vocational Training as well as gender equality ✓ Entrepreneurs of Medium & Large firms are mostly educated & aware of the latest trends 	<ul style="list-style-type: none"> ✓ Low rate of induction of semi-skilled workforce trained through vocational institutions due to uncompetitive wages ✓ Structural unemployment due to skills mismatch between potential employees and the employer ✓ Weak in-house training and development of the existing workforce ✓ Management perceives training and management as expense rather than investment ✓ Non-conducive working environment to attract the workforce especially for women ✓ Low productivity level ✓ High turnover 	<ul style="list-style-type: none"> ✓ Cooperation between the support institutions and the industry ✓ Availability of rural young population ✓ Government interventions through improved skill services ✓ Footwear companies can improve the labor turnover rate by employing better HR practices ✓ Government support in internship or apprentice schemes. youth internship schemes can be coupled for compensation of manufacturing workforce partly ✓ Footwear companies can improve labour turnover and skills retention. ✓ Room for substantial improvement in labour productivity by adopting latest operations management tools and techniques ✓ Curriculum development has started Introduction of ✓ DAEs & BS programs are adding towards footwear sector development 	<ul style="list-style-type: none"> ✓ In terms of labor productivity, Pakistan's regional competitors have comparative advantage either due to lower wage (Bangladesh, Sri Lanka) rates or higher labor productivity (China, India, Vietnam) or both. ✓ Availability of alternate job opportunities for the potential workforce ✓ Strong development & implementation of best practices by regional competitors (Vietnam, China, India etc) ✓ Adoption of best manufacturing practices by regional competitors gives them a comparative advantage ✓ Diminishing concept of Ustad-Shagird system.



Porter's Diamond Model

4.4 Porter's Diamond Model

Porter's Diamond Model assumes that the competitiveness of businesses is related to the performance of other businesses. Other factors are tied together in the value-added chain in a long distance relation or a local or regional context. In the diagram below, these factors and their linkages with each other are depicted.





A general analysis of the Diamond Model of the Lahore footwear cluster reveals that while the firms are able to sustain local competition and thrive in the domestic market, they are unable to compete internationally. For the firms to remain globally competitive and reach high-level quality both in products and human resources, they need to adopt international best practices in terms of productivity, research and development and establishment of the allied industry.

Improvement in the purchasing power of masses, trust in the government and in its laws are important points for further attention as well.

In terms of demand conditions, factor conditions and rivalry, the Lahore footwear cluster has characteristics of competitive advantage. The companies that want to expand to new markets internationally need to have the confidence to establish their brands abroad and improve their base in the local market through innovation and expansion.

Pakistan has registered some reasonable improvements in the factor conditions. For instance, communication services, financial market sophistication and overall infrastructure has improved. However, the efficiency of legal framework, equity market access and quality of training is going down. In terms of context of firm strategy & rivalry, Pakistan has improved in lowering of trade barriers although the local competition is high and the regulatory standards are not satisfactory. In general, Pakistan has showed some progress in the Diamond conditions as compared to the past.

The footwear industry is used to surviving in difficult conditions such as fluctuating trends in economy and consequently that of its customers, high bureaucracy, complex fiscal and tax system, logistics and incertitude. The ability of the industry to not only exist but grow in such a complex environment is an indicator of its resilience. With the right attitude, flexibility and organization, it will be able to achieve the same level of competitiveness as the older and internationally renowned players globally.

4.5 VALUE CHAIN ANALYSIS

Value chain analysis of the leather footwear begins from procurement of basic raw material i.e. leather and through value addition at various processes, it ends with transfer of the final product to the end consumer.

In this report, we have done value chain analysis of both the formal & casual leather shoe. This has been done by depicting the value addition at each phase of the shoe manufacturing through a waterfall diagram.

The figures shown are meant for explaining the broader phases of value addition of footwear and are based on the average industry estimates for formal and casual shoes, which are frequently made & sold in the men's shoe category.



4.5.1 Men's Formal Shoe

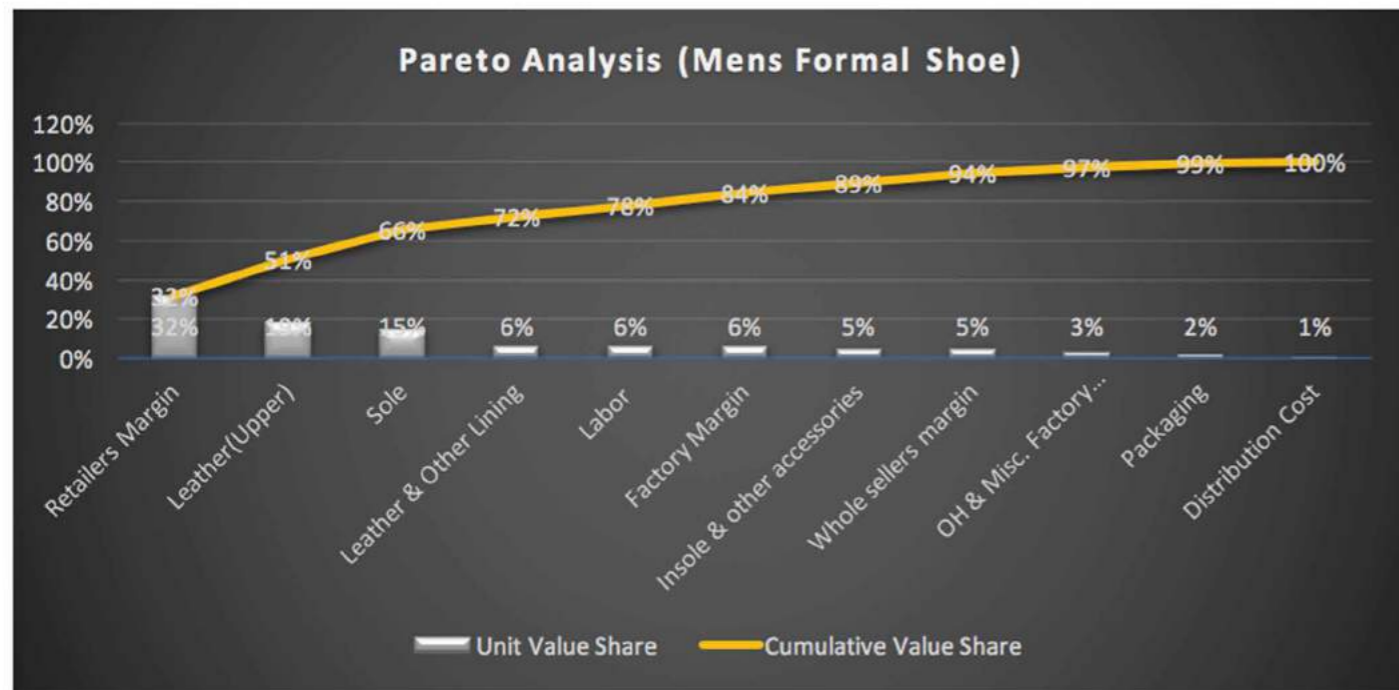
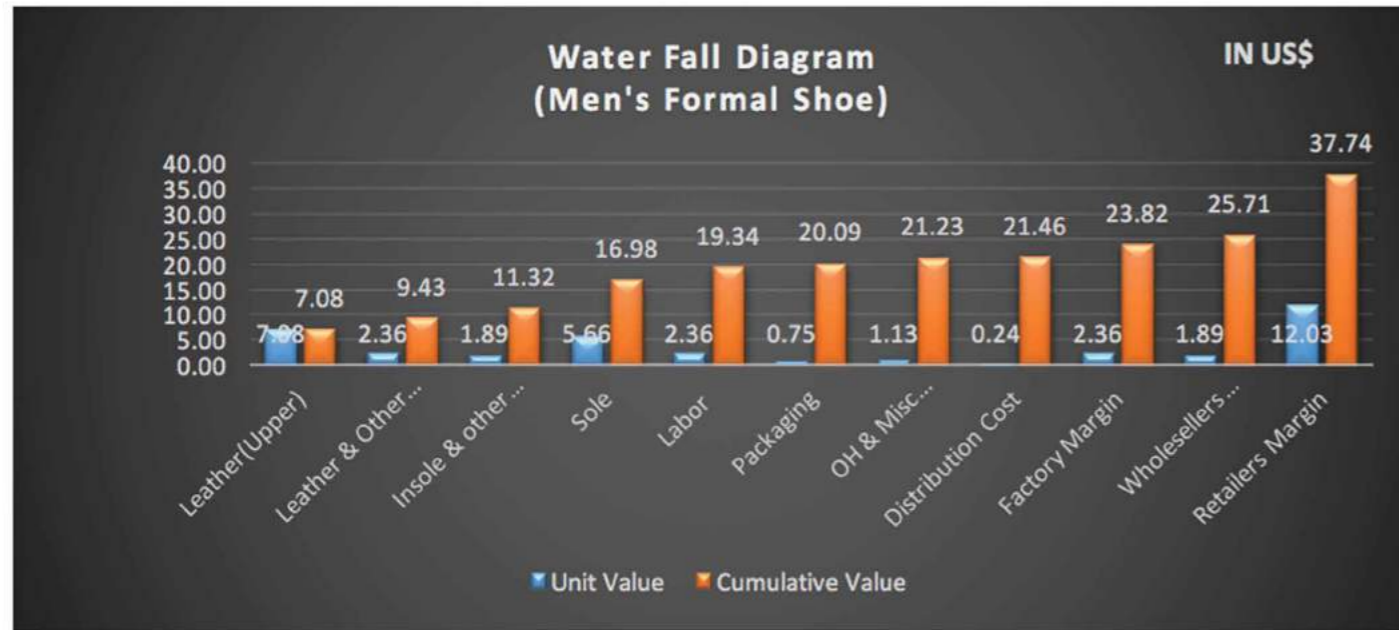
(In US\$)

Component	Unit Value	Cumulative Value	Unit Value Share	Cumulative Value Share
Leather(Upper)	7.08	7.08	19%	19%
Leather & Other Lining	2.36	9.43	6%	25%
Insole & other accessories	1.89	11.32	5%	30%
Sole	5.66	16.98	15%	45%
Labor	2.36	19.34	6%	51%
Packaging	0.75	20.09	2%	53%
OH & Misc. Factory Expenses	1.13	21.23	3%	56%
Distribution Cost	0.24	21.46	1%	57%
Factory Margin	2.36	23.82	6%	63%
Whole sellers margin	1.89	25.71	5%	68%
Retailers Margin	12.03	37.74	32%	100%

The analysis for the formal shoe reveals that the prime cost i.e. raw material & labor collectively account for 51% of the consumer price. Retailers are capturing the largest share (32%). Factory margins are in single digits and account for 6% of total value. One of the reasons for this is the intense rivalry among shoe manufacturers. The profit margin of manufacturers usually remains at 5-10% of the shoe cost. Wholesalers are also getting less margin. Their share adds 5% towards the total value. According to industry sources, the Wholesalers are earning 4-6% profits whereas the maximum earning remains at the end of retailers who usually earn over 20%. As retail margins in this industry are high, a number of manufacturers are also opening their own retail shops as well as giving franchises.

ILLUSTRATION OF VALUE ADDITION IN LEATHER FOOTWEAR

Men's Formal Shoe



Comparing the Price Structure with CBI Cost Estimations:

Price structure is a key topic while entering a new market. Price is also an important point of comparison when evaluating our product against the competitors. Due to oversupply and competition, prices for mainstream footwear have been under greater pressure. Large retailers have even put more pressure on prices and margins in the footwear supply chain by purchasing in substantial quantities. As an exporter or manufacturer, it is advised to concentrate on the exclusiveness of footwear, for example, by introducing original footwear that meets the style, design, size and comfort needs of a specific target group. In this case, price is often less important.

The prevailing estimated average prices of formal & casual shoes produced in Pakistan are compared with the price structure elaborated in "CBI Market Survey: The Footwear Market in the EU" to understand the variation under different stages of footwear manufacturing & selling; for ease of understanding, the factory cost of the shoe is taken as the base for comparison with CBI standard cost structure for footwear.

COMPARISON WITH STANDARDIZED PRICE CALCULATIONS USED BY CBI

(FORMAL SHOE)

Description	Using CBI Standard Pricing	Actual Prevailing Costs/Prices	Deviation from CBI Costing	% Change
Materials	6.77	16.98	-10.21	151%
Labor	6.77	2.36	4.41	-65%
Others	4.06	2.12	1.94	-48%
Factory Margin (35%)	6.23	2.36	3.87	-62%
*Factory Price	23.82	23.82	0.00	0%
Wholesellers Margin (35%)	8.34	1.89	6.45	-77%
Wholesale Price	32.16	25.71	6.44	-20%
Retailers Margin (60%)	19.29	12.03	7.26	-38%
Consumer Price	51.45	37.74	13.71	-27%

*baseline used same as per illustration of VCA-Waterfall Diagram

CBI Market Survey- Footwear Market in EU

4.5.2 Value Chain Analysis (Men's Casual Shoe)

ILLUSTRATION OF VALUE ADDITION IN LEATHER FOOTWEAR



Men's Casual/Semi-Formal Shoe

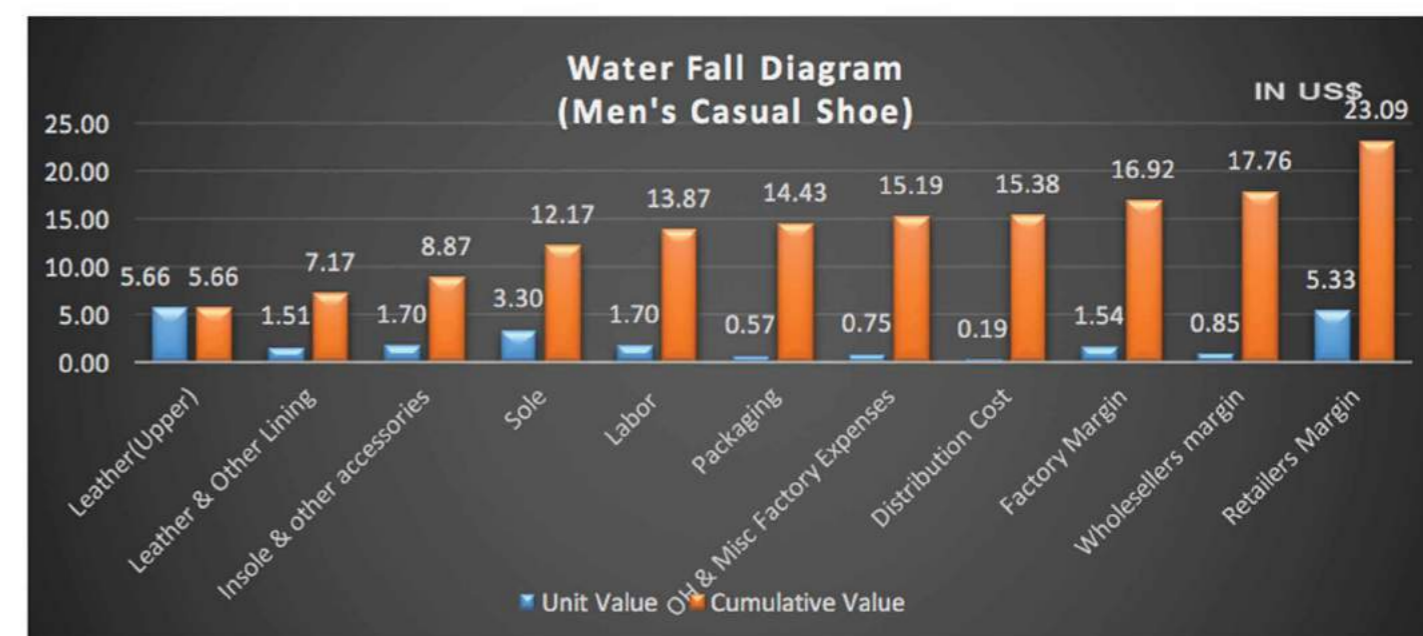
(In US\$)

Component	Unit Value	Cumulative Value	Unit Value Share	Cumulative Value Share
Leather(Upper)	5.66	5.66	25%	25%
Leather & Other Lining	1.51	7.17	7%	31%
Insole & other accessories	1.70	8.87	7%	38%
Sole	3.30	12.17	14%	53%
Labor	1.70	13.87	7%	60%
Packaging	0.57	14.43	2%	63%
OH & Misc Factory Expenses	0.75	15.19	3%	66%
Distribution Cost	0.19	15.38	1%	67%
Factory Margin	1.54	16.92	7%	73%
Whole sellers margin	0.85	17.76	4%	77%
Retailers Margin	5.33	23.09	23%	100%

Men's Casual Shoe



This analysis reveals that raw material & labor collectively account for 60% of the final price. Basic raw material i.e. leather for shoe uppers is the major cost (25%), after which the retailers are capturing the 2nd largest share (23%). Factory margin is in single digit and accounts for 7% of total value. One of the reasons is the intense rivalry among shoe manufacturers. The profit margins of manufacturers usually remain at 5-10% of the total shoe cost. Wholesalers sellers also get less margin. Their share adds 4% of the total value as the whole sale margins are very low; whereas the maximum earning remains at the end of retailers who usually earns > 20% and in some cases the profit can reach 70-80%; in our above illustration the retailers margins accounts for 23% of the retail price.



4.6 Cooperation Matrix

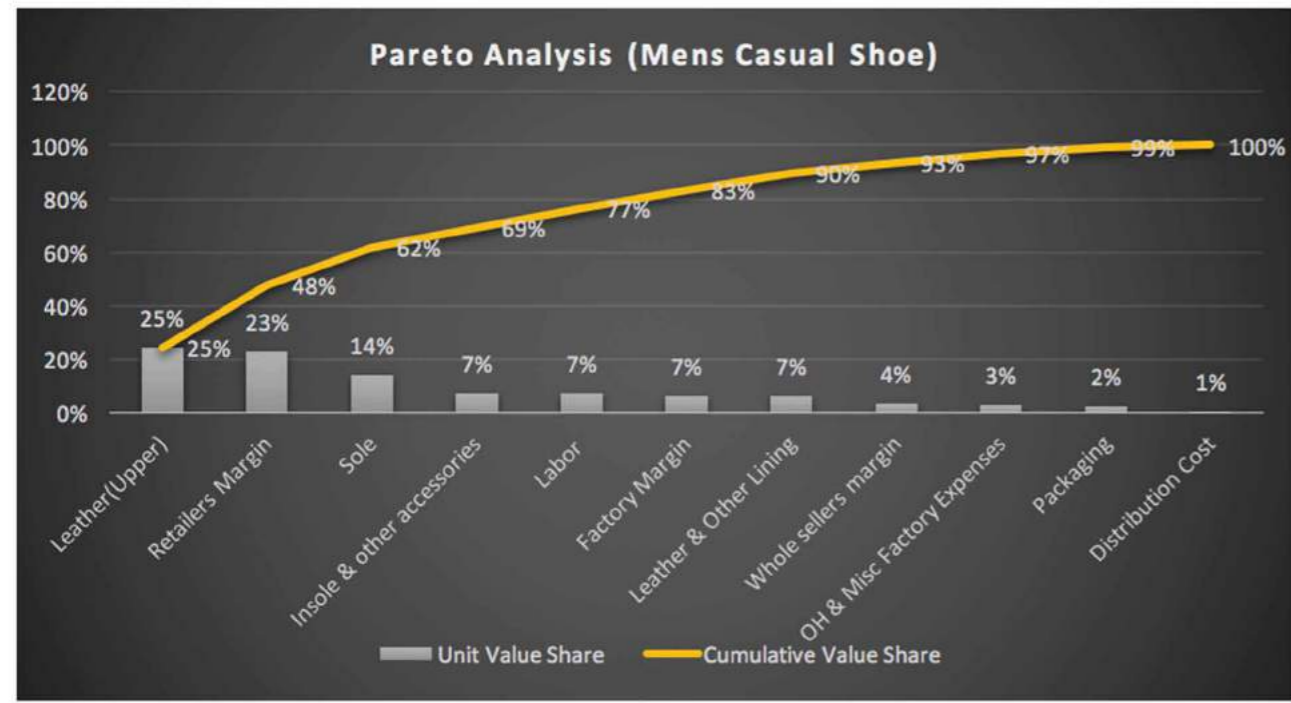
Cooperation Matrix																				
Name	IC&ID	PVTC	PSDF	SMEDA	TDAP	PCSIR	NPO	PBIT	PSIC	TEVTA (GILT)	PFMA	LCCI	Govt. Universities	Pvt. Institute	Pvt. BDSPs	Banking and Financial Institution	Raw Material Supplier	Certification Agencies	Donor Agencies	Total
IC&ID	X	2	2	2	2	1	1	4	4	4	1	2	2	2	2	2	0	0	2	35
PVTC	2	X	2	3	0	0	0	0	1	2	2	3	1	2	2	1	3	1	3	28
PSDF	2	2	X	2	1	0	0	1	1	3	2	3	1	2	0	0	3	0	4	27
SMEDA	2	3	2	X	3	0	3	2	2	2	2	3	3	3	2	2	2	1	4	41
TDAP	2	0	1	3	X	1	2	3	2	0	3	3	2	2	2	1	3	2	3	35
PCSIR	1	0	0	0	1	X	1	0	1	1	1	2	3	2	1	0	2	4	2	22
NPO	1	0	0	3	2	1	X	0	0	1	1	3	2	2	3	1	1	1	3	25
PBIT	4	0	1	2	3	0	0	X	3	1	0	3	1	1	0	2	0	0	3	24
PSIC	4	1	1	2	2	1	0	3	X	2	2	2	2	2	1	3	1	1	2	32
TEVTA(GILT)	4	2	3	2	0	1	1	1	2	X	3	1	1	1	1	0	2	0	3	28
PFMA	1	2	2	2	3	1	1	0	2	3	X	3	2	2	1	2	4	2	3	36
LCCI	2	3	3	3	3	2	3	3	2	1	3	X	2	2	2	2	1	2	3	42
Govt. Universities	2	1	1	3	2	3	2	1	2	1	2	2	X	3	1	1	1	1	2	31
Pvt. Institute	2	2	2	3	2	2	2	1	2	1	2	2	3	X	1	2	1	1	2	33
Pvt. BDSPs	2	2	0	2	2	1	3	0	1	1	1	2	1	1	X	2	2	2	2	27
Banks & Financial Institutions	2	1	0	2	1	0	1	2	3	0	2	2	1	2	2	X	2	1	2	26
Raw Material Suppliers	0	3	3	2	3	2	1	0	1	2	4	1	1	1	2	2	X	3	3	34
Certification Agencies	0	1	0	1	2	4	1	0	1	0	2	2	1	1	2	1	3	X	1	23
Donor Agencies	2	3	4	4	3	2	3	3	2	3	3	3	2	2	2	2	3	1	X	47
Total	35	28	27	41	35	22	25	24	32	28	36	42	31	33	27	26	34	23	47	X

The Cooperation Matrix helps in highlighting relationships and linkages, both strong and weak, among the relevant institutes in the cluster. As far as the footwear sector is concerned donor /international agencies have a comparatively strong relationship with the stakeholders. MDF & GIZ have made interventions for this sector by assisting in setting-up of Lasts & Molds making units and improvement in the skillset respectively. They also have regular interactions with various stakeholders like PSDF, SMEDA, GILT & PFMA.

GIZ is currently working for the development of curriculum for footwear with TEVTA & PVTC so that the outdated curriculums are made in-line with the industry needs and new courses are introduced. Since donor agencies are key players in footwear sector, they can reinforce this sector by synergizing efforts with other key players. There is an acute shortage of good stitchers and lasters, an area which can be improved by collaborative efforts of training institutes like GILT & PVTC with technical & financial support of international donor agencies.

SMEDA is promoting the SME sector in the country and has established good relationships with donor agencies, private and public sector institutes and can link the stakeholders for promoting better entrepreneurship culture, skills transformation and advocacy with the federal & provincial government department to uplift the footwear sector by providing liberalized policies and an enabling environment. Being a federal government entity SMEDA can be a prominent stakeholder in recommending policy level interventions for this neglected sector where we can gain a lot in terms of value addition and can earn sizable revenue. SMEDA can raise awareness about footwear sector with the raw material suppliers & BDSPs and better link them with donor agencies & PFMA so that the exact needs of this sector can be well managed by the existing & new entrants.

PFMA is the key representative of the footwear sector of Pakistan; PFMA has established good relationships with training institutes, foreign donor agencies and educational institutes. It is currently planning to establish a small CFC with the support of ASSOMAC. This CFC will provide a testing facility. CAD/CAM will be made available to the PFMA members.



COMPARISON WITH STANDARDIZED PRICE CALCULATIONS USED BY CBI

(CASUAL SHOE)

Description	Using CBI Standard Pricing	Actual Prevailing Costs/Prices	Deviation from CBI Costing	% Change
Materials	4.81	12.17	-7.36	153%
Labor	4.81	1.70	3.11	-65%
Others	2.88	1.51	1.37	-48%
Factory Margin (35%)	4.42	1.54	2.88	-65%
*Factory Price	16.92	16.92	0.00	0%
Wholesellers Margin (35%)	5.92	0.85	5.07	-86%
Wholesale Price	22.84	17.77	5.07	-22%
Retailers Margin (60%)	13.71	5.33	8.38	-61%
Consumer Price	36.55	23.10	13.45	-37%

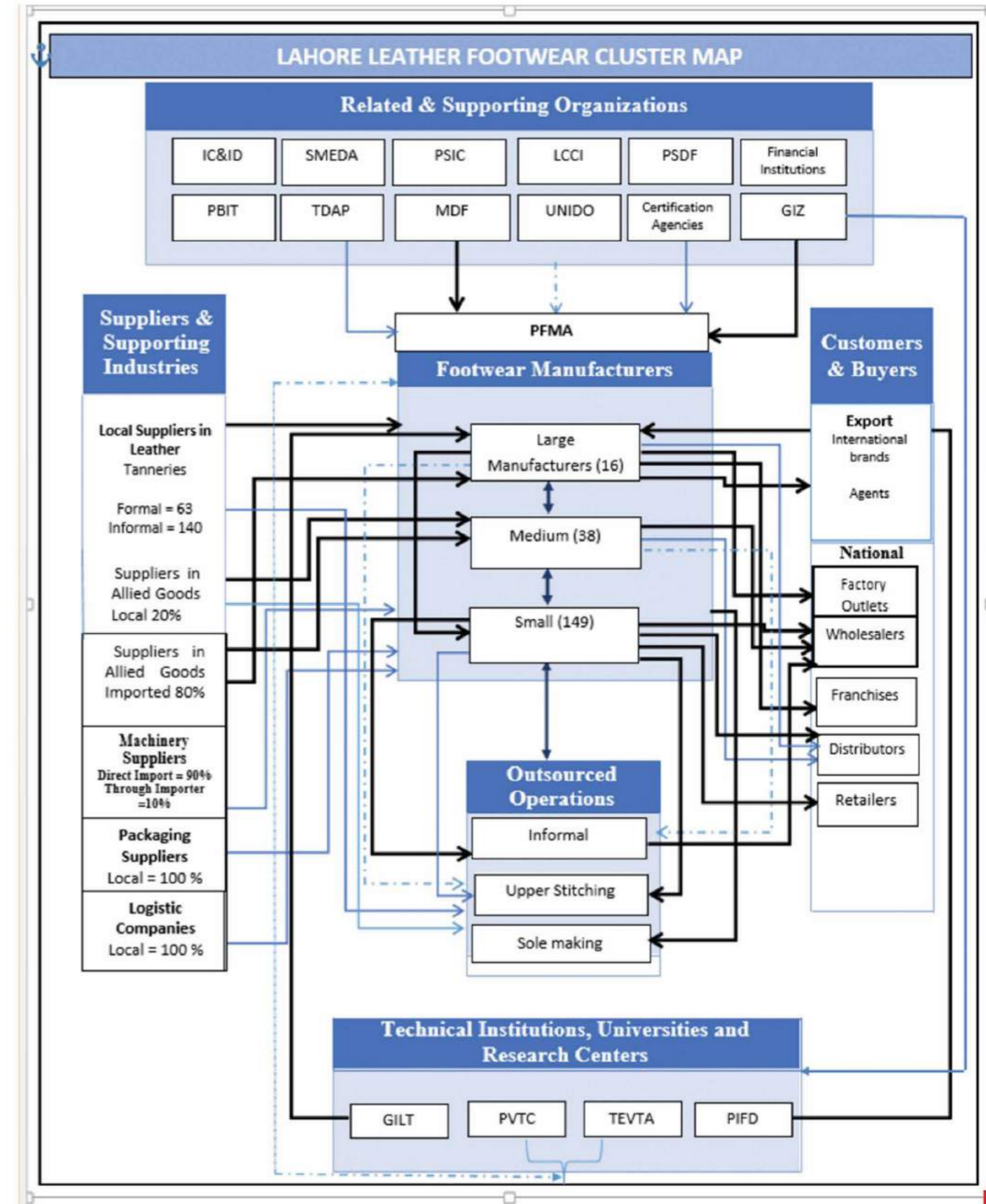
*baseline used same as per illustration of VCA-Waterfall Diagram

4.7 Cluster Map

PFMA has also worked to develop curriculum for footwear sector with TEVTA and was successful in launching a 3 years Diploma of Associate Engineering (DAE) for Footwear Technology at GILT. PFMA is currently working with PVTC & GIV to launch a complete cut-to-pack course to develop HR, which can be fitted in any area of production. PFMA along with international agencies and LCCI can start advocacy with the government for incentivizing this sector so that it can grow as in the neighboring countries like India, Bangladesh & China. Moreover, in the interest of the local industry, the heavy imports from China needs to be relooked at to safeguard the local industry, which is already in the worst condition.

GILT is a premier institute for leather & footwear sector. With a long history of serving the footwear sector, GILT is now redeveloping its courses and diplomas to cater to the changing needs of the footwear sector. GILT has strong linkage with footwear manufactures. GIZ has supported GILT in development of new courses & curriculum with input of PFMA. Besides getting semi-trained youth from GILT, industrialists are demanding customized courses for the on-job-training to upgrade the labour skills at the workplace. GILT can work to develop master trainers at factories who can transform the skills to other workers.

Besides the above institutes, LCCI being the premier association of the industrialists can raise issues of the footwear sector along with PFMA to the relevant institutes and departments.





Key Constraints, Explanations & Recommendations

Recommendations

After an analysis of the current situation of the Lahore footwear cluster, it has been identified that there are a number of constraint areas that impede the growth and development of this industry. All or most of these translate into lower productivity. While it is not possible to completely eliminate all of them, they can be addressed in a way so as to not only minimize their effect but also help the industry become self-sufficient to a considerable degree by improving its business infrastructure and adopting better policies and practices.



Key Recommendations

<p>In-house designing capability to be enhanced introducing designing & sole technology courses Collaboration with PIFD and private sector for superior quality finishing courses with practical training Industry-academia linkages</p>  <p>Product Design & Development</p>	<p>Brand Development E-commerce Exploring new markets Dedicated b2b meetings in target market</p>  <p>Marketing & Markets</p>	<p>Upgrading curriculum Customized short courses Certified Labour Training of supervisory staff to develop technical competence in critical operations Effective student enrollment policy Common training facilities Awareness seminars for Socio-Cultural issues</p>  <p>Skill Development</p>
<p>Supporting industrialists to invest in ancillary items Support to improve existing product quality and operations</p>  <p>Promoting Allied Industry</p>	<p>Assisting private and public labs through capacity building to offer wider range of tests as per international requirements i.e EU's REACH</p>  <p>Reaching Compliance & Standards</p>	<p>Support association in lobbying for a change in duties and tax structure Consulting industry in decision making process regarding policies Government support for establishment of a Footwear Service Center, dedicated for the footwear industry Promoting local products through imposing duties on shoe imports</p>  <p>Policy, Rules & Regulations</p>

A summary of the key constraints, their explanation and possible intervention areas are listed below.

Key Constraint 1: Weak Product Development & Design

Explanation

- The Pakistan footwear industry primarily caters to the local market.
- Local demand of low priced, low value shoes is growing
- Stiff competition from the low cost imported shoe
- Due to frequently changing fashion and weak designing capability, the cluster cannot cater to the needs of the market
- Due to even more frequently changing styles in the women's shoes, coupled with more complicated and precise procedures, most of the manufacturers focus on producing men's shoes. This gap is then filled by imported shoes, or

Recommendation

- Support the manufacturers in developing in house design capabilities and improving product development capacity
 - Training institutions may be assisted in updating curriculums, incorporating design and sole technology courses. Joint collaboration with international trainers and counterparts may be sought. Moreover, industry-academia linkages may be strengthened.
 - CFC facility being developed by PFMA may be supported to enhance design skills and product range to scale up operations. International trainers with expertise in design and product finish may be hired for capacity building. This will cause both spill over and spin over effects, which will be beneficial for the industry.
- A joint program with the Pakistan Institute of Fashion & Design may commence with active support from the industry in superior product finishing to compete with regional partners.

Key Constraint 2: Lack of Expertise in Markets & Marketing

Explanation

- Pakistan's footwear industry primarily exports to Europe, where the buyers are highly quality conscious
- Lack of access to international events and exhibitions especially for the small and micro firms, resulting in limited or no exposure to international quality standards (for example in packaging)
- Currently, TDAP provides subsidized access to international fairs and exhibitions, but allows limited visibility and access to customers
- Lack of export market intelligence
- Manufacturers are not dynamic in experimenting with new business models and marketing to consumers directly
- Brands are not established internationally

Weak marketing consultancy and services regarding forecasting future trends in marketing & branding.

Recommendation

- Capacity building of manufacturers in innovative branding and modern marketing including e-commerce and e-retailing
 - Adoption of appropriate marketing plans and strategies for market penetration and diversification
 - TDAP, in addition to providing subsidized access to international trade exhibitions and shows may allow the industrialists to plan their participation and the arrangements
 - Assisting the industry in exploring new markets
- The Pakistani missions abroad, through targeted market research and penetration sessions , may arrange dedicated b2b meetings with new customers in existing markets



Key Constraint 3: Insufficient Skilled Labour

Explanation

- Lack of certified skilled workers
- No preference in requirement for minimum formal education in labour, which ultimately contributes to lower productivity
- The industry find it difficult to hire and retain skilled labour
- Larger proportion of labour, owing to the seasonality factor, is hired on piece rate/ contractual basis. This leads to a higher turnover, especially within the stitching department (30%).
- Lasting is another department in which workers are in high demand. Within this, toe lasting is the most critical job.
- Line and floor supervisors lack competence and technical knowledge in key areas such as optimal work flow, workers management and motivation, machine maintenance, health and safety, inventory and storage etc
- Fresh workers are continuously hired and trained to fill the gap. However, these workers do not stay with the company for long due to different reasons including unclear growth trajectory, job insecurity, better salary offer etc
- Female employment remains low due to social, cultural and working environments.
- Women are unable to enroll in majority of the courses offered by training institutes, as due to cultural factors they are unable to attend mixed classes.
- Training institutes offer limited courses in leather footwear and struggle to maintain enrolment. Training institutes like GILT do not have adequate running funds to cover practical costs. A meager amount is sanctioned for practical trainings which cannot provide for better materials to cover cost of practical training.

Recommendation

- Training curriculums need to be upgraded and made appropriate to the industry needs through enhanced collaboration between responsible authorities and industry
 - Short term courses with more focus on practical training may be introduced by the training institutes
 - Courses for junior supervisory staff may be planned and introduced to develop technical competence in critical operations
 - An effective student enrollment policy in consultation with the industry may be planned, based on success stories in other clusters.
 - A policy of minimum period of service by the trainee may be developed by the association for enterprises that are willing to participate in training programs, so as to ensure retention
 - The jobless football stitchers may also be trained to engage in the leather industry as they already have the basic skills and can become proficient in a short time.
 - Assist companies to improve working conditions and benefits, women friendly environment, anti-harassment policies etc. For example, it is preferable to have female supervisors or aged male supervisors for the women only production floors to encourage more female employment
- Support associations and consortiums between key industry players to foster partnerships with training institutes

Key Constraint 4: Limited Presence of Support Industry & Technology

Explanation

- Negligent investment in the support industry in footwear sector has resulted in the industry importing ancillary items, increasing both lead time and cost.
 - The import lowers profit margins as well as the efficiency.
 - Use of technology is very limited, most of the firms are still working on manual operations due to lack of resources to automate processes and train labor
 - Very few companies are using laser cutting machines and direct injection technology.
- Limited awareness about and access to best practices, in terms of technology and production techniques

Recommendation

- Facilitate investment in local companies to invest in ancillary items for example, through feasibility studies etc.
- Existing local industry in plastic lasts and moulds, may be supported to improve their product quality and operations
- Technology and business service providers may be capacitated and collaborated with joint programs to provide input & services for the footwear sector

Key Constraint 5:

Lack of Third Party Compliance Support

Explanation

- The GSP Plus status conferred on Pakistan waives off all duties and taxes for the European market for ten years, subject to meeting certification requirements. This includes REACH (Registration, Evaluation, Authorization & Restriction of chemicals)
 - Some laboratories have been built by the public sector including PCSIR and CPC. However, these labs lack international accreditation
 - Private companies including TTI, SGS and Intertek offer limited testing services. Most of the tests are conducted abroad, increasing the cost and time.
 - For the tanneries, Leather Working Group (LWG) certification is not only expensive and become mandatory by 2020, the companies are reporting that the trainers for LWG are reluctant to come to Pakistan due to the negative image.
 - LWG certification will affect the leather industry and its buyers significantly, especially those in exports
- Currently, no third parties are located which are offering certification of compliance of environmental and socially responsible business (ESRB) conditions.

Recommendation

- Assist the private and public labs to expand their operations to include a wider range of tests as per international requirements i.e. EU's REACH
- Capacity building of labs in acquiring accreditation, to reduce cost and lead time

Key Constraint 6:

Rules & Regulations

Explanation

- Lack of dedicated policy/ strategy regarding the footwear sector
 - Political instability and law and order situations causes insecurity amongst the manufacturers and buyers alike. Furthermore, it causes delays in meeting deadlines which adversely affects customer relationships
 - The industry is either not part of policy making or is not given the whole picture. This results in formulation of policies which are not beneficial to the industry
 - The industry is critical of taxes and duty drawback structure by the government. Over the years, the duty drawback has amounted to significant sums of money
- The informal sector is able to bypass laws and produce footwear at lesser cost, adversely affecting the formal counterparts

Recommendation

- Facilitate public private dialogue towards sector-specific policies and strategies, through for example, roundtable discussions, commissioning in depth studies to identify issues, the resolution of which can be formulated jointly etc
- Support associations in lobbying the government for a change in duties and tax structure
- Government should actively consult the industry in decision making process regarding policies. The process must be transparent, so all sides can be considered
- PFMA in collaboration with the industry is working towards building a Center of Excellence for Footwear. The Government may assist the industry in providing subsidized land or other facilities as this will be very beneficial for the entire industry.



5. SNAPSHOT OF FIELD VISITS

Sr No.	Company Name	Type	Major Products
Principal Firms			
01	Sartaj Shoes	SME	Formal Shoes, Casual Shoes, School Shoes, Boat Shoes, Safety Shoes
02	Elelegant Shoes	Large	Formal Shoes, Semi-Formal Shoes, Casual Shoes, Boat Shoes
03	Starlet Pvt Limited	Large	Formal Shoes, Casual Shoes, Joggers
04	Xarasoft Pvt Limited	Large	Formal Shoes, Casual Shoes, Sandals, Joggers
05	Deluxe	Large	Formal Shoes, Casual Shoes, Sandals, Slippers
06	Askari Shoes	SME	Formal Shoes, Casual Shoes, Joggers, Army Shoes
07	Simba Enterprises	SME	All Ladies Shoes Variety (Synthetic)
08	Footpetals	Large	Slippers, Chappals, Formal Shoes, Casual Shoes and Safety Shoes
09	Bani Shoes	Micro	All Ladies Shoes Variety (Synthetic)
10	Creative Shoes	SME	Formal Shoes, Casual Shoes, School Shoes, Boat Shoes, Safety Shoes
11	Stylo Shoes	Large	All Ladies Shoes Variety (Synthetic)
12	Shafi Pvt Ltd	Large	Formal Shoes, Semi-Formal Shoes, Casual Shoes, Boat Shoes
13	EPCOT Shoes	Large	Formal Shoes, Semi-Formal Shoes, Casual Shoes, Boat Shoes
14	Service Industries	Large	All Ladies, Gents and Kids Variety
15	Relaxo Footwear	Large	All Ladies, Gents and Kids Variety
16	Bata Pakistan	Large	All Ladies, Gents and Kids Variety
17	Aasia Sharif Leather Manufacturing	SME	Mens Formal Shoes
18	Bawa Shoes	Micro	All Ladies Shoes Variety (Synthetic)
19	Aqib Shoes	Micro	All Ladies Shoes Variety (Synthetic)



Sr No.	Company Name	Type	Major Products
Principal Firms			
20	Behreen Leather Enterprises	SME	Leather Belts, Vallets and Key Chains
21	Fayva Shoes	SME	Formal Shoes, Semi-Formal Shoes, Casual Shoes
22	Five Star Marketing	SME	Army Shoes
23	IFMI Footwear	SME	School Shoes & All Ladies Variety (Synthetic)
24	Metro Apparel	SME	All Ladies Shoes Variety (Synthetic)
25	Gift Shoes	SME	School Shoes & All Ladies Variety (Synthetic)
26	HAPPY FEET	SME	All Ladies Shoes Variety (Synthetic)
27	Shoe Bar	SME	All Ladies Shoes Variety (Synthetic)
28	Firhaj Footwear	Large	Formal Shoes, Semi-Formal Shoes, Casual Shoes
29			Formal Shoes, Casual Shoes, School Shoes, Boat Shoes, Safety Shoes
BDSs/Support Institution/ Donor Agencies			
29	Intra core	SME	Shoe Lasts
30	Trade Development Authority of Pakistan	BDSs/Support Institution	Organizing international trade events and HR Development Programs
31	Pakistan Footwear Manufacturers Association	BDSs/Support Institution	Representative body of footwear manufacturers in Pakistan with around 115 members
32	Gujranwala Institute of Leather Technology	BDSs/Support Institution	Educational institute offering courses, diplomas and 3 years dedicated study program in shoe designing
33	Punjab Skills Development Fund	BDSs/Support Institution	Funding agency for various skills sector programs through implementing agencies and educational institutes to cater industrial needs for skilled labour
34	Punjab Vocational Training Council	BDSs/Support Institution	Vocational training institute providing short courses and diplomas in various fields now planning to start a dedicated course for footwear sector (cut to pack)
35	Pakistan Institute of Fashion & Design	BDSs/Support Institution	Federally chartered degree awarding institute offering a bachelor's degree in footwear designing
36	Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ)	BDSs/Support Institution	Assisting in technical education policy framework to cater needs of industry

6. List of abbreviations:-

PFMA	Pakistan Footwear Manufacturers Association
PCSIR	Pakistan Council of Scientific & Industrial Research
PIFD	Pakistan Institute of Fashion & Design
TDAP	Trade Development Authority of Pakistan
SMED	A Small & Medium Enterprise Development Authority
MoC	Ministry of Commerce
MDF	Market Development Fund
GILT	Government Institute of Leather Technology
CAD/CAM	Computer-Aided Design and Computer-Aided Manufacturing
MI&P	Ministry of Industries & Production
TEVTA	Technical Education & Vocational Training Authority
PVTC	Punjab Vocational Training Council
LCCI	Lahore Chamber of Commerce & Industry
PSIC	Punjab Small Industries Corporation
SME	Small & Medium Enterprise
SBP	State Bank of Pakistan
EU	European Union
LDC	Least Developed Country
IC&ID	Industries Commerce & Investment Department
CDI	Cluster Development Initiative
APICCAPS	Portuguese Footwear, Components, Leather Goods Manufacturers' Association
BSCI	Business Social Compliance Initiative
ISO	International Standards Organization
UNIDO	United Nations Industrial Development Organization
GIZ	Deutsche Gesellschaft für Internationale Zusammenarbeit
PBIT	Punjab Board of Investment & Trade



7. References:

1. World Footwear Year Book-2012, 2016 by Portuguese Shoes
2. ADB. 2013. Key Indicators: Asia's Economic Transformation: Where to, How, and How Fast? Manila, and R. Amjad. 2013.
3. Economic Management under Musharraf and Coalition Rule: Key Lessons for Sustainable Growth, in R. Amjad and S. Burki, eds. 2013.
4. Pakistan: Moving the Economy Forward. Lahore: Lahore School of Economics.
5. ITC-Trade Map
6. Ministry of Finance, Economic Survey of Pakistan, Islamabad.
7. <http://stat.wto.org/CountryProfile/WSDBCountryPFHome.aspx>
8. H. Ahmed et al. 2013. Exports: Lessons from the Past and the Way Forward in R. Amjad and S. Burki, eds.
9. Planning Commission. 2011. Pakistan: Framework for Economic Growth. Islamabad.
10. <http://www.bilaterals.org/?-Pakistan>
11. World Bank. 2014. World Development Indicators. <http://data.worldbank.org/data-catalog/world-development-indicators> (accessed 24 December 2014).
12. <https://www.adb.org/sites/default/files/linked-documents/cps-pak-2015-2019-pa.pdf>
13. British Council, Pakistan: The Next Generation. Islamabad, 2009 United Nations Development Programme. 2014. Human Development Report, Sustaining Human Progress: Reducing Vulnerabilities and Building Resilience. New York.
14. Pakistan Bureau of Statistics, Pakistan Employment Trends 2013. <http://www.pbs.gov.pk/content/pakistanemployment-trends-2013>.
15. Aga Khan University, Pakistan Medical Research Council, Pakistan Ministry of Health. 2011. National Nutrition Survey Report 2011. Karachi.
16. United Nations Development Programme. 2012. Pakistan MDG Status. <http://www.pk.undp.org/content/pakistan/en/home/library/mdg/infographic---pakistan-mdgs-status-2012.html>.
17. Guidance - Doing business in Pakistan: Pakistan trade and export guide, Department for International Trade of the government of UK, <https://www.gov.uk/government/publications/exporting-to-pakistan/doing-business-in-pakistan-pakistan-trade-and-export-guide>
18. Pakistan in the 21st Century Vision 2030
19. Climate Change Vulnerability Index (2010). <http://maplecroft.com/about/news/ccvi.html>.
20. Leather Sector Analysis By Osman Bin Saif (PITAD)
21. Diagnostic Study on Leather Goods, Sialkot (PSIC) S. M. ATHER RAZA ZAIDI/TAHIR HAFEEZ
22. FOOTWEAR CONSUMER 2030 by Portuguese Shoes Incorporating Global Trends to Foresight Footwear Market
23. Footwear Sector Skills by PSDF
24. CBI Market Survey- Footwear Market in EU
25. Punjab Small Industries Corporation (PSIC) rural enterprise study Syed Turab Hussain Usman Khan Syed M. Hasan March 2017 F-37322-PAK-1
26. Punjab Small Industries Corporation (PSIC) Diagnostic study of industrial and handicrafts clusters in Punjab
27. Inclusive Sector Growth Strategy – Leather Market Development Facility – Pakistan
28. Brazil: An Application of Porter's Diamond and Attractiveness Analysis For French Fdi
29. OECD Due Diligence Guidance for Responsible Business Conduct Responsible Supply Chains in the Garment and Footwear Sector
30. Merkato Leather Footwear Cluster – UNIDO Cluster Development Project in Ethiopia
31. THE UNIDO APPROACH TO Business Investment Technology Services Key Principles and Project Experiences for Inclusive Growth Cluster Development