

April-2014



EMERGING TRENDS: INDIAN LEATHER INDUSTRY

Indian Leather Industry poised to grow manifolds

ONICRA
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EXECUTIVE SUMMARY

The Indian leather industry today has established itself as a prominent industry both in international as well as in the domestic market. Apart from being the ninth largest exporter of leather and leather products it is also the second largest producer of footwear and leather garments, with an annual revenue of USD 8,500 million for 2011-12 with exports of USD 4,868.71 million. The sector itself employs more than 2.5 million people and is one of the top foreign currency earners in India. Abundant raw material, skilled work force, compliance with environmental standards and growth shown by the associated industries has helped the sector to grow manifold.

The units are generally spread across large, medium, small and household units with the small and household units contributing almost 80% of the production. Large and medium units are generally tanneries or either big companies which are involved in manufacturing of footwear.

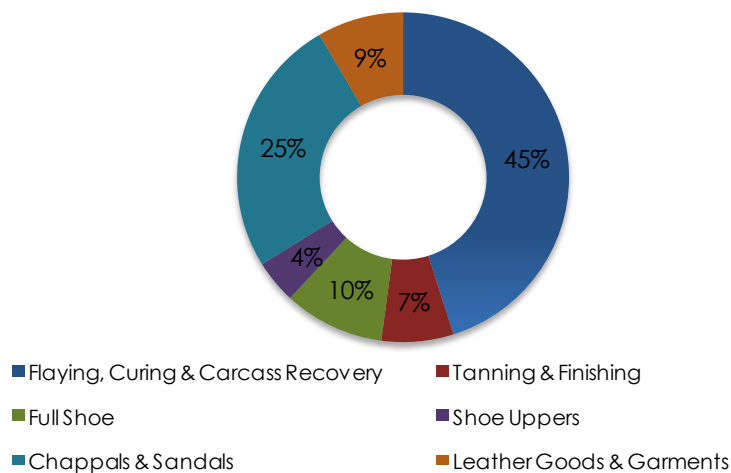
With the majority of the manufacturing units belonging to the unorganised sector the industry faces many challenges. Timely availability of raw materials, high labour cost, lack of product innovation and lack of presence in global fashion market are few of them.

To support the sector the Government of India has taken several initiatives from de-licensing the sector, allowing 100% FDI and duty free imports, providing funding assistance to the manufacturing units, assisting in promotion of the industry through industrial parks to implementation of various industrial development programmes. Keeping in view the historical performance, strength of the sector and support from the government, the Indian leather industry is poised to grow manifold.

STRUCTURE AND SIGNIFICANCE OF LEATHER INDUSTRY IN INDIA

The Indian leather industry holds a significant position in the Indian economy in terms of high potential shown for employment, growth and exports. It is estimated that the industry employs around 2.5 million work force directly or indirectly and 30% of the workforce are women. The skilled and semi-skilled workers constitute nearly 50% of the total work force. The graph below shows the percentage wise workforce employed in different segments of the industry:

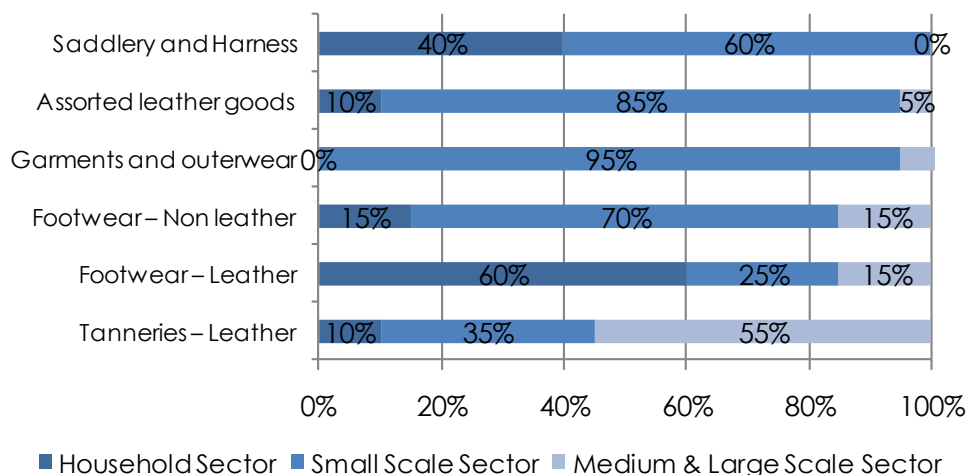
Workforce Employed in Different Segments (in %)



It is amongst one of the industries in which India has abundance of raw material (India is endowed with 21% of world cattle & buffalo and 11% of the world goat & sheep population), adequately skilled manpower and technology, apart from compliance with all international environmental standards and support from associated industries. Since the last three decade the Indian leather industry has undergone a significant structural change, from being merely an exporter for raw materials during 1960's to a preferred supplier of value added products, the industry is now one of the top ten foreign exchange earners for the country.

The sector comprises of tanneries (where hide and skins are transformed into leather) and manufacturing units (where leather footwear, garments and outerwear, and assorted leather goods are manufactured). These production facilities are spread over organized and unorganized (mostly family owned) units/ production centers with the unorganized units dominating almost 80% of the total production. The production base of leather and leather products in the country is given in the table below:

Production Base of Leather and Leather Products



Source: IICCI – Short Market Overviews

It should be noted that the unorganized units generally cater to the domestic market, while the organized units cater to both domestic and international market. Further the sector can be classified based upon its production ranges. The estimated production capacity of leather products for 2011-12 is shown in table below:

Item	Capacity
Leather Footwear	909 Million Pairs
Leather Shoe Uppers	100 Million Pairs
Non – Leather Footwear	1056 Million Pairs
Leather Garments	16 Million Pieces
Leather Goods	63 Million Pieces
Industrial Gloves	52 Million Pairs
Saddlery & Harness	12.50 Million Pieces

Source: Council for Leather Exports

The major production centers for leather and leather products are located at Tamil Nadu (Chennai, Ambathur, Ranipet, Vaniyambadi, Tiruchirappalli, Dindigul) followed by West Bengal (Kolkata), Uttar Pradesh (Kanpur, Agra, Noida). Maharashtra (Mumbai) has the lowest number of manufacturing units. The table below provides the Top 8 states in terms of manufacturing units:

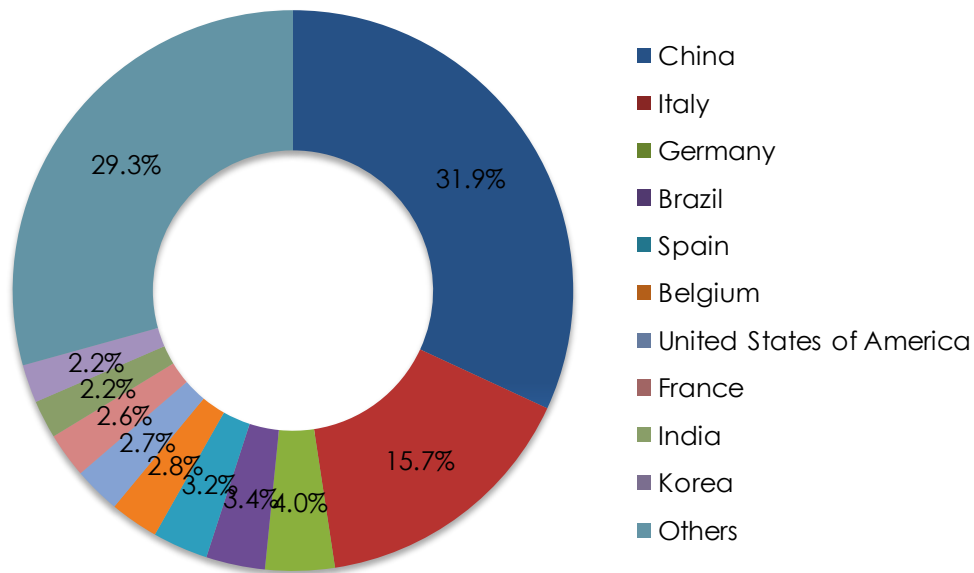
State	Clusters	No. of manufacturing units
Tamil Nadu	Chennai, Ambathur, Ranipet, Vaniyambadi, Tiruchirappalli, Dindigul	758
West Bengal	Kolkata	666
Uttar Pradesh	Kanpur, Agra, Noida	290
Chandigarh, Punjab & Haryana	Chandigarh, Jalandhar, Ambala, Gurgaon, Panchkula, Karnal	171
Delhi	Delhi	155
Andhra Pradesh	Hyderabad	138
Karnataka	Bengaluru	88
Maharashtra	Mumbai	68

Source: Council for Leather Exports

INDIA IS THE NINTH LARGEST EXPORTER OF LEATHER & LEATHER PRODUCTS

The global trade in leather and leather products has been increasing over the years from a mere USD 4 billion in 1972 to USD 221.3 billion¹ in 2012. Although, the exports of Indian leather and leather products have grown manifold during the past decades, India's share in global trade is only around 2.2% (occupying 9th position) of the total leather exports².

Composition of World Export Average:2001-2005



However, prospect of Indian leather industry seems to be bright in near future. The country has emerged as a credible and reliable supplier of leather and leather products. As of today several international brands import leather and leather products from India. The table below furnishes the name of the brands (both Indian & International) that sources leather and leather products from India:

¹ The data has been extrapolated based on India's share of 2.2% to global exports

² Source: Council for Leather Exports, ITC

Footwear	Leather Garments	Leather Goods / Accessories
<p>Acme, Ann Taylor, Bally, Charter Club, Clarks, Coach, Colehann, Daniel Hector, Deichmann, DKNY, Double H, Ecco, Elefanten, Etienneaigner, Florsheim, Gabor, Geoffrey Beene, Guess, Harrods, Hasley, Hush Puppies, Kenneth Cole, Liz Claiborne, Marks & Spencer, Nautica, Next, Nike, Cole Haan, Nunn Bush, Pierre Cardin, Reebok, Rockport, Salamander, Stacy Adams, Tommy Hilfiger, Tony Lama, Versace, Yves St. Laurent, Zara, Johnston & Murphy, Docksteps, Timberland, Armani, Geox, Diesel, Ted Baker, Lacoste, Kickers, Calvin Klein, Sioux, Brasher, Zegna, Massimu Dutti, Buggatti, Lloyd, Christian Dier, Salamander, Camper, Bata, Espirit, French Connection, Legero, Mercedes, H & M and many more famous brands</p>	<p>Armani, Zegna, Abercrombie & Fitch, Marco Polo, Mango, Colehaan, Andre, Maarc, Guess Pierre Cardin, Tommy, Hilfiger, Versace, DKNY, Liz Claiborne, Ann Taylor, Nautica, Kenneth Cole, Charter Club, Daniel Hector</p>	<p>Coach, Liz Claiborne, Harrods, Yves St, Laurent, Tommy Hilfiger, Etienne Aigner, Geoffrey Beene, Marks & Spencer, Guess, Next, Pierre Cardin, Prada, GAP, Levis, H & M, British Home, Stores, Banana Republic, Furla, American Eagle, Outfitters, Bracciliani, Walmart etc.</p>

MNC Brands Sold in India

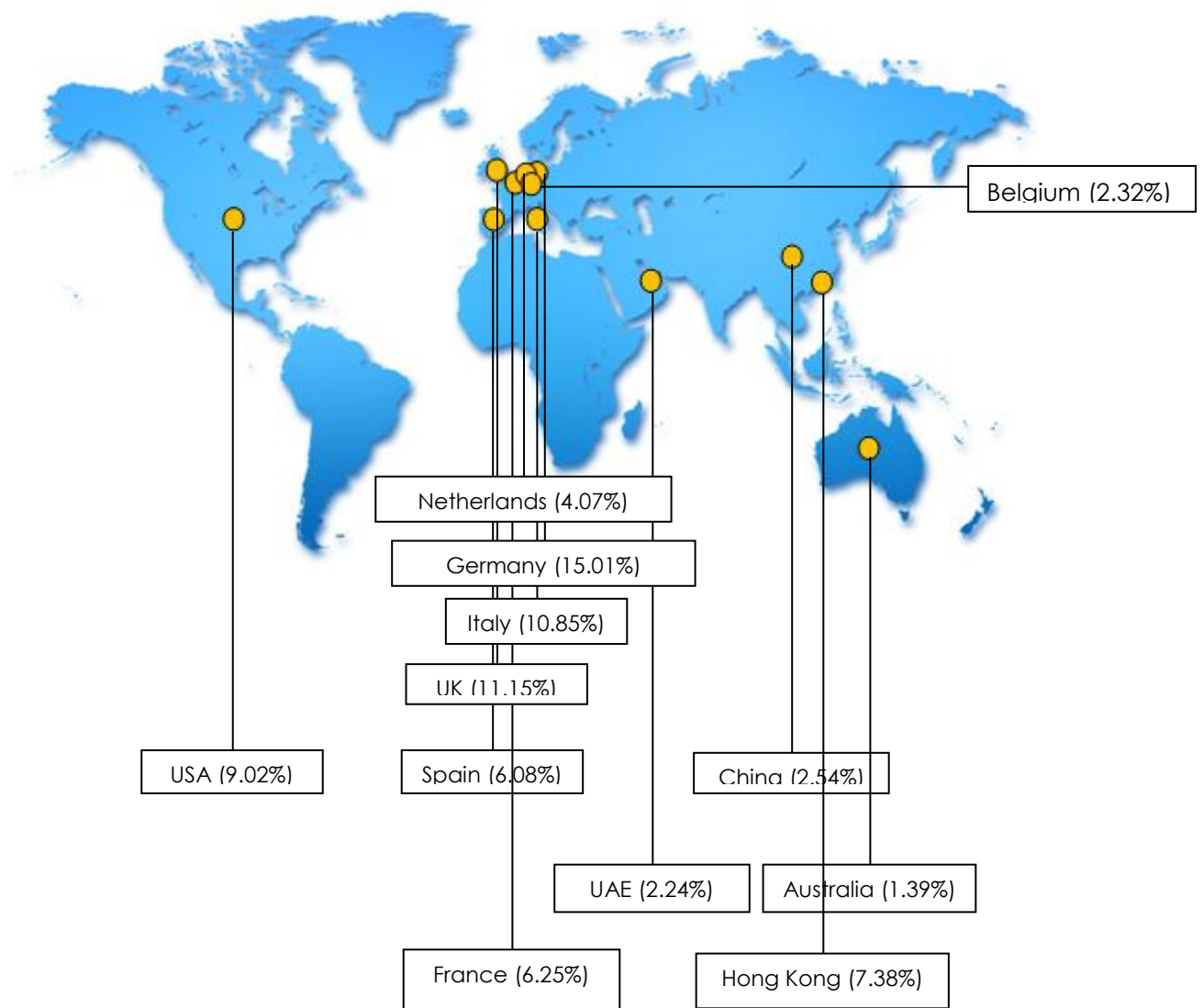
Aldo, Bally, Clarks, Ecco, Florshiem, Ferragammo, Hush Puppies, Lee cooper, Lloyd, Marks & Spencer, Nike, Nine West, New Balance, Reebok, Rockport, Stacy Adams, Tod's, Geox , Louis Vuitton

Indian Brands Sold in India

Red Tape, Bata, Liberty, Khadims, Lakhani, Metro, Action

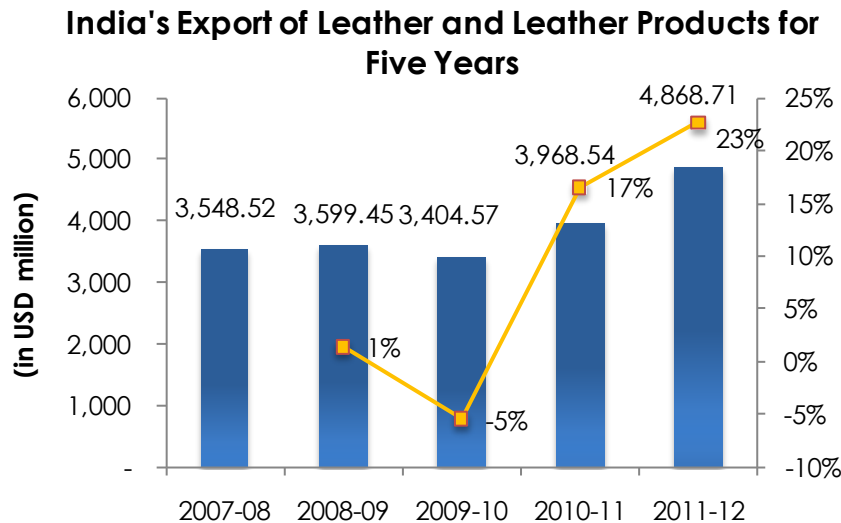
Source: Incredible India: Leather Industry

The major markets for Indian leather and leather products are European Union (EU), United States of America (USA), Hong Kong, United Arab Emirates (UAE) and Australia among others. European Union itself consumes around 58.78% of the total Indian leather exports. The map below shows the key export destination of India for leather and leather products:



EMERGING TRENDS IN INDIAN LEATHER INDUSTRY

Export of leather and leather products for the period 2011-12 touched USD 4,868.71 million as against the performance of USD 3,968.54 million for the period 2010-11, recording a significant growth of 23%.



Source: Council for Leather Exports

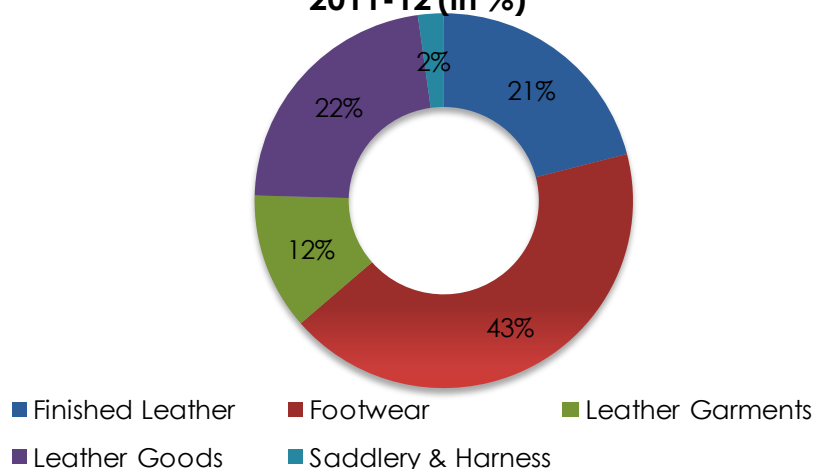
The Footwear Segment Driving the Growth

India is the second largest producer of footwear after China, accounting for 13% of overall global footwear production of 16 billion pairs. India produces 2065 million pairs of different categories of footwear which includes leather footwear of 909 million pairs, leather shoe uppers of 100 million pairs and non-leather footwear of 1056 million pairs. India exports about 115 million pairs. Hence, nearly 95% of its production goes to meet its own domestic demand³.

However, if we take into consideration the leather and leather products export of India; Indian footwear sector has a significant position in the leather industry. Out of the total exports of USD 4,868.71 million 42.67% constitutes of footwear followed by leather goods, which constitutes 22.35% and is far below the footwear segment. The chart below shows the percentage wise contribution of each product segment in India's export of leather and leather products for 2011-12:

³ <http://www.leatherindia.org/products/footwear-23-4-13.asp>

Contribution of Each Product Segment for 2011-12 (in %)



Source: Council for Leather Exports

Significant Growth Trajectory for Export of Leather Garments

In terms of growth rate, leather garment sector showed a significant growth of 35% from 2010-11 to 2011-12. The table below shows India's export of leather and leather products for five years:

Products	2007-08	2008-09	2009-10	2010-11	2011-12
Finished Leather (in USD million)	807.19	673.37	627.95	841.13	1,023.21
Growth (in %)	NA	-17%	-7%	34%	22%
Footwear (in USD million)	1,489.35	1,534.32	1,507.59	1,758.67	2,077.27
Growth (in %)	NA	3%	-2%	17%	18%
Leather Garments (in USD million)	345.34	426.17	428.62	425.04	572.54
Growth (in %)	NA	23%	1%	-1%	35%
leather Goods (in USD million)	800.46	873.44	757.02	855.78	1,088.09
Growth (in %)	NA	9%	-13%	13%	27%
Saddlery & Harness (in USD million)	106.18	92.15	83.39	87.92	107.60
Growth (in %)	NA	-13%	-10%	5%	22%

Source: Council for Leather Exports

GOVERNMENT POLICIES IN SUPPORT OF THE LEATHER INDUSTRY

The Government of India (GoI) has taken several initiatives to support the growth of the domestic leather industry. Given below are some of the policy initiatives that the GoI has taken to improve the prospects and to facilitate speedy expansion of the leather industry:

Government policies

The leather industry is de-licensed and de-reserved

100% Foreign Direct Investment (FDI) and Joint Ventures (JVs) are permitted through the automatic route

100% percent repatriation of profit and dividends, if investments are made in convertible foreign currency. Only declaration to this effect is required to be made to the Reserve Bank of India

Promotion of industrial parks (one each in Andhra Pradesh, West Bengal and two in Tamil Nadu)

Funding support for modernizing manufacturing facilities

Funding support for establishing design studios

Duty free import of raw materials (namely raw skins, hides, semi finished leather and finished leather) and of embellishments and parts under specific scheme

Concessional duty on import of specified machinery for use in leather sector

Duty neutralization / remission scheme

Source: The Indo-Italian Chamber of Commerce & Industry

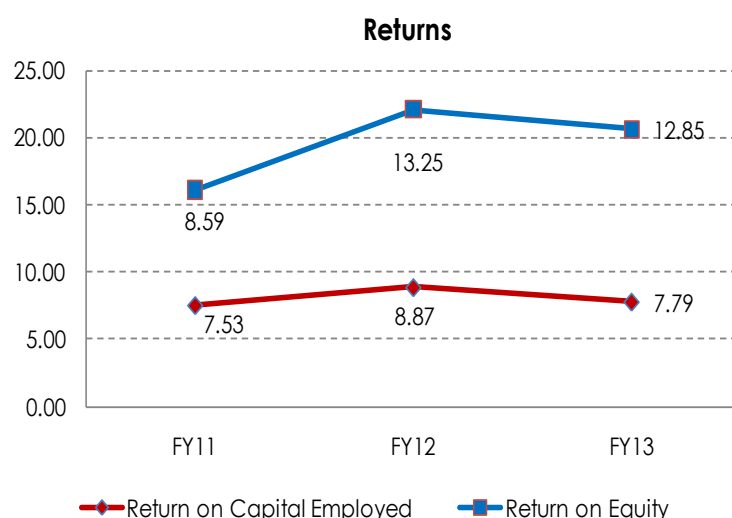
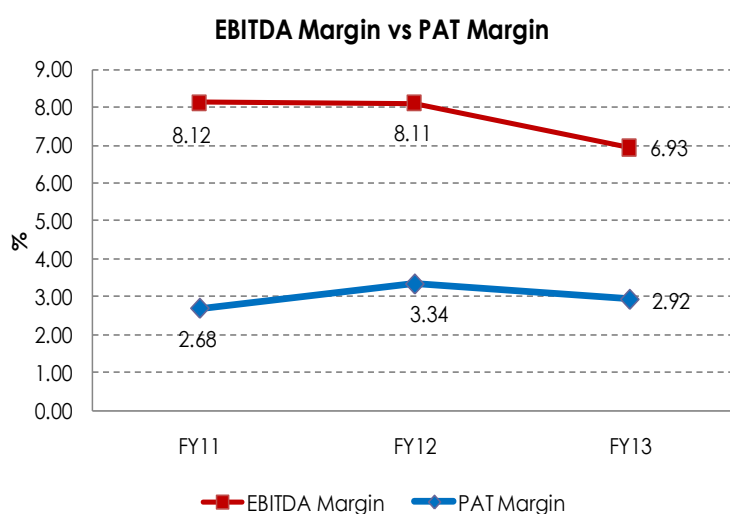
Apart from the above, to support the growth of the sector, Indian Leather Development Programme (ILDP) was started by the Department of Industrial Policy & Promotion (DIPP) in the 11th five year plan (2007-2012). The total outlay for the programme was Rs. 1,25,129 Lacs for the period. However, in the 12th five year plan (2012-2017) the outlay has been increased to Rs. 3,60,000 Lacs. The IDLP was initiated to support the industry in terms of technology upgradation, innovation, resolving environmental issues, human resource development as well as to support artisans in technical skill development and to establish institutional facilities.

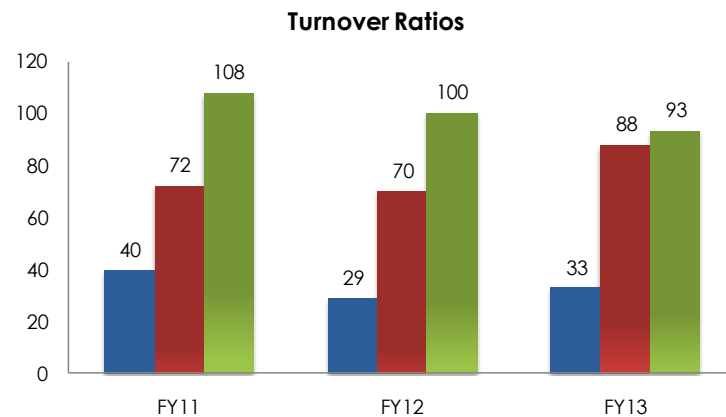
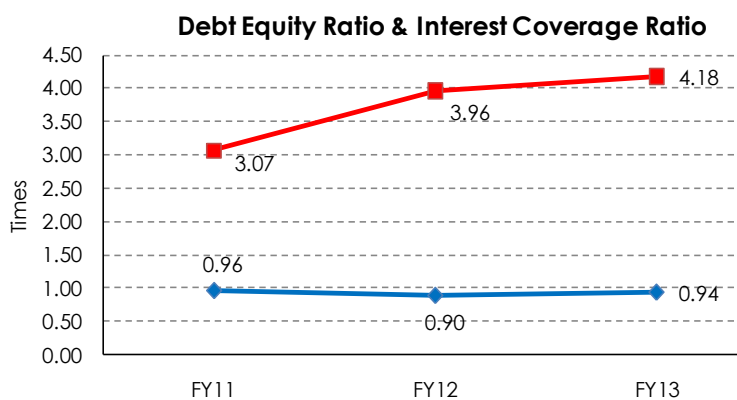
ONICRA'S OUTLOOK ON SMEs IN LEATHER INDUSTRY

The Indian leather industry has a significant share in the overall exports of the country. SMEs are the most important segment of this industry and close to 80 per cent of the business of this industry comes from them. India is the second largest producer of footwear and leather garments in the world. Apart from the exports, India's domestic market for leather and footwear products is also very lucrative.

Financial Performance

A financial analysis of SME units engaged in manufacturing of leather and leather products was undertaken to understand the dynamics of the SMEs in leather & leather products industry. A sample set of 30 units was chosen from the entities that have been rated by Onicra over the period April 2013 to March 2014. The results of the financial analysis have been detailed below.





—●— Adj. Gearing (Total Debt/Equity) —■— Interest Coverage Ratio

■ Debtor Days ■ Creditor Days ■ Inventory Days

Growth in revenue remained strong; however, margins remained low for all the years under study –

The sample SME units engaged in manufacturing of leather and leather products posted a growth in revenue. However, the margins remained low on account of high cost of skilled labour and electricity. Apart from this due to intense competition, leather and leather product manufacturing units are unable to pass on the rising cost of raw materials to the market thereby increasing pressure on the margins.

Return generated on the capital employed is lower as compared to the returns generated on the equity –

Return on capital employed has remained moderate during the period under study. However return on equity has been higher. The EBITDA and the net profit of the SME units have increased at a slower pace than the increase in the capital employed and equity respectively. This signifies lower efficiency rate of the capital employed and equity

Low dependence on borrowed funds and satisfactory interest coverage ratio – As can be seen in the graph above, the dependence on external borrowings has been low during the period under study. Also due to moderate level of profitability achieved by the companies operating in this industry, the interest coverage ratio has remained strong.

The cash conversion cycle of the SME units has been satisfactory – The units engaged in the manufacturing of leather products are able to re-cycle their working capital faster which can be seen by the operating cycle of 38 days.

CHALLENGES THAT ONICRA FORESEES FOR SMEs IN LEATHER INDUSTRY

- A major proportion (around 80%) of the industry is unorganized and has limited scope of mobilizing funds through private equity and bank loans
- Although India has abundant supply raw material for leather and leather products, timely availability of raw materials remains a constraint.
- High labour charges for skilled workforce
- Lack of strong presence in the global fashion market
- Unawareness of international quality standards by many players
- Lack of product innovation: most of the units work on sub-contract basis where all the design and other specification of the product are provided by the buyer

OUTLOOK

India is the ninth largest exporter of leather & leather products and accounts for 2.2% of the global leather and leather products export. The Indian leather industry is expected to grow manifold thereby creating large scale employment and high foreign exchange revenue. Apart from this, the high growth in domestic market due to growing demand of footwear and leather articles will further accelerate the growth. Accordingly, the government has also taken several initiatives and implemented various industrial development programmes along with export promotional activities. The Mega Leather Cluster scheme under IDLP is one such scheme which is undertaken by the government to help the sector in infrastructure development, human resource development and research. Added to this are the inherent strength of the industry like, availability of adequate raw material, skilled human resource, compliance of international environmental standards and growth shown by the associated industries which will further support the sector.

However, due to highly unorganised nature of the industry, availability of financing facility remains a major challenge. Apart from this timely availability of raw material, high cost of skilled human resource and lack of product innovation still remains an issue. Given the contribution shown by the SMEs in leather industry towards employment generation and foreign exchange earnings the government should take further initiatives and develop policies which particularly focus on the growth of SMEs in leather industry.

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