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INDONESIA COMPETITIVENESS PROGRAM

FOOTWEAR AND LEATHER INDUSTRY COMPETITIVENESS REPORT

FOOTWEAR AND LEATHER INDUSTRY OVERVIEW

JULY 2007 – STTA JAMES PARCHMAN

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DISCLAIMER

The author's views expressed in this publication do not necessarily reflect the views of the United States Agency for International Development or the United States Government.

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1. OVERVIEW OF THE REPORT

The purpose of the report was to assist SENADA in developing an understanding of the needs and opportunities for increasing competitiveness of the domestic Indonesian footwear/leather industry. The thirty-day LOE included meetings with footwear and leather companies, industry trade associations, and related research and training institutions throughout Indonesia. Recaps of the visits are included in Annex I – IV. The trip culminated with a SENADA sponsored Dialog Roundtable, *How to Increase the Competitiveness of the Indonesian Footwear Industry*, with participation by members of each of the major groups above plus the relevant Indonesian Government Ministries and Agencies.

Throughout the report the consultant provided the SENADA team written briefing on topics important to the footwear / leather industry and various resources that would be important for the project. These are not included in the report due to length but the topics are listed in Annex VI. Likewise, the consultant's remarks at the roundtable are also not included in this report but were provided to the SENADA team and participants of the roundtable. Topics discussed during the event are listed in Annex V.

2. CONCLUSIONS AND RECOMMENDATIONS

2.1. CONCLUSIONS

SENADA has a great opportunity to provide meaningful and needed assistance to the Indonesian footwear/leather industry. There is every reason to believe that a knowledgeable and professional approach can greatly increase the competitiveness of the industry, provide substantial opportunities for individual companies, increase the quantity and quality of industry employment, and be a beneficial use of the USAID funds.

The major shortcoming of the industry and the individual companies is in export marketing/promotion. The industry has done little in promoting the opportunities of Indonesia as a footwear producing country, even though the sector ranks high in employment and foreign currency earnings. Successful foreign footwear production companies operating in Indonesia are more from a spillover from other Asian countries or because of an interest in using the supply of quality raw leather for a combined tanning/footwear production process (ECCO) than from any proactive recruitment by Indonesia.

Noncompetitive costs in Indonesia are a result of poor productivity, slow movement of materials/finished goods due to traffic/port/customs problems, and lack of year-round utilization of full production capacity. Factory labor rates in Indonesia average lower than in China, India, or Vietnam. Foreign-owned footwear/leather production companies operating in Indonesia pay higher wages and offer better working conditions and benefits than Indonesian companies, while competing globally by addressing the above issues. SENADA does not have the technical expertise to identify areas of poor production productivity or provide skill training for productivity improvement. The opportunity, developed during this trip, to cooperate with UNIDO will allow SENADA to concentrate on Industry Value Chain activities with a market orientation, while the focus of UNIDO would be in its core expertise of technical production assistance in the footwear and leather industry and the training institutions.

APRISINDO is a weak organization, with a small base of member companies, and an even smaller base of companies that have export marketing potential. The organization is politically connected but ineffective in any task except government lobbying activities. SENADA should not assume that the goals or capabilities of this association will be of great benefit in assisting SENADA to achieve its own goals.

The *Directory of Indonesian Leather Tanners* being developed by SENADA is a necessary and helpful product for promoting greater interaction between domestic leather and footwear producers. This product, the efforts at linking domestic raw material suppliers with manufacturers, and educating companies in the export promotion process are valuable steps, and appreciated by the industry.

Indonesian companies have a desire to focus on big markets (Europe, USA) and seek large orders but complain of noncompetitive pricing. The most appropriate markets are those that are closer in proximity including Australia, Japan and UAE, all of which have international footwear exhibitions. Legitimate foreign buyers will visit Indonesia before placing orders and improvement and promotion of the ILF exhibition in Jakarta is an opportunity for them to see a wide variety of Indonesian companies at one time. Success in trade fairs comes through preparation and repeated participation. Companies should not expect an immediate return on their show investment in the first or second attempt.

The Indonesian domestic market offers an excellent and growing opportunity for footwear manufacturers. A few Indonesian companies are taking advantage of this with development of brands, operating their own retail stores, and selling foreign owned hypermarkets operating in Indonesia. Many of the smaller companies should be encouraged to pursue this market and increase their business acumen before becoming heavily focused on exporting. Instances of brand counterfeiting seem lower than in other Asian countries. An exception is widespread counterfeiting of American brand Harley-Davidson on clothing and personal goods.

SENADA has a wide range of product sectors. There are many opportunities to work on tasks crossing several of these sectors. SENADA can make best use of its resources and develop areas of expertise in certain areas that will be important for the industry. Several of these have been suggested throughout the trip (Social Accountability, Logistics, SATRA Assistance, etc.).

2.2. RECOMMENDATIONS

1. **UNIDO assistance.** SENADA should immediately develop for the Indonesian Ministry of Industry a formal request for UNIDO assistance (format and contact provided separately) and expedite its submission.
2. **External promotional efforts.** SENADA should develop a plan for assisting the industry in increasing its export promotion process. This major effort should encompass the current industry activities (GDS participation) and expand those with the development of a promotional/informational web site (example in Annex VII), improvement of the ILS exhibition, additional participation in appropriate international trade shows, and sponsored visits of foreign footwear press and buyers/investors. Press releases and articles in international footwear / leather trade publications will be developed and submitted by the consultant over the upcoming weeks. Additional suggested export promotion tasks which SENADA should implement are included in the task worksheet of May 2007.
3. **Raw material supply issues.** Directory of Indonesian Tanneries should be completed and distributed prior to ILS 2007. Additional suggested raw material supply tasks which SENADA should implement are included in task worksheet of May 2007.
4. **Association assistance and benchmarking.** SENADA should consider an effort to increase the viability of both APRISINDO and APKI by subsidizing the cost of a full time manager for a limited period of time, with the goal of increasing the association's membership base along with its member services to mirror those provided by footwear/leather associations in competing countries.
5. **Social accountability issues.** SENADA should develop the capability to acquaint Indonesian companies with worldwide SA standards (SA 8000, WRAP) and to use these in a positive and proactive manner for marketing purposes. This capability should encompass all of SENADA's product lines.
6. **Industry promotion.** Assist Indonesian Government Agencies in Becoming Effective Resources in Promoting the Footwear/Leather Industry. SENADA should develop a process to educate the responsible Indonesian Ministries as to how they can become promoters of Indonesian products and providers of opportunities such as foreign tender notices and competitive intelligence, beneficial to the industry. This can be accomplished via individual meetings or workshops and should include Ministry of Foreign Affairs and the responsible Export Promotion and Investment Promotion Agencies.
7. **Donor leveraging.** Building upon a cross project approach, SENADA should contact the foreign organizations ICE (Italy) and GTZ (Germany), both involved in footwear/leather related efforts in Indonesia to gain an understanding of their work and develop areas of cooperation.

3. ANNEX I

VISIT REPORT FOR JAKARTA AREA COMPANIES

Overview

Companies in the Jakarta area have been visited throughout the trip. These include both large (4,000 + employees) and SME (200+/-). The Prima operation was the only sport shoe company visited during the trip. Most of the companies were operating at 60-70% of capacity and had at least a 4-month per year slow season when production was even lower. Companies were exceptionally worried about Chinese competition. About half the companies visited were APRISINDO members, some were officers, with the other companies believing the organization was ineffective outside of government lobbying issues.

The consultant visited less than 10 companies in the Jakarta area. He believes there is much more to understand from this center of this footwear industry that would be important in developing foreign buyer interest and partnerships. He would urge the project to develop a more detailed list of companies in the area. However, these comments likely reflect the situation for the domestically operated footwear industry in the area.

- **Product and marketing.** The majority of the companies visited were serving both the domestic and export markets. Domestic companies were using brands to some degree. Companies were using the web mostly as an e-mail communication device. English language capability varied widely but was seen in the companies exporting widely. Much product and design information came from customers, with others searching via the web. Some had exhibited at the previous Jakarta Leather Exhibition. Several of the companies had attended the previous German GDS fair and had some amount of interest and orders. The domestically focused companies had countrywide distribution, usually in specialized markets. Singapore accounted for some sales, but it was not the priority it should be. One firm had good relationships with Bata and was selling their local and foreign operations. There was a large fear of Chinese competition and a seeming inability to compete although Indonesian wage rates are no higher than China and Vietnam.
- **Manufacturing, raw materials, efficiency and quality.** Manufacturing in Jakarta area companies included DMS, cement, Goodyear-welt, stitchdown, and California. Productivity varied greatly and was higher at companies with foreign production management (Korean). Raw materials were domestic and import. Finished quality on all footwear destined for export seemed good, with auditing process in place. Patternmaking skills also seemed to be acquired in house.
- **Industry trade associations.** About half the footwear companies were APRISINDO members, including officers and felt the organization was effective in lobbying issues but lacked resources for other efforts. The non-members felt APRISINDO was not an effective organization or whose interests were slanted toward a special group of companies.
- **Skill training facilities.** All skill training was in house. Some companies such as Prima and Sepatu Mas Idaman had an in house worker training program; other companies said they preferred to hire workers with shoe manufacturing experience.

- **Business Operational Issues.** Several of the companies were clients of SENADA and some, including Mulia, had received several business improvement services offered by the project. The larger Jakarta companies seem to have a good understanding of financial reporting, costing, and seem to be computerized throughout their operation. Companies had at least a 2nd tier of managers and some, but not all seemed to delegate responsibility for functions downward.
- **Social Accountability Issues.** The working conditions in all factories visited were more than adequate and above those observed in any part of Indonesia. The company Mulia was the least worker-friendly but it was not objectionable in most areas and produces only for the domestic market. The Jakarta area companies are likely to receive the most attention from workers rights groups and should be aware of the issue and the legal requirements.
- **Key Points and Opportunities.**
 - The consultant has contacted buyers in Europe and the Mid East concerning a couple of Jakarta companies. He has supplied listings of Mid East tendering agencies to the project for CV Mulia.
 - Jakarta companies are the most open-minded about leather sourcing from multiple (domestic, foreign) suppliers. While it is very unlikely that the project will be able to influence purchasing decisions, a good first step is the leather producer directory providing information and contacts.
 - Simple steps such as introduction of subscription for Italian design magazine (ARS SUTORIA) would be helpful if a method can be so as the product can be shared. Knowledge of current designs is lacking and material and buyer contact information is also contained in each issue.
 - Several companies would greatly benefit from productivity improvement services offered by SATRA. If cross project cooperation with UNIDO becomes possible, productivity improvement should be a key focus. Note that some Jakarta companies are members of SATRA individually but should benefit with lower fees if APRISINDO joins.
 - Companies had little focus on making and selling uppers. Possibly due to productivity but this is a strategy they should be willing to follow until reaching capacity. Making uppers for leather or sport shoes follows the same process. Companies such as Prima are one client suppliers and wish to remain so. This is a dangerous long-term strategy.
 - Companies including Pelita Tomangmas PT have benefited greatly from attendance at foreign trade shows in Germany and Italy. Some companies are selling in Japan and Australia but there is not enough focus on these markets.
 - SENADA should consider the Social Accountability issue area as one to become involved in as the process and regulations can be duplicated across industry sector and across the branch offices. The consultant previously supplied information on SA 8000 and WRAP and the project has the capability in house to research both domestic and international standards and put a program in place. Jakarta companies excel in this area and have nothing to worry about there has likely already been audit requirements at some companies.
 - SENADA should identify more quality footwear companies in the Jakarta area for evaluation and export marketing opportunities. Of the 6 listed, at least 3 are not candidates for foreign buyers for various reasons, leaving too little to draw interest.
 - SENADA should propose to assist all companies who register for the Jakarta Leather Exhibition in the preparation steps that they did previously for GDS. This exhibition, while small, is a key for bringing buyers to Indonesia. In preparing these companies, there is no reason why the project could also not record sales that were achieved at the show as part of its effort. The project should discuss with event organizer options including multi-year pricing and subsidies to increase participation in the event for the purpose of encouraging foreign buyer attendance.

4. ANNEX II

VISIT REPORT FOR BANDUNG AND GARUT AREA COMPANIES (APRIL 17-21, 2007)

Overview

The dozen visits in Bandung / Garut included SENADA client and non-client firms of various size and capability. All companies would be classified in the SME, less than 1,000-employee category. The average company was well less than 100 employees but expanded their capacity through outside contract work via home-based shops. More than half of the companies visited were concentrating (properly) on the domestic market, a couple produced for both markets, with the rest totally focused on exporting. Of the 2 leather tanneries visited, 1 produced only finished leather for the domestic market, while the other produced semi-finished for export. Most companies were quick to describe their problems as “price” or “lack of quality raw material availability.” Most companies were operating at 60-70% of their stated capacity. This varies by season but generally lasts half the year. Exports from this area require shipment via Jakarta. The Indonesian companies seem to work well within their group, the Chinese-Indonesians seem to work well within their group, but there is limited interaction between the groups.

- **Product marketing.** A wide variety of footwear is produced in Bandung. Predominant is finished leather upper casual and semi dress shoes for men and women, although one company was using great creativity and enjoying national success in producing/marketing “Colette” branded synthetic women’s shoes of a ballet style design. Several companies produce small amounts of sport shoes in addition to their core “brown shoe” products. The company Fortuna produces welted (stitched on soles) of the classic British / America style, at a high price level (50 Euro) for export to Europe and Japan. Several of the companies produce footwear, with brands well-known across Indonesia including: Max Baren’s, Colette, BE-BOB and Weidenmann.

The Bandung companies involved in domestic marketing seem to have a good understanding of how to access the market and communicate information on their products. Several of the domestic branded companies had catalogs and product literature, and most had some type of a sales force and/or distribution network. Several of the companies use all forms of media, including television, to advertise their products. Product packaging seemed adequate and several companies differentiated their products by using several brands or brand tags. Many of the companies had their own stores; some with multiple locations across Indonesia. The company producing the Donatello brand, whose factory is basically adequate, also owns several retail stores. The retail store visited proved to display a very impressive presentation of products, some purchased outside but produced under the Donatello brand. Another small company currently is a subcontractor for BATA, which makes up 90% of its business, and had just received a large order (6,000 pair). Likely outside production will be necessary to complete.

Most of the companies visited stated they had and used e-mail for communications and 1 firm had an operating web site and retail storefront. A couple of the companies that focus on exports seemed to have a fair to good amount of English language capability. Most product and design information came from customers, with others searching via the web. A small number had exhibited at the previous Jakarta Leather Exhibition. Several of the companies had attended the previous German GDS fair and had some amount of interest and orders. Several were selling in Japan, Australia, Singapore, and New Zealand, and Dubai UAE.

As in Surabaya, there is little to no outward industry specific export promotion efforts being carried out by industry group or government agency and the only previous assistance has been the GDS (German) trade show subsidy.

- **Manufacturing, raw materials, efficiency and quality.** With the exception of Fortuna, which imports most of their leather from Europe, the remainder of the companies manufacture footwear using locally produced finished leather or imported synthetic materials. This is due to price, quantity requirements, difficulty and lack of knowledge of the import process, and most likely financial reasons. Other foreign made footwear materials and findings are procured locally as needed, at costs higher than direct import. The 3 Chinese-Indo companies were directly importing most materials needed in their footwear production (mostly synthetic) using 20' and 40' containers of assorted materials. They report large savings, ease of purchase of any component, and speedy transport to Indonesia, but major problems in customs clearance (sometimes lasting months). Companies claim that domestic leather producers can respond to their needs in 3 weeks time for most leathers. The Garut leather tanneries confirm this but this is likely the case only for normal leathers. Garut leather tanners prefer to use the splits from hides for other products including edible fried skins, as they say they can make higher profits than is possible from the split leather.

Manufacturing in all factories except Fortuna was by some version of the cement process. Productivity seemed about the same level in all companies and equipment varied with the product but was older tech and more Chinese than European. Some Italian equipment was observed, that was inoperative due to no local service or parts availability. Finished quality on all footwear destined for export seemed good, with auditing process in place. Efficiency to get the quality seemed low but at about normal Indonesian pace. Factories with more male workers had a slower pace.

- **Industry trade associations.** The leather companies visited were members of APKI and a regional office was present in Garut. Its services were limited but the owner of a Garut tanner is Vice-Chairman of APKI. APRISINDO had only recently opened a branch in Bandung and the local official had a good knowledge of the companies in the area but had only recently begun recruiting members and no services except social and government lobbying were taking place. Less than half the companies visited were members. Non-members felt the organization was ineffective or played favorites.

The home based-footwear producers in Bandung could greatly benefit from a viable footwear association. As is the case in most countries, these small businesses usually do not attempt to belong, and in many cases are not welcomed into an organization such as APRISINDO. Sometimes a secondary association is formed that caters to the needs of the small businesses, but this also causes a division of effort and lack of industry cohesiveness that is very badly needed.

Small Home-Based Footwear Producers

As previously mentioned, there are hundreds of small home-based footwear producers in the Bandung area. Some work as sub-contractors for the larger companies, some produce hand-made footwear for their own retail shops, and some produce footwear for sale in the local market. Assistance to these companies is a very difficult issue to address, and usually the most that can be accomplished is: (1) Foster communication between this group and the larger companies for potential sub-contracting opportunities. (2) Survey the group to determine if there is a simple machine (sewing, trimming, etc.) that could improve their product quality and output and that could be centrally located and used by all.

- **Social accountability issues.** These issues are usually very misunderstood and exaggerated in the media, however the project should be prepared for and have an understanding of the local / national workplace regulations in the event questions are raised. There were exceptions, but the companies visited in the Bandung area are of a size and of a traditional family business make-up that working conditions and pay levels are likely at the low end of the industry. As a general statement, the Chinese-Indo companies (PT Primarindo Putra Perkasa, Sejahtera Manunggal) employed more workers that appeared younger and were working off the floor and in less well lighted, ventilated, and comfortable surroundings than did the traditional Indonesian companies. These conditions all lead to poor quality and productivity issues, and probably worker dissatisfaction and turnover, as opportunities arise. Labor cost is a small portion of the product cost for these companies, so they look at rework as being cheaper than upgrading facilities and slow handwork cheaper than more productive but expensive machinery.

With the exception of Fortuna, the working conditions in the Bandung area footwear companies were less desirable than the companies visited in Jakarta. The conditions in the factories appear comparable to those of similar size and capability in countries across Asia. The working conditions in the tanneries visited are also similar to like size operations in much of the world.

- **Key points and opportunities.**
 - After interest expressed by UNIDO to have a delegate for their international leather conference, Mr. Bapak Haji Nadiman was proposed by SENADA. If he is selected to attend the conference an article or press release can be produced for local and international publicity. Mr. Nadiman's attendance at the conference in Brazil offers the opportunity for a gain in knowledge and developing potential relationships in the international leather community.
 - Bandung is a destination for shoppers from Jakarta and other cities, due to its many factory outlet stores, and offers opportunities to SENADA to develop a pilot project which would operate such a store, offering products made by its client companies or small home-based workshops. This outlet could include products produced across many of SENADA's product lines.
 - Most companies had only a single source for domestic leather (usually within their group Indo or Chinese). It is very unlikely that the project will be able to change company traditional trade patterns but a good first step is the leather producer directory that will at least provide information.
 - Simple steps such as introduction of subscription for Italian design magazine (ARS SUTORIA) would be helpful if a method can be so as the product can be shared. Knowledge of current designs is lacking and material and buyer contact information is also contained in each issue.
 - All companies would greatly benefit from productivity improvement services offered by SATRA. If cross project cooperation with UNIDO becomes possible, productivity improvement should be a key focus. This comment was made for Surabaya but applies to Bandung also. The company Fortuna has a good product but priced at high end of the range, which limits opportunities. Productivity seemed very low, using a very labor-intensive process.
 - SENADA should consider the Social Accountability issue area as one to become involved in as the process and regulations can be duplicated across industry sector and across the branch offices. The consultant previously supplied information on SA 8000 and WRAP and the project has the capability in house to research both domestic and international standards and put a program in place. This is becoming a necessity for export industries and especially for European markets.
 - SENADA should propose to assist all the companies who register for the Jakarta Leather Exhibition in the preparation steps that they did previously for GDS. This exhibition, while small, is a key for bringing buyers to Indonesia.

5. ANNEX III

VISIT REPORT FOR SURABAYA AREA COMPANIES (APRIL 23-26, 2007)

Overview

The companies visited in Surabaya included both large and SME (<1,000 employee operations). The ECCO operation had over 4,000 employees and a couple of the Eva Slipper manufacturing companies produce in excess of 15,000 pair per day. The ECCO operation was the only company that had true world class technology. ECCO operated at full capacity and all the other companies quoted as being 50-60% of claimed capacity. There are 4-6 months when they these companies are busy and the other months seem to be about half full or less. The companies are taking advantage of Surabaya port for shipping, with ECCO distributing worldwide by sea and air from Surabaya. The Indonesian companies seem to work well within their group, the Chinese-Indonesians seem to work well within their group, but there is limited interaction between the groups. The consultant got a good overview of companies of all sizes and capabilities in the Surabaya area. While he believes there is more there to understand, and did not visit any of the major sport shoe companies, these comments likely reflect the situation for the domestically operated footwear industry in the region.

- **Product and marketing.** A good portion of the companies visited were serving both the domestic and export markets. Domestic companies were using brands and in some cases differentiated products by brand. One company was using licensing of international movie brands for the sale of his children's products. Companies were using the web in only a small degree and mostly as an e-mail communication device. English language capability varied widely but was seen in the companies exporting widely. Much product and design information came from customers, with others searching via the web. Companies exporting were selling in Europe, mostly via trading companies and agents.

Major products produced were eva sandals or various design and complexity, leather children's shoes, health sandals for Japan, safety toe sneakers for Japan, leather safety toe boots for Australia, special shoes for horses for USA, and leather casual shoes. A small number had exhibited at the previous Jakarta Leather Exhibition. Several of the companies had attended the previous German GDS fair and had some amount of interest and orders. The domestically focused companies had countrywide distribution channels through agents, distributors, branch outlets, or a combination of all. They were advertising their brands via print and/or television and seemed to have a good understanding of local opportunities. Some were attempting to sell in Singapore but it was not the priority it should be. A couple of the firms had good relationships with Bata and were selling their local and foreign operations.

There was a large amount of concern about Chinese competition that was considered subsidized and unfair, and a great amount of concern about Chinese companies using Indonesian Certificate of Origin's to get around anti-dumping regulations and which could cause Indonesia to be hit with similar restrictions. International marketing, as in developing foreign customers and partnerships is seen as the key weakness by most of the companies. There is little to no outward industry specific export promotion efforts being carried out by industry group or government agency and the only previous assistance has been the GDS (German) trade show subsidy.

- **Manufacturing, raw materials, efficiency and quality.** Manufacturing was in all cases based on some version of the cement process. Productivity seemed about the same level in all companies and equipment varied with the product but was older tech and more Chinese than European. Most raw

materials came from domestic sources and late shipments were quoted as a major problem, but ordering quantity seemed low or spread over many colors. Finished quality on all footwear destined for export seemed good, with auditing process in place. Efficiency to get the quality seemed low but about normal Indonesian. Training was conducted in house or was quoted as “we hire already experienced workers.” Patternmaking skills also seemed to be acquired in house. IFSC reported supplying graduates to the companies but did not seem to be operating short or long term training or skill preparation classes in conjunction with the companies.

- **Industry trade associations.** The leather companies visited were members of APKI and felt the national organization was of importance in dealing with several serious issues affecting the industry. The foreign company ECCO was complimentary of APKI but very negative on APRISINDO. Approximately half the footwear companies were APRISINDO members and felt the organization was effective in lobbying issues but lacked resources for other efforts. The non-members felt APRISINDO was not an effective organization or whose interests were slanted toward a special group of companies. It was noted that this regional chapter of APRISINDO was the most active and best politically connected of any in the country. There seems to have been some previous interaction between this APRISINDO group and the comparable American association (AAFA), likely no follow up and few details were available.
- **Skill training facilities.** The IFSC has a modern facility and complete footwear making equipment for the processes being used in most companies. They seem to be operating well below capacity but report supplying graduates to the local companies. They do not seem to be offering short term or specific skills improvement classes in conjunction with the industry. They report a lack of funding and a need for experienced foreign trainers.
- **Business operational issues.** The SENADA team has worked with companies in operational areas such as business licensing. The larger companies seem to have a relatively good understanding of financial reporting, costing, and seem to be computerized in at least a basic manner. Companies had at least a 2nd tier of managers and some, but not all seemed to delegate responsibility for functions downward.
- **Social accountability issues.** The working conditions in all factories visited were more than adequate and generally above those observed in Bandung. ECCO was superior to any and world class. One company, PT Hamiljaya, reported having been audited by a foreign company concerning Social Accountability issues. The result was the addition of lighted exit door signage.
- **Small home based footwear producers.** One company (Fashion) with a retail store in front and workshop in back was visited. They turned out a large variety of shoes using basic handwork, the quality was at local market level and the prices were very attractive. The retail store was very attractive and offered good presentation and reports were that this newer location did good business. Several of the footwear operations were taking advantage of the home based shops for contracting opportunities, to lower costs and increase capabilities. One company (Jalur Rejeki) had developed an extensive operation of home based workers who were applying the beadwork on their creative sandals. The company had hundreds of these workers in villages and had set up the material transport and collection systems necessary to make this process work. For some of the extensively beaded pieces workers were paid approximately .50 US\$ and could make 4 pair per day. A QC unit operated at the factory to check every finished product. Other companies used outside worker but not in such a developed process.

- **Key points and opportunities.**

- Surabaya companies had far too much focus on only large orders, even when operating far below capacity. This indicates that material procurement for them is difficult and becomes a real problem as the number of individual orders increase.
- Indonesia is a large country and the capability of having an international airport in Surabaya offers the potential of foreign buyers visiting directly. Consideration for a 2 day program from countries such as Australia and NZ should be given depending on flight schedules and connection opportunities.
- Most companies had only a single source for domestic leather (usually within the group Indo or Chinese). It is very unlikely that the project will be able to change company traditional trade patterns but a good first step is the leather producer directory that will provide information.
- The consultant should be able to develop 1 article for an international publication based around ECCO. There may be potential for an article and/or press release to footwear media concerning Surabaya footwear companies (not certain) the horse boots made by one and the beaded sandals by another could be topics of interest.
- Simple steps such as introduction of subscription for Italian design magazine (ARS SUTORIA) would be helpful if a method can be so as the product can be shared. Knowledge of current designs is lacking and material and buyer contact information is also contained in each issue.
- All companies would greatly benefit from productivity improvement services offered by SATRA. Whether the process was a training of trainers at IFSC and then spread to companies or company specific work, this should be considered. If cross project cooperation with UNIDO becomes possible, productivity improvement should be a key focus.
- Companies had little focus on making and selling uppers. Possibly due to productivity but this is a strategy they should be willing to follow until reaching capacity. Making uppers for leather or sport shoes follows the same process.
- There was a focus by the Surabaya group on trade exhibitions like GDS, where there was previous government sponsorship. While this is a very large international fair, those that seem more appropriate are in Australia, Japan, and Dubai UAE.
- One company owner was leaving to visit a materials show in China. There are several, most now in various cities in China. SENADA should consider sponsoring a national or regional group to attend one of these, possibly under the banner of APRISINDO.
- SENADA should consider the Social Accountability issue area as one to become involved in as the process and regulations can be duplicated across industry sector and across the branch offices. The consultant previously supplied information on SA 8000 and WRAP and the project has the capability in house to research both domestic and international standards and put a program in place. This is becoming a necessity for export related industry and especially for European markets. The fact that one company in Surabaya has been audited means there is activity already on this issue.
- SENADA should propose to assist all the companies who register for the Jakarta Leather
- Exhibition in the preparation steps that they did previously for GDS. This exhibition, while small, is a key for bringing buyers to Indonesia. In preparing these companies, there is no reason why the project could also not record sales that were achieved at the show as part of its effort. The Surabaya APRISINDO group mentioned the need for this at the Jakarta exhibition. If it is a way to encourage more exhibitors it is of good value.

6. ANNEX IV

VISIT REPORT FOR YOGYAKARTA COMPANIES (MAY 1-2, 2007)

Overview

The Yogyakarta region is more focused on leather tanning than production of footwear. Production firms visited include a small tannery of less than 20 employees finishing domestic leather for an export oriented furniture company, a large tannery producing over 1,000,000 sq. ft. of leather a month for export, and the Jakarta manufacturer of Adidas footwear (Prima). Another tannery produced finished sheepskin leather for export oriented garment (gloves) companies, and two Ministry of Industry operated research and skill training institutes. Also visited was a leather products company currently exporting their bags to Europe. The consultant believes that while there are additional quality tanneries in the Yogyakarta area, he has a good understanding of the industry and of the opportunities, constraints, and resources available in the region.

- **Product and marketing.** The main product produced in the region was cow, sheep, and goat leather in either finished or semi-finished destined for footwear, garment, and furniture manufacturing companies in Indonesia or abroad. Most was sold via agents the companies had worked with for many years. Some was sold direct. One company in the region had become a subcontractor for ECCO, producing lining leather.

Companies were using the web in only a small degree and mostly as an e-mail communication device. English language capability varied widely but some capability was found in all the companies. Much product and design information came from customers, with others searching via the web. Europe was the major foreign market, with some exports to China. A small number had exhibited at the previous Jakarta Leather Exhibition. Several of the tanneries had attended Italian and/or Chinese leather exhibitions. Maleha regularly attended a major European leather-products exhibition in Germany.

One tannery reported that they had stopped selling footwear firms because of slow payment in the industry. Another reported limiting its sales to 1 creditworthy firm for the same reason. All exports were via L/C with immediate payment. The leather tanneries were strongly in favor of restrictions on leather exports of semi finished hides.

- **Manufacturing, raw materials, efficiency and quality.** Production work at the leather product factory (Maleha) was by hand work and very old tech machinery. Productivity was correspondingly low. Quality was relatively good but with excessive handwork required for customer acceptability resulting in high price / low profit / low competitiveness issues. The leather tanning companies manufacturing process varied from old tech to relatively modern, but always below the finish quality, design, or efficiency achieved by ECCO. A small company such as Fajar Makmur produced relatively good finished leather, destined for export products, in small amounts while using very old technology. As a contrast, PT Budi Majmur Jaya Murni was producing finished and semi finished leather using more modern technology, but still far below that used by ECCO.

Raw materials were a combination of domestic and imported. Imports of sheep/goat skins were from East Africa with various reports of customs issues. Imports of cowhides were described as difficult because of health certification issues.

Finish quality of leather was at high enough level at BMJM to allow sales to Italy and for Adidas produced in Indonesia for export. Reports were that foreign companies were requesting more semi-finished as opposed to finished leather and it is likely that this trend will only expand. Most companies were operating at a higher percentage of capacity than was seen in footwear firms.

- **Industry trade associations.** The leather companies visited were members and officers of APKI and felt the national organization was of importance in dealing with several serious issues affecting the industry. The chairman of APKI is a local tannery owner and reports that all association work is voluntary and it is difficult to persuade members to make even small contributions such as a membership fee.
- **Skill training facilities and research institutes.** The Balai Besar Kulit Government Research Institute (Ministry of Industry) is a large organization of over 200 employees, engaged in various type of research, certification, and training/production activities pertaining to footwear, leather, and plastics. The institute was outfitted with an extensive amount of testing and production equipment, some as much as 50 years old, and most donated by various projects (USAID, UNIDO, ADB, etc.) through the years. The facility received earthquake damage and plans and funding is supposedly in place for new construction and improvements this year. There seemed to be quite extensive amounts of testing of footwear sold to the Indonesian military on tender, in the areas of safety toe impact and drop, sole abrasion, and leather flex. There is work in process to have the laboratory accredited by foreign institutions, which will be a great help to local exporters who now have to send products or materials to accredited labs in other countries for required tests (EU material, etc). There is a full footwear production facility contained in institute (not functioning since the earthquake) and a full tannery that is being used for research in developing new leathers (fish, reptile, etc) and new uses for current products. This institute reports understanding of and focus on private industry needs.

The Akademe Teknologi Kulit (ATK), also operated by the Ministry of Industry, is a training institute offering short and degree (3-year) courses in footwear, leather, and leather goods design and production. This facility has a staff of approximately 70 and enrollment of approximately 450. The highest demand course is in footwear and the lowest for leather tanning technology. There is functioning production machinery in the facility as well as a computerized research department. There was extensive damage to the facility in the earthquake and funding for renovation and new buildings has supposedly been approved. The ATK has been successful in supplying interns for industry firms including ECCO. The ATK has received funding from the EU during 2005-6 and currently from GTZ through 2007. Their focus seems very much on increasing donor funding for activities.

- **Social accountability issues.** Leather tanneries are not the best environment under even ideal circumstances. The working conditions in the Yogyakarta companies were much better in the larger companies such as PT Budi Makmur Jayamurni and PT Adi Satria Abadi than in small companies such as Fajar Makmur, where machinery setup and lighting / ventilating systems could use improvement. The situation even in the smaller companies is no worse than seen elsewhere in Indonesia and in competing countries.
- **Key points and opportunities.**
 - Tanners were concerned about the declining supply and quality of domestic hides. Some were importing raw sheepskin from Africa but were becoming concerned as more countries banned export of unprocessed hides. SENADA's competitiveness work should encourage hide imports from the most opportune location and facilitate discussion with the Ministry of Agriculture and Customs to make the process work smoother as the general consensus was

the Indonesian process was too cumbersome and Ministry of Agriculture regulations too restrictive and enforced unequally.

- The leather processing companies in the Yogyakarta area are not as likely to receive a great amount of attention on Social Accountability issues. The most the project should do in this area is to provide information concerning the Indonesian regulations in this area and stress their importance.
- A copy of the design and trend publication ARS Sutoria was provided to the BBK as they were working from older Chinese material. Knowledge of current designs is lacking and material and buyer contact information is also contained in each issue. The ATK seemed in about the same situation and both would benefit from a regular subscription to products of this type.
- An opportunity was provided to APIK to provide Indonesian hide pricing information to a Swiss company that is the best known in this field. The company would provide access to its information services, valued at \$1,000 USD annually for short market reports 2 times per month.
- There was knowledge of the larger Yogyakarta companies of major worldwide exhibitions including Italy and China and some amount of attendance.
- SENADA should propose to assist all the companies who register for the Jakarta Leather Exhibition in the preparation steps that they did previously for GDS. This exhibition, while small, is a key for bringing buyers to Indonesia. In preparing these companies, there is no reason why the project could also not record sales that were achieved at the show as part of its effort.
- The research institute BBK would become a valuable asset to Indonesia's footwear and leather industry were its testing facility to achieve accreditation by international organizations or in partnership with SATRA. This would relieve individual companies the necessity and expense of shipping products/materials to Europe and Hong Kong for necessary EU or buyer required tests.
- Assistance to BBK and/or ATK can best be accomplished via the proposed cooperation with UNIDO. ATK is currently receiving support from GTZ, the focus of their work should be understood before any other support was provided. BBK has had much donor-provided support in the past including UNIDO, ADB, and USAID. UNIDO efforts are likely the best future option for this institution. SENADA should encourage a greater amount of private industry involvement and support for both organizations.
- Companies that would be very good examples of certain practices: Lembah Tidar – (Located in Magelang Central Java and not visited due to owner being away on international travel) This tannery is the only one in Indonesia having the combination of product quality, productivity, and entrepreneurial management to become a certified supplier (leather lining) for ECCO. Also is said to produce upholstery leather for Indonesian auto industry.

7. ANNEX V

INDUSTRY ROUNDTABLE AT LE MERIDIEN HOTEL, JAKARTA (MAY 10, 2007)

Discussion Topics:

- Improving international promotion of the Indonesian footwear Industry.
- Strengthening the supply of domestic and import raw material inputs.
- Building capacity of Indonesian footwear associations.
- Role of social accountability.
- Productivity improvement utilizing external resources.
- Access and distribution of current design information.
- SENADA's proposed activities.

8. ANNEX VI

TOPICS AND RESOURCE INFORMATION COMMUNICATED TO SENADA

- American Apparel and Footwear Association
- Trademark and Brand Registration Issues
- Carrefour and Hypermarket Opportunities
- Competitiveness Theory
- Middle East Tender Opportunities
- Furniture and Automotive Upholstery Leather
- IFSC
- Indonesia Leather and Footwear 2007 Exhibition
- Industry Directory
- Sauer Leather Report
- SATRA
- Security Industry Opportunities
- Social Accountability Issues
- UNIDO

9. ANNEX VII

SAMPLE OF A MARKET DEVELOPMENT WEB PAGE PRODUCT



<http://members.cox.net/westnash/>

10. ANNEX VIII

LIST OF COMPANIES VISITED

Jakarta Area Companies

CV Mulia

Sepatu Mas Idaman

Prima

PT Mangul Jaya

Fumiko Yongki Komaladi

PT Pelita Tomangmas

Bandung and Garut Area Companies

Sinar Bintang Buana (Donatello)

Donatello – retail

Fortuna

Clarion Perusahaan Sepatu

General Shoe Factory

PT Primarindo Putra Perkasa (Colette)

PT Dhaya Tuhumitra

CV Sejahtera Manunggal (BE-BOB)

Max Baren's

Edward Forrer - retail

PT Karya Lestari Mandiri Leather

Endies Leather Company

Surabaya Area Companies

PT Kharisma Indonesia

Fashion Shoe Retail and Production

PT Tirtadaya Adi Perkasa

APRISINDO East Java Business Meeting

PT Rajawali Tanjungsari

Jalur Rejeki

Indonesian Footwear Service Centre

ECCO Indonesia

PT Halimjaya Sakti

PT Halimjaya Sakti

PT Gradial Perdana Perkasa

Yogyakarta Area Companies

Maleha (SaSa Design)

Fajar Makmur

PT Budi Makmur Jayamurni

Akademi Teknologi Kulit

Balai Besar Kulit, Karet Dan Plastik

PT Adi Satria Abadi (APKI Chairman)

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