

The effect of the international financial and economic crisis on the home decoration sector in developing countries

Summary

The financial and economic crisis will be felt most keenly by home decoration exporters in DCs in terms of an expected decrease in exports to Europe. The decrease in exports is a direct result of declining demand. Export margins are also expected to shrink, and unemployment is expected to rise in the sourcing countries. Interviewees approached for this survey said exports are already declining. The orders placed by importers are diminishing, as importers seek to use their own stocks first. The low-end market segment, where consumers are cutting back spending, is being hit hardest by the crisis.

Another major issue is the restricted access to credit as a result of the crisis. Smaller companies, in particular, face this problem. In the survey, respondents were asked to assess the effect of the crisis on their access to working capital, investment capital, and export financing. Access to working capital has become the most problematic; banks are also reluctant to put up investment capital and export financing. As a result of these restraints, exporters are having a hard time obtaining the pre-financing they need to produce orders and many of them are unable to invest in product development and market access strategies, such as visits to trade fairs. Ironically, the survey also shows that product development and trade fair visits are considered the most vital elements of economic survival at this time. As for opportunities arising from the crisis, these lie mainly in the middle and upper market segments, where margins for producers are higher. Critical success factors for products include innovativeness, uniqueness and high quality. Exporters can also distinguish themselves by investing in Corporate Social Responsibility (CSR) and in a sustainable production chain. Finally, it is important that exporters actively profile themselves, while investing as much as they can in marketing in order to catch the attention of potential buyers in the upper market segment.

To overcome the financial crisis, the exporters interviewed believe they must invest in product development and market information so that they can adapt their products to European demand. This means, again, that access to credit is a must – as are more frequent visits to trade fairs. Exporters also believe they must pay special attention to the marketing of their products with a view to finding new buyers.

Introduction

This report offers an overview of the impact the financial crisis is having on home decoration exporters in DCs (home decoration and accessories, home textiles) and the consequences for European imports from these countries. The priority countries for the home decoration sector are, in order of importance: Pakistan, Vietnam, Bangladesh, Indonesia, Egypt, Moldavia, Sri Lanka, Colombia, South Africa, Ethiopia, Kenya, Tanzania, Ghana, Rwanda, Uganda and Yemen

Primary Research

1. Online questionnaires

The following parties were asked to fill out sector-specific online questionnaires: BSOs (Business Support Organisations), exporters in developing countries, European buyers importing from these countries, European associations.

This online questionnaire was held between February 23 and March 2, 2009, and yielded the following response:

Table I Response to online questionnaire, home decoration sector

	Partner Countries	Other CBI Client Countries	EU	Total
Exporters	31	12		43
BSOs	13	14		27
EU Buyers			10	10
Associations				0
Total	44	26	10	80

2. Interviews

A number of representatives of these groups were approached for in-depth interviews. In the interviews, these players were asked questions about the impact of the crisis, specific institutional and private needs, opportunities, and the different levels at which they seek assistance in promoting exports. A total of 23 interviews were conducted: 12 with exporters, 4 with BSOs and 5 with importers. A CBI expert and Programme Manager were also consulted.

Priority countries

The primary research for this report focused largely on a shortlist of priority countries. The interviews, for instance, were conducted mainly with respondents from a selection of priority countries. The selection was made on the basis of trade statistics and input from CBI experts. The countries covered in this report are therefore all priority countries. Secondary Research Background information was drawn from recent articles and Internet news sources as well as articles recommended by the CBI expert.

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1 Consequences for Companies

1.1 Consequences in Partner Countries

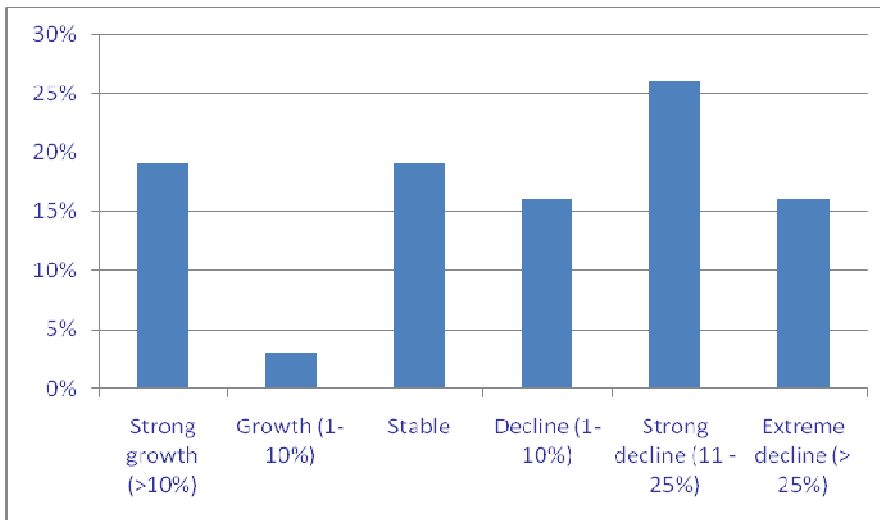
The responses from the exporters and BSOs in partner countries clearly indicate that the economic crisis has already led to a decrease in exports, lower margins and the inevitable layoff of employees. Secondary sources confirm this. In Vietnam, for instance, statistics covering 38 provinces reveal that 9 craft-centred villages have already gone bankrupt and another 124 are in bad shape, with mass redundancy as a result. If help does not arrive soon, more than half of the country's home decoration production companies will face closure (www.lookatvietnam.com, 2009).

Of the 31 exporters in partner countries who filled out the online questionnaire, 58% expect a decline in exports in 2009, 22% expect exports to rise and 19% expect exports to remain stable. Figure 1.1 offers an overview of the answers given by exporters.

Similar percentages apply to exporter's expectations regarding job losses.

Interviews with an exporter and a BSO representative – both reporting rising exports – suggest their growth is a result of extra investments in product development (exporter) or extra support from their own government (BSO Moldavia). Of the 12 BSOs who filled out the online questionnaire, 83% expect exports to decrease, 8% expect growth and another 8% expect stability. Interviews with exporters and BSOs show that overall exports have already gone down this year as compared to last year.

Figure 1.1 Expected developments in the exports of decorative items from partner countries (2009 as compared to 2008)



Source: online questionnaire February 2009

The experts interviewed for this survey share the general expectation of declining exports from the partner countries. They observe that the number of orders placed at last February's Ambiente trade fair, a leading trade event for this sector held in Germany, was lower than usual. Exporters enrolled in the CBI's Export Coaching Programme (ECP) reported that the value of orders they received during the fair was 75% lower than last year. Another important development is that orders are shrinking in size as well. Buyers are importing slightly more frequently, but import volumes are steadily shrinking, which means small stocks. Existing customers, furthermore, are seeking to sell their stocks before placing new orders.

The regions hit hardest by the crisis are the ones most dependent on the United States' markets, as the crisis began and has thus far been more severe there than in Europe. This means South-American home decoration exporters are suffering most from the crisis. To a slightly lesser extent, Asia and Africa have also been affected. Experts forecast a further decline in exports from the latter two continents to Europe.

From various interviews it appears that the crisis will hit hardest in the low market segment, as this is where consumers are most likely to cut spending. Also, margins in this segment were already smaller than in the middle and upper segments.

Products currently selling well are characterised by uniqueness, high quality and good, new designs. Companies distinguishing themselves by means of corporate social responsibility (CSR) or environment-friendly production methods are also in a favourable position. On the other hand it must be noted that according to four BSOs approached in this survey the crisis is negatively impacting CSR and sustainability within the supply chains. The remaining BSOs do not believe the crisis will have any effect in these areas. The experts confirm that CSR calls for the kind of investment easily economised on at present, but that CSR can also be used as a marketing tool.

The expert interviewed for this survey says the effects of the crisis can be seen most clearly in declining sales of products and hesitance among importers. Obtaining financing is also a major problem. Almost all of the companies confirm this (see also Chapter 2). From several interviews it is apparent that smaller businesses are being hit hardest. The main problems faced by BSOs are membership cancellations as a result of declining sales and limited access to financing.

1.2 Consequences in the EU

According to the expert, EU buyers are hesitant, placing fewer and smaller orders and using up stocks first. Half of the 10 European importers that filled out the online questionnaire say the crisis is negatively impacting their trade with DCs. The other half, however, report a positive impact. Two of the five European importers interviewed expressed a keen interest in products from DCs, assuming these provide higher margins. The crisis is forcing them to search for more competitively priced products. However, this development is not strong enough to counter declining exports as the imported volumes and their margins are shrinking.

The importers interviewed also said they are in search of reliable suppliers who regularly make an appearance at trade fairs, are innovative and noticeably keyed into the European market. The expert notes that most European importers would have difficulty with suppliers whose cash-flow is problematic and with producers who no longer have the capacity to innovate. Also, buyers are less inclined to offer advance financing, whereas the need among exporters for advance payments has increased due to the reluctance of the banks.

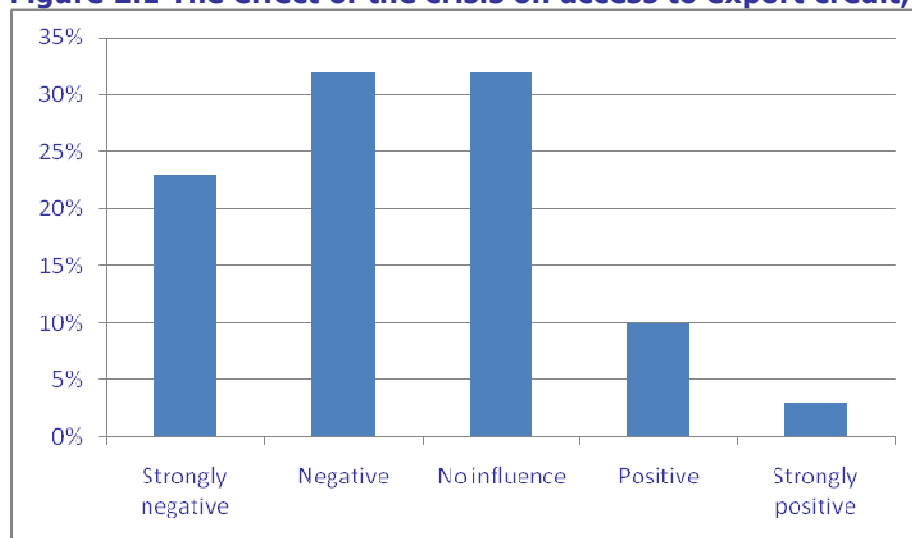
Several Internet sources confirm the trend that the crisis is increasingly driving companies in the home decoration sector to countries offering lower-cost products. These importers can thus maintain acceptable margins, while offering consumers lower prices. It is also clear that importers are ordering smaller volumes (rather than requiring mass production) as consumers are buying fewer products due to the crisis (Global Sources Ltd, 2009). To diversify their procurement, importers are increasingly in search of alternatives for China, such as Vietnam. Vietnam is viewed as an emerging country in this sector. Bangladesh is also mentioned because of its low production costs as compared to those of American and European manufacturers (Thedailystar.net, 2009).

2 Credit

Both the online questionnaires and the interviews clearly indicate that the reluctance of banks in response to the crisis is one of the biggest problems this sector faces. Exporters are having far more difficulty obtaining credit today than a year ago.

Of the 31 exporters who filled out the questionnaire, 32% say the crisis is negatively affecting access to export credit, and 23% even speak of a very negative influence (see Figure 2.1). This means the majority of exporters at this time are struggling to obtain financing for their exports. Half of the BSOs report a negative influence on access to export credit, and 17% report a very negative influence. The remaining BSOs say the crisis has not influenced credit availability.

Figure 2.1 The effect of the crisis on access to export credit, according to exporters



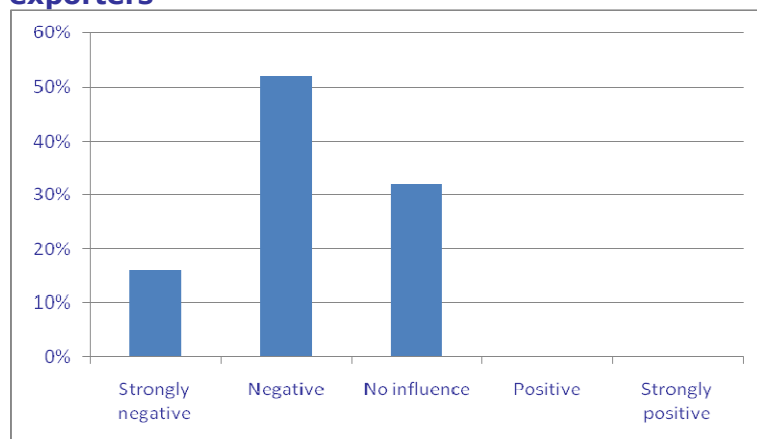
Source: online questionnaire February 2009

Access to investment capital is being similarly affected by the crisis, except that the number of exporters experiencing 'no influence' in this area is slightly higher, whereas the number reporting a 'positive influence' is smaller. The BSOs are more negative about access to investment capital than they are about access to export capital.

As Figure 2.2 indicates, the effect of the crisis on access to working capital is more severe for the exporters in the partner countries. None of the exporters report a positive effect in this area, and 68% report a negative or very negative effect. Most of the BSOs (84%) agree that the crisis is having a (very) negative impact on the availability of working capital; only two say they do not see any such influence at all.

From interviews with exporters it appears that banks have become a lot less willing to put up loans since the crisis broke out. This means exporters are restricted in their access to (advance) financing of procurement, market access and product development – the very activities they depend on to counter declining sales. Smaller enterprises, especially, are struggling to obtain financing, a fact confirmed by the expert. Getting export credit was already a challenge in the partner countries and the crisis has made matters worse. In the interviews, the exporters also said they believe interest rates have rocketed recently, which makes operating on credit a lot less attractive anyway.

Figure 2.2 The effect of the crisis on access to working capital, according to exporters



Source: online questionnaire February 2009

The European importers interviewed agree that the reluctance of banks is hindering trade with DC companies. As banks in the partner countries are also reluctant, some importers have had to invest in production there themselves. However, the trade restrictions may also be attributable to European bankers' attitudes, as it is fairly common for them to avoid giving credit for advance import financing.

3 Opportunities

Despite the economic crisis, opportunities for exporters in the partner countries to sell their products on European markets do still exist. The BSOs are largely negative about the existence of such opportunities, but more than half of the exporters (62%) see possibilities.

The Middle and Upper Market Segments: Innovation

The interviews with both the exporters and the expert suggest that the middle and upper market segments, where consumers continue to seek unique and high-quality products, offer the best opportunities. Profit margins for producers are higher in these segments as well. The key to success here lies in offering unique products and continuously innovating by means of product development. It is also essential that products are in step with European market demand. One Indonesian exporter, for instance, says his company's exports to Europe are currently rising as a direct result of product development.

Corporate social responsibility (CSR) and developing a sustainable supply chain are important aspects of product development, according to the expert. As both of these trends continue to gain momentum, they offer exporters an opportunity to distinguish themselves, which is vital in the upper markets. Offering unique products (in smaller volumes), moreover, corresponds with the current desire among importers to import smaller volumes more frequently.

The weakening of competition from China is another favourable development for smaller exporters from partner countries. China is a strong competitor because of the sharp prices its producers can realise due to mass production. However, the crisis has already forced large numbers of Chinese companies into bankruptcy, according to the expert, partly because of declining demand in the lower market segments they tend to target. The Chinese textile industry alone lost 4.6 million employees to this development between January and May 2008. In the same period the year before employment was on the rise (www.newharbor-textile.com, 2008).

Finding New Buyers

According to the CBI Programme Manager, exporters first and foremost must focus on existing customers. But if exports to these buyers start to drop, finding new importers becomes imperative. This means exporters must attend trade events and conferences more frequently to demonstrate their stability. Exporters should travel to Europe more frequently to seize the opportunities available.

Both the exporters and the expert say the retail branch currently offers new opportunities. With importers requiring smaller volumes, exporters can supply retailers directly. This can also help them increase their export margin, as it means bypassing intermediate traders.

4 Needs

To make use of the opportunities available in the market, export businesses need various forms of support. Table 4.1 shows the forms of support mentioned by exporters and BSOs in the partner countries, in order of importance.

Table 4.1 Needs of exporters and BSOs in partner countries

Exporters	BSOs
Access to capital	1. Access to capital
Product development	2. Marketing
Marketing	3. Government support

Trade fair visits	4. Trade fair visits
Market research	5. Staff training
Human resources development	

Source: online questionnaire February 2009

As the table indicates, access to capital is the most urgent need. More than half of the exporters and BSOs say they are in need of financing. As described in Chapter 2, access to financing is difficult at this time. Many companies are thus effectively kept from developing new products, while product development is crucial for reaching the middle and upper market segments. Lack of capital can also lead to lack of capacity for fulfilling orders (as buyers only submit partial advance payments).

The second most urgent need in the eyes of exporters is the need for product development support. Support in marketing products is also important, particularly if aimed at helping exporters adapt their products to the upper market segment. This need is confirmed by the BSOs. Like the necessity of visiting trade fairs more frequently, this need arises from the search for new customers, as existing customers are cancelling or downsizing orders.

There is also a need for information regarding European markets and for staff training, as many employees lack management skills. This need is shared by the BSOs, some of which also indicate a need for support from their local government.

The expert largely agrees with these points, but places product development at the top of the priority list, as it is essential for acquiring new customers and maintaining export levels. He also attaches considerable value to market information as a means of helping exporters adapt their products to European market demand. Finally, exporters should show up more frequently at trade fairs and conferences, according to the expert.

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