

Report On

**Backward integration of Leading Footwear industries in
Bangladesh: Problems & Possibilities**

By

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19382016

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partial fulfillment of the requirements for the degree of
Masters in Procurement and Supply Management

BRAC Institute of Governance and Development (BIGD)

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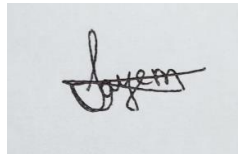
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Declaration

It is hereby declared that

1. The internship report submitted is my/our own original work while completing degree at Brac University.
2. The report does not contain material previously published or written by a third party, except where this is appropriately cited through full and accurate referencing.
3. The report does not contain material which has been accepted, or submitted, for any other degree or diploma at a university or other institution.
4. I/We have acknowledged all main sources of help.

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MD Sayem Al Amin
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Supervisor's Full Name & Signature:

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GM, SCM
APEX Footwear Ltd.

Letter of Transmittal

Mr. Mir Mehbubur Rahman
Faculty, MPSM
BRAC University
66 Mohakhali, Dhaka-1212

Subject: Submission of report on “Backward integration of Leading Footwear industries in Bangladesh: Problems & Possibilities”

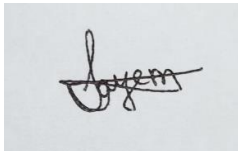
Dear Sir,

This is my pleasure to display my report on “Backward integration of Leading Footwear industries in Bangladesh: Problems & Possibilities”, which I was appointed by your direction.

I have attempted my best to finish the report with the essential data and recommended proposition in a significant compact and comprehensive manner as possible.

I trust that the report will meet the desires.

Sincerely yours,



MD Sayem Al Amin
19382016
BIGD ,BRAC University
Date: 30th April, 2021

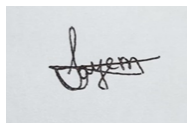
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DISCLOSING PARTY



Name: Mr. Syed Imtiaz Hossain; Date: 30.04.2021

RECEIVING PARTY

Name: MD. Sayem Al Amin; Date: 30.04.2021

Abstract

Backward integration refers to integration of any operation or service prior to the specific main operation or service. In other words, BI means acquiring an operation or service within the business unit which were outsourced before. These operations hold the success factors of entire production, hence the industry. Bangladeshi footwear industries have faced many problems throughout the years while material purchasing. Procurers have been facing problem in finding a reliable domestic source, delay in delivery and so many issues.

In this report, we'd like to see the current condition of the supplier chain of Bangladeshi footwear industries, how different factors of the procurement function can affect the productivity and profitability of a footwear manufacturing industry while we observe the impact of these purchase on production & profitability.

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List of Acronyms

SCM- Supply chain management

FIN- Financial

BI- Backward integration

RM- Raw material

LR- Leather

PU- Polyurethane

MF- Microfibers

PVC- Poly vinyl chloride

MOQ- Minimum order quantity

Global source- Other manufacturer and sources located outside of Bangladesh

JV- Joint Venture

Chapter 1

Backward integration

1.1 Introduction:

Backward integration is a process in which a company acquires or merges with other businesses that supply raw materials needed in the production of its finished product. Businesses pursue backward integration with the expectation that the process will result in cost savings, increased revenues, and improved efficiency in the production process. Companies also use backward integration as a way of gaining competitive advantage and creating barriers to entry to new industry entrants. We can try to depict the scenario like following figure:

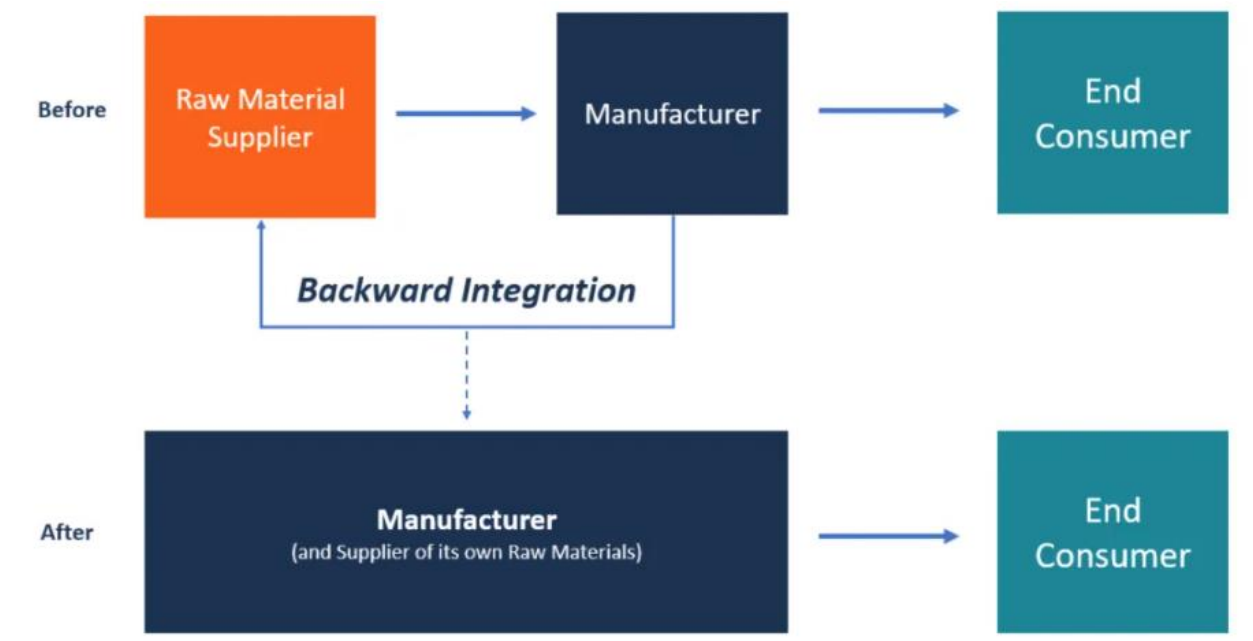


Figure 1: Backward integration

1.2 Backward integration in Footwear industries:

In case of Footwear manufacturing industries, backward integration refers to acquiring the production of raw materials like leather, outsole, adhesive, thread etc by footwear manufacturers. These raw materials are produced internally through in house facility or merging with other manufacturers. Currently main sources of footwear raw materials are generally based in Bangladesh, Italy, China, Russia, Taiwan, India & Pakistan. Buying raw material from local

sources saves a lot of time and freight while purchasing from global suppliers can ensure the value of quality.

1.3 Methodology:

All data and relevant information related to this project work was gathered by interviewing industrial experts from 8 leading industries of Bangladeshi footwear sector through a common set of questionnaire. The questionnaire was preset using suggestions from academic & professional supervisor as well as using expert suggestions. Among the interviewees, 40% carries senior management position (Manager to above) and 60% interviewees are in mid management position (Executive to Deputy Manager). Throughout these activities, we've tried to shortlist main materials of footwear industries, gather knowledge about source of materials, customer's satisfaction level, financial aspects and their feedbacks about current and future aspects. All gathered data was analyzed afterwards and exhibited in percentile based stacked columns to compare in required cases.

A big number of data have been gathered through informal meetings as well. Problems and possibilities are sorted out both from interviews and informal meetings with interviewees and supervisors.

Blank questionnaire is attached in annex-1 and list of participant organization is attached in annex-2.

1.4 Materials used in Footwear industries:

Through our interviews with footwear industry SCM specialists, we've gathered knowledge about the basic material requirement in a footwear industry. Though there are more than 100 types of materials used in a footwear manufacturing operation, based on the volume & value of use, we got 8 basic materials in this list. These are:

1. Leather
2. PU/MF (Microfiber)
3. PVC
4. Outsole
5. Insole
6. Ornaments/Accessories
7. Foam
8. Adhesive

These are the most commonly used materials. And our study will be limited within these 8 types only.

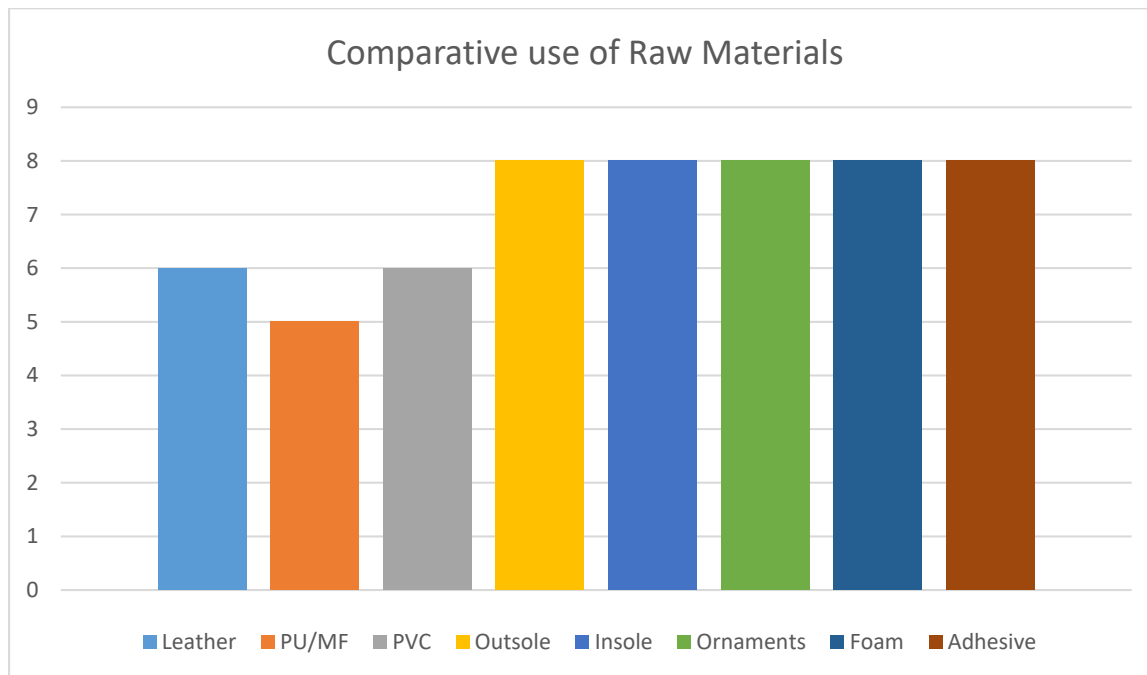


Figure 2

Chapter 2

Data interpretation

We've analyzed our gathered data and sorted all information according to type of materials to learn more about their SCM & FIN aspects (all data and information shared bellow are gathered through interview).

2.1 Leather

Out of the factories interviewed, 75% factories uses leather as RM where 50% of them Purchases it locally & 50% of them uses both local & import sources.

40% factories from who purchase leather locally, have their own leather processing units (tanneries) while remaining 60% uses other domestic sources.

Out of the domestic buyers, almost 60% are satisfied with it while nearly **40% customer are unsatisfied**. Yet they continue to purchase locally because of short lead time & low price from local sources.

Interview revealed that the main reasons of importing leather is the low capacity of local sources, quality of required leather & poor commitment from domestic manufacturers.

A total of 10% Duty/ Vat+Tax needs to be paid while importing leather and takes 20-60 days to import, time varying from different regions.

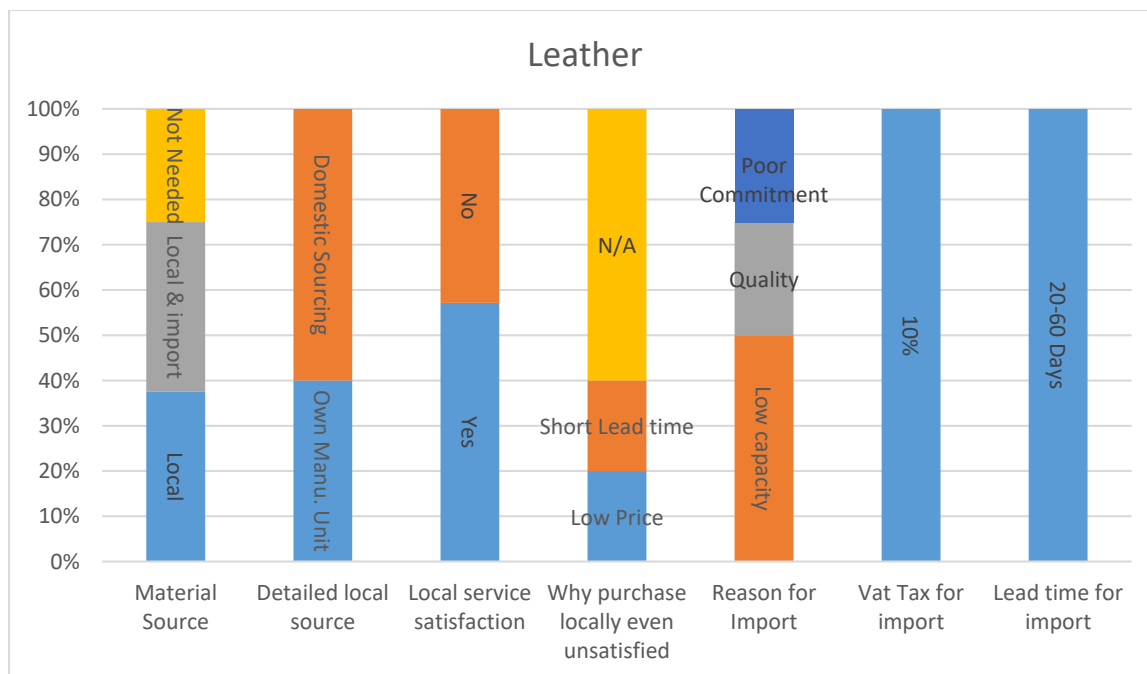


Figure 3

2.2 PU/MF

75% of the factories uses PU or MF as RM and 90% of them imports it from global sources while 10% factories purchase it locally.

Everyone who purchase from local sources purchase it from local importers and traders, meaning that there is no local manufacturer of this product. None of the customers in this segment is satisfied with their products, still they keep buying locally because of low MOQ and short lead time to purchase.

Main reason for importing PU/MF is that there is no local manufacturers.

A total of 65% Duty/ Vat+Tax needs to be paid while importing PU/MF and takes 15-25 days to import, time varying from different regions and mode of transport.

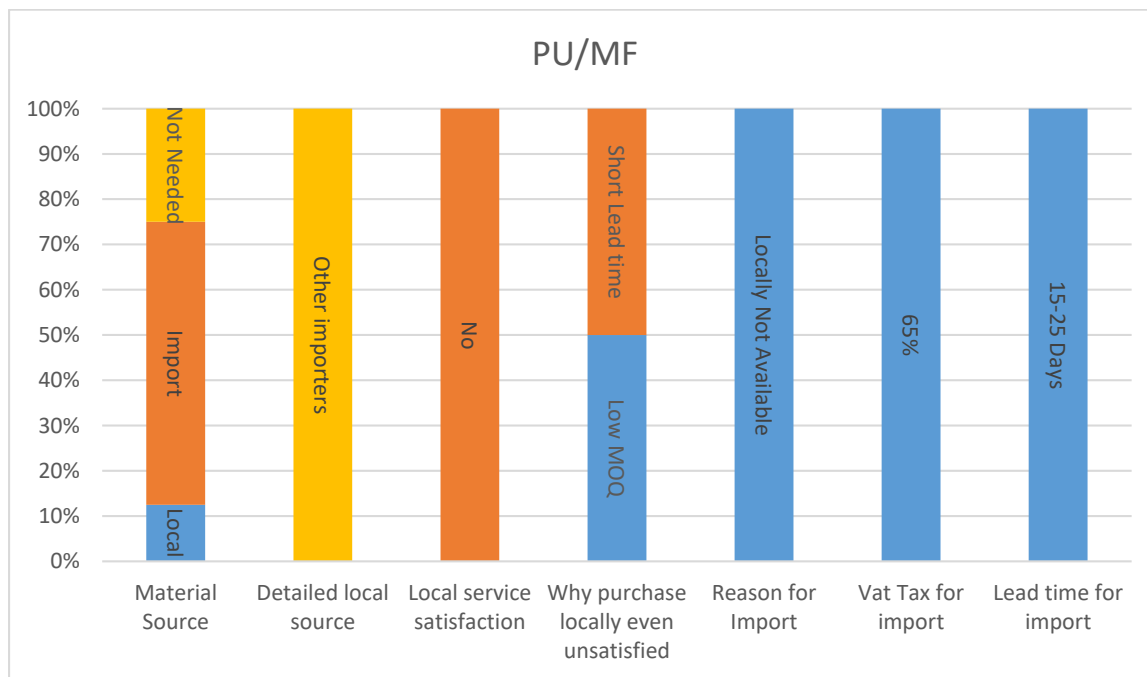


Figure 4

2.3 PVC

90% of the factories uses PVC as RM and 90% of them purchase it locally while 10% factories imports it from global sources.

Everyone who purchase from local sources purchase it from domestic manufacturers. PVC has a strong domestic supplier base just like leather which is quiet sufficient to meet domestic demand in most of the cases.

Just 10% factories import PVC from global sources because of some specific quality requirement, which too will sorted out locally soon. Main reason for importing PVC is a specific type of PVC material which can't be done by local manufacturers.

A total of 65% Duty/ Vat+Tax needs to be paid while importing PVC and takes 15-25 days to import, time varying from different regions and mode of transport.

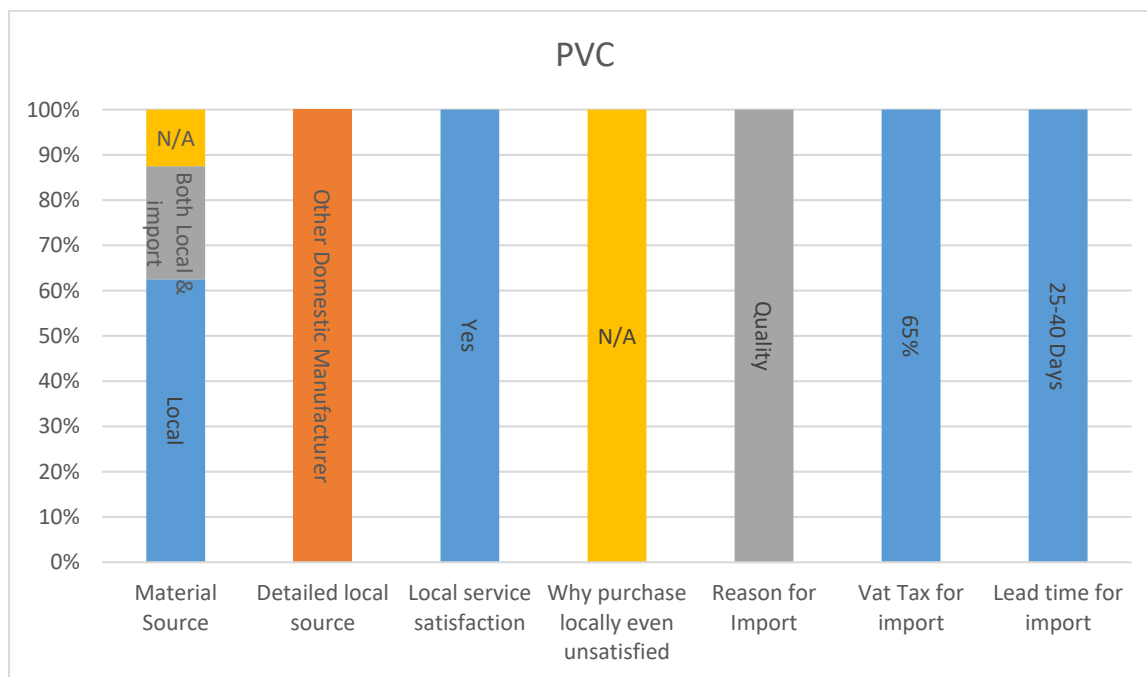


Figure 5

2.4 Outsole

All factories use outsole as RM where 40% of them purchase it only locally & 60% of the factories purchase both from local & import sources.

40% of factories from who purchase outsole locally, have their own outsole manufacturing unit while remaining 60% uses other domestic sources.

Out of the domestic buyers, more than 70% are satisfied with it while nearly 30% of customers are unsatisfied. Yet they continue to purchase locally because of easy return policy, short lead time & low price from local sources.

Interview revealed that the main reasons of importing outsole is the low capacity of local sources, quality of required product, high price of some high quality outsole & poor commitment from domestic manufacturers.

A total of 35% Duty/ Vat+Tax needs to be paid while importing ornaments and takes 15-45 days to import, time varying from different regions.

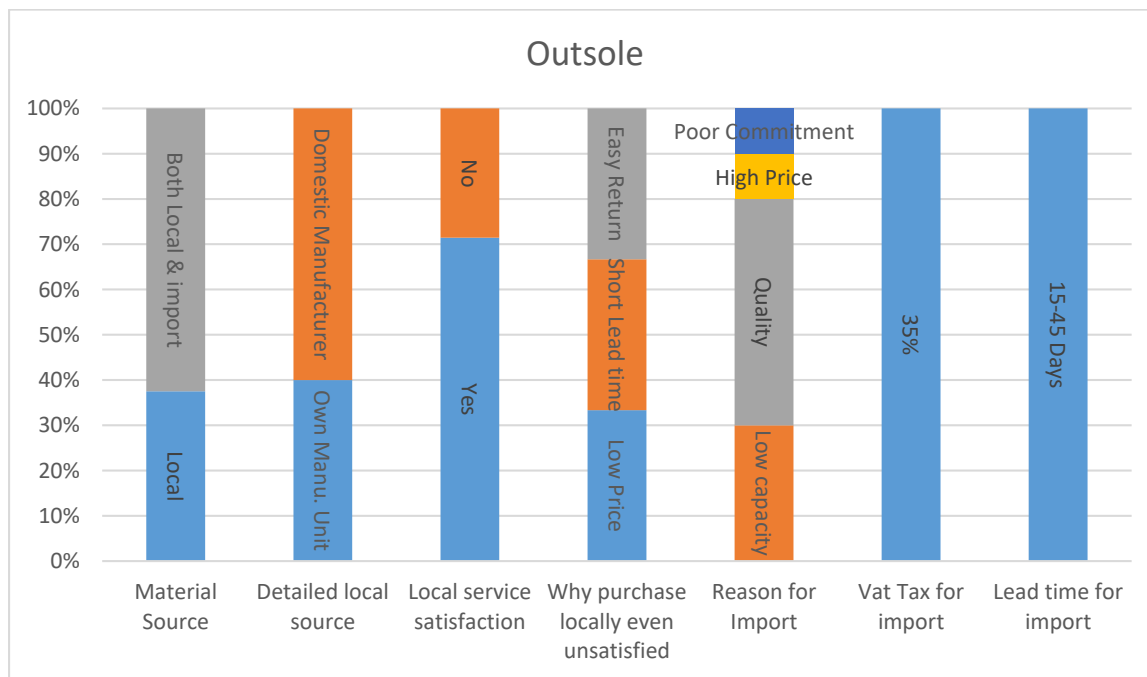


Figure 6

2.5 Ornaments/Accessories

All factories use ornaments/accessories as RM where 35% of them purchase it only locally & 65% of the factories purchase both from local & import sources.

60% of factories from who purchase ornament locally, purchase it from other domestic manufacturing unit while remaining 40% uses other domestic importers service.

Out of the domestic buyers, only 10% are satisfied with it while nearly 90% customer are unsatisfied. Yet they continue to purchase locally because of easy return policy, short lead time & low price from local sources.

Interview revealed that the main reasons of importing ornament is the low capacity of local sources, quality of required product, high price of good quality ornaments & poor commitment from domestic manufacturers.

A total of 35% Duty/ Vat+Tax needs to be paid while importing outsole and takes 15-45 days to import, time varying from different regions.

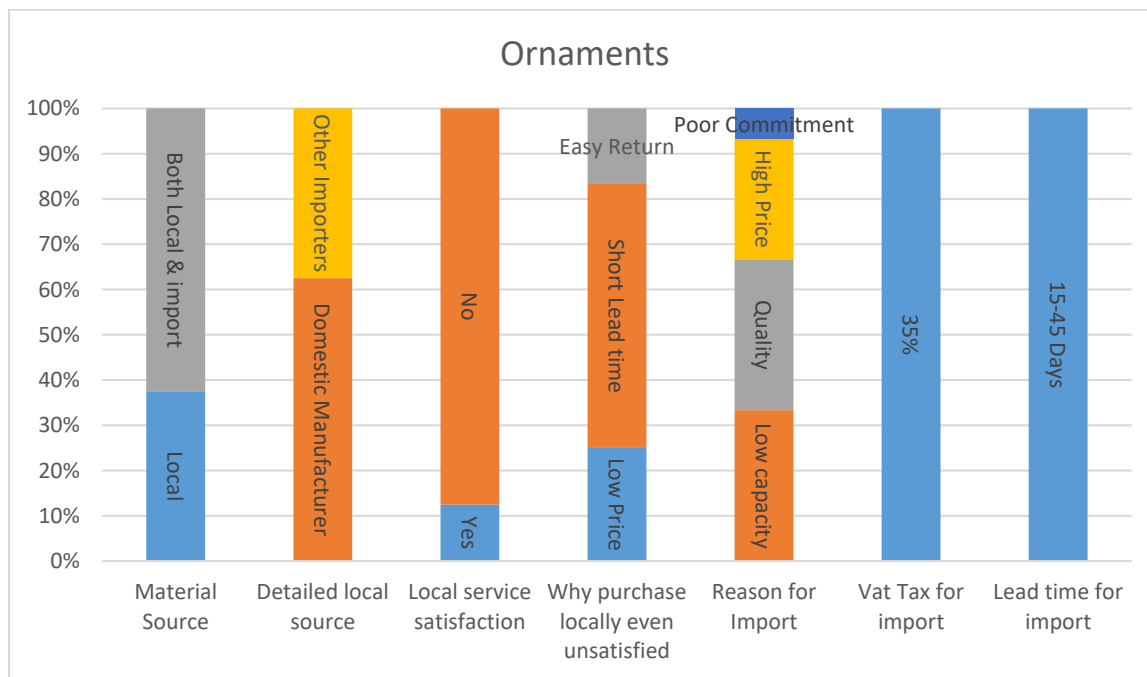


Figure 7

2.6 Insole

All factories uses insole as RM where only 10% of them purchases it only locally & 90% of the factories import from global sources.

All of the local procurers procures insole material from other domestic importers as there is no insole manufacturing plants locally. None of them are satisfied with the local sources yet they purchase locally because of easy return policy and short lead time.

Interview revealed that the main reasons of importing insole is the low capacity of local sources, quality of required product, high price of some high quality outsole & poor commitment from domestic sources. Also, one big reason of import is unavailability of local manufacturers of insole materials.

A total of 35% Duty/ Vat+Tax needs to be paid while importing insole and takes 15-30 days to import, time varying from different regions.

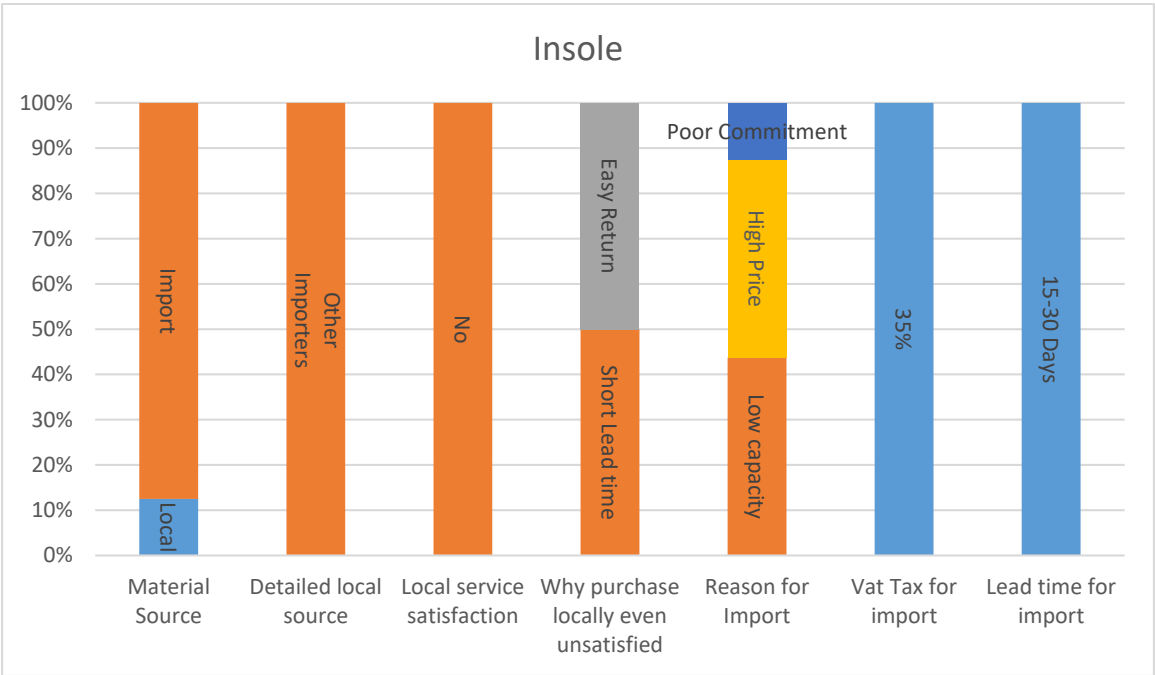


Figure 8

2.7 Foam

All factories use foam as RM where almost 75% of them purchase it locally & 25% of the factories import from global sources.

All of the local procurers procure foam from other domestic manufacturers with great satisfaction. This interview reveals that Bangladesh has some good manufacturers of foam in domestic market and they serve the purpose well.

Few customers who import from global sources procure some special quality product which have low manufacturing capacity in domestic sources.

A total of 65% Duty/ Vat+Tax needs to be paid while importing foam and it takes 15-30 days to import, time varying from different regions.

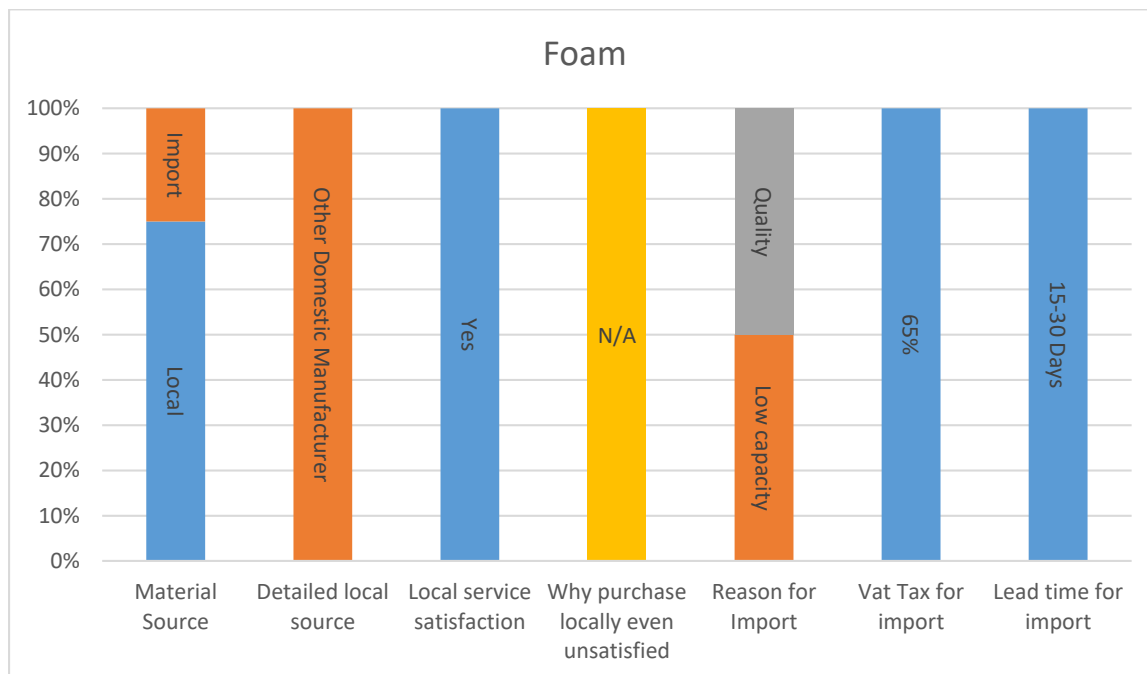


Figure 9

2.8 Adhesive

All factories use adhesive where only 25% of them purchase it locally & 75% of the factories import from global sources.

All of the local procurers procure adhesive from other domestic importers as there is no adhesive manufacturing plants locally. None of them are satisfied with the local sources yet they purchase locally because of easy return policy and short lead time.

Interview revealed that the main reasons for importing insole is unavailability of local manufacturing facility of adhesive. Also, importers' price is too high.

A total of 35% Duty/Vat+Tax needs to be paid while importing insole and takes 25-30 days to import, time varying from different regions.

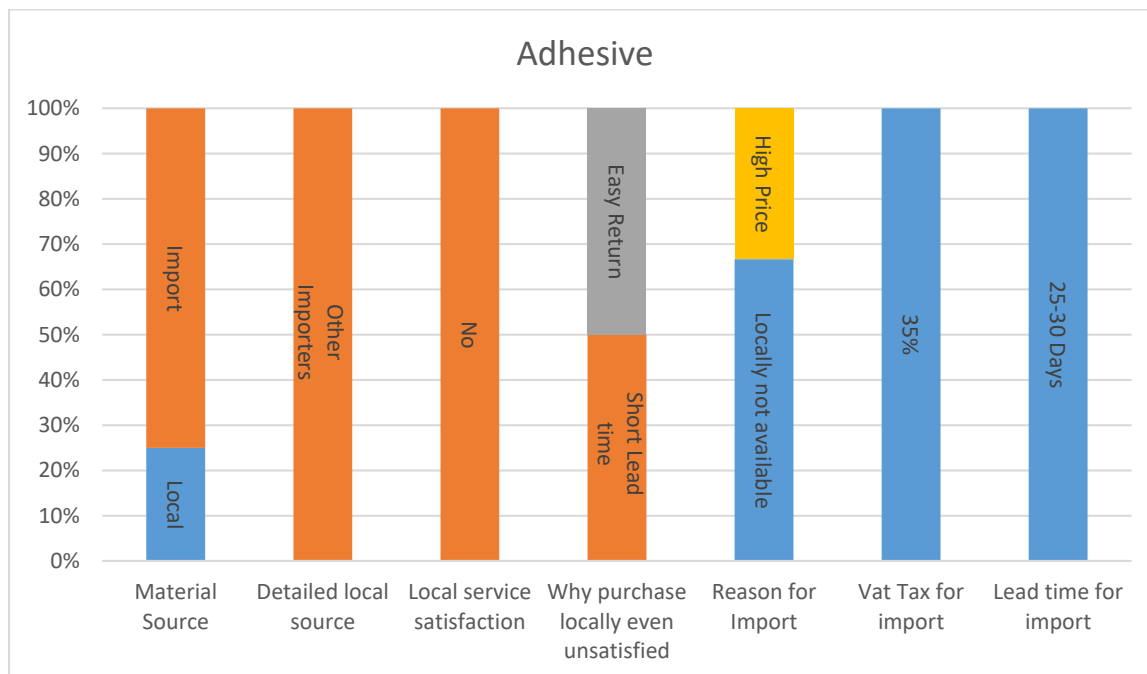


Figure 10

Chapter 3

Summarizing data

3.1 Problems

Based on current situation, interviewees shared their feedback on import materials impact on production, deliveries & quality related issues.

Delivery time: It's a dire relief that most of the time, factories can meet production deadline after importing goods, though sometimes they face penalty for delay in delivering goods.

Quality of material: Around 15% shipment face penalty due to material quality that factories settle with supplier later in different ways.

Claim settlement: If origin of claimed material is domestic sources, factories can return goods to supplier & ask for replacement. However, in case of imported materials, returning (re-export) is not possible due to government rules and regulations. In that case, claim is being settled by adjusting claimed value with next orders.

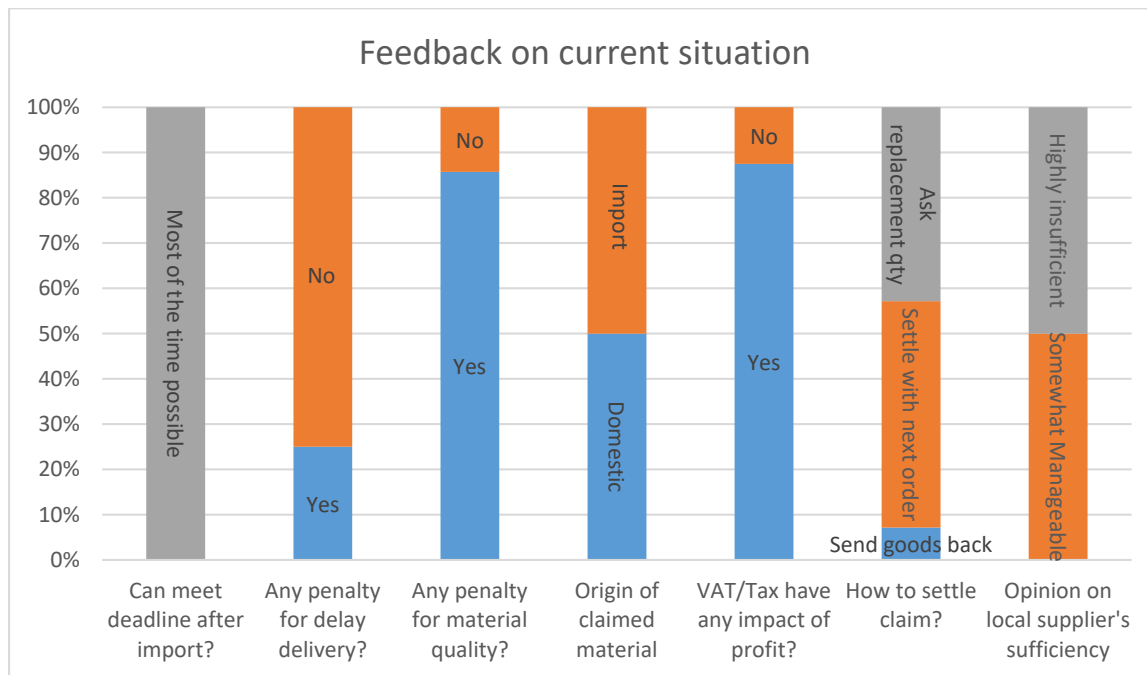


Figure 11

Availability of local sources: Availability of raw materials from domestic sources are matter of great concern to all of the interviewees as 50% of them said that existing sources are somewhat manageable while rest of them cited it to be highly insufficient.

Financial Impact: Out of all the interviewed factories, almost 90% think that imported goods VAT/TAX has impact on their profit/price and in most of the cases, these impacts are negative. However, 10% factories still believe that VAT/TAX don't have any impact on their profit/price.

3.2 Possibilities

From gathered information & figures illustrated in this report, it can clearly be stated that only PVC material and Foam have stable and good quality sources available in Bangladeshi domestic market which is sufficient to fulfill demand of domestic footwear industries. All other basic raw materials including Leather, PU or Microfibers, Outsole, Ornaments, Insole, Adhesive needs special and urgent attention as these raw materials remain import oriented mainly.

This report proposes that there is still ample opportunities of business expansion for Bangladeshi Footwear industries. As most of the raw materials are still import oriented, there's a vast opportunity of industrialization awaits for this country which will strengthen countries economy while eliminating unemployment problems.

Strengthening leading local factories backward integration will help those factories, as well as other factories directly. As they'll get these materials at reduced cost (due to no duty, less tax/vat) locally, it will give them opportunities to make them more competitive in global market by lowering their prices. On the other hand, it will give them opportunities of profit maximization as well.

Properly integrated backward chain will enable the factories to function autonomously without depending on other supplier bases. It will make them more confident and aggressive in production and will allow them to fulfill production commitment.

MOQ always plays a vital role in import oriented procurement system, so factories can't work on variety, instead they need to focus on volume of the products. With the support of strong and dependable backward integration of domestic business leaders, small manufacturers will have options to display volume products as well as fashion products to their customer bases which will increase their chances of getting orders.

Reduction of unemployment problem will increase social standards and standard of living.

So overall, this reports shares optimistic views for the future of this BI.

3.3 Suggestions for improving situation

This project also focused on finding any possible solution and suggestions that might help factories to enable proper Backward Integration in domestic supplier chain.

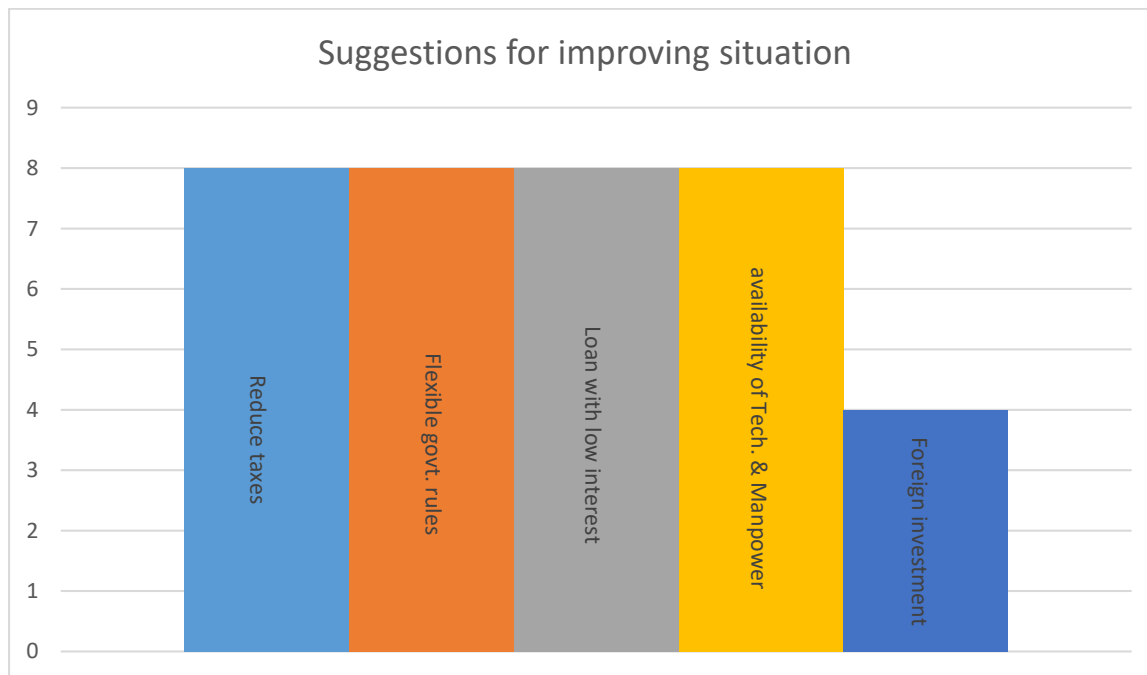


Figure 12

Major suggestion to enable proper backward integration includes but not limited to:

1. Reducing raw materials taxes
2. Make flexible government rules to encourage new entrepreneurs in these sectors.
3. Easy financing with low interest rate can be an excellent approach to expand current business, also encouraging new endeavors to come to light.
4. Making availability of technology and skilled manpower
5. Making foreign investment friendly policy. Foreign investments and other JV plans can solve most of the problems related to skill and technology. So government must focus on this option to increase foreign investment.

Chapter-4

Conclusion

As part of the rising economy of the next super economy of South Asia, Bangladesh, has a good opportunity to capture the large market share of footwear sector. With the trade war running between two super economic giants USA & China, Bangladesh can grab a large share of the shifting footwear market. With its semi-skilled and extremely economy manpower, Bangladeshi footwear industries can walk a long way if the Backward & Forward integrations are linked properly with the manufacturing hubs.

In this circumstance, with a very limited domestic RM sources, it will be nearly impossible to match the domestic and global demands. Besides, filling the gaps of raw materials will help to reduce dependency on imported goods which will not only save time & money, but will increase efficiency and productivity as well.

As like most of the development sectors, this sector will require a lot of attention from Government and Policy makers to make all the possibilities come to light.

ANNEX-1:

Questionnaire:

Your name :

Organization :

Your designation :

Number of employees:

1. When this organization started operations?

Please select year here

2. What is your main product?

☐ Sandal

☐ Formal Shoe

☐ Sports shoe

☐ Boot

☐ Others

(Please Specify)

PROCUREMENT SECTION:

3. What are the main raw materials for your product/s?

☐ Leather

☐ PU, Microfibers

☐ PVC

☐ Outsole

☐ Ornaments & Accessories

☐ Insole

☐ Foam

☐ Adhesive

☐ Others

(Please Specify)

Leather

4. Where do you buy leather from?

☐ Local Choose an item.

☐ Import Choose an item.

- ☐ Both
- ☐ Not needed
- 5. If local, where do you buy from?
 - ☐ Own manufacturing unit
 - ☐ Other domestic manufacturers
 - ☐ Not Applicable
- 6. Are you satisfied with the quality & services from local sources?
 - ☐ Yes
 - ☐ No
 - ☐ Not Applicable
- 7. If import, what's the reason for import?
 - ☐ Locally not available
 - ☐ Locally available, but capacity not fulfilling my demand
 - ☐ Locally available, but quality doesn't meet my demand
 - ☐ Locally available, but price too high
 - ☐ Locally available, but commitment & service too poor
 - ☐ Not Applicable
- 8. If import, how much duty & VAT you have to pay on imported leather?
- Choose an item.
- 9. If import, what's the lead time to get the product in-house?
- Choose an item.

PU/Micrifiber

- 10. Where do you buy PU/Microfiber from?
 - ☐ Local Choose an item.
 - ☐ Import Choose an item.
 - ☐ Both
 - ☐ Not needed
- 11. If local, where do you buy from?
 - ☐ Own manufacturing unit
 - ☐ Other domestic manufacturers
 - ☐ Not Applicable
- 12. Are you satisfied with the quality & services from local sources?
 - ☐ Yes
 - ☐ No
 - ☐ Not Applicable
- 13. If import, what's the reason for import?x
 - ☐ Locally not available
 - ☐ Locally available, but capacity not fulfilling my demand

- ☐ Locally available, but quality doesn't meet my demand
- ☐ Locally available, but price too high
- ☐ Locally available, but commitment & service too poor
- ☐ Not Applicable

14. If import, how much duty & VAT you have to pay on imported PU/Microfiber?

Choose an item.

15. If import, what's the lead time to get the product in-house?

Choose an item.

PVC

16. Where do you buy PVC from?

- ☐ Local Choose an item.
- ☐ Import Choose an item.
- ☐ Both
- ☐ Not needed

17. If local, where do you buy from?

- ☐ Own manufacturing unit
- ☐ Other domestic manufacturers
- ☐ Not Applicable

18. Are you satisfied with the quality & services from local sources?

- ☐ Yes
- ☐ No
- ☐ Not Applicable

19. If import, what's the reason for import?

- ☐ Locally not available
- ☐ Locally available, but capacity not fulfilling my demand
- ☐ Locally available, but quality doesn't meet my demand
- ☐ Locally available, but price too high
- ☐ Locally available, but commitment & service too poor
- ☐ Not Applicable

20. If import, how much duty & VAT you have to pay on imported PVC?

Choose an item.

21. If import, what's the lead time to get the product in-house?

Choose an item.

Outsole & insole

22. Where do you buy Outsole & insole from?

- ☐ Local Choose an item.
- ☐ Import Choose an item.
- ☐ Both

- ☐ Not needed
23. If local, where do you buy from?
- ☐ Own manufacturing unit
- ☐ Other domestic manufacturers
- ☐ Not Applicable
24. Are you satisfied with the quality & services from local sources?
- ☐ Yes
- ☐ No
- ☐ Not Applicable
25. If import, what's the reason for import?
- ☐ Locally not available
- ☐ Locally available, but capacity not fulfilling my demand
- ☐ Locally available, but quality doesn't meet my demand
- ☐ Locally available, but price too high
- ☐ Locally available, but commitment & service too poor
- ☐ Not Applicable
26. If import, how much duty & VAT you have to pay on imported Outsole/Insole?

Choose an item.

27. If import, what's the lead time to get the product in-house?

Choose an item.

Ornaments

28. Where do you buy Ornament from?
- ☐ Local Choose an item.
- ☐ Import Choose an item.
- ☐ Both
- ☐ Not needed
29. If local, where do you buy from?
- ☐ Own manufacturing unit
- ☐ Other domestic manufacturers
- ☐ Not Applicable
30. Are you satisfied with the quality & services from local sources?
- ☐ Yes
- ☐ No
- ☐ Not Applicable
31. If import, what's the reason for import?
- ☐ Locally not available
- ☐ Locally available, but capacity not fulfilling my demand
- ☐ Locally available, but quality doesn't meet my demand
- ☐ Locally available, but price too high

- ☐ Locally available, but commitment & service too poor
- ☐ Not Applicable

32. If import, how much duty & VAT you have to pay on imported Ornament?

Choose an item.

33. If import, what's the lead time to get the product in-house?

Choose an item.

34. If any of the products are imported, Can you meet your production deadline after getting the product in-house?

- ☐ Yes
- ☐ No
- ☐ Most of the time possible
- ☐ Most of the time not possible.

35. Did you ever face penalty from buyer due to delay in delivery?

- ☐ Yes
- ☐ No

36. Did you ever face penalty from buyer due to poor quality of material?

- ☐ Yes
- ☐ No

37. If you import raw materials, the additional VAT & duty have any impact on your product cost & profit?

- ☐ Yes
- ☐ No

38. If the imported material doesn't meet your requirement, how do you settle the claim?

- ☐ Send goods back to origin
- ☐ Ask for replacement qty
- ☐ Settle claim value with next order

39. Do you think the supplier's based on Bangladesh are sufficient to fulfill the Footwear industries demand?

- ☐ Sufficient
- ☐ Somewhat manageable
- ☐ Highly insufficient

40. What measures can be taken to improve situation to create new supplier base?

- ☐ Reducing raw material taxes
- ☐ Make flexible govt. rules
- ☐ Easy financing with low interest rate
- ☐ Making availability of technology and skilled manpower

ANNEX-2:

List of interviewed factories and person:

1. APEX Footwear Ltd.
 - a. Mr. Atikul Islam (Dty. Mgr, SCM)
2. BAY Footwear Ltd.
 - a. Mr. MD. Sunny (Asst. Mgr, SCM)
3. BMTF
 - a. Mr. Naimur Rahman (Manager, Sourcing & development)
4. FB Footwear Ltd.
 - a. Mr. Nazmul Hassan Biddut (Executive, SCM)
5. Bangladesh Footwear Ltd.
 - a. Mr. Mostafa Mahmud (Agm, Procument)
6. Pragati footwear Ltd.
 - a. Mr. Khairul huda Ohi (CEO)
7. Runner Footwear Ltd.
 - a. Mr. Easrib Sharik (Asst. Manager, SCM)
8. Walker Footwear Ltd.
 - a. Mr. Proshenjit Halder Topu (Asst. Manager, Buying)

References

1. <http://www.customs.gov.bd>
2. <https://www.nbr.gov.bd>
3. <https://www.apexfootwearltd.com>
4. <https://corporatefinanceinstitute.com/resources/knowledge/strategy/backward-integration/>