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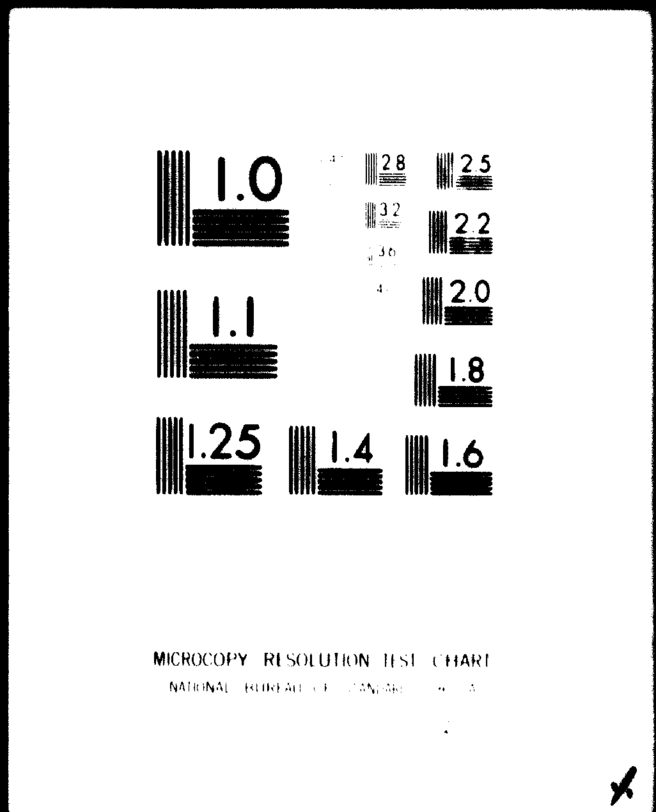

ADDITIONAL STUDY

ON

FOOTWEAR INDUSTRY IN CARICOM REGION

IS/RLA/72/101.

by

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OCTOBER 1974

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REGION: Member Countries of the Caribbean Community.

DUTY STATION: Guyana **DATE:** October, 1974

OFFICIAL: H.A. El-Sharawy

PROJECT NO: IS/RLA/72/101/11-01/12

FIELD OF WORK: Industrial Planning

ADDITIONAL STUDY ON

FOOTWEAR INDUSTRY IN CARICOM REGION

C O N T E N T S

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INTRODUCTION AND SUMMARY

A previous study on Footwear Industry in the CARIFTA/CARICOM Region was carried out by the UNIDO Senior Industrial Adviser assigned to CARICOM Secretariat, giving special attention to the interests of the LDCs.

However, in the First Meeting of the Working Party of CARICOM Industrial Planners held in Barbados on 3rd - 4th September, 1974, the meeting requested the UNIDO Senior Adviser to investigate the following additional points:

(a) to calculate separate consumption figures for the LDCs since their market can effectively be regarded as a sub-regional market;

(b) to re-calculate the Rate of Return on Capital, assuming a loan interest of 8%;

(c) to calculate the Local Value Added by the project proposed for the LDCs and to determine the Tax Holiday to which the project may be eligible under the Harmonisation of Fiscal Incentives Scheme.

The investigation of the above three points was, therefore carried out, especially that CARICOM Secretariat considered this a first priority.

In addition, the UNIDO Senior Adviser made new estimates for the projected consumption or demand of leather footwear by 1980 in the CARICOM Region and the ECCM Sub-region on the basis of a 3% Rate of Growth instead of the previous estimate based on a 2% rate.

The four points covering this additional study are discussed in the following.

/I. ...

I. CONSUMPTION OF FOOTWEAR IN THE LDCs

The LDCs have no footwear production on an industrial scale until present. Therefore, the consumption of footwear in the LDCs can be represented as the imports less re-exports.

Table 1 shows the apparent consumption of all types of footwear in the LDCs (1967-70).

TABLE 1

APPARENT CONSUMPTION OF ALL TYPES OF FOOTWEAR IN THE LDCs (1967 - 1970)

(000 pairs)

	1967	1968	1969	1970
TOTAL IMPORTS	1313	960	2948*	1721
TOTAL RE EXPORTS	9	19	13	11**
APPARENT CONSUMPTION	1304	941	2935*	1710**

* Imports of 1969 were particularly higher than actual demand as explained before in the previous Study on Footwear Industry in CARIFTA/CARICOM.

** Data on Re-export of most of the LDCs in 1970, are not available, and therefore the apparent consumption in 1970 would accordingly be higher than the actual demand in that year, although considerably less than the abnormal year 1969.

/Table 2 ...

Table 2 shows also the apparent consumption of leather footwear in the LDCs (1967-69).

TABLE 2

APPARENT CONSUMPTION OF LEATHER FOOTWEAR IN THE LDCS (1967-1969)

(000 pairs)

	1967	1968	1969
TOTAL IMPORTS	623	594	798*
TOTAL RE EXPORTS	7	17	4
APPARENT CONSUMPTION	616	577	794*

* Imports of 1969 were particularly higher than actual demand as explained before in the previous Study on Footwear Industry in CARIFTA/CARICOM.

/II. ...

II. ESTIMATION OF PROJECTED CONSUMPTION OF FOOTWEAR IN CARICOM AND LDCs

A - In the CARICOM Region

The projected consumption of all types of footwear and of leather footwear in the entire CARICOM Region has been re-estimated on the basis of a 3% rate of growth instead of a 2% rate of growth according to the previous study. This attempt was made since the present available data on the consumption of footwear are indicating a rate of growth which is much closer to 3% rather than 2%.

Tables 3 and 4 show these estimated projections for 1971 - 1980 taking 1967 as base year.

TABLE 3

PROJECTED CONSUMPTION OF ALL TYPES OF FOOTWEAR IN CARIFTA/CARICOM REGION (1971 - 1980)

Base Year 1967 = 10,000 (000 pairs)

1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
11,255	11,593	11,941	12,299	12,668	13,048	13,439	13,842	14,258	14,685

Rate of growth 3%

TABLE 4

PROJECTED CONSUMPTION OF LEATHER FOOTWEAR IN CARIFTA/CARICOM REGION (1971 - 1980)

Base Year 1967 = 3,450 (000 pairs)

1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
3,883	4,000	4,119	4,243	4,370	4,501	4,637	4,776	4,919	5,066

Rate of growth 3%

Table 3 shows that the projected consumption of all types of footwear in the entire CARICOM Region by 1980 would be about 14,700,000 pairs instead of 12,950,000 pairs, as estimated in the previous study which was based on a 2% rate of growth.

Table 4 shows that the projected consumption of leather footwear in the CARICOM Region would be about 5,100,000 pairs by 1980 instead of 4,800,000 pairs as estimated in the previous study which was based on a 2% rate of growth. In this case the balance between the total demand of 5,100,000 pairs in 1980 (based on 3% rate of growth) and the total available production capacities in the Region in 1976 (as given in the previous study), will be about 1,500,000 pairs, instead of 1,200,000 pairs (if based on 2% rate of growth).

The deficit production capacity of 1,500,000 pairs of leather footwear in the CARICOM Region by 1980 could, therefore, be included in the Regional Long-term Plan in the form of several footwear projects to be established in different locations in the Region.

B - In the LDCs

The projected consumption of the LDCs of all types of footwear and of leather footwear was also estimated on the basis of 3% rate of growth.

Tables 5 and 6 show these estimates for 1971 - 1980 taking 1967 as base year.

However, for the sake of comparison with the estimates given in the previous study, estimates of the projected consumption of all types of footwear and of leather footwear in the LDCs were also made on the basis of 2% rate of growth..

/Tables 5a ...

Tables 5a and 6a show these estimates for 1971 - 1980. It is the opinion of the Adviser that data given in Tables 5 and 6, based on 3% rate of growth, are the more likely possible projections.

TABLE 5

PROJECTED CONSUMPTION OF ALL TYPES OF FOOTWEAR IN THE LDCs (1971 - 1980)

Base year 1967 = 1304 (000 pairs)

1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
1468	1512	1557	1604	1652	1701	1752	1805	1859	1915

Rate of growth 3%

TABLE 5a

PROJECTED CONSUMPTION OF ALL TYPES OF FOOTWEAR IN THE LDCs (1971 - 1980)

Base year 1967 = 1304 (000 pairs)

1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
1411	1440	1469	1498	1528	1558	1590	1621	1654	1687

Rate of growth 2%

...

/TABLE 6 ...

TABLE 6

PROJECTED CONSUMPTION OF LEATHER FOOTWEAR

IN THE LDCs (1971 - 1980)

Base year 1967 = 616 (000 pairs)

1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
693	714	736	758	780	804	828	853	878	905

Rate of growth 3%

TABLE 6a

PROJECTED CONSUMPTION OF LEATHER FOOTWEAR

IN THE LDCs (1971 - 1980)

Base year 1967 = 616 (000 pairs)

1971	1972	1973	1974	1975	1976	1977	1978	1979	1980
667	680	694	708	722	736	751	766	781	797

Rate of growth 2%

/III. ...

III. RE-CALCULATION OF THE RATE OF RETURN ON CAPITAL FOR THE PROPOSED TWO PROJECTS FOR THE LDCs, ASSUMING A LOAN INTEREST OF 8%

At the request of the First Meeting of the Working Party of CARICOM Industrial Planners, the Senior Adviser re-calculated the Rate of Return on Capital, assuming 8% Loan Interest, in the case of the proposed Two Projects for the LDCs previously studied by him.

Table 7 shows the Operating Costs and Benefits for Project 1 (48,000 pairs per annum) on the basis of a loan interest of 8%. [redacted]

TABLE 7

PROJECT 1 : (48,000 pairs/annum)

OPERATING COSTS AND BENEFITS

(Assuming 100% Production and Sales Efficiency)

(US$000)

Year	Materials	Overhead (Other inputs)	Labour	Total Inputs	Sales	Operating Cash Flow
1	94	73.5	56	223.5	162	(61.5)
2	94	73.5	56	223.5	243	19.5
3	125.5	73.5	56	255	324	69.0
4	125.5	73.5	56	255	324	69.0
5	125.5	73.5	56	255	324	69.0
6	125.5	73.5	56	255	324	69.0
7	125.5	73.5	56	255	324	69.0
8	125.5	73.5	56	255	324	69.0
9	125.5	73.5	56	255	324	69.0
10	125.5	73.5	56	255	324	69.0

NOTES:
1. During the first year 75% of raw materials are used and 100% labour is engaged with 50% sales achieved.
2. During the second year 75% of raw materials are used and 100% labour is engaged with 75% sales achieved.
3. During the third year 100% production and sales efficiency achieved.

The following Table 8 shows the Amortization of Loan of US$160,000 at 8% for Project 1.

TABLE 8

PROJECT 1 : AMORTIZATION OF LOAN OF US$160,000

AT 8% INTEREST

(US$000)

Year	Interest	Principal	Total	Balance
0	6.0	-	6.0	160.0
1	12.8	-	12.8	160.0
2	12.8	15.0	27.8	145.0
3	11.6	16.2	27.8	128.8
4	10.3	17.5	27.8	111.3
5	8.9	18.9	27.8	92.4
6	7.4	20.4	27.8	72.0
7	5.8	22.0	27.8	50.0
8	4.0	23.8	27.8	26.2
9	2.1	26.2	28.3	-0-
10	-	-	-	-

NOTE: Loan of US$160,000 at 8% interest of which US$75,000 is used in year 0 with 2 years Moratorium and US$85,000 is used in year 1 with 1 year Moratorium. Repayment of Principal over 8 years thereafter.

The following Table 9 shows the Capital Cost and Net Cash Flow for Project 1 on the same basis of 8%. The Rate of Return in this case is 8%.

TABLE 9

PROJECT 1 : Capital Costs and Net Cash Flow
(Assuming 100% Production and Sales Efficiency)

(US$000)

Year	Loan Interest	Loan Principal	Machinery and Re-investment	Investment in Inventories	Total	Operating Cash Flow	Net Cash Flow
0	6.0	-	75.0	-	81.0	-	(81.0)
1	12.8	-	3.5	85.0	101.3	(61.5)	(162.3)
2	12.8	15.0	3.5	-	31.3	19.5	(11.8)
3	11.6	16.2	3.5	-	31.3	69.0	37.7
4	10.3	17.5	3.5	-	31.3	69.0	37.7
5	[illegible].9	18.9	3.5	-	31.3	69.0	37.7
6	7.4	20.4	3.5	-	31.3	69.0	37.7
7	5.8	22.0	3.5	-	31.3	69.0	37.7
8	4.9	23.6	3.5	-	31.3	69.0	37.7
9	2.1	26.2	3.5	-	31.8	69.0	37.2
10	-	-	-	-	-	69.0	154.0
Residual Values	Nil	Nil	Nil	85.0			

NOTES:

1. Loan of US$160,000 assumed to cover investments in machinery and inventories.
2. Additional re-investment for components of US$3,500 is assumed annually (other then loan) from year 1 to year 9.
3. Rate of Return on Capital, or the D.C.F. Rate of Return on Capital is 8%.

Table 10 shows Operating Costs and Benefits for Project 2 on the same basis of 8% interest.

TABLE 10

PROJECT 2 : Operating Costs and Benefits
(Assuming 100% Production and Sales Efficiency)

(US$000)

Year	Materials	Overheads (Other inputs)	Labour	Total Inputs	Sales	Operating Cash Flow
1	188	105	112	405	324	(81.0)
2	188	105	112	405	486	81.0
3	251	105	112	468	648	180.0
4	251	105	112	468	648	180.0
5	251	105	112	468	648	180.0

NOTES:

1. During the first year 7[illegible]% of raw materials are used and 100% labour is engaged with 50% sales achieved.
2. During the second year 75% of raw materials are used and 100% labour is engaged with 75% sales achieved.
3. During the third year onward 100% production and sales efficiency achieved.

The following Table 11 shows the Amortization of Loan of US$231,000 at 8% interest.

TABLE 11

PROJECT 2 : Amortization of Loan of US$231,000 at 8% Interest

(US$000)

Year	Interest	Principal	Total	Balance
0	6.0	-	6.0	231.0
1	18.5	-	18.5	231.0
2	18.5	51.2	69.7	179.8
3	14.4	55.3	69.7	124.5
4	10.0	59.7	69.7	64.8
5	5.2	64.8	70.0	-0-

NOTE: Loan of US$231,000 at 8% interest of which US$75,000 is used in year 0 with 2 years Moratorium and US$156,000 is used in year 1 with 1 year Moratorium Repayment of Principal over 4 years thereafter.

The following Table 12 shows the Capital Costs and Net Cash Flow for Project 2 on the same basis of 8% interest. The Rate of Return on Capital in this case is 10%.

TABLE 12

PROJECT 2 : Capital Costs and Net Cash Flow
(Assuming 100% Production and Sales Efficiency)

(US$000)

Year	Loan Interest	Loan Principal	Machinery and Re-investment	Investment in Inventories	Total	Operating Cash Flow	Net Cash Flow
0	6.0	-	75.0	-	81.0	-	(81.0)
1	18.5	-	7.0	156	181.5	(81.0)	(262.5)
2	18.5	51.2	7.0	-	76.7	81.0	4.3
3	14.4	55.3	7.0	-	76.7	180.0	103.3
4	10.0	59.7	7.0	-	76.7	180.0	103.3
5	5.2	64.8	-	-	70.0	180.0	266.0
Residual Values	Nil	Nil	Nil	156			

NOTES:
1. Loan of US$231,000 assumed to cover Investments in Machinery and Inventories.
2. Additional Re-investment for components of US$7,000 is assumed annually (other than Loan) from year 1 to year 4.
3. The internal Rate of Return on Capital, or the D C F Rate of Return on Capital is 10%.

The Amortization of Loan of US$231,000 and the Rate of Return on Capital have also been calculated on the basis of a 6% Loan Interest on account of the fact that the life-time of Project 2 is shorter than Project 1 (only 5 years).

Table 13 shows the Amortization of Loan of US$231,000 at 6% interest. The Rate of Return on Capital in this case is 11% as shown in Table 14.

TABLE 13

PROJECT 2 : AMORTIZATION OF LOAN OF US$231,000 AT 6% INTEREST

(US$000)

Year	Interest	Principal	Total	Balance
0	4.5	-	4.5	231.0
1	13.9	-	13.9	231.0
2	13.9	52.8	66.7	178.2
3	10.7	56.0	66.7	122.2
4	7.3	59.4	66.7	62.8
5	3.8	62.8	66.6	-0-

NOTE: Loan of US$231,000 at 6% interest, of which US$75,000 is used in year 0 with 2 years Moratorium and US$156,000 is used in year 1 with 1 year Moratorium. Repayment of Principal over 4 years thereafter.

TABLE 14

PROJECT 2: Capital Costs and Net Cash Flow
(Assuming 100% Production and Sales Efficiency)

(US$000)

Year	Loan Interest	Loan Principal	Machinery and Re-investment	Investment in Inventories	Total	Operating Cash Flow	Net Cash Flow
0	4.5	-	75.0	-	79.5	-	(79.5)
1	13.9	-	7.0	156	176.9	(81.0)	(257.9)
2	13.9	52.8	7.0	-	73.7	81.0	7.3
3	10.7	56.0	7.0	-	73.7	180.0	106.3
4	7.3	59.4	7.0	-	73.7	180.0	106.3
5	3.8	62.8	-	-	66.6	180.0	269.4
Residual Values	Nil	Nil	Nil	156			

NOTES: 1. Loan and Additional Re-investment as in Table 12 except that Loan Interest is 6%.

2. The Internal Rate of Return on Capital is 11%.

IV. CALCULATION OF THE LOCAL VALUE ADDED BY THE PROJECTS PROPOSED FOR THE LDCs AND DETERMINATION OF THE TAX HOLIDAY

This calculation was made for the proposed Projects 1 and 2 as shown in Tables 15 and 16. In both projects the unweighted as well as the weighted Local Value Added is above 50%.

Therefore, the Tax Holiday to which either project may be eligible under the Harmonization of Fiscal Incentives Scheme is 15 years.

TABLE 15

CALCULATION OF THE LOCAL VALUE ADDED AND TAX HOLIDAY FOR PROJECT 1 PROPOSED FOR THE LDCs

	US$	US$
Total Ex-Factory Sales		324,000
Deduct:		
A. Payments made in respect of:		
(i) Cost of raw materials, fuels, components and raw material content of locally produced components imported from outside CARICOM	125,500	
(ii) Salaries and wages paid to non-CARICOM nationals Factory Manager $12,000 Production Trainer $ 8,000	20,000	
(iii) Profits and dividends paid to non-CARICOM Residents	-	
(iv) Interest (does not include interest paid to a Resident Branch or agency of a Bank not Resident in a CARICOM Country)	-	
(v) Management Charges) Paid or accruing to persons or companies not resident in a CARICOM Country	-	
(vi) Royalties)	-	
(vii) Licences)	-	
(viii) Fees)	-	
(ix) Professional Services)	-	
(x) Other Payments)	-	
Total Payments (A)	145,500	
B. Depreciation of imported plant, machinery, equipment and spare parts	7,500	
Total Deductions		153,000
Excess (Total Sales - Total Deductions)		171,000

/Local ...

TABLE 15 (cont'd)

Local Value Added

$$= \frac{171,000 \times 100}{324,000} = 52.8\%$$

Local Labour Weighting (according to agreed upon concept in CARICOM)

$$= \frac{56,000 \times 100}{324,000} = 17.3\%$$

Weighted Local Value Added

$$= \frac{52.8 \times (100 + 17.3\%)}{100} = 61.9\%$$

Since the Weighted Local Value Added is more than 50% of the Value of Ex-Factory Sales,

therefore, with respect to the Harmonization of Fiscal Incentives Scheme of CARICOM, this project belongs to Group I Industries, and will be eligible for a relief from Tax and Customs Duties (holiday) for 15 years.

/Table 12 ...

TABLE 16

CALCULATION OF THE LOCAL VALUE ADDED AND TAX HOLIDAY FOR PROJECT 2 PROPOSED FOR THE LDCs

		US$	US$
Total Ex-Factory Sales			648,000
Deduct:			
A. Payments made in respect of:			
(i) Cost of raw materials, fuels, components and raw material content of locally produced components imported from outside CARICOM		251,000	
(ii) Salaries and wages paid to non-CARICOM nationals			
Factory Manager $12,000 Production Trainer $ 8,000		20,000	
(iii) Profits and dividends paid to non-CARICOM Residents		-	
(iv) Interest (does not include interest paid to a Resident Branch or Agency of a Bank not Resident in a CARICOM Country)		-	
(v) Management Charges	Paid or accruing to persons or companies not resident in a CARICOM Country	-	
(vi) Royalties		-	
(vii) Licences		-	
(viii) Fees		-	
(ix) Professional Services		-	
(x) Other Payments		-	
Total Payments (A)		271,000	
B. Depreciation of imported plant, machinery, equipment and spare parts		15,000	
Total Deductions			286,000
Excess (Total Sales - Total Deductions)			362,000

/Local Value ...

TABLE 16 (cont'd)

Local Value Added

$$= \frac{362,000 \times 100}{648} = 55.9\%$$

Local Labour Weighting (according to agreed upon concept in CARICOM)

$$= \frac{112,000 \times 100}{648,000} = 17.3\%$$

Weighted Local Value Added

$$= \frac{55.9\% \times (100 + 17.3\%)}{648,000} = 65.6\%$$

Since the Weighted Local Value Added is more than 50% of the Value of Ex-Factory Sales,

therefore, with respect to the Harmonization of Fiscal Incentives Scheme of CARICOM, this project belongs to Group I Industries, and will be eligible for a relief from Tax and Customs Duties (holiday) for 15 years.

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