

FURNITURE INDUSTRY IN DAMIETTA

AN OVERVIEW

Submitted by:

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To

DEVELOPMENT ASSOCIATES

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(CCLS) Project**

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ACRONYMS

BOD	Board of Directors
CAPMAS	Central Authority for Public Mobilization & Statistics
CAD	Computer Aided Design
CAM	Computer Aided Manufacture
DEPRA	Development Economic Policy Reform Project
ECES	Egyptian Center for Economic Studies
EXPOLINK	Egyptian Exporters Association
FAS	Foreign Agricultural Service
ILD	Instituto Libertad y Democracia
LRF	Legal & Regulatory Framework
MOFT	Ministry of Foreign Trade
MOTS	Ministry of Trade and Supplies
NGOs	Non-Governmental Organizations
SMEs	Small & Micro Enterprises
TQM	Total Quality Management
UNIDO	United Nations Industrial Development Organization
USDA	US Department of Agriculture

TABLE OF CONTENTS

Acknowledgement	2
	3
Acronyms	
I. The Furniture Manufacturing Sector	4
A. Brief Historical Overview	5
B. Size Distribution	5
C. Growth	6
D. Foreign Trade Balance	8
II. Conditions Facing Furniture Manufacturing	10
A. Input Conditions	10
B. Process (Production) Conditions	14
C. Marketing Conditions	16
III. The Macro-Environment	17
A. The Legal & Regulatory Framework	17
B. The Institutional Framework	18
C. General Economic Conditions	19
IV. General Recommendations	19
V. Recommendations Matrix	21

I. The Furniture Manufacturing Sector

A. Brief Historical Overview

Egypt has a long tradition in furniture manufacturing that spans for centuries, if not millennia, during which the Egyptian artisan was exposed to several influences that have similarly affected Egyptian history and thought. These include Coptic, Islamic, French and British influences that are still obvious in today's Egyptian households and furniture. In the early 20th century, with the influx of foreign minorities, foreign French and Italian steel furniture manufacturing companies started to appear in Egypt to cater for their needs. With the increase in production and the rise of the 1952 regime, furniture imports were ended in the early fifties and exports started by the end of the decade. Throughout the 60s and early 70s exports were mainly targeting the former Soviet Union and the Eastern bloc. During the latter half of the seventies Egyptian furniture began reaching western markets. By the eighties however, the quality of the furniture products deteriorated, and Egypt started importing furniture¹.

B. Size Distribution

The furniture manufacture sector in Egypt, like the rest of the Egyptian manufacturing sector, has a characteristic size distribution that is numerically skewed to the favor of micro (1-4 employees) establishments. As per the 1996 census conducted by the Central Authority for Public Mobilization and Statistics (CAPMAS) there were 70,905 private establishments engaged in furniture manufacturing with an average size of 2.7 workers per establishment. The following table (based on the same census) compares the size distribution of Egyptian manufacturing enterprises in general to the furniture manufacture sector both in Egypt and in Damietta.

Sector/Subsector	Size Distribution			
	Micro (1-4)	Small (5-14)	Medium (15-49)	Large (> 50)
Manufacture (Egypt)	83.91%	13.75%	1.78%	0.56%
Furniture (Egypt)	93.26%	6.46%	0.25%	0.03%
Furniture (Damietta)	92.39%	7.51%	0.09%	0.01%

Size distribution within the furniture sector appears to be more skewed towards micro enterprises than the manufacture sector. Damietta's furniture manufacturing sector seems to mirror the sector on the national level, though with a slightly larger average firm size of 2.8 workers.

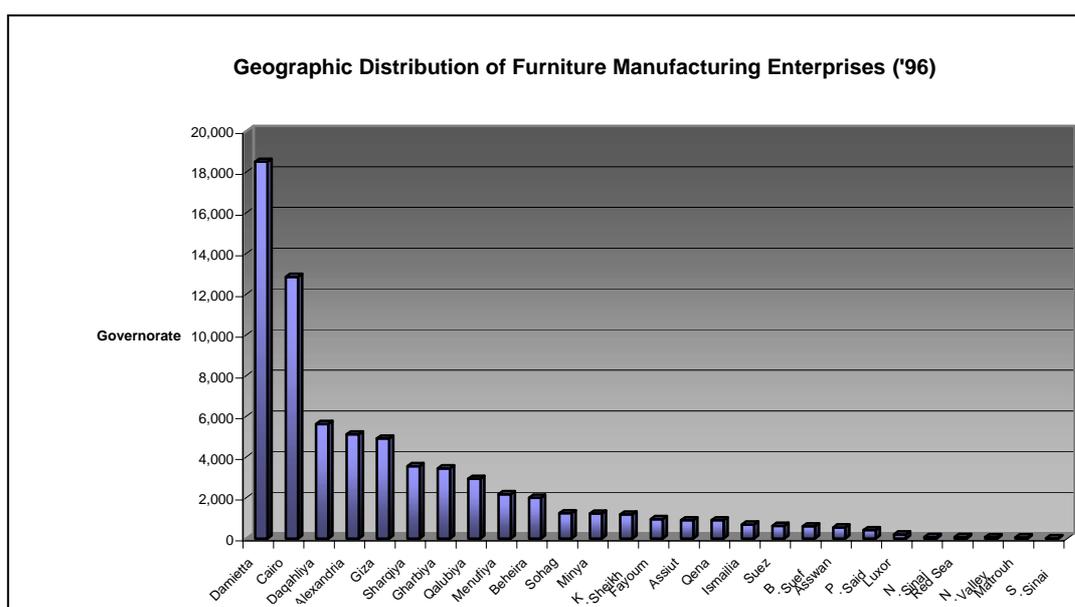
Accurate figures for the size of the sector in Damietta are almost non-existent. CAPMAS most recent (1996) data show 18,507 enterprises out of a total of 28,569 manufacturing enterprises in Damietta. Other estimates range from 36,000 to 60,000 establishments, if not more². This difficulty, in addition to the various factors rendering

¹ Development Economic Policy Reform Analysis (DEPRA) Project, Enhancing Egypt's Exports: Annex: Economic Analysis of Five Industries. February, 1999. P. 71-72.

² Collaboration for Community Level Services (CCLS) Project, Collaboration for Community Level Services in Dumyat: Preliminary Research Findings and Implications. (Unpublished)

national statistics extremely unreliable, stems from the existence of a massive informal sector in furniture manufacturing in Damietta.

Damietta is traditionally considered the focus of furniture manufacturing in Egypt. Estimates regarding the share of Damietta in the gross production of furniture in Egypt range from 40%, as reported by the Development Economic Policy Reform Project (DEPRA)³, to 80%, as reported by the Ministry of Trade & Supplies (MOTS)⁴. Damietta alone, per official statistics (CAPMAS), accounts for over 1/4th of the enterprises working in furniture manufacturing, as well as 1/4th of the entire labor force in the sector, ranking the highest by far in both categories across all Egyptian governorates.



C.

Growth

<i>Size Category</i>	<i>Factor of Change (76-86)</i>		<i>Factor of Change (86-96)</i>	
	<i>Damietta</i>	<i>Egypt</i>	<i>Damietta</i>	<i>Egypt</i>
<i>Micro (1-4 workers)</i>	1.58	1.55	1.39	1.72
<i>Small (5-14 workers)</i>	1.08	1.5	6.35	4.17
<i>Medium (15-49 workers)</i>	2.8	2.56	1.21	2
<i>Large (above 50 workers)</i>	3	1	0.33	1.15
<i>Total Sector</i>	1.57	1.55	1.48	1.79

Examining the results of the last three censuses conducted by CAPMAS reveals that Damietta however has started to lose its status in the Egyptian furniture industry between the two census years of 1986 and 1996, compared to the 10 year period, separating the 1976 & 1986 censuses. During the period (76-86) the number of furniture

³ Development Economic Policy Reform Analysis (DEPRA) Project, An Egyptian Furniture Industry Assessment; Part I: Trade Policy and Market Opportunities, August 1999. P.3

⁴ Ministry of Trade & Supplies (MOTS), Foreign Trade Sector, A Study of the Export Efficiency of Egyptian Production of Wood Products, 1999 (Unpublished).

manufacturing enterprises witnessed a net growth by a factor⁵ of 1.57, which is higher than the 1.55 by which the sector grew all over Egypt. During the 86-96 decade however, the growth of the sector in Damietta dropped to a factor of 1.48 compared to a rise in the all Egypt factor, which stood at 1.79. The following table takes a closer look at the growth pattern across the different size categories (micro, small, medium and large):

What the above table essentially means is that during the 86-96 decade, and contrary to the earlier decade of 76-86, the furniture sector in Damietta has been growing at a slower rate than it has been in Egypt as a whole.

Taking the above within the context of the Dossenbach typology⁶ of Egyptian furniture manufacturers shown on the opposite box is quiet revealing. Firms identified by Dossenbach as having a capacity to export all fall in our “large” enterprise category. As the table above shows, this size category has witnessed marginal net growth in the furniture sector all over Egypt (a factor of 1.15). Moreover, it has actually witnessed a significant decline (a factor of 0.33) in Damietta between 1986 and 1996, thus signifying an actual drop in Damietta’s furniture exports.

<u>Dossenbach’s Typology of Furniture Manufacturers in Egypt</u>	
❖	Type I (< 20 workers): small, outdated, undercapitalized, unfocused, cottage industry with a low probability to export.
❖	Type II (20 – 50 workers): small outdated unfocused with little or no systems and a very little likelihood to export successfully.
❖	Type III (50 – 150 workers): some updated machinery and equipment, maybe focused, limited systems in place, with some export potential.
❖	Type IV (150+ workers): some updated machinery and equipment, maybe focused, with export potential or limited exporting now.

MOTS data covering the period 93/94 – 96/97 point to a drop in production from L.E. 2 billion to L.E 1.1 billion⁷. The United Nations Industrial Development Organization (UNIDO) sources estimate a drop in the value added from \$35,644,000 in 1985 to \$28,156,000 in 1996. Moreover, during the period 85-98, the same source’s statistics point to a negative average annual growth rate in value added of –0.71%⁸.

At present, the furniture industry accounts for 0.3% of the country’s total industrial output, its contribution to overall output has fallen from 0.65% a decade ago as a

⁵ Calculated by dividing the number of establishments recorded at the '86 census by that recorded at the earlier census.

⁶ Dossenbach, Tom, Furniture Sector Export Growth: Assessment and Strategy”, Expolink, October, 1998. P. 3.10

⁷ Ministry of Trade & Supplies (MOTS), Foreign Trade Sector, A Study of the Export Efficiency of Egyptian Production of Wood Products, 1999 (Unpublished).

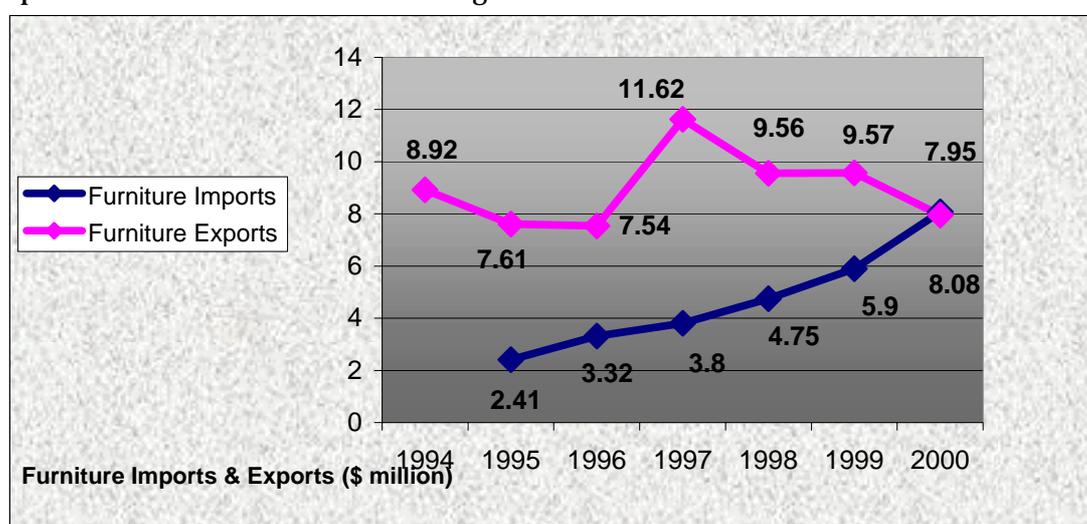
⁸ www.unido.org/data/stats/

number of other industries have flourished (e.g., food products, refined petroleum, non-metallic mineral products, non-electrical machinery and apparel)⁹.

D. Foreign Trade Balance

The following graph compares the development of Egypt's furniture exports and imports starting the mid-90s. If we take 1994 as a starting point, one would find that Egypt's exports have declined from about \$9 million in 1994 to less than \$8 million in the year 2000. On the other hand, our imports show an exponential increase from less than \$2.5 million in 1995 to over \$8 million in 2000.

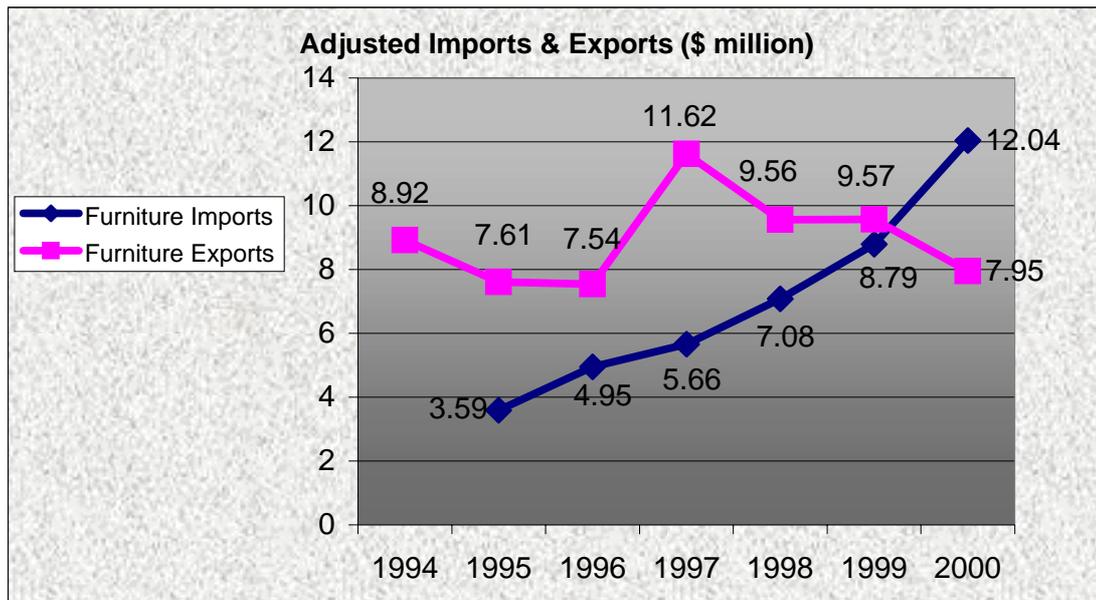
Even if the year 1995 is taken as a starting point (hence showing a marginal increase in our furniture exports from above \$7.5 million to less than \$8 million in 2000), the fact remains that our balance of trade has deteriorated significantly over the last 5 years from a positive value of \$5.2 million to a negative value of -0.13 million in 2000.



This takes place at the time when furniture industry is one of the most highly protected industries in Egypt. While the mean average tariff for manufacturing activities in Egypt is just over 25%, the tariff for furniture imports is 40%, ranking fourth after automobiles, liquor and tobacco manufacturing. Economists estimate that this 40% tariff has led to a 49% decline in the volume of imports¹⁰. If not for this artificial support, the situation would have been as shown in the following graph.

⁹ Development Economic Policy Reform Analysis (DEPRA) Project, An Egyptian Furniture Industry Assessment; Part I: Trade Policy and Market Opportunities, August 1999. P.3

¹⁰ Ibid. p. ix



As the above graph shows, our balance of trade would have deteriorated faster ending up with a negative balance of more than \$4 million in the year 2000, if not for the 40% tariff on imports. In fact comparing the two graphs one would say that what the tariff did was to delay the inevitable.

Taking either graph (the actual or the adjusted balance of trade), one cannot escape the conclusion that furniture manufacturing is an industry in crisis. This crisis does not manifest itself merely in the fact that Egypt is rapidly losing its share in the global market. Despite the frequently uttered claim that due to high tariffs and the transaction costs of exporting, the local market has proven more lucrative in the recent years than export markets, Egypt is also rapidly losing the local market as well. In short, Egyptian furniture is increasingly becoming uncompetitive.

While the loss of market share in the global market constitutes a blow to the larger enterprises in the industry, the loss of market share in Egypt constitutes a fatal blow to the vast sea of micro and small and medium entrepreneurs, the vast majority of whom rely exclusively on the local market. In a few years, with the removal of tariffs and other forms of trade barriers (including the 40% tariff), the livelihood of those working in this segment of the furniture sector will be severely compromised.

Currently, as one expert puts it, “the sector as a whole is generally 20 to 30 years behind its world competitors”¹¹. Several factors both internal and external to the industry have combined to lead to this situation. The next section attempts to outline and analyze some of these factors.

¹¹ Dossenbach, Tom, Furniture Sector Export Growth: Assessment and Strategy”, Expolink, October, 1998. p. 3-12.

II. Conditions Facing Furniture Manufacturing

A reading of the situation suggests that the sector is facing constraints in virtually every aspect of its operations including inputs, manufacturing, management, and marketing. These intersect with other significant constraints related to the regulatory framework, the general economic situation and other aspects of the macro-environment.

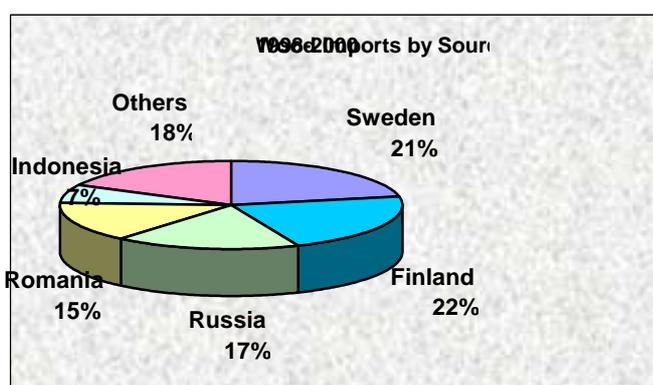
A. *Input Conditions:*

With the possible single exception of labor, furniture manufacturing relies on importing all of its inputs including machinery and tools, raw wood, glues, finishing paints and stains and fittings. The production-weighted average tariff on inputs is as high as 25%, thus raising the production costs¹². Price however is not the only constraint. These inputs, especially wood, were reported to be both expensive and of poor quality.

1. Raw Material

- *Lumber*

Egypt is not a wood producer. Accordingly, it has to rely on wood imported from abroad¹³. Studies show that a major problem facing furniture manufacturers is the **poor quality** of wood manifesting itself in high moisture content, infestation with insects, and lack of clarity (has more knots than adequate).



According to furniture experts, moisture content in wood should be in the range of 6-8%, otherwise furniture will suffer from warped panels, splits, cracks and failed glue joints. Reports indicate that the moisture content of the wood used in furniture manufacturing in Egypt is usually above 15%. In fact it was reported that in some cases wood imports were admitted into the country while having 40% moisture levels¹⁴. According to a report issued by the US Department of Agriculture (USDA) in 1999, with the purpose of informing US wood exporters about the Egyptian market, "Egyptian importers and end-users prefer to buy lumber with moisture content not exceeding 19% at the time of inspection."¹⁵

¹² Development Economic Policy Reform Analysis (DEPRA) Project, An Egyptian Furniture Industry Assessment; Part I: Trade Policy and Market Opportunities, August 1999. P. 19-20.

¹³ Most of the wood imported by Egypt (90%) is softwood, which is used by the construction sector (70%), with the remaining 30% for doors, windows, and other purposes, including low-quality furniture. Hardwood is almost exclusively used for furniture manufacturing (see USDA/FAS/Global Agricultural Information Network Report # EG9028, Egypt: Forests Products, 1999. P. 2.)

¹⁴ As reported by Dossenbach (op cit.)

¹⁵ USDA/FAS/Global Agricultural Information Network Report # EG9028, Egypt: Forests Products, 1999. P. 3.

Most lumber is imported from eastern European countries (see chart above)¹⁶ that lack proper drying technology and equipment. Most imported lumber is shipped to Alexandria, where there are no importers or distributors who have drying equipment. Egyptian manufacturers have to dry their wood using vacuum kilns, which do not produce the best results¹⁷.

While some accusations were made against some wood importers who sought to realize quick profits by selling cheap wood, it is also true that there is a weakness, if not a lack, of grade regulation that allowed for the importation of poor quality lumber. In either case, the fact remains that, as the most recent USDA report informs potential US wood exporters, the Egyptian hardwood market is "more price-sensitive than quality sensitive"¹⁸. Remarks pointing to the same conclusion were made by Dossenbach, in his 1998 report on the furniture industry in Egypt.

Despite the above, there are signs of quality sensitivity that are slowly starting to appear in the market. Moreover, the Damietta governor has taken steps to prevent the entry of this low-quality wood through Damietta port. Nevertheless, low quality wood still finds its way to the market through the Alexandria port, which accounts for almost 70% of the wood that enters Egypt¹⁹.

A related problem is the relatively *high price* of good wood, which seem to have multiple causes:

1. Increasing the import tariffs on wood from 5% to 8% (in addition to 5% sales tax and 3% customs fee)²⁰.
2. Rise in the US \$ exchange rate.
3. Reportedly, there was a decline in the global production of wood, due to pressures from environmental activists.
4. The application of the second and third stages of the sales tax²¹.

The above factors have combined to raise the price of high-quality wood. For example, according to recent estimates, the price of red wood has increased from L.E.1,900/m to L.E. 2,200/m. This naturally raises the production costs in general and pushes small workshops to buy low quality wood due to its cheaper price and their inability to buy better quality wood.

¹⁶ Source: Trade Point, Ministry of Foreign Trade (unpublished report, specially generated for this assignment).

¹⁷ Dossenbach, Tom, Egypt: The New Frontier?, W&WP, January 2001, p.1/4.

¹⁸ USDA/FAS/Global Agricultural Information Network Report # EG9028, Egypt: Forests Products, 2000. P. 4

¹⁹ Ibid, p.3.

²⁰ According to the Chairman of the Wood Importers Branch in the Federation of Chambers of Commerce, this raise has actually lead to a 60% increase in prices. A weekly paper has recently reported that there are rumors that the GOE shall raise the tariff on imported wood to 30% (see The Furniture Business, El-Alam El-Yoam, 11/9/2001).

²¹ The Furniture Business, El-Alam El-Yoam, 11/9/2001.

- *Panelwood*

The panelwood used was similarly reported to be of low quality. Some of the defects cited include lack of uniform thickness and lack of proper drying thus leading to voids, uneven places and wavy panels.

- *Veneer*

Veneer imports were likewise reported to be of a low quality due to high import dues on high-quality veneer, thus adversely affecting the end-product quality.

- *Staining & Finishing Material*

The industry, with a few exceptions, still relies on shellac and varnish in finishing the product, as opposed to the better quality nitrocellulose lacquer, which is currently in demand in global markets²².

2. Machinery and Equipment

In addition, tariffs and sales tax on tools and machinery raise the production costs and contribute to pushing Egyptian furniture manufacturers out of competition. This takes place while, as Mr. Taqey Allah Helmy, a leading industry figure, argues that the industry is facing intense competition from Europe due to their use of modern technologies that enable them to produce better quality at larger quantities and at relatively lower costs²³. In fact several experts have stressed the need to enhance and upgrade the mechanization and computerization of furniture production in order to minimize lumber waste, produce better quality and decrease production costs, hence enabling the sector to become more competitive.

There is also a need to use better tools and fixtures alongside the machinery. In his trip to Egypt Tom Dossenbach made the observation that “finding good quality screws is a challenge in some areas of the country”. Not using good quality fixtures does not only affect the appearance of the product. For example, good fastening devices add to the structural integrity of the product. It should be noted that many manufacturers do not use such devices because they are not made available. In addition, even when available, import tariffs and sales tax may prohibitively raise their prices discouraging small producers from buying them²⁴.

3. Labor

Labor, especially skilled labor, is considered by many to be the main competitive advantage the industry has. For years, if not decades, Damietta was famous for its craftsmanship. In addition, the labor costs in Egypt are still relatively low compared to other countries. Lack of skilled labor and its migration to other activities however, has lately been a recurrent complaint. In fact it has also been argued that neighboring

²² A fairly comprehensive analysis is found in Tom Dossenbach's Furniture Sector Export Growth: Assessment and Strategy”, Expolink, October, 1998

²³ The Furniture Business, El-Alam El-Yoam, 11/9/2001

²⁴ Dossenbach, Tom, Egypt: The New Frontier?, W&WP, January 2001, p.2/4.

countries like Tunisia and Libya are currently attracting labor from the furniture sector in Damietta.

These long held beliefs regarding the comparative advantage derived from labor, as well as its low costs however might need to be reconsidered. UNIDO statistics show a negative average annual growth rate of value added per employee of -6.27%, thus indicating an exponentially diminishing labor productivity in this sector. Moreover, the value added per employee (at current prices) has similarly declined from \$7,075 to \$2,902 during the period from 1985 to 1999²⁵.

In addition, several industrialists in the sector argue that manual carving no longer constitutes a competitive edge in the first place. Modern technologies are now able to produce the output of the manual carver more efficiently, accurately, on a much larger scale, and at a relatively lower cost²⁶.

4. Designs

Designs of exported furniture were a major source of complaints in export markets. The traditional styles that Egypt, especially Damietta, has excelled in producing are no longer in demand as they used to be decades ago. This, it should be noted, is not only the case with export markets. Even in the local Egyptian market, traditional highly ornate designs are increasingly losing market share to simpler and more practical furniture that does not involve as much carving.

Design does not only involve the appearance of the furniture unit, but also its intended use. In this regard, professional market research is of paramount importance. For example, as a 1998 report argues, formal dining has diminished, thus leading to lower demand on the traditional dining room. This has lead furniture designers to design new products that are more suitable for the new lifestyle that emerged in recent years. In addition to the above, design involves the creation and establishment of a 'character', and hence a market niche, for furniture products. Egyptian manufacturers have been focusing on reproducing Italian and French style furniture, rather than producing 'Egyptian' furniture that can be identified and actively sought on the market²⁷.

The virtual absence of professional furniture designers from the Egyptian furniture industry poses a threat that has to be met and resolved if the Egyptian furniture industry is to become competitive. Competitors to Egypt are increasingly relying on computer-aided design (CAD) and computer aided manufacture (CAM) applications to produce sophisticated furniture effectively and efficiently.

5. Financial Tools and Mechanisms

These include a range of financial products that should be adequately and efficiently provided for any industry to flourish. Such tools and mechanisms include, among others:

²⁵ www.unido.org/data/stats/

²⁶ The Furniture Business, El-Alam El-Yoam, 11/9/2001

²⁷ Dossenbach, Tom, Furniture Sector Export Growth: Assessment and Strategy", Expolink, October, 1998. p. 4.5

- Short-term credit for working capital requirements, especially for small and micro enterprises.
- Long-term credit to facilitate the acquisition of assets and machinery.
- Leasing to facilitate the growth of the sector's industrial base.
- Factoring to ease liquidity constraints facing manufacturers.
- Trade financing.

These financial products need to be made available on the bases of expanded outreach, financial soundness and sustainability, as well as economic costs, in order to facilitate industrial development as a whole.

6. Other Inputs

Other inputs were also problematic especially in the case of Damietta. These included irregular electrical supply and water supply, both of which affect the production process by wasting time, as well as possibly having negative repercussions on the state of certain equipment.

B. Process (Production) Conditions:

Overall, as mentioned above furniture manufacturing in Egypt is estimated to be 20 –30 years behind its competitors. Furniture manufacturing faces various constraints that are faced by the Egyptian industry at large. However, it has some basic characteristics that should be considered.

Quality Control

The current position (and trend) of the Egyptian furniture in both the global and the local markets is largely a result of its deteriorating quality. While, as demonstrated above, the poor quality of raw wood is a major reason for this situation, there are other aspects involved as well.

For example, the furniture manufacturing process is a complex multi-staged process that is traditionally divided among different sub-sectoral enterprises. These are engaged in several activities, including:

- Wood-cutting
- Carpentry
- Carving
- Staining and polishing
- Upholstery.

In addition, it involves other supporting industries, like glass and marble, as well as traders and manufacturers of metal fittings and various accessories. These constitute some of the links in the value chain of the furniture industry, at each of which value is added to the product. While bigger size enterprises tend to consolidate at least most of the above processes in their plants, the fact remains that the vast majority of producers, predominantly of the micro and small size, are engaged in a complementary relationship with other enterprises involved in other aspects or stages of the process.

The complexity of the process is a challenge that quality control efforts have to face. If any of the enterprises involved in any of the stage of the process underperforms for any reason, the end result would be a poor quality uncompetitive product. The challenge, while still significant, becomes more manageable in the case of larger enterprise that have resorted to vertical integration. These however have to instill quality control procedures if they are to remain competitive, especially in global markets (which they are targeting), especially since in today's markets TQM, ISO and other quality assurance certifications and warranties bring added value to the product²⁸.

Another trait of the industry in its current state that poses quality challenges is the fact that furniture manufacturing is generally labor intensive in nature. This makes it difficult for the industry to compete with other countries that use mass production and advanced technological techniques. These techniques and the use of machinery enable them to standardize their production, reduce their costs and meet large orders. With the excessive reliance on manual labor on the other hand, the error factor is higher, standardization becomes more difficult and the likelihood of adequately meeting large orders is significantly reduced.

Finishing

Finishing is a common flaw in Egyptian industry. Likewise, in the case of Egyptian furniture manufacturing, finishing is a major concern for international and local buyers. In fact, some countries like Turkey, Israel and Saudi Arabia, import unfinished furniture from Egypt, and then re-export them after doing the finishing themselves²⁹.

While the world has already moved years ago to nitrocellulose finishing, Egyptian manufacturers, with few exceptions, are still reliant on shellac and varnishes, which do not produce the currently required quality, in addition to their adverse effects on the health of the workers³⁰.

In addition to the finishing material and systems used, the process of finishing itself was found to be lacking in several respect. For example more steps are needed in order to improve the finishing quality. Furthermore, contrary to the prevailing practice of undertaking the finishing process in open well-ventilated areas, "to produce a quality finish, relatively air-tight rooms will need to be constructed with air make up units to give clean air pressure inside these rooms"³¹. The construction of such rooms might be more difficult for micro and small manufacturers than it is for the more established ones.

Packaging

Packaging was reported as another problem with Egyptian furniture exports. Improper packing contributes to the deterioration of the quality, and sometimes the structural

²⁸ Ibid., p. 5.6 & Development Economic Policy Reform Analysis (DEPRA) Project, An Egyptian Furniture Industry Assessment; Part I: Trade Policy and Market Opportunities, August 1999. P. 14

²⁹ The Furniture Business, El-Alam El-Yoam, 11/9/2001

³⁰ Dossenbach, Tom, Egypt: The New Frontier?, W&WP, January 2001, p.2/4

³¹ Dossenbach, Tom, Furniture Sector Export Growth: Assessment and Strategy", Expolink, October, 1998. p. 5.6

integrity, of the product during the journey to its destination. Packaging has to be done in a way, and using materials, that allow the product to endure the trip to the customer³².

Specialization

Lack of product specialization was perceived by experts to be another challenge that has to be tackled to improve the competitiveness of the sector. Most manufacturers would try to manufacture any furniture product based on the customer's request. Needless to say, with the lack of specialization, quality becomes a challenging target. "A highly skilled and trained workforce can only be trained to make a limited number of furniture types of high quality standards." Some manufacturers on the other hand, again, predominantly large ones, have defined their area of strength and specialized in it. The result was in several instances a competitive product that performed adequately on both the global and the national levels³³.

C. Marketing Conditions

The balance of trade graphs, shown earlier, point to the current position and trends of Egyptian furniture in both the global and the Egyptian markets. While it can be deduced from the above discussion that product quality (in terms of design, quality of inputs, production and finishing) is a main impediment, other factors should also be considered. These include the lack of professional specialized marketing efforts whether on the level of the firm, the governorate, or the entire sector.

By now, it is an established fact that marketing should precede production; otherwise the producer would run the risk of ending up with a large stock of products, a phenomenon that the furniture sector is currently witnessing, despite the exponentially rising furniture imports. Unfortunately, it seems that this is not the prevailing practice in Egypt. Research shows that there is a need to develop and implement marketing tools and strategies on the firm level, the level of Damietta, and the level of the entire sector all over Egypt. Generally speaking, a marketing effort should start by identifying the market to be targeted, conducting market research to identify its needs, preferences, specifications, prices...etc., and then designing products that meet the market demand. In addition, aggressive marketing and advertisement efforts should be exerted to inform and educate potential buyers about the merits of the product.

In addition to quality and market sensitivity the Egyptian furniture manufacturing sector lacks the concepts of customer service and support. To quote Dossenbach's report: "there seems to be a general attitude of poor response to problem solving. When problems occur, there is a resistance to prompt resolution of the problem."

Finally, market visibility is barely existent with a very low level of participation by manufacturers in trade shows and fairs in Europe, as well as an absence of promotional and public relations programs targeting potential buyers. In addition, sales material and brochures are "highly inconsistent and uninformative"³⁴.

³² Ibid, p.5.6.

³³ Dossenbach, Tom, Egypt: The New Frontier?, W&WP, January 2001, p.2/4

³⁴ See Dossenbach, Tom, Furniture Sector Export Growth: Assessment and Strategy", Expolink, October, 1998. Also The Furniture Business, El-Alam El-Yoam, 11/9/2001

III. The Macro-Environment

The previous sections attempted to focus more on the constraints faced within the industry. This section of the report tackles constraints pertaining to the macro environment. Most, though not all, of these are not industry-specific in nature. Rather they relate more to the overall functioning of the economy with its various sectors.

A. The Legal and Regulatory Framework (LRF)

It is a well-known fact that in many respects the Egyptian economy is over-regulated. For example, a recent report prepared by the ILD and ECES shows that the registration and licensing procedures for enterprises in Egypt take up to 372 days³⁵. Prior to establishing a one-stop-shop in Mansoura city, it took an entrepreneur 336 days to finish his/her paperwork. The problems posed by the LRF do not just affect the enterprise at the establishment stage, but also continue to affect it during its operation. According to a statement made by Prime Minister Ebeid, some 24 entities are involved in managing the LRF regulating private enterprises in Egypt. With regards to furniture manufacturers, according to one of the members of the BOD of the Wood Manufacturing Chamber of the Federation of Egyptian Industries, the industry has to deal with 18 supervisory bodies³⁶. These bodies often have overlapping, if not conflicting mandates and command a large corps of government inspectors charged with monitoring compliance, adherence to standards and identifying violations. The resultant interruptions of enterprise operations and waste of management time constitute a burden that entrepreneurs have to bear. In addition, the entangled web of legislations, decrees and regulations create a favorable environment for favoritism, corruption and abuse of power. These burdens, it should be stressed, are more fatal in the case of micro and small enterprises that lack the necessary skills and resources to deal with these issues.

Given the above, it is not surprising to end up with a large informal sector within furniture manufacturing. Official (CAPMAS) estimates document only 18,507 enterprises. The most modest other estimate encountered during the preparation of this report is almost double this size (36,000 enterprises). Another estimate that is also said to be conservative is 60,000 enterprises. This huge informal sector is a sign that from a cost-benefit analysis, a vast majority of producers chose to stay outside the system.

With regards to the furniture sector, two aspects of the LRF have paramount importance. The first aspect has to do with the ***tariffs on imported inputs***. As mentioned above, the average production weighted tariff on furniture inputs is relatively high (almost 25%). Presumably, the LRF, through its drawback system, allows for the reimbursement of this 25% to exporters who export furniture containing these inputs. The system however is not functioning properly and very few exporters, if any, are actually using it. According to furniture manufacturers it takes up to a year in the best-case scenario to succeed in getting back tariff payments on imported inputs.

The combination of both the tariffs and the malfunctioning drawback system serves in fact to create an anti-export bias that economists estimate to equal the 40% tariff

³⁵ Presentation by Institute of Liberal Democracy and the Egyptian Center for Economic Studies, Cairo, November, 2001.

³⁶ The Furniture Business, El-Alam El-Yoam, 11/9/2001

imposed on imported furniture³⁷. Hence the system functions to raise the costs of furniture whether targeting export markets or the local one.

Another source of complaints is the *sales tax*, specially stages II & III. According to Mohamed Wali, Director of the Damietta Chamber of Commerce, contrary to the proposal made to the Ministry of Finance officials, to have a unified sales tax of 3% for both registered and unregistered workshops, the government raised the sales tax for the unregistered workshop to 6%. In addition, similar attempts were made to increase the registration threshold to L.E. 300,000 in order to provide a breathing space for small and micro enterprises, however, by placing the threshold at L.E. 150,000, several small shops and workshops were adversely affected.

The effects of the sales tax on the furniture sector were particularly bad primarily due to the desegregation of the furniture manufacturing process (see above) among different shops and enterprises. The application of a sales tax at each stage or workshop, is expected to significantly raise the costs of production, by raising the cost of machinery and equipment, as well as intermediary goods and services. In addition, the introduction of the sales tax at a time when the economy was going through a recession actually accentuated the adverse effects, especially on the small producers, many of whom have reportedly closed down and/or laid off a significant portion of their workforce³⁸.

B. The Institutional Framework

The institutional framework governing furniture manufacturing is no different from that governing the other industrial sectors. A recurring complaint of manufacturers, as well as others, is the absence of effective representative and transparent institutions to represent and promote their interests in an equitable fashion. This equitable representation becomes a challenging task at best with regards to small and micro enterprises and workshops, which are usually institutionally underrepresented, compared to larger enterprises that are clearly much more visible and active.

The pattern is not different in Damietta from the rest of Egypt. Both chambers of commerce and industry fall under line ministries that appoint about 50% of their board members, as well as second employees to staff their organizations. In addition, micro and small entrepreneurs are convinced that these bodies represent more the interests of large businessmen, than they represent their interests. The result is a set of organizations that are detached from their constituencies (or at least a large portion of it) and more susceptible to governmental influence than they should be³⁹.

Cooperatives in fact do not fare much better. With minor exceptions, if any, cooperatives in Egypt were developed during the fifties and sixties as instruments of state control and cooptation, rather than being collective organizations established by and for their members. While ideally providing valuable services to their members (e.g., purchase

³⁷ Development Economic Policy Reform Analysis (DEPRA) Project, An Egyptian Furniture Industry Assessment; Part I: Trade Policy and Market Opportunities, August 1999. P. 33.

³⁸ Hozayen, Atef, The Execution of Dumyat City, Al-Ahram Al-Araby, July 21,2001, No. 226.

³⁹ Collaboration for Community Level Services (CCLS) Project, Collaboration for Community Level Services in Dumyat: Preliminary Research Findings and Implications. (Unpublished).

of raw material and marketing of products), their ineffectiveness has been another source of complaints for years.

NGOs and other forms of civil society and voluntary activity are likewise closely controlled and monitored by the state. In addition, due to various reasons they suffer from several constraints including a weak resource base, as well as institutional fragility, weak links to the grassroots, lack of adequate human resources and susceptibility to politicization.

These factors combine to create an institutional environment that is largely ineffective as means for interest aggregation, articulation and lobbying for the interests of furniture manufacturers. Efforts have to be exerted in cooperation with the various governmental and non-governmental stakeholders and parties, before this framework is vitalized and empowered to perform its functions properly.

C. General Economic Conditions

The general economic conditions of Egypt undoubtedly have an effect on the conditions of the furniture industry. For instance the diminishing purchasing power of a large portion of the Egyptian population has an adverse effect on the local demand for furniture. In addition, the rising exchange rate of the US \$ serves to increase the price of inputs to the industry thus further increasing the price of furniture beyond the reach of the majority of the population. A third factor is that the lack of liquidity and the delayed payments by the government affect various sectors of the economy. The decline of tourism, and the ensuing decline in investment in hotels and resorts likewise has a downward effect on the demand for furniture, in addition to its effect on the incomes of those who are directly or indirectly involved in tourism.

IV. General Recommendations

As outlined above, the furniture industry appears to be an industry in crisis. Overcoming this situation requires the use of several measures some of which may constitute a radical break with the traditional way of thinking and implementing interventions. The following table presents some tentative recommendations on the firm, governorate, sector and policy levels. These recommendations are not meant to be exhaustive in nature, but are rather provided as sign posts that can be used to develop more elaborate suggestions.

Generally speaking, lifting trade barriers completely in a few years will serve to place our furniture industry (which is already twenty to thirty years behind its competitors) in an unfavorable position to say the least. It appears that only a tiny portion of the sector can withstand this competition (though not without incurring significant losses). The real concern however is the future of SMEs (small and micro enterprises) in the sector, especially when placed in a few years time in a more competitive context. Unless small entrepreneurs innovate ways to utilize economies of scale and modern manufacturing methods and techniques, they are unlikely to survive the competition. A significant portion of this sector is already weakened by the rapidly declining market share, the general economic conditions, in addition to the introduction of the sales tax, as well as a host of other factors.

Facing this threat involves not just enhancing the competitiveness of the entire sector. Rather it involves enhancing the competitiveness of the entire institutional setup. Old mentalities, management and governance methods have to be done away with to the favor of new more effective ones. For example, in a global free economy, state control of associational life can stifle the business sector. The institutional framework has to be liberated of old legal constraints and practices to become more effective, transparent and democratic, as well as more accountable to its true constituency members.

Protectionism, in addition to delaying the inevitable, has in fact encouraged inefficiency to prosper and weakened the incentive for the sector to modernize. Now the furniture sector finds itself in a situation whereby it is supposed to learn the new rules of the game, and actually excel in playing this new game at a time when it is already behind its competitors.

	Firm	Governorate	Sectoral Organizations	Policy
Inputs	<ul style="list-style-type: none"> • Become more quality oriented in the choice of inputs. • Introduce modern production technologies and machinery. • Actively seek foreign partners to establish joint ventures. • Introduce modern up-to-date designs that are in demand globally and nationally. 	<ul style="list-style-type: none"> • Continue the ban on poor quality woods and extend it to other imported inputs if applicable. • Cooperate with central authorities to solve issues related to power and water supply, in addition to the provision of adequate services to New Damietta. • Upgrade the quality of services provided to new industrial zones. 	<ul style="list-style-type: none"> • Promote quality orientation in the choice of inputs. • Provide assistance to manufacturers in identifying and purchasing modern machinery and equipment. • Provide information on new designs and their specifications in different markets. • Obtaining good lumber-drying equipment to provide drying services at cost. 	<ul style="list-style-type: none"> • Eliminate tariffs on imported inputs. • Establish and enforce sound criteria and grade regulation for imported inputs. • Eliminate sales tax on machinery and tools used in production. • Provide a variety of financial tools on an expanded scale and with economic costs to Egyptian manufacturers. • Develop furniture vocational and technical training through the introduction of curricula that reflect market needs, obtaining equipment (for practical training) that match the currently available equipment in the sector, developing a well-qualified cadre of trainers. • Encourage foreign direct investment to facilitate technology transfer.

	Firm	Governorate	Sectoral Organizations	Policy
Process	<ul style="list-style-type: none"> • Large firms should introduce TQM and ISO systems in their plants. • Adhere to quality standards in production. • Move to nitrocellulose based finishing. • Introduce Polishing cabinets. • Specialize in a limited range of products. • Small firms should be encouraged to merge into larger entities, or develop forms of association that would allow them to benefit from the economies of scale, at least in some stages or aspects of the process. 		<ul style="list-style-type: none"> • Sponsor training in modern manufacturing techniques and TQM. • Introduce product certification. • Encourage specialization among furniture manufacturers. • Provide facilities for small firms to use in some stages of the production process (e.g. finishing or polishing). 	<ul style="list-style-type: none"> • Establish and enforce adequate quality standards on exports. • Streamline LRF to facilitate firm establishment, operation and growth.
Marketing	<ul style="list-style-type: none"> • Introduce marketing and marketing research early in business plans. • Attend more international trade shows and fairs. 	<ul style="list-style-type: none"> • Organize an annual international furniture trade fair or similar events. • Develop a promotional campaign, in cooperation with central authorities, to promote the image of Damietta as the capital of furniture manufacturing in the region. 	<ul style="list-style-type: none"> • Assist firms, specially smaller ones, in their marketing efforts through the provision of market information, new designs, identification of marketing opportunities, sponsoring participation in trade shows and fairs...etc. • Develop a sector market strategy and a PR campaign targeting European markets. 	<ul style="list-style-type: none"> • Vitalize the role of trade points, commercial representation offices and similar entities. • Provide incentives for international trading houses and marketing companies to start operating in Egypt. • Reducing travel and transportation costs associated with trade shows and international fairs.

	Firm	Governorate	Sectoral Organizations	Policy
Legal & regulatory Framework		<ul style="list-style-type: none"> • Liaise with central authorities on the demands of furniture manufacturers regarding the LRF. 	<ul style="list-style-type: none"> • Liaise with central authorities on the demands of furniture manufacturers regarding the LRF. 	<ul style="list-style-type: none"> • Reduce the regulatory burdens associated with firm establishment, operation and growth. • Eliminate tariffs on imported inputs, or at least reduce these tariffs and streamline the drawback system. • Eliminate sales tax on machinery and equipment. • Reconsider the way the sales tax is applied on the furniture sector.
Institutional Framework	<ul style="list-style-type: none"> • Become more active players in sector organizations to introduce positive change. 	<ul style="list-style-type: none"> • Vitalize and strengthen the relationship between the governorate, civil society sector organizations, and furniture manufacturers. 	<ul style="list-style-type: none"> • Become more effective and active players in representing the sector and pushing for change. • Be more sensitive to the needs and interests of small and micro enterprises. • Actively seek autonomy from government control. 	<ul style="list-style-type: none"> • Liberate sector organizations, and other forms of civil society from government control.