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INTERNATIONAL AND LOCAL BUYER ANALYSIS

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INTRODUCTION

It is by now well established that firms are coming under increasing pressure as globalisation blurs those boundaries between countries that have traditionally offered their industries some protection from competitive pressure. From the perspective of the localised firm, the global playing field is anything but even – competitors draw on labour pools with vastly different levels of skill, and at vastly different costs. Different countries have regulatory environments that impact differently on their domestic firms. Access to finance, to technology and to knowledge differs dramatically between countries. Competing under these conditions often seems impossible, with firms (and particularly small and medium firms) involved in an exhausting game of catch-up with their competitors. However, given a global regulatory environment that entrenches the notions of international competition (on both a regional and global level), catch-up and compete is ***exactly*** what firms have to do.

For firms in developing countries, the task of breaking into the international market is even more complex than for their industrialised country counterparts. Developing country firms suffer disproportionately from the barriers to entry outlined above, with often-unstable political regimes, shaky economic climates and a host of social problems impacting negatively on individual firm competitiveness. In addition, a significant proportion of world trade takes place between industrialised countries. Developing country firms wishing to capture a share of lucrative industrialised country markets must successfully develop an understanding of a consumer market much more demanding than the domestic market they are used to supplying.

South African industry finds itself in a unique position within the context of globalisation. On the one hand, South Africa's relatively developed infrastructure (both physical and financial) and long history of formal sector manufacturing make it a strong contender amongst developing countries trying to access global markets. On the other hand, South Africa's history of apartheid-prompted economic sanctions has kept the country's industry tied to outdated notions of protectionism and import-substituting industrialisation long after competitors have shifted their focus to the possibilities of export-led growth. An additional liability of economic isolation has been the development of a particular culture of production amongst South African firms, sometimes termed racial Fordism, which has in turn created a very insular management culture (Barnes *et al* 1998). The impact of this culture has been felt, amongst others, in a lack of customer-focus and a reticence amongst firms to adjust to the demands of the new industrial era of flexible, market-focused production.

The problems facing firms trying to compete in a global market have been widely explored from the perspectives of both small and medium enterprises (SMEs), and of developing country firms (Kaplinsky 1994; Nadvi & Schmitz 1994; Schmitz & Musyck 1993). The timber furniture industry is a particularly useful case study in this regard: while global trade in furniture has increased dramatically in recent decades, the sector tends to be dominated by SMEs. Furthermore, this is a sector favoured by developing countries for its relatively low barriers to entry, value-adding properties and labour-intensive nature (UNIDO 1991). While developing country firms are late entrants to the international furniture market, and face a number of weaknesses in their attempts to attain the status of international competitor, they can, with effort, benefit from the experience of industrialised country forerunners.

This research report is the second in a series of working papers / research reports that will focus on the nature of the South African timber furniture industry, with an emphasis on the opportunities and constraints facing South African manufacturers as they strive for international competitiveness. The first paper set the scene by examining international trends in the timber furniture industry, both in terms of trade and production, and in terms of the nature of global market demand. That paper went on to outline two scenarios for competition in the global marketplace often caricatured as the 'high road' or the 'low road' to international competitiveness. An examination of the unit value of British furniture imports from a number of countries suggested that South African furniture producers are currently following a low-road 'map'. Given the intense price pressure that producers on the low road face, this is an extremely precarious route to international competitiveness. However, a shift away from price-based competition brings a new range of competitive demands to bear on producers. Although price remains a critical aspect of competitiveness, at the top end of the market quality, design, flexibility and a range of other criteria are seen as equally essential. A number of key constraints that limit how effectively South African furniture manufacturers operate in the export market were identified. These included design, quality and price issues, the complexity of foreign marketing and limited production capacity. Finally, the paper proposed that co-operative action offered a viable solution to the difficulties of competing on the high road.

This research report moves forward to consider in greater detail how well South African furniture firms are positioned to catch up and compete in the global furniture market, and is based on a survey of South African furniture manufacturers and local and foreign furniture retailers. The research report recognises that it is not just exporting firms that need to be concerned with developments on the international front: domestic-market focused firms are no longer protected by tariff barriers from foreign competition. The report is thus divided into two parts, the first considers the domestic market, while the second looks at exporting firms. The intention of this study was to gain some insight into *how well* manufacturers understand the demands placed on them by their markets, by understanding *the nature of relationships* in this sector. It is only through an accurate assessment of the demands placed on them that firms can begin to respond appropriately, flexibly and rapidly to these demands. Ultimately it is this responsiveness to changing market demands that determine how well South African furniture manufacturers are positioned to respond successfully to competition from global players.

SECTION ONE: METHODOLOGY

In its simplest form, the goal of the research on which this report is based was to establish how well furniture manufacturers understand market demands, and how well they are performing relative to these demands. In order to achieve this the research had to explore the opinions of two separate stakeholder groups: furniture retailers and furniture manufacturers. One part of the research involved a survey of both local and international retailer perceptions of the demands of their end consumers, as well as their assessment of the performance of their timber furniture suppliers. The other part of the study involved a similar survey of manufacturers aimed at gauging their perceptions of both market demand and their own performance relative to this demand. Each of these two parts of the study had three phases that sought to cover a representative sample of the stakeholder group in question.

1.1 Building Credibility

Reliable industry-level research is not possible without the co-operation of individual manufacturers. In essence, this research undertaking commenced well before the actual survey was conducted, beginning with the first contacts established between the Industrial Restructuring Project (IRP) research team and the furniture industry. The study began in KwaZulu-Natal (KZN) for a number of reasons. Firstly, KZN is the home base of the IRP and secondly, the province is one of three centres of the timber furniture industry in South Africa. Finally, some industry level support for research into the province's timber furniture industry already existed. The Timber Products Exporters' Association[1] (TPEA) had for some time been trying to attract government funding (through the Sector Partnership Fund) for a group of furniture exporters willing to work jointly to improve individual performance. The Industrial Restructuring Project's research was seen as having potential synergies with these efforts. In September of 1998 the TPEA provided introductions to two exporting timber product firms. A subsequent request to the Federation of Furniture Manufacturers of South Africa provided a number of other firm contacts, so that a total of six interviews were conducted as a means of gaining a qualitative impression of some of the key problems (and opportunities) facing the industry. This was supplemented by a thorough review of the international literature to discern the current trends in the timber furniture industry, and the key issues with implications for South African manufacturers.

In order to build on the perceived grassroots support within the industry, the IRP decided to offer a free full-day workshop for furniture manufacturers interested in learning more about the concepts of industrial restructuring. The workshop, held in November 1998, was attended by representatives of seven firms, and was judged a success based on the enthusiastic input of the delegates. From the perspective of the IRP research team the workshop was critical both as a means of confirming impressions about the dominant issues in the South African furniture industry, and, more importantly, as a means of building the credibility of the research project. At the workshop it was agreed that the IRP would undertake research into the nature of demand in the furniture market, with the support of the firms present, who all agreed to be interviewed.

1.2 Survey of Manufacturers

Obviously seven firms is an inadequate sample for a reliable survey. Identifying other firms willing to co-operate in the research was complicated, as is often the case in South Africa, by the absence of a single, up-to-date register of firms. While it appeared that the industry Bargaining Council was the best source for this purpose, confidentiality agreements meant that this list could not be accessed. Instead, several sources were used to identify suitable firms. These were references obtained from

[1] The TPEA is an association of about twenty exporting firms located throughout South Africa, although predominantly in KwaZulu-Natal.

the local Furniture Industry Training Board (FITB), the Durban Chamber of Commerce, the KwaZulu-Natal Furniture Association, the TPEA and the Braby's Business Directory. From previous discussions with firms it was determined that the problems of lounge suite manufacturers and customised kitchen manufacturers were quite different to those facing manufacturers of 'case goods', that is, wood-based furniture such as beds, wardrobes, dining rooms suites, wall units and other such items. Manufacturers of the former two product groups were consequently excluded from the sample population at this early stage. From the various industry sources a list of about seventy firms was compiled, and all of these firms were telephoned in order to determine their number of employees, the products they manufactured, and whether they exported. Finally, it was decided to exclude firms with less than fifteen employees from the sample. While this was an arbitrarily determined cut-off, it was deemed appropriate, as the IRP does not look specifically at the needs of small enterprises, while it does try to focus on the role of South African firms in the context of the global economic environment. After the exclusion of these smallest firms, the study was left with a population of approximately forty firms.

In this first phase of the survey of manufacturers, letters introducing the study were sent to all forty KwaZulu-Natal based manufacturers, and after a series of follow up calls, interviews were eventually set up with thirty-one of these firms. These interviews were administered on a one to one basis, and were based on a carefully constructed questionnaire. The questionnaire set out to explore the nature of the market served by the manufacturer in question, before asking the manufacturer to rate the importance of a number of competitive criteria in this market segment. Finally a number of questions explored the relationship between manufacturer and retailer, as well as exploring developments around a number of critical competitive criteria (quality, design and environmental standards) in more detail. Because this phase of the survey was conducted directly by the project researcher, it allowed for greater exploration around critical issues, and facilitated research in later phases of the survey.

The second phase of the manufacturer survey extended the geographic range of the survey. KZN shares its position as one of the centres of the timber furniture industry with two other provinces, Gauteng and the Western Cape. In an effort to expand the study, a Gauteng-based doctoral student whose research interests included the furniture industry was contracted to conduct questionnaire-based interviews with furniture manufacturers in Gauteng. This phase of the study provided nineteen completed questionnaires, all the product of face-to-face interviews.

The final phase of the manufacturer survey was intended to access a broader base of furniture manufacturers. A postal survey was conducted of two hundred furniture firms, with names drawn from the recently published 1999 South African Wooden Furniture Directory. The directory provided the names and postal addresses of firms, but no details as regards telephone numbers or the name of the manager, and this made follow-ups difficult, and had a discernible negative impact on the response rate. Unfortunately just twelve completed surveys were received. Nonetheless, this survey, which used a simplified version of the questionnaire used in the first two phases, was a useful exercise, as a number of completed questionnaires were received from the Western Cape, the third major centre of the wooden furniture industry in South Africa. In addition, two completed questionnaires were received from other regions in South Africa.

1.3 Retailer Survey

The retailer survey was conducted concurrently with the manufacturer survey described above, and was initially envisaged as having two phases. Of the sixty-two manufacturers surveyed, just over one-third were involved in some exporting activities. Given that the aim of the retailer survey was to give an independent assessment of manufacturer performance, and to act as a proxy for consumer demand, it became necessary to survey not just domestic retailers, but also foreign retailers.

In the first phase of the survey of retailers, questionnaire-based interviews were conducted with buyers from thirteen retailers. Seven of these interviews were conducted with retail chains, and at least one chain from each of the furniture groups was surveyed[2]. The remaining Six respondents were 'independents', and included one small office furniture chain, a marketing agent representing a number of small furniture manufacturers and four independent retail outlets targeting the upper end of the market.

The second phase involved a survey of foreign retailers. This phase of the survey was conducted by students at the Institute of Development Studies at the University of Sussex in the United Kingdom. Seven surveys were completed in the United Kingdom, and another six in Spain. It was on completion of the analysis of this second phase data that the need for a third phase of the retailer survey became apparent. The interviews in Spain and the UK allowed us to do three things:

- develop a picture of the nature of demand in the export market
- see how closely South African exporters' assessment of foreign market demand corresponds with this picture
- compare South African exporters perceptions of their own performance to foreign retailer demands

However, only one of the thirteen European firms surveyed purchased any furniture from South Africa. Thus what this second phase of the survey did *not* do is to give any independent assessment of how well South African manufacturers are performing in the export market. This highlights the need for a third phase of the retail survey that will specifically target a summarised questionnaire at foreign retailers known to purchase from South African manufacturers. It is intended that an updated version of this paper will utilise findings from this third phase of the retailer survey to fill the remaining gaps in this analysis of market demand in the timber furniture sector.

[2] As we will discuss in Section Four, the South African furniture retail sector is extremely concentrated, with five 'groups', each comprising a number of furniture chain stores controlling at least 90% of the South African furniture market. The concentration of the South African furniture retail sector is the subject of a doctorate by Claudia Manning (1996).

SECTION TWO: THE SURVEY SAMPLE

Before moving on to analyse the survey responses it is important to briefly describe the population sample. As outlined above, the survey was predominantly located in KZN and Gauteng. In fact, 48% of the sample were manufacturers based in KZN, and 36% were based in Gauteng, while 13% were from the Western Cape. The remaining 3% represent the two questionnaires received from the North-West and Mpumalanga respectively. When compared to the latest Stats SA data (see Table One), which unfortunately is the 1993 Survey of Manufacturing, it would appear that the sample is skewed in favour of KwaZulu-Natal. This, is however, not unexpected, and no information has been uncovered to suggest that the problems of KwaZulu-Natal furniture manufacturers *within particular sub-sectors (e.g. suppliers to retail chains, exporters)* are significantly different from those of other furniture manufacturers.

Table One:

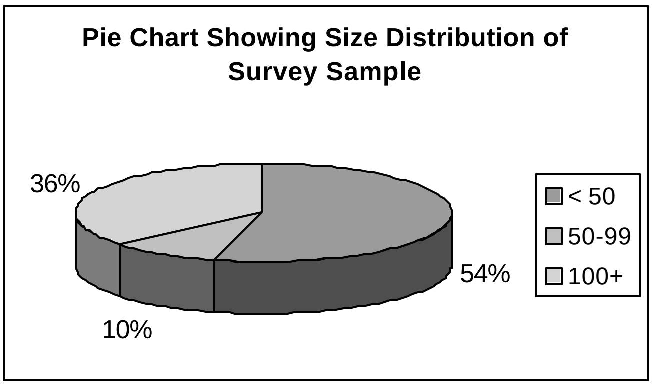
Comparison of Provincial Distribution of Survey Sample and 1993 Manufacturing Survey Data

Province	Survey of Manuf. – 1993*	Survey Sample
Gauteng	43%	35.5%
KwaZulu-Natal	23%	48.4%
Western-Cape	21%	12.9%
Other provinces	13%	3.2%

*Source: Stats SA (1993)

As mentioned in the previous section, firms with less than fifteen employees were excluded from the sample. One can therefore expect a higher average firm size than might otherwise be the case. In fact, the average firms size was one hundred and twenty eight employees, with the smallest firm having fifteen employees, and the largest eight hundred. Fifty-five percent of the firms surveyed had less that fifty employees, 10% between fifty and ninety-nine, and 35% more than one hundred.

Figure One:



When compared to the data from the 1993 Manufacturing Survey the admitted bias of the sample towards large firms is quite obvious.

Table Two:

Comparison of Size Distribution of Survey Sample and 1993 Manufacturing Survey Data

Size Category	No. of Employees	% of Plants in Manufacturing Survey*	% of Sample
Micro	1 to 4	17.9%	0%
Small	5 to 49	68.4%	55%
Medium	50-199	10.8%	26.7%
Large	200+	2.9%	18.3%

*Source: Stats SA (1993)

Another way of measuring firm size is in terms of turnover. The average firm turnover for the sample was R8.9 million, while the smallest firms had an annual turnover of just half a million rand, and the largest a maximum of forty-eight million rand.

Due to extremely high levels of industrial concentration in South Africa, understanding ownership patterns is always very important in analysing economic activity in the country. In the furniture manufacturing sector the industry has long been dominated by Afcol (Associated Furniture Companies), a group of fourteen companies manufacturing furniture end products and six companies producing furniture industry inputs (Manning 1996). Last April Afcol and Pat Cornick merged to form the Cornick Group (http://www.edata.co.za). Another significant player in the South African furniture market is the German Steinhoff Group, which has recently consolidated its position in the South African market by orchestrating a merger with the smaller Megacor group of firms (Natal Mercury, 28-04-99). Most recently it has been reported that plans are underway for a merger between Steinhoff and the Cornick Group (Natal Mercury, 28-04-99; http://www.edata.co.za). In 1996 Afcol estimated that it controlled 35% of the domestic furniture market (Manning 1996). Certainly, then, the proposed furniture giant will have a significant impact on the South African furniture sector

Table Three:

Ownership Patterns in the Sample of Timber Furniture Firms

Ownership	No. of Firms	% of Sample
Cornick	4	6.5%
Steinhoff	3	4.8%
Independent[3]	55	88.7%

A final characteristic of the sample that should be highlighted is the end market for production. In total, eighty-one percent of the sampled firms' sales went to the domestic market, while sixteen percent went to overseas exports, and just two percent to neighbouring countries. While the latter figure is not unexpected – South Africa's neighbours are not wealthy, and demand for furniture is closely correlated with disposable income – it may appear lower that it actually is. One of the large furniture groups that dominate the South African furniture retail sector has a chain that serves neighbouring country markets, and it became apparent that manufacturers did not always consider this as 'selling into a neighbouring country market'. The export figure deserves a similar word of caution. Some manufacturers of customised furniture recorded as exports those sales that left the country informally, such as when a customer ordered new furniture shortly before emigrating. What was clear was that ninety two percent of the sample sold at least some of their production into the domestic market, while at least 36% of the sample considered at least part of their sales to go into the *overseas* export market. However, if one considers only those manufacturers that export at least half

[3] For the purpose of this paper firms that are not part of either of the two major furniture groups were considered independent, although they may in fact belong to a smaller industrial group.

of their production then the latter figure drops substantially to 16% of sampled firms.

SECTION THREE: THE DOMESTIC FURNITURE INDUSTRY

This section sets out to explore the nature of and prospects facing the domestic furniture industry. The domestic retail sector is one that is h in a state of flux. It is dominated by a very high level of retail concentration, so that developments in the retail sector can have dramatic impact on furniture manufacturers. Poor general economic conditions mean that the domestic furniture market has experienced a period of contraction, and this, coupled with the high level of retail concentration makes for an extremely competitive market. The market for furniture is also a highly differentiated one, and if firms are to compete in this environment they need to accurately assess and then meet the demands of their chosen market segment. This section considers the dominant role of retail chains in determining the nature of relations in the industry, and then examines some of the other ways in which domestic demand for furniture is differentiated. Thereafter we analyse the results of an exercise used to rate the importance of various competitive criteria, assess manufacturer performance, and determine how accurately South African manufacturers are reading domestic market demand. Finally we consider some crucial issues that are likely to have an impact on the domestic market in the future.

3.1 The Nature of the South African Furniture Market

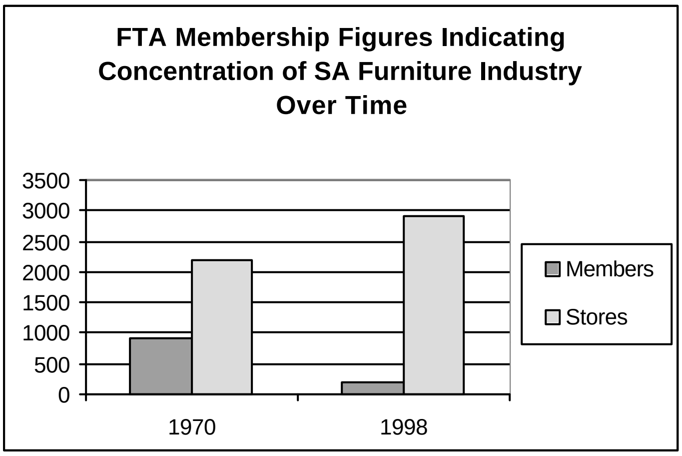
It is impossible to understand the domestic furniture market without taking cognisance of the extreme retail concentration that characterises the industry. At the same time, focusing solely on this aspect of the South African furniture market ignores the full extent of differentiation in the industry.

High Levels of Retail Concentration

A 1996 study (Manning 1996) showed that seven furniture retail groups controlled *ninety* percent of the South African furniture retail market. In 1999 this concentration has in fact *increased:* due to two mergers the number of groups in operation in the South African market is down to five, with nothing to suggest that this market share has substantially declined. These groups do not specialise, but rather compete with one another across a range of markets aimed at different socio-economic categories, with each group represented in the marketplace by a number of specialised chains.

The ongoing concentration of the retail sector is strikingly evident when one looks at the membership figures of the South African Furniture Traders' Association (FTA), as indicated in Diagram 2, below. In 1970 the FTA had about 900 members representing 2200 stores. In 1998 the number of stores had increased slightly to 2900, while the number of *members* had dropped substantially to 188 as ownership became more concentrated. (Interview 12-01-1999).

Figure Two:



For manufacturers, focusing on supplying the chains may prove to be a double-edged sword. With such a high level of retail concentration, manufacturers are effectively limited in the competitive strategy that they can pursue – linking into a retail chain is very important for generating throughput, yet excessive control over the market allows chains to place extremely heavy demands on manufacturers. While this might conceivably be in the interests of the industry if it improved overall competitiveness, this is not necessarily the case, as we shall discuss in Section Four. During the course of the interviews it became clear that manufacturers viewed the dominant position of the retail chains in the industry as problematic. Chains are seen as parasites feeding off the value added by manufacturers. Manufacturers complained that chains are bad with their payments, take excessive profits and are not loyal to their suppliers. In short, as one retailer put it: “The chains are killing us”. At the same time however, access to chains was seen as crucial for increasing throughput and overall profitability. In addition, supplying only one or two chains makes manufacturers extremely vulnerable to developments in the retail sector. One manufacturer commented that recent trouble within the Beares Group and the subsequent closure of its retail outlets left them exposed to sixty less stores.

The fact that such a small number of buyers are responsible for such a large percentage of industry purchases makes for an industry where “everyone knows everyone”. The South African furniture sector operates on the basis of long standing relationships and personal contacts. Retailers become aware of new manufacturers through word of mouth or after contact is initiated by manufacturers. Formal media such as the Internet, furniture fairs and agents play little part in establishing contact between buyers and sellers in what is a relatively small and concentrated market. In a question about how initial contact was established with buyers, ninety two percent of the manufacturer respondents stated that they had either contacted the buyer directly, had been contacted by a prospective buyer, or simply had a longstanding relationship with their buyers. In such a small industry, with such low barriers to entry, reputation is also critical for business success, and for this reason, as we shall see in Section Four, a peculiar blend of service-oriented criteria warrant unusual importance in firm competitiveness. At the same time, an industry run on personal contacts can be a very unstable one for manufacturers. One manufacturer pointed out that if a particular buyer left, access to an entire chain of stores might be lost. As one respondent accurately phrased it: how well you do depends on “who you know and how happy you keep them”.

A Highly Segmented Market

Despite the significance of the market dominance exercised by the retail groups, it is critical that we do not lose sight of the many other ways in which the furniture market in South Africa is segmented. Most obviously, small independent retailers play an important part in allowing manufacturers to ride out fluctuations in demand from the retail chains. Several manufacturers consciously choose to focus on this market segment, seeing it as one that allows them some element of control in the manufacturer-retailer relationship. Other manufacturers choose instead to sell directly to the public through their own retail outlets. Yet another aspect of market segmentation is reflected by manufacturers who manufacture customised furniture, working either for the end consumer, or for an interior decorator representing the end consumer. However, not supplying the retail chains brings its own problems. Several manufacturers complained of a high level of closures among independent retailers. Customised furniture manufacturers were similarly feeling the pressure of poor economic conditions. While demand appears to have been stagnating throughout the furniture retail sector, there are two reasons why this might be particularly apparent in the segments mentioned above. Firstly, these segments generally serve the upper income group, and there is the common perception amongst manufacturers that this income segment is shrinking, partly through a high level of emigration. Secondly, as Manning (1996) pointed out, much of the furniture groups' profits come not from furniture sales, but rather from the finance they offer consumers in the form of hire purchase agreements. Poor economic conditions are thus likely to have a less immediate effect on the profits of retail groups than on those of independent retailers.

Market segmentation can of course take a variety of forms other than simply the manner in which furniture products are transferred from manufacturer to end consumer. The furniture market is a highly differentiated one, and this has a significant impact on the competitive strategies open to manufacturers. We have briefly mentioned the issue of market segmentation by income group. Serving the upper end of the market often means smaller runs, which requires a much greater level of flexibility. An extreme example of this would be customised furniture made to the exact specifications of a particular end customer. At the upper end of the market quality requirements are especially demanding, and firms must find a way of balancing superior quality with reasonable cost. While manufacturers perceive this upper end of the market as shrinking, they are also aware of the growing black market, and recognise the need to understand and meet a new set of demands. By way of example, the provision of state housing subsidies is expected to create a demand for furniture amongst those able to purchase their first home. However, the limited purchasing power of the subsidy means that houses are likely to be very small, and manufacturers wishing to benefit from this growing demand will have to produce small and possible multi-purpose items of furniture. At the same time a growing black middle and upper class brings to bear its own demands on manufacturers. If manufacturers are to make the transition from the 'shrinking' traditionally white market, they are going to have to respond to these shifts in market demography.

The domestic furniture market is also segmented according to the type of raw material input used. Products may be chipboard or Superwood (Medium Density Fibreboard) with a natural veneer or a paper foil, or may be laminated. Some products combine veneered board with solid hardwood timber such as oak, while others are produced from solid, locally grown pine softwood, or imported hardwoods such as oak or beech. While it is difficult to generalise, the low end of the market is likely to be dominated by foiled products, and the middle by natural veneers, combinations of veneers and solids, and pine. Pine products are sold both in unfinished and finished form. Finally, at the upper end of the market products may be of hardwood or of pine. Interestingly, at this upper segment design may surpass material in importance, so that it is not unusual to find upmarket customised furniture manufacturers working with some form of composite board. Similarly, the pine products sold into this market segment are likely to fall into the category of 'cottage' furniture, and to be sold specifically as 'Oregon' or 'Cypress' pine.

A final segmentation of the domestic furniture market is along the lines of the purpose for which the product is designed. At its simplest this may be household, office, hospitality industry and garden furniture. Within this categorisation, household furniture is best conceptualised as customised kitchen and wardrobe furniture, upholstered lounge furniture, and case goods, which includes dining room suites, bedroom suites and a range of occasional furniture. The demands placed on manufacturers in each segment might be quite different. Manufacturers of customised kitchens and wardrobes were excluded from this study early on as it became clear that their most significant problem lay in the threat from informal sector operators who, by circumventing applicable legislation, could undercut formal sector operators. Similarly, lounge suite manufacturers were excluded because the inputs that they utilise (fabric and foam, in addition to timber) are significantly different from those of case good manufacturers. While case goods manufacturers supplying household, office, hospitality industry and garden furniture were all included in the study, it was apparent that manufacturers needed to meet different competitiveness criterion in each sub-sector. For instance, ergonomic design was extremely important in the office furniture subsector, while delivery reliability might be crucial for the hospitality.

3.3 Hearing the Market

As we have said, understanding and meeting shifting market demands is key to competitiveness in the current era. A failure to meet market demands opens up a gap for competitors; it is therefore crucial that firms accurately gauge market demands and their own performance. To this end we asked both manufacturers and retailers to gauge domestic market demand, and to similarly assess manufacturing performance. Using individual manufacturers' assessments of the demand in their particular market segments we have been able to compile an aggregate assessment of market demand in the domestic furniture market. We have produced a similar aggregate figure for the retail sector, and using this as a proxy for end-customer demand, this section considers how well South African manufacturers focusing on the domestic market understand market demands. Finally, we consider how well these manufacturers perform relative to the demands being placed on them.

When asking manufacturers and retailers to rate demand and performance, a simple scale of one to five was used. In the case of demand criteria, a score of one meant that the criteria in question was rated as not at all important to the end customer, while a score of five meant that the criteria was critical for competitiveness. The same scale was then used to measure performance, with one reflecting extremely poor performance, and five reflecting performance that surpassed market requirements. These scores were then translated into 'radar charts' that allow one to easily compare either the assessments of two different parties, as is the case in Figure Three below, or alternatively, to compare market demand with firm performance.

Figure Three:

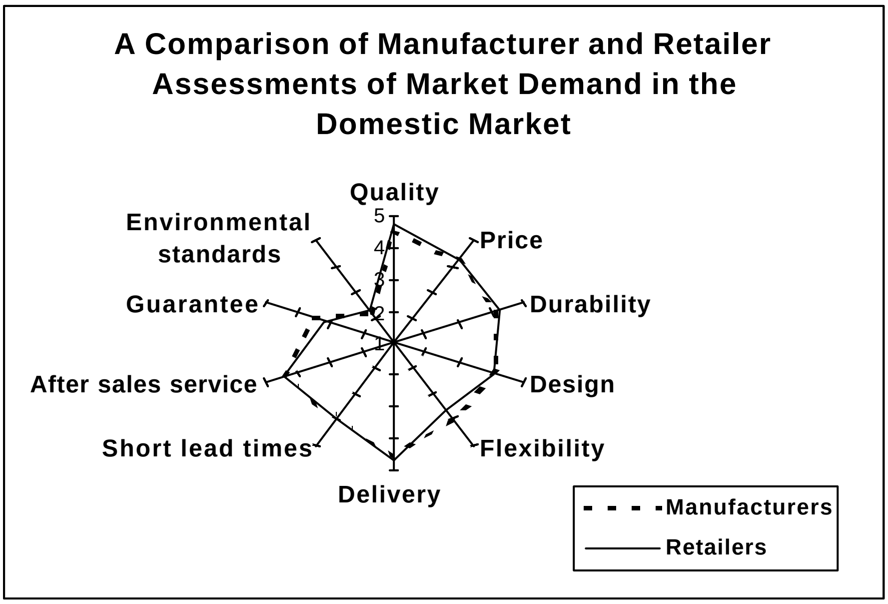


Figure Three, above, shows manufacturers' assessment of market demand plotted against retailers' assessment of market demand. The results show that manufacturers see delivery reliability as the most important criteria for doing business in the South African market, followed closely by quality and after sales service, then durability, price and design. Short lead times, flexibility and guarantees follow, with environmental standards the least important criteria on the domestic market. Retailers rate the various competitive criteria in a very similar fashion with quality, delivery reliability and after sales service the three most important criteria, followed by price, durability and short lead times, with design, flexibility, guarantees and environmental standards least important. This very similar assessment is a reflection of the relatively close ties between retailers and their manufacturers. It should be noted, however, that this closeness has less to do with a willingness on the part of retailers to upgrade their suppliers through a continual flow of information, and more to do with the precarious nature of retailer-manufacturer relations. To put it simply, if manufacturers to not accurately assess the demands of their retailers they stand to lose the retailers business.

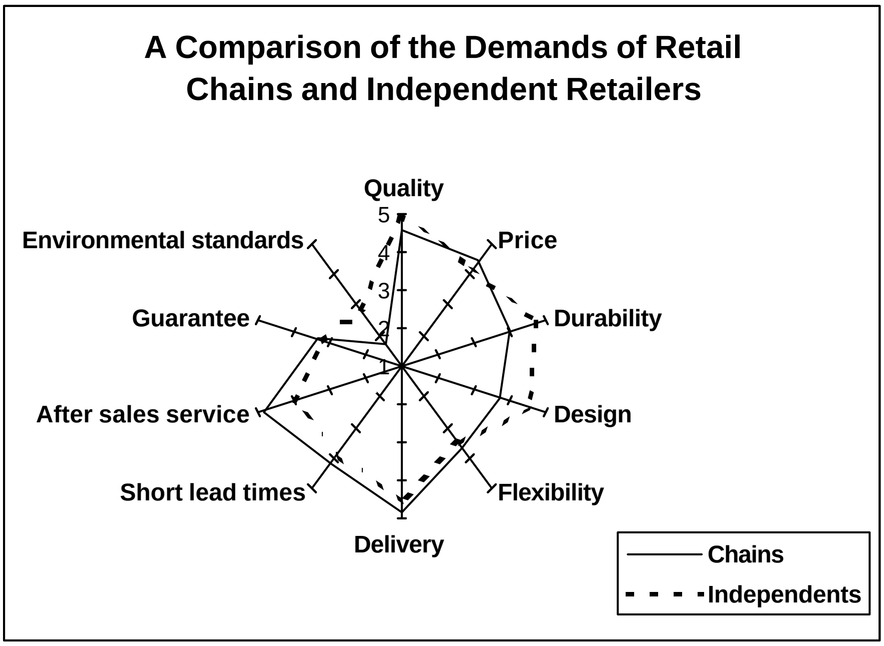
Several comments should be made regarding the relative rating of these criteria. Firstly, it is perhaps surprising that design and flexibility are rated as relatively unimportant market demands. Internationally the trend in manufacturing is towards higher levels of customisation, and the breakdown of markets into ever narrowing niches. Given these trends, as well as the growing status of furniture as a 'fashion item' one would expect both design and flexibility to rate as amongst the most important competitive criteria, along with quality and price. There are a number of possible reasons why this is not yet the case in the domestic market. Several manufacturers reported that the retail chains in South Africa are extremely conservative, and retail chain buyers in turn insisted that their end consumers do not like change. In addition, unlike the clothing market, for example, furniture is an expensive and irregular purchase, so that shifts in style attract much less attention, *particularly* at the lower and middle segments of the market served by retail chains. The most important reason for slow shifts in design, however, relates once again to the issue of retail concentration. As a result of the hire purchase system South African chains tend to "sell credit rather than furniture". Given the fact that the credit service offered by South African retail chains is crucial in allowing the majority of the buying public to access furniture, chains have something of a captive market. In addition, there are no foreign retail chains operating in South Africa that might serve to increase public awareness about changing styles.

Secondly, environmental standards score a notably low rating. As we shall see in the section on the export market, this is in stark contrast to developments in the export market, and reflects the extent to which South African consumers have been cut off from developments in global consumer culture. In the export market the growing awareness of environmental issues is usually transmitted to manufacturers via retailers who have, in turn, come under often severe pressure from the end consumer.

Thirdly, while service criteria are becoming more important for competitiveness in a range of sectors, their relatively high rating in Figure Three once again reflects the peculiarities of the South African market. Within the context of the rise of mass production and the subsequent shift over time to more flexible modes of production the basis for competition has shifted. While price was once the order-winning criterion for market dominance, over time it has become an order-*qualifying* criterion, that is, a prerequisite for entry into the marketplace. Other issues such as quality and flexibility have in turn gained priority as order-winning criteria. In the South African furniture market the three most important criteria that occupy these positions - quality, after sales service and delivery reliability – are an unusual combination worthy of comment. Firstly, the inclusion of after sales service as a key criterion for competitiveness seems unusual in the context of the furniture market, given that furniture is a durable item that would seem to require little service. The context of the research offers two explanations. The first is that quality is unusually poor in the South African furniture sector. This viewpoint would suggest that quality is traded off against after sales service so that poor quality is ‘accepted’ to the extent that it is accompanied by a high level of after sales service. Another possible explanation relates to the system of hire purchase in place in the South African furniture retail sector. Hire purchase agreements effectively extend the relationship between retailer and customer, with a corresponding extension in the duration of the relationship between manufacturer and retailer around a particular item of furniture. Secondly, delivery reliability also appears to be given unusual attention as the basis for market success in South Africa. More than any other competitiveness criteria, manufacturers drew attention to issues related to product delivery as posing severe problems. Retail chains in South Africa demand ‘to-store’ rather that ‘to-warehouse’ deliveries, and this poses undue problems for small and medium sized furniture manufacturers. In addition, chains do not source regionally, so that a manufacturer in KwaZulu-Natal may be expected to deliver to stores throughout South Africa, and in some cases the neighbouring countries. This appears to be yet another example of the way in which retail chains in South Africa are able to wield excessive market influence to their benefit.

One way to test these conjectures about the competitive criteria that drive the South African furniture market is to split our data on the competitiveness criteria according to whether the respondents were chain stores or independent retailers, as we do in Figure Four below.

Figure Four:



The results are as expected. Design appears to be more important to independent retailers who serve the more design-conscious upper market segments. Independent retailers’ services generally do not include credit provision, and this forces them to be more responsive to consumer demands. Environmental standards are noticeably more important to independent retailers, and this reflects a growing awareness amongst customers, at least in the upper segments of the market, to environmental concerns. After sales service is, indeed, less important to independent retailers than to chain stores who offer hire purchase agreements.

Our suggestion that after sales service and quality are in some way ‘traded off’ against one another in the South African market seems to be supported by the above diagram, with retail chains’ demands for after sales service higher, and quality lower than is the case with independent retailers. Delivery reliability appears to be of similar importance to both groups of retailers, which may in part be a reflection of higher levels of imports amongst independent retailers, and a concomitant concern with transport delays. Finally, it is necessary to caution that the above diagram is based on our interviews with thirteen retailers, of which six were independent, and seven chain stores. Given such a small initial sample splitting the sample does reduce the reliability of results somewhat, but certainly all indications are that chain stores and independent retailers reflect quite different market demands.

3.4 Assessing Manufacturer Performance in the Domestic Market

When we plot manufacturers' assessment of their own performance against the demands they see being placed on them (Figure Five) it becomes apparent that South African manufacturers are fairly confident of their position in the domestic market. Manufacturers believe that they are meeting or exceeding most demands placed on them. It is only in terms of quality and delivery reliability (notably two of the most important competitive criteria according to retailers) that manufacturers admit to falling noticeably short of retailer demands. Manufacturers also see themselves as falling marginally short of market demand in terms of after sales service and short lead times. Examining retailer perceptions of market demand and manufacturer performance (Figure Six) reveals a less rosy position however.

Figure Five:

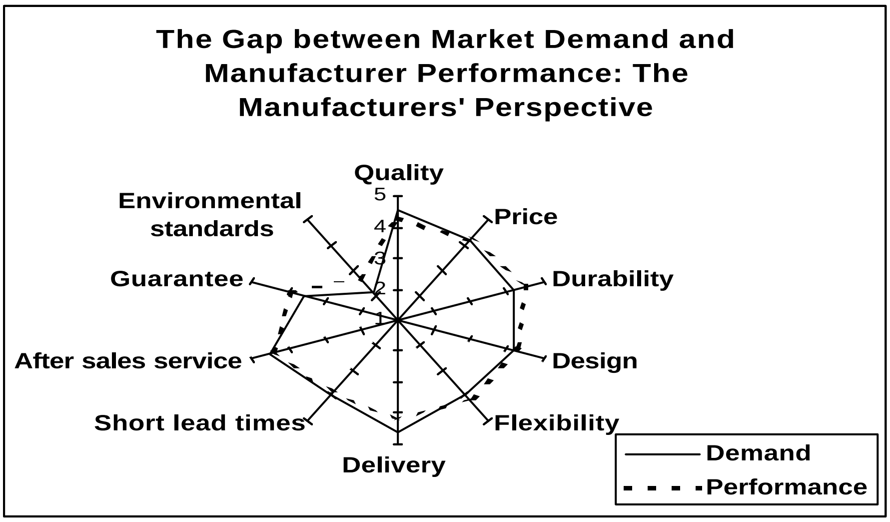
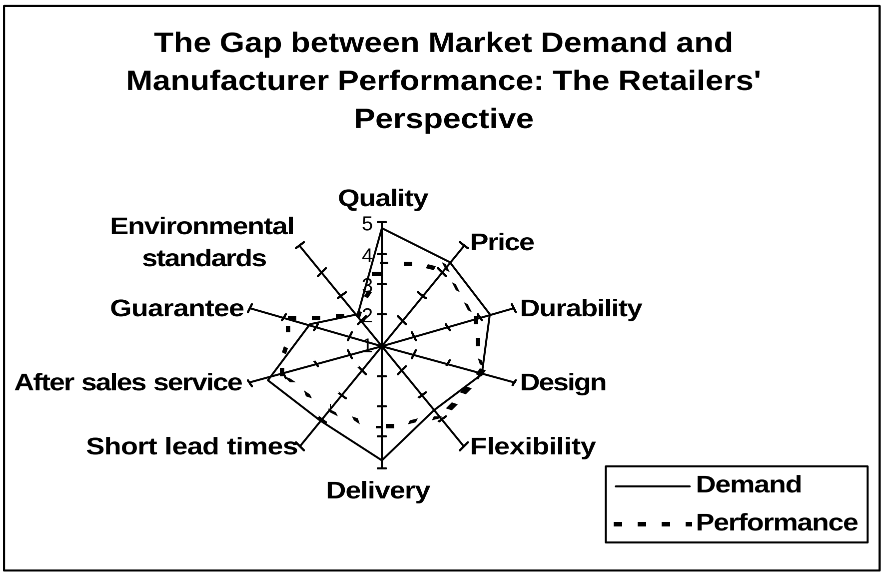
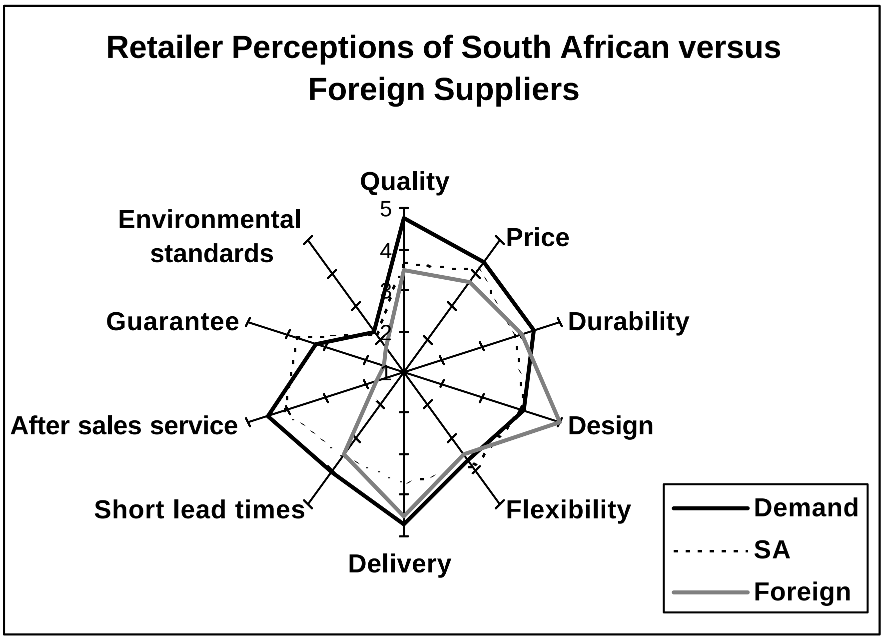


Figure Six:



As Figure Six clearly shows, retailers feel that the performance of local manufacturers falls short of their expectations on a number of issues. Retailer perceptions accord with those of manufactures in that the most noticeable gaps between demand and performance are in the case of quality and delivery reliability. However, retailers also perceive manufacturers as falling significantly short of their demands in terms of durability, lead times and after sales service. To a lesser extent manufacturers also fail to live up to price demands. Why, one might wonder, given these gaps between demands and local manufacturer performance is the local market not flooded with imports? While there are a number of explanations, part of the answer can be seen in Figure Seven, where retailers' perceptions of the performance of both their foreign and local suppliers are shown.

Figure Seven:



As Figure Seven indicates, foreign manufacturers have, for the most part, fallen short of retailer demands, and in fact of local manufacturers' performance, although notably foreign manufacturers perform better than their South African counterparts in terms of design and, rather surprisingly, delivery reliability. It would be naï ve for South African manufacturers to assume that this means that they are safe from international competition on domestic markets. As more and more developing countries enter the global furniture market, competition in this sector is likely to increase. South Africa has yet to see any massive inroads by China, Poland or Brazil into the domestic market, with imports so far limited to small amounts of Zimbabwean, Indonesian and Malaysian furniture. While retailers at present appear satisfied with local manufacturers, and not inclined to look for foreign sources of supply any number of events could change this situation. Local manufacturers cannot afford to ignore shifts in market demand if they are to survive.

3.5 Prospects in the Domestic Market

The best way to characterise the domestic furniture market at the moment is to say that it is in a state of flux. The past few years have been tough for the industry, with firm closures, and several significant mergers in both the retail and manufacturing sector. It is accordingly difficult to predict with any sense of certainty what the industry will look like in the future. Both retailers and manufacturers were asked what key developments were likely to drive the industry in the next five years. Responses were mixed at best. However, what did emerge from the interviews was a sense of several key *areas* where developments would determine the course of the South African furniture industry:

Mergers and Firm Size

The Afcol-Pat Cornick merger, followed by the Steinhoff-Megacor, and more recently the proposed Steinhoff-Cornick mergers have substantially altered the face of the South African furniture industry. It is widely believed that the concentration of both the retail and manufacturing sectors is likely to continue, although others suggest that control of the furniture manufacturing industry cannot effectively be held in one set of hands, and that the mergers will break up over time. There is a lot of uncertainty about the implications of the growing concentration in the furniture manufacturing sector. Some manufacturers believe that chains will prefer to deal with manufacturing conglomerates, as these 'mega-firms' are more financially stable. Conglomerates also benefit from economies of scale, both in terms of production, and perhaps more importantly, delivery. Others feel that the chains will be reluctant to relinquish their dominant position in the domestic market, and will thus prefer to deal with the remaining small and medium suppliers. At the same time the greater flexibility (in terms of both production and price negotiations) of smaller firms is seen as an advantage, while service is seen to decline with mergers. Conglomerates are seen to be at a disadvantage due to higher overheads, and inflexible management hierarchies. At the same time small manufacturers acknowledged that being part of a group has advantages in the form of 'back-up' that adds stability to manufacturing operations.

The same uncertainty is apparent amongst the chains we spoke to. For the most part retailers seemed to believe that concentration amongst manufacturers would continue, with larger manufacturers surviving and absorbing their smaller competitors. While the manufacturing groups are seen to offer better management skills, retailers feel that large groups, especially those that export, are more likely to let local retailers down.

Labour and Automation

Almost without exception labour problems and unions are seen as the greatest threat facing manufacturers, and retailers echoed this sentiment. Manufacturers complained about high and rising wages, and the effects of the Employment Equity Bill. Moves to extend Bargaining Council boundaries were seen as a particular threat to the competitiveness of rural furniture manufacturers. Foreign labour was perceived as cheaper than South African labour, and while this is in fact not always the case, certainly low productivity levels and lack of skills do appear to pose a problem for manufacturing efficiency. The question then is whether automation is a viable and likely solution to labour problems in the South African furniture industry.

Several manufacturers and retailers saw automation as the only viable way to survive under price pressure from retailers while remaining competitive against the threat of Asian imports. However, given the poor performance of the furniture industry recently, investments in new machinery may be out of reach of most manufacturers. In addition, as two manufacturers argued, investment in machinery is not necessarily the solution, as most factories in South Africa are already reasonably well equipped. The problem lies rather in low demand – factories are running at below capacity, and returns on assets are low.

Notably, very few manufacturers raised the issue of the need to train labour and reorganise production in order to improve productivity and performance. Those that did complained that the

Furniture Industry Training Board did not meet their training needs. In addition, smaller enterprises complained about the difficulty of releasing staff from work to attend training courses.

Exports and Imports

Manufacturers were clearly aware of the threats and opportunities posed by globalisation, and importing and exporting was clearly on their minds. None of the manufacturers or retailers we spoke to were optimistic about being able to compete in the export market with chipboard or superwood veneered product ranges. Locally produced inputs are not priced competitively for the global market, and distance from the main global markets is seen as a major problem. However, pine manufacturers were clearly in a different position with pine furniture already established as a South African export. Some manufacturers in this segment recognised that exports were crucial for increasing volumes and expanding turnover, but at the same time manufacturers felt that there was little support available for firms wanting to enter the export market.

The picture regarding the threat from imports was more mixed. While cheap mass producers in Malaysia and Indonesia were seen as possible competitors, most manufacturers recognised that South African producers are uniquely positioned to meet the needs of the local market. At the same time furniture does not lend itself to long distance transportation except in knock down form, and this concept has so far met with great resistance from the South African consumer. Retailers backed these statements, but at the same time mentioned several circumstances under which they might increase imports. At the high end of the market the 'trendiness' of Asian furniture encouraged imports. At the low end retailers complained that they may have to increase imports in order to counteract the high level of design duplication prevalent amongst retailers and manufacturers in the South African furniture sector. While none of the retailers foresaw increasing imports to more than 20% of their purchases, there is no room for South African manufacturers to be complacent. An industry observer recently noted that a loss of manufacturing capacity due to firm closures may place the industry under threat should the sector face an upswing in demand. A recent article detailing the proposed Steinhoff-Cornick merger quoted a retail executive as suggesting that furniture chains would 'investigate importing routes'. Clearly, the level of imports is dependent on future developments in the local industry.

3.6 The South African Furniture Market: Part of a Whole

As the evidence gathered by our survey suggests, South African manufacturers focusing on the domestic market have so far been insulated from the full impact of the globalisation of the furniture industry. While it seems unlikely that these manufacturers will be faced with a flood of imports in the near future, it is imperative that manufacturers consider this a window of opportunity. As the discussion presented here has suggested, South African manufacturers fall short of retailer demands on a number of criteria. At the same time the South African consumer market and retail sector appear to be lagging behind international trends, and demands for design innovation and environmentally-friendly furniture have yet to make their full impact felt on the domestic market. In the future South African manufacturers may well find themselves under pressure from two sides as imports begin to flow in from more efficient foreign manufacturers, and local retailers and customers become more demanding.

South African furniture manufacturers are to some extent handicapped by the unusually high degree of market control exercised by furniture retail chains. While the relationship between retailers and manufacturers often plays a crucial role in upgrading manufacturer performance, South African retailers do not seem to have taken on this role. Rather, they appear to place undue pressure on manufacturers in terms of a range of service-oriented criteria such as delivery and after sales service, while doing little to upgrade manufacturer performance in other key areas. While 72% of manufacturers focusing on the domestic market felt that quality demands had increased in the past five years, just 25% felt that the retailers they supply had offered them any constructive assistance to improve their performance.

If they are to survive the *long term* impact of globalisation, South African manufacturers will have to concentrate on looking beyond retailer demands to understanding the demands of the end consumer, and to identifying and closing any gaps between market demand and manufacturing performance.

SECTION FOUR: THE EXPORT SUB-SECTOR

In the first paper emanating from the IRP furniture research programme it became clear that South African manufacturers face a number of constraints that limit how effectively they operate in the export market. In this section we examine some of the characteristics of exporting furniture firms, before assessing the nature of market demand in this critical sub-sector of the industry, from the perspectives of both South African manufacturers and overseas retailers. Finally we make some preliminary comments regarding the performance of South African manufacturers relative to this market demand, allowing for the fact that, as mentioned in Section 2.3, further research is needed to ascertain how foreign retailers rate South African exporters relative to their other suppliers.

On average 16% of the sample's sales went to the export market. However, this hides a huge range, with thirty-nine firms not exporting at all, and five firms exporting 100% of their production. The remaining eighteen firms sold between 1% and 80% of their sales in the export market.

The top export destination amongst sampled exporters appeared to be the UK. South African exporters have been successful in accessing a range of other markets however, including the USA and Germany, as well as the French Islands, Scandinavia, France, Ireland, Australia, and the Middle East. The firms surveyed predominantly exported pine knock-down furniture, although some success is being experienced in the export of Saligna Hardwood furniture.[4] Clearly, establishing contact with buyers is far more difficult in the export market that it is in the local market. While manufacturers still approach prospective buyers directly, and are occasionally contacted by buyer, this is far less common than on the small domestic market. International furniture fairs and import/export agents play a significant role as a means of establishing contact with overseas buyers, with 49% of contacts initiated this way. Distance is always a factor in relations in the export market, and below we consider whether this has any impact on how well manufacturers are *hearing* their markets, and responding to market demands.

4.1 Hearing the Export Market

In order to gauge foreign market demand a postal survey was conducted of retailers in the United Kingdom and Spain respectively. A total of thirteen retailers responded to the survey, and between them they sourced from Western Europe and North America, Asia, Eastern Europe (Croatia), Latin America and, in one case, South Africa. As we outlined in Section Two, the survey yielded inadequate results to draw accurate conclusions regarding foreign retailers' perceptions of the performance of South African manufacturers. We are currently undertaking research aimed specifically at filling this gap knowledge. However, with the data at hand we are able to generate some idea of how well South African manufacturers are 'hearing' their markets, and of where South African exporters see their strengths and weaknesses as lying.

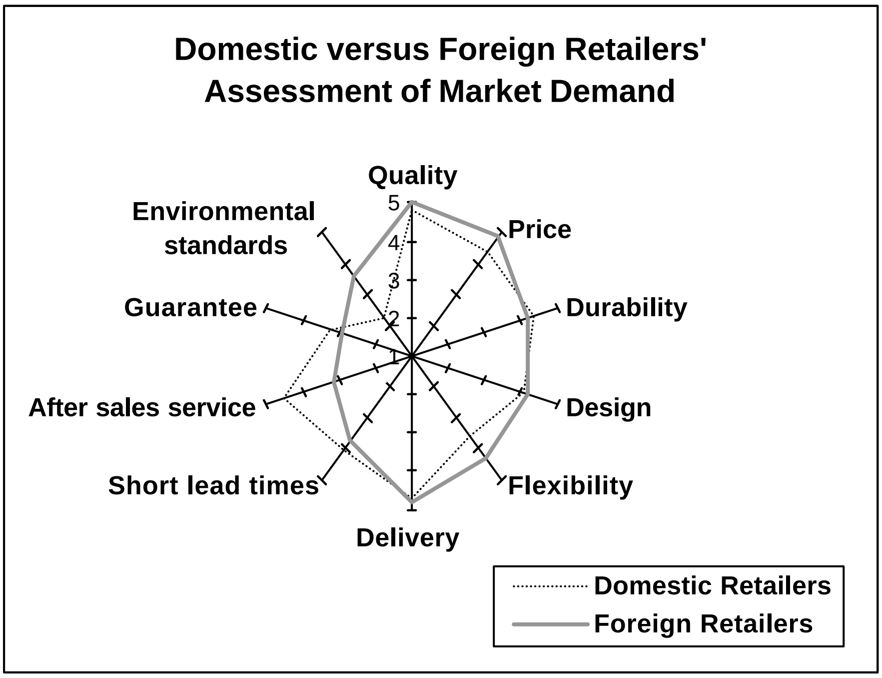
Comparing Domestic and Export Market Demand

As radar charts are a reflection of relative ratings, it is difficult to use them to accurately compare different markets, such as the domestic and export markets. However, it *is* useful to compare the way in which domestic and foreign retailers rate the various competitive criteria in their respective

[4] Saligna Hardwood is a locally grown renewable resource. Traditionally used for production at the low end of the market, its value is increasingly being recognised as an alternative to non-renewable rainforest timber. South African users of Saligna are enthusiastic about the possibilities for improving its international profile at the upper end of the market, and to this end there have been significant moves towards co-operation amongst value-chain stakeholders. The subject of the Saligna Hardwood value chain will be the subject of the next paper in the IRP furniture research programme.

markets, to the extent that this gives us a picture of the kinds of criteria that are important in the different markets.

Figure Eight:

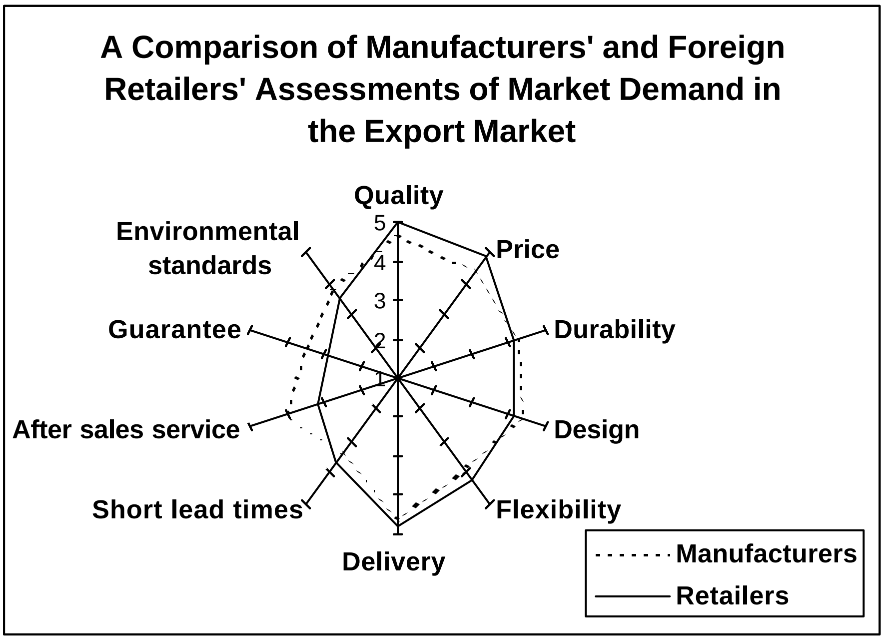


As we can see from Figure Eight, environmental standards are noticeably more important to foreign retailers than they are to South African retailers, and this accords with what we know about the relative level of sophistication of the two markets. Similarly, we have suggested that the high levels of retail concentration in the domestic furniture market makes for a highly demanding (and unequal) relationship between local retailers and manufacturers. This in turn makes after sales service an important criterion in keeping the domestic retailer happy and thus maintaining manufacturer access to distribution channels. While one cannot draw any firm conclusions from this sort of analysis of radar charts, what needs to be recognised is that market demands can differ dramatically between different market, and that manufacturers *must* be aware of these differences if they are to tailor their responses accordingly. Understanding market demand in foreign markets is extremely complex and problematic, especially for small and medium manufacturers. Manufacturers may well wish to look towards Italian and other European examples of inter-firm co-operation around marketing and exporting arrangements if they are to overcome these barriers to export marketing.

Certainly, our discussions with South African manufacturers suggests that they perceive the export market as more demanding than the domestic market, particularly in the areas of quality, design and environmental standards. Fifty percent of firms selling at least half of their sales into the export market adhered to some form of recognised quality standard, compared to just 15% of firms focusing on the domestic market. While environmental certification such as FSC or ISO 14000 is still relatively rare, with just 20% of exporters boasting such standards, 78% of all exporters feel that export demands have increased in the past five years, compared to 18% of domestic-market manufacturers. One manufacturer described environmental issues as the 'wildcard' in the export market, and certainly South African manufacturers are aware of the growing concern around environmental issues in the international market.

Overall, however, as Figure Nine indicates, South African exporters still tend to underestimate the relative importance of a number of competitiveness criteria in the export market, while at the same time overestimating the importance of others.

Figure Nine:

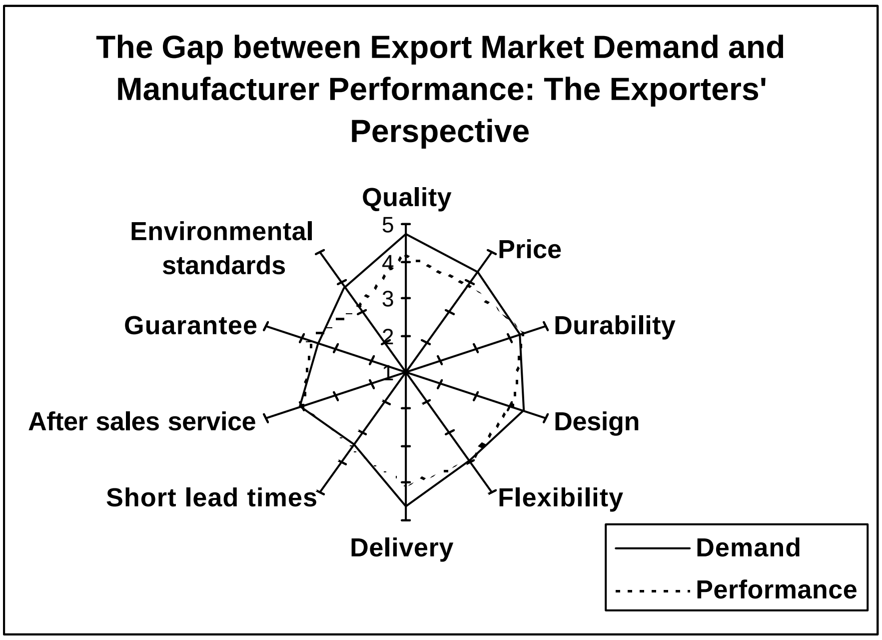


South African manufacturers may tend to overestimate the importance of after sales service as a result of its unusual importance in the South African market. The importance of environmental standards may be slightly overestimated due to the shifting role of this criterion as a determinant of competitiveness. However, given the long lead time manufacturers face in putting in place environmental certification, this may be to the benefit of South African exporters. More worryingly, it appears as though South African exporters have a tendency to underestimate the quality and price demands of foreign retailers, and these misconceptions will have to be addressed if firms are to remain competitive in the medium to long term.

Export Performance

Finally, moving on to the gaps between demand and performance, we see that, as shown in Figure Ten, South African manufacturers are aware that their performance on the export market falls short of market demand on a number of competitive criteria.

Figure Ten:



Worryingly, exporters feel that their performance is not adequate in terms of either quality or price, both critical competitiveness criteria where, as we saw in Figure Nine, South African exporters already appear to be underestimating market requirements. Manufacturers also feel that their performance falls short of demands in terms of design and delivery, as well as environmental standards, although, as Figure Nine suggested, South African exporters may be overestimating the latter gap.

In order to draw any firmer conclusions as to the weaknesses and strengths of South African exporters, as well as their performance relative to other national players, we would need to access foreign retailers who currently source from South Africa, or have done so in the past. It is this final phase of the study that is currently underway. Once complete this research will give us a more accurate picture of how well South African exporters are currently perceived in the export market; how accurately they perceive their own performance; and what areas they will have to focus on should they wish to improve their current market position.

CONCLUSION

As we outlined in the introduction to this paper, the furniture sector is one in which global trade is growing rapidly. In this context of increasing global competition both South African manufacturers focusing on the domestic market and their exporting counterparts need to be aware of shifts in market demand if they are to remain internationally competitive.

An accurate understanding of market demand is critical if firms are going to respond rapidly and appropriately to the challenges inherent in shifting consumer demand as well as to the challenges posed by competitors. The question then remains as to how well South African firms are positioned to respond to these challenges. The answers to this question lie in the relationship between manufacturers and the retailers they supply, in efficiency at the intra-firm level, and finally in intra-industry, or value-chain efficiency.

This paper has examined the extent to which South African manufacturers understand the demands placed on them by the markets they serve, and more importantly, how accurately they perceive their performance relative to this market demand. While there is certainly room for improvement at both the domestic and export levels, the experiences of the furniture sector in countries such as Italy show us that rapid learning *is* possible in the face of global competition. It remains to be seen whether the South African furniture industry has sufficient capacity to make the changes necessary for sustained international competitiveness. The issue of intra-firm efficiency will be the focus of future IRP furniture research, and will reflect to some extent the industry's strengths and weaknesses, as well as its capacity to change. However, change often requires an external catalyst, and international experience has suggested that this often comes in the form of retailer-manufacturer relationships that encourage the upgrading of manufacturer performance, or alternatively, in the common learning inherent in intra-industry co-operation.

This paper has gone some way towards examining the nature of manufacturer-retailer relations that impact on the industry, at least in the domestic market. To date there seems little to suggest that South African retailers are likely to play the role of catalyst in the upgrading of the domestic furniture industry. While we have inadequate information on the export market to make any firm judgements, it would appear that foreign retailers are far more likely to take on this role of catalyst than are their South African counterparts. The second catalyst to change mentioned comes in the form of inter-firm co-operation that has the potential to propel firms along the road to international competitiveness as groups of firms put aside traditional notions of competition to their mutual benefit.

Even in low-trust environments such as the South African manufacturing sector the possibility for inter-firm, intra-industry co-operation *does* exist. In fact, an initiative is currently underway in the South African timber products industry to solve the common problems of users of the Eucalypt hardwood, Saligna, through co-operation along the value-chain. Later research will examine this value-chain, with the intention of exploring the extent to which a re-organisation and re-conceptualisation of value-chain relationships can act as a catalyst to international competitiveness.

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