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## China, Peoples Republic of

### Market Development Reports

### All China Leather Exhibition

### 2008

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**Report Highlights:**

The scale of the 10th All China Leather Exhibition (ACLE) surpassed previous records of international exhibitors and it is becoming the best platform to link the leather industry with the retail market in China.

Critical issues in china's leather industry are ever-increasing environmental concerns, declining exports of leather goods, increasing labor costs and issues with VAT policy. This will affect China's domestic industry and ultimately affect exports of U.S. hides and skins. Despite recent turbulence in the financial markets, the demand for leather and leather products continues to develop in volume and the market trend is towards higher product quality.

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Shanghai ATO [CH2]  
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**2008 ACLE, Happy 10<sup>th</sup> Birthday**

The All-China Leather Exhibition (ACLE) held its 10th anniversary show in Shanghai in conjunction with the China International Footwear Fair (CIFF) and Moda Shanghai from September 3-5. The show included an extensive profile of exhibitors with a full category of products ranging from raw materials to processed chemicals and dyes, tanning and footwear manufacturing machinery. The ACLE show is recognized as the best platform to link the leather industry and the retail market in China, featuring the latest products and services from both international and mainland companies. ACLE reflects this huge and fast moving industry which is why it is considered China's premier and most international exhibition for sourcing the full range of leather sector requirements. Among the exhibitors were also suppliers of chemicals and technical solutions for all stages of leather production.

Exhibits Profile	
ACLE - Hides and Skins - Semi-Finished / Finished Leather - Exotic Leather - Man-made Leather - Synthetic / Natural Materials - Process Chemicals and Dyes - Component and Accessories - Equipment and Tools - Tanning Machinery - Shoe Machinery - Technology (e.g. CAD, CAM System)	CIFF/Moda Shanghai -Footwear -Garment -Handbags & Leather Goods -Fashion Accessories -Travel wares -Related Service

Since it was established in 1998, the ACLE has become firmly entrenched as the business-to-business forum which has opened up China's leather market to the world. The scale of this year's show surpassed previous records with the highest-ever participation of international exhibitors, and with a floor area of 57,500 square meters, the show attracted 1,126 exhibitors from 36 countries/regions. There were 24 country pavilions, including those from Argentina, Australia, Bangladesh, Brazil, Canada, China, Czech Republic, Egypt, Ethiopia, France, Germany, Hong Kong, India, Indonesia, Iran, Italy, Japan, Korea, Mexico, New Zealand, Pakistan, Portugal, Russia, Singapore, Slovenia, South Africa, Spain, Switzerland, Taiwan, Thailand, the Netherlands, Turkey, the United Kingdom, Uruguay and the USA. Seminars were scheduled on eco-friendly leather, innovative chemicals, design trends and

developments, Registration on Regulations, Evaluation, Authorization and Restriction of Chemicals (REACH).

Organized by the U.S. Hides and Skins and Leather Association, and supported by the Leather Industries of America, the U.S. pavilion embraced nineteen companies this year, all traders and processors of hides and skins. ATO conducted several interviews with exhibitors at the U.S. pavilion. For the majority of exhibitors, the show presented a great opportunity to meet friends and business partners. In comparison with APLF, the largest annual leather show in Hong Kong, some exhibitors said that they would likely not participate in that show next year due to the high cost, and more importantly, they felt the growing success of ACLE gives them confidence in finding new potential customers or buyers. An official from the Leather Industries of America (LIA) reported that she was pleased that the show attracted a solid traffic of professional visitors and provided a good platform for U.S. exhibitors to develop and maintain relationships with buyers. She believes that advanced processing techniques, experienced staff and superior quality enabled the U.S. leather industry to compete against other players. She added that LIA also considered India to be an important and growing market for U.S. hides and skins.

According to the show organizer, most of the association's members were happy with the trade fair. They were very satisfied with what they saw as a healthy show and had seen all the people they had hoped to. However, some hide traders complained that many prospective exhibitors and visitors were unable to obtain business visas because of the difficulties during the Olympics, consequently there were fewer visitors than expected this year.

### **Current Issues & Trends**

Critical issues in China's leather industry are ever-increasing environmental concerns, decreasing exports on leather garments, issues with VAT policy and increased use of new materials. All of this will affect the development of China's domestic leather industry and subsequently have an effect on U.S. hides and skins exports. Despite the recent turbulence in the financial markets, the growing demand for high quality leather and leather products continues to fuel growth in the leather industry.

#### *Strict Pollution Control*

Rising concerns about environmental protection and emission reductions of tanneries, particularly discharged wastewater, and the worldwide attention the Olympic Games brought

to China have forced the government to make drastic changes in effluent treatment rules. The government is now cracking down on any polluting industry and that includes the tanning industry. Many tanners and shoe manufacturers are looking at other Asian countries to make leather and shoes; Vietnam, Indonesia and Thailand are all under pressure to increase production. Nevertheless, their governments are also resisting any urge to expand polluting industries. In addition, moving tanning production to other countries is not that easy and building a tannery takes years, including the necessary water treatment facilities, requiring substantial capital investment which adds to the costs. Some industry specialists believe that although the most spectacular growth period in the China market is actually already over, the new reality for the leather and allied industries in China is not easy to estimate. Therefore, innovative processes and products are needed for companies to survive. On the other hand, considering the market size, there is no doubt that China is still recognized as the biggest and most important market for years to come.

The Chinese government has implemented very strict regulations to limit the expansion of energy and water-intensive tanneries. According to the CLIA, the new environmental regulations will become effective as of October 1, 2008. The aim is to reduce energy consumption by 20% and pollution by 10% per unit of GDP. The Chinese government also wants tanneries to be located together to facilitate an effective central control of wastewater treatment. In summary, strict pollution control conducted by the Chinese government will limit the future development of the industry.

#### *Decreasing Leather Good Exports*

The export volume of the main leather products, including shoes, garments, and gloves has continued to decrease. The import and export volume and export value of finished and semi-finished leather has decreased significantly. According to official data from the China Leather Industry Association (CLIA), from January to July of 2008, the exports of leather garments amounted to 11.99 million pieces with a value of \$520 million, down 29.7 percent and 17 percent, respectively, from the same period last year. Imports totaled 40,000 pieces valued at \$16.71 million, up 29 percent and 91.8 percent for the year before. The reasons for decreasing exports are the continuous appreciation of the RMB and the U.S. dollar's devaluation, and adjustments of the export tax rebate. In addition, China's shoe exports face challenges from various political and economic decisions this year, including anti-dumping taxes levied by the EU and the continuous increase of material and labor costs. The continuing decline in China's leather goods exports will ultimately affect its import demand for raw materials in the future.

*VAT Issues*

The Ministry of Finance, the State Administration of Taxation and China Customs jointly announced that tariffs for wet-blue skins would be subject to regular import duties of 7% plus an additional 17% VAT for hides and skins converted into finished leather products and then re-exported. This has also had a negative impact on the development of the Chinese tanning industry. The constant rise in hide prices has made profit margins impossible to maintain without substantial increases in leather prices. The new policy demonstrates the central government's intention of restraining the export of low value-added leather goods.

*Increasing Costs*

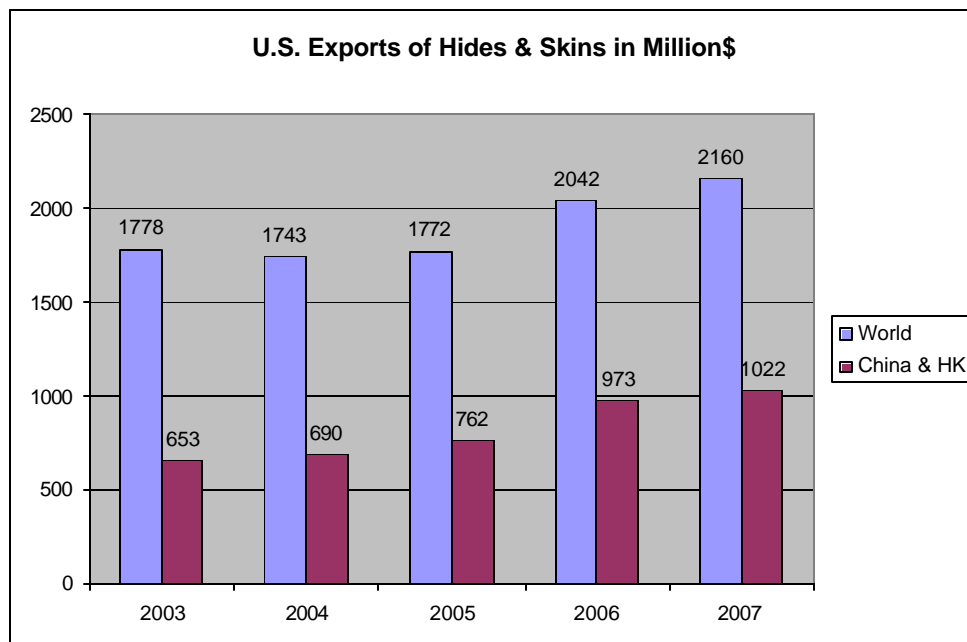
Appreciation of the Chinese RMB continues to put pressure on export oriented leather goods businesses. The average unit price for leather shoe exports has grown for five consecutive years, particularly in the last two years due to adjustments of macro economic policy. The rising price of raw materials, energy and labor costs have all led to the rise in overall production costs. According to China Customs statistics, during the first seven months of 2008, the average unit price for exported leather shoes was up nearly 19 percent from a year ago, to \$8.18. Increasingly, manufacturers are obliged to produce more value-added products, with a higher profit margin that allows them to absorb those extra costs.

*Imports of Finished Good Rising*

According to the CLIA, the total import volume of leather garments in the first half of 2008 was 28,000 pieces with a value of \$10.5 million, an increase of 26% and 106.6% respectively. The import value of fur garments increased 44.3% in the same period, which is one indication of China's growing middle class, representing a large and still growing market of those with enough disposable income to purchase high-end leather goods. China is not only a manufacturing platform but also a fast growing market for finished leather products.

*Imports from U.S. Maintains a Healthy Growth*

Driven by continuing strong demand from China's domestic market, U.S. hides and skins exports have increased dramatically in recent years. China continues to be the primary destination for U.S. hides and skins. According to official data from the U.S. Hides, Skins & Leather Association (USHSLA), U.S. bovine hides and wet blue exports set another record in 2007. The export value reached \$1.7 billion for hides and \$669 million for wet blues. China/Hong Kong continues to grow as a market and currently accounts for 43 percent of U.S. hide exports. From January-July 2008, the exports to China and Hong Kong reached \$665 million, an increase of \$40 million over last year.



Source: U.S. Hides, Skins & Leather Association (USHSLA)

### *Brand Building*

As the leading producer and exporter of shoes in the world, China's annual output has exceeded 10 billion pairs during the past several years, accounting for 66% of the global manufacturing total. However, some specialists believe that quality, efficiency and upgrading should be the future direction for China's shoe manufacturing industry in view of the difficult economic environment. Upgrading, restructuring and transferring will be the trend for China's leather shoes and garment industry in order to become more competitive. According to CLIA, the Chinese government encourages the development of the middle and high-end market over the low-end market and realizes that it is crucial for companies' brand building and marketing in order to survive and create higher profit margins in the international markets.

### *Eco-friendly Artificial Leather*

In order to reduce harmful emissions, a new type of artificial leather produced by using an eco-friendly, "green" manufacturing process, is made of unique fibers to give a texture and appearance comparable to natural leather while preserving the functionality of artificial leather. A considerable variety of products, ranging from car seats and interior textiles to sportswear, bags as well as IT product materials are available nowadays and gaining popularity in China. This trend towards eco-friendly artificial leather has drawn a great deal of attention from specialists in China's leather industry.

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