

IMPORT SUBSTITUTION

MANUFACTURING OPPORTUNITIES FOR ECONOMIC GROWTH

Billions of dollars' worth of goods imported in to West African countries can be produced domestically. Entrepreneurs who embrace innovation, adapt technologies and diversify into new sectors stand to lead the way in an area with enormous potential.

WORDS Wole Lawuyi & Eric Stambler

Ship Shape
\$42 billion dollars worth of goods are shipped into Nigeria annually, including to Apapa Seaport in Lagos, one of the busiest in Africa.

An estimated \$42 billion worth of imports were brought into Nigeria last year. The situation at Apapa's highly overcrowded seaport is characteristic across most of West Africa, which relies on imports to sustain its economies and meet daily needs.

While it is true that some of these products – those needed for transportation, power plants and heavy equipment, for example – must come from outside the region, many do not have to. Nevertheless, foreign-produced goods continue to pour in due to inadequacies in the local manufacturing base. The result is pressure on foreign exchange, a lack of well-paying jobs and continued dependency on outside supplies.

No one is suggesting that automobiles or power ▶



turbines should be produced in the region, nor agricultural goods that cannot grow effectively in the local climate, such as wheat. However, many items, such as soaps and detergents, fertilisers, pharmaceuticals, sugar, rice, fish and processed foods can be produced domestically.

The situation is particularly bleak in the manufactured goods sector where entire industries, such as tyre manufacturing and textiles have either failed or are on the verge of collapse in the face of import competition. According to statistics released by the Manufacturers Association of Nigeria, more than 800 manufacturing firms shut down operations between 2000 and 2009. But that was caused by a variety of factors and that doesn't mean that all manufacturing businesses are not viable.

Many of Nigeria's entrepreneurs contend that the failure of Government to tackle such unfavourable operating conditions as the high cost of power and poor infrastructure are responsible in part for the inability of some local producers to compete effectively with their foreign counterparts. This is not to excuse those businesses that fail to offer the goods and services that fit customer needs or that fail to provide the right marketing programs.

An entrepreneur who wants to embark on import substitution should embrace innovation. This might include diversifying into new sectors or experimenting with new product lines. Technologies from established producers in world markets could be adapted to meet local conditions, perhaps by bringing in expertise from abroad to operate production for a period of time.

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Whole industries often arise out of the experimental efforts of lone entrepreneurs. Garments in Bangladesh, cut flowers in Colombia, IT in India, and salmon in Chile are some of the better-documented cases.

Competitive Advantages Of Local Production

The advantage of local manufacture over imports can be profound.

Eliminating the cost of transportation from Europe, North America or China can mean savings of 5 to 10 per cent. Furthermore, duties can be avoided. Another positive effect is that inventories can be reduced. Since shipments can take six to seven weeks to arrive, local customers have to maintain high stocks of the goods they need to protect themselves against possible shipping delays. For certain products, using local production instead of imports can cut costs by 25 to 50 percent. Globalisation may sometimes increase the efficiency of manufacturing production, but it has become very inefficient for food distribution. In the West in 1900, the average farmer received roughly 40 cents out of a dollar's worth of food. By 1990 the farmer received only nine cents on the dollar, while the rest went to such things as advertising,

Fabric of a Nation
Entire industries in Nigeria such as textile manufacturing have either failed or are on the verge of collapse

transportation, refrigeration, distribution and retailing.

Compounding the inefficiencies of global distribution are rising energy costs. A linchpin of global trade has always been cheap shipping. But now, as higher energy costs drive up the cost of shipping, local producers will realise a competitive advantage over global producers who are transporting goods from faraway places. The costs of shipping can be expected to rise even higher, and thus the competitive outlook for local production will become even better.

Each local transaction multiplies many times over. When one buys a thousand naira's worth of rice from a local farmer, the farmer in turn spends the naira at a local store, the store owner uses part of that thousand naira to pay his employees, and the money circulates again. The more times 1,000 naira is spent in the community and the faster it circulates without leaving the area, the more income, wealth, and jobs it generates. If a country is importing rice or sugar rather than growing it, that multiplier effect migrates to farmers and their linkages in other countries.

According to Ngozi Okonjo-Iweala of the World Bank, Nigeria needs to "think of agriculture in a modern way, since it is a sector that can provide much employment."

The replacement of imports has a variety of benefits. Not only does it create jobs, but it allows the country to save money, increases the availability of products in the market and reduces costs.

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replacement of imports in many developing economies is the production of cleaning and personal hygiene products. Local factories can be established to produce soaps, colognes, perfumes, shampoos and other toiletry items, in addition to cleaning and cosmetic products. Local manufacturers can produce items that are competitive in both quality and price and create brands that the population can identify with.

Health care: Many of the basic medicines needed by the population can be produced locally rather than imported. These medicines include antibiotics, skin treatments and anti-inflammatory, anti-asthmatic and anti-parasitic medicines.

Home Hire
The replacement of imports such as cosmetics and medicines create jobs and allows the country to save money

Success Factors

Knowledge of customer needs and desires - Local producers are better able to understand consumer tastes and preferences towards products in their native markets. First-hand knowledge of cultural norms, in food and beverages, for example, means that local businesses are able to make better decisions about flavour, colour, packaging etc. when designing new products, than foreign counterparts. This could offer a key competitive edge in the marketplace.

Closeness to the market - Being closer to end customers can offer local producers a competitive advantage by reducing the costs of shipping and import duties. For this reason, local producers can sell small packaged items at affordable prices of N10 and N20, where importers would struggle to compete. They are also better placed to demand that their orders are made to a customised

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A focus on essentials like food, shelter and consumer goods would leave economies less vulnerable to risk

Something Fishy
Nigeria relies heavily on imported products such as fish

specification, thereby ensuring more efficient production and a better quality finished product.

Scale - Producing at a large enough scale is critical, especially in markets where availability of raw materials is limited to a few suppliers. Producers who are able to source raw materials in significant quantities have a cost advantage.

Cost advantage - Relying on a customer's patriotism to select a locally-made product over an imported one may not be enough to guarantee sales. Local producers should ensure that their products sell for less than - or at most, equal to - those of imported goods.

Quality - As well as pricing, quality remains important. In an era where customers are becoming more sophisticated, inferior goods have little chance of surviving. Local producers should therefore focus on implementing the right technology to produce at comparable or superior quality even if it requires that foreign expertise be brought in.

What Should Governments Do?

A coordinated effort to support, invest in and boost local production of essential products could lead to a gradual replacement of imports. With a focus on

essentials like food, shelter and consumer goods, this would leave economies less vulnerable to the risks and costs involved in relying on products from abroad.

Developing economies need to encourage private initiative within a framework of public action that encourages restructuring, diversification, and technological dynamism beyond what market forces would generate on their own.

In the case of Brazil, the steel, aircraft and shoe industries all resulted from import substitution policies. The government provided high levels of protection, public research and development and subsidised credit to generate results for entrepreneurs investing in new areas. In Chile, industrial policies played a huge role in creating strong industries for grapes, forestry, and salmon.

The overall plan should include incentives for those firms that make efforts to attract top technical expertise and strategic partners to the market. The strategy should also include planning for the needed workforce through vocational training; supplementing private venture capital with public funds according to transparent guidelines; building appropriate and efficient public infrastructure; encouraging international technology transfers, and encouraging research and development.

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