

## THE GAP ANALYSIS AS A TOOL TO IMPROVE THE COMPETITIVENESS OF WOOD PROCESSING SECTOR IN BOSNIA AND HERZEGOVINA

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### **ABSTRACT**

*This article provided a summary of the key factors related to the competitiveness of the wood processing sector in BiH as identification of gap analysis for that sector. The article is intended to provide a detailed model of production and export chains in BiH wood products industry. Through the market analysis, the author gained a more in-depth understanding of the market opportunities for wood processing sector. The author developed a draft market survey instrument with the objective to develop a questionnaire that is short, concise and easy to complete but captures the critical data for the market survey.*

*Gap analysis was conducted in order to determine points at which one or more interventions could help to significantly improve the competitiveness of the sector's small and medium enterprises (SMEs). This GAP Analysis assesses the status of Small and Medium-sized Enterprises (SME) in BiH wood processing sector, within the model of production and export value chains in forestry and wood processing sectors. The focus of this article also highlights the proposal for Point of Interventions (POI) within the pilot project.*

**Key words:** Gap analysis, wood processing sector, competitiveness, B&H.

### **1. INTRODUCTION**

This article is the overview of GAP Analysis of the sectors of wood processing and forestry in Bosnia and Herzegovina [1]. The author was conducted a special survey of wood processing and forestry sectors in BiH [1]. The survey was commissioned by and for use of the Swiss Import Promotion Programme (SIPPO) which is financed by the State Secretariat of Economic Affairs (SECO) and is being carried out by OSEC for the period 2009-2011. The programme's objective is to reduce poverty in selected countries through the facilitation of improved access to the EU and Swiss market for export-oriented SMEs [2].

### **2. SURVEY FINDINGS**

The emphasis of the survey is on those products which are of importance to domestic wood processing industry. Production and export value chains in wood processing sector, analyze the interaction options provided on market by different stake-holders, detailed information on the typical business services required by the producers and exporters within the value chain and proposal for Point of Interventions (POI) within the pilot project is provided. Trends and forecasts, as well as opportunities for and threats to BiH wood processing companies are highlighted and sources for more information are provided. The primary activities in the wood processing sector are divided over round wood, sawmilling and wood-based panels. Secondary activities are joinery and carpentry, and packaging. Sometimes the furniture industry is also included, but "pure" wood processing excluded furniture production. As part of the production process, forests are at the beginning of the value chain.

Therefore, sustainable forest management is necessary to provide those industries with the resources needed. To guarantee this sustainability of management, forests have been labelled with the FSC certification[3]. Forest management companies (FMCs) have different organization in FBiH and RS. In FBiH FMCs are established on the cantonal level while in RS there is only one company for management of the state forests. In FBiH there are 30 Forest Management Units (FMUs) and in RS there are 20 FMUs [4].

The wood processing sector in BiH is characterized by a large gap between its current performances and its real potential. Due to the influence of the transition and privatization processes, some very large, sophisticated, fully-integrated companies were disintegrated or even collapsed. Within this period, their technologies and equipment became obsolete; as a result, many factories for final wood processing are still not working in their full capacity. It is estimated that there are more 1800 companies operating in the wood processing sector today. A large number of sawmills in BiH operated illegally, without being licensed More than 260 companies (more than 80 producers of furniture) now make up this group producing more than 80 different types of products[5]. At the moment, there only plywood and associated veneer products, are made in BiH. Beech plywood is currently being produced in BiH, but of a minor quality. Consequently, the local furniture industry is obliged to import particleboard and MDF. BiH has a traditional joinery industry with a good reputation in Europe. Most of SMEs and they use domestic sawn softwood and hardwood for raw material. Some of producers have their own sawmill to guarantee consistent supply and quality. There are joinery facilities in every area of BiH. Technical skills exist thanks to a long tradition in the sector, but additional investment in continuing education / modernization is needed (e.g. design, hand-carving, etc).

The Author identified several BSOs in the wood processing industry, which are successfully offering services to wood processing industry. These services are offered predominantly for saw mills and furniture element producers. They provide industry information and consulting services via traditional market channels and this survey indicates that such service could be delivered using high impact ICT applications as well, especially Internet. According to the Author<sup>1</sup>, the situation with design development and adoption within the BiH wood processing industry is unlike that of the technologically developed countries. In addition, with the dissolution of big wood manufacturers such as Krivaja and Šipad, the BiH wood industry lost its research and development component, because this component was their integral part. The newly formed small and medium enterprises within the wood sector could not invest in this aspect of their business, which resulted in serious development problems and consequently hindered the exports. The European market requested FSC certified timber from wood processing industry in BiH, because this kind of certification enjoys the highest consumer recognition among the European customer. The focal point of wood producers in BiH should be to become (FSC) certified. As a new exporter aiming to penetrate the European market, it will almost be impossible to gain market share if products “made in BiH” are not FSC-certified. There are currently several FSC certificates held by companies in FBiH and by Forest Public Management Company in RS. The individual exporters taking part in trade need to own a Chain of Custody (CoC) certificate, in order to assure the certified timber to the end-customer. European importers expect exporters from BiH to be able to adjust to their requirements. The European market sets high demands on quality. Compulsory standards should always be met. Today, a necessary precondition for wood products export is for producers to have safety, materials, and quality standard certifications. Entering foreign markets and generating sufficient profit is only possible with innovative products and modern design. The focal point of producer in BiH should be to become (FSC) certified. Whilst FSC was first an opportunity, it has now evolved from being a trend to being a must. As a new exporter aiming to penetrate European market, it will almost be impossible to gain market share if “made in BiH” products are not FSC-certified. The European furniture industry is still a major importer of wood-based panels. This is opportunity for BiH wood processing industry, because the European furniture industry is under heavy pressure as a result of increased competition by exporters of furniture from developing countries.

Based on the Author’s experience and numerous SWOT analyses on SME sector done by domestic and international experts all barriers for SME sector development could be split in two groups:

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<sup>1</sup> Source: I.Alagić, 2008.

external and internal barriers. External barriers effects unfavourable business environment like: lack of SME legislation, SME strategy and policy on state level, slow company registration process, high bureaucracy, bad performed privatisation process, low level of investment in research, development, innovation and education, disharmonized BiH economic space, long-life education and vocational policy, uncompetitive industrial sectors without focus on perspective sectors for perspective SME value chains. Internal barriers effects low level of productivity and competitiveness of SMEs like: low level of skills in ICT and management, old technology, SMEs bounded to traditional production sectors with low added value, low export readiness of SMEs<sup>2</sup>. The surveyed companies appear not to have clearly defined their marketing objectives. Different companies have different marketing objectives. One of the objectives that were ranked as more important was to increase the sales of existing products. Most surveyed companies do not intend to develop new products for foreign markets. Generally, accessing new foreign markets and increasing sales in domestic and foreign markets are the most important marketing objectives for companies in the sample.

Most surveyed companies follow market trends in formulating their prices. Only small numbers of surveyed companies calculate their prices based on cost plus mark up. Generally, promotional activities of wood processing companies in BiH are poor and insufficient. In promoting their sales, most surveyed companies use two or more promotional activities. Small number of surveyed companies uses only one promotional activity. In terms of type of promotional activity, personal (mostly family) contacts and television and radio advertising are the most commonly used by the surveyed companies in promoting domestic sales. While, visit and participating at trade fairs and Internet advertising are the most commonly used by the companies in promoting foreign sales.

Slovenia, Croatia, Bulgaria and Romania are Bosnia and Herzegovina's main competitors in wood processing sector. Further competitors are Serbia, Hungary and partly Montenegro, as well as the Ukraine. All these countries offer products made out of identical raw materials, in similar product ranges and designs, but at lower prices due to higher productivity. It is of vital importance that BiH wood processing exporters comply with the requirements of the EU market in terms of product quality, packaging, labelling and social, health & safety and environmental standards. The BiH construction sector is the important market for timber and wood processing products, followed by the further processing industry (most notably the furniture industry) [6].

World Investment News noted that the BiH wood processing sector's key advantages in the global marketplace were its low-cost labour and forest resources. In terms of the companies' primary business, research results indicate that the wood processing companies in BiH tend to have more than one business activity. While the majority of companies specialize in only one business activity, some have a broader range of activities (two or more business activities). As it is indicated in the survey, some 70% of companies export to Western Europe. They export many products ranging from sawmill products, boards, joinery to prefabricated houses. Out of the surveyed companies, some 44% export predominantly to countries of former Yugoslavia, mimicking the old market. Customers in this industry are very diverse, from specialized agent type of companies that employ skilled people with knowledge of computers and foreign languages to saw mills that employ a low skilled labour force. Over the past five years there has been a decline in the number of people employed in this industry. There can be various reasons, but it is clear that the competition in the wood processing linked with reduced supply of lumber has pressured SMEs to become more lean and efficient in operations. Most of surveyed companies use only one distribution channel for their products. A small number of companies use two (three) or more distribution channels. However, some channels that are preferred by sawn mills do not suitable for construction joinery. Most wood processing companies distribute their products through a company salesperson-own people. Additionally, some of these companies distribute their products through independent agents or some of them do sales through showrooms<sup>3</sup>. The smallest number of surveyed companies distribute their products through stores making it the least

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<sup>2</sup> Source: I.Alagić, „Final report on the results of Evaluation of market and production potential in the wood processing sector in BiH and Evaluation of BiH companies for participation in SIPPO match making activities 2009-2011“, SIPPO, July 2008.

<sup>3</sup> Source: I.Alagić: „Final report on the results of Evaluation of market and production potential wood processing sector in BiH and Evaluation of BiH companies for participation in SIPPO matchmaking activities 2009-2011, SIPPO, July 2008.

common distribution channel in the sample. Large companies use more distribution channels, while majority of small companies use only one distribution channel for distribution of their products. Generally speaking, the percentage of sales achieved through agents as distribution channel is increasing and proportional to the frequency of use of this channel. Large companies most commonly rely on company salespersons and are the least interested in distribution via stores. Small companies use all distribution channels, and are also least interested for distribution through stores. Generally, distribution of wood processing products through stores is decreasing distribution channel in the sample. Exporters of timber in BiH have to make intelligent use of improved communication facilities like Internet (e-commerce). By using these facilities, they may be able to circumvent the importer and trade directly with timber dealers. There is a lot of attention for e-commerce in the timber sector. A number of Internet sites in BiH are developing cooperation arrangements. Internet is increasingly becoming an important medium in the timber trade. Education was identified as a major obstacle to general improvement of the wood processing industry in this report. This was also confirmed by the gap analysis and research from various sources (USAID CCA, REZ, PRISM, UNDP, etc.). The survey clearly showed that almost all of the surveyed companies agreed that education is needed. The surveyed companies also indicated that they often acquire such education from domestic BSOs or international partners, which is often expensive and not readily available. Assistance with market entry for BiH exporters could be offered by different type of organisations.

Before approaching organisations abroad, an exporter from BiH should first check with local business support organisations. Brand leadership could be achieved with the “Bosnian Beech” brand.

### **3. CONCLUSION**

The emphasis of the survey is on those products which are of importance to domestic wood processing industry. According to this survey, exporters’ wood processing products from BiH should pay extra attention to: Developing Bosnia Beech branding; Developing promotional materials; Identifying appropriate market niches; Developing an effective marketing strategy and; Ensuring an adequate supply of the wood processing products is available before promoting it.

Brand leadership could be achieved with the “Bosnian Beech” brand. This term has a positive image historically and worldwide in this field. The “Bosnian Beech” product can be promoted through both the solid wood and the veneer sectors [3]. Beech wood is one of the more relatively valuable wood species, and thus a cheap price strategy, must not be applied if a sustainable and internationally comparable level of earning is to be achieved. Overall, the GAP analysis and direct interviews indicate that there is a not as single predominant service that SIPPO programme can offer in order to reach increasing export of BiH wood processing sector . The findings indicate that a portfolio of services is needed in order to achieve success.

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