Export networking challenges and opportunities for manufacturing firms from developing countries

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Chapter 10

Factors that Determine the Export Governance Structure Choice: Comparative study

10.1 Introduction

This chapter conducts a comparative study of the Netherlands and Ugandan footwear and textile export markets to find out the specific conditions that influence the network design. From our case studies in chapter six and chapter seven we understand that the wholesalers and retailers in the Netherlands and Uganda are not interested in subcontracting and joint venture agreements. Therefore a flexible supply contract is the available alternative for entering the Netherlands and Ugandan footwear and textile export markets. The Eritrean footwear and textiles manufacturers have three alternative flexible supply contract possibilities. These are selling directly to wholesalers and retailers in the export markets from the manufacturing site, assigning agents at the export market (externalisation) and direct entry (internalisation).

Table 10.1 Similarities and differences between the Ugandan and the Netherlands footwear markets

Netherlands	Uganda
-*Business relationship is long term and based on trust and mutual benefit*	-*Business relationship is short term and based on personal supervision and lack of trust*
-*Purchasing initiative starts with careful market study and product design.*	-*Purchasing initiative starts with limited market study and without product design.*
-*To start business, information about production capacity, number and type of machines, skill of employees on fashion, and even personality of the manufacturers is critical.*	-*The footwear displayed on the market is the point of negotiation. Ugandan buyers have no interest in the manufacturer or his background.*
-*Characterised by strict procedural requirements*	-*Characterised by personal supervision*
-*Order is placed after demand is guaranteed.*	-*Purchase is made by wholesalers on the assumption that there are buyers in the domestic market*
-*Agents play an important role in facilitating the transaction*	-*Agents have no role in the purchasing process*
- *Suppliers information on the internet at trade fairs and formal education play a role in introducing the buyer to the import market*	-*Relatives play an important role in introducing beginners to the import market*
-*Previous business relationship is critical in starting business*	-*Previous business relationship is secondary in starting business*
-*Personal relationship is instrumental in minimising transaction costs*	-*Personal (family) relationship is instrumental in minimising transaction costs*

(Source: Chapter six and Chapter seven)

In the first case the title of the footwear and textiles passes when the wholesalers and retailers receive them where as in the second case the title passes when the manufacturer's agent at the export market sells the footwear and textiles to a third party. By direct entry we mean that an Eritrean footwear or textiles manufacturer opens a sales outlet in the Netherlands or Uganda to sell the footwear and textiles. In the following section we examine the importance of the aforementioned alternatives to the Eritrean footwear and textile manufacturers in relation to the opportunities that exist in the two markets.

The similarities and differences between the Ugandan and the Netherlands export markets outlined in Table 10.1 are used as basis for comparing the two markets. Five factors determine the export governance structure choice in the two export markets (Figure 5.1). These are asset specificity, uncertainty, volume and frequency of transaction, organisation capacity and room for resource mobilisation, and linkages.

10.2 Asset specificity

The specific investments required for entering the two export markets depend on which actor assumes the market research costs, product design costs, training (learning) and branding costs.

-*Market research and design*

Our findings in chapter six indicate that the incumbent middlemen in the Netherlands export market conduct the market research. They design the footwear and textiles based on the market data and forward this to the manufacturers mainly in Southeast Asia. For instance the purchasing process at Eegim shoe starts with idea collection. The trend watcher, mostly someone from the styling department, gathers ideas about the fashion trend for the next year. The ideas are collected from trade fairs, retail shops, and directly from consumers. The design department creates a design from the ideas. A group of marketing specialists and some selected members discuss the feasibility of the sketches and makes a selection. The designs are sent to the branch office in Taiwan. The branch office concludes an agreement with the manufacturers in Taiwan and other surrounding countries to produce a sample.

Table 10.2 Importance of distribution functions assumed by middlemen

Netherlands								
Asset specific investments	Footwear wholesalers and retailers				Textile wholesalers and retailers			
	Comforta	Eegim Shoe	Hoogen bosch	Scapino	Susan fashion	Vadotex	Zeeman	Hans Textile
Market research	VI	VI	VI	VI	VI	VI	VI	VI
Product design	VI	VI	VI	LI	VI	VI	LI	VI
Branding	I	I	I	LI	LI	I	LI	I
Training	VI	VI	VI	LI	I	VI	LI	VI
Uganda								
Asset specific Investments	Footwear wholesalers and retailers				Textile wholesalers and retailers			
	Fame Italian	Arafat Agencies	Mike Tusibera	Samuska enterprise	U.G. M.	Muyinza Trading	School Outfitters	NOB Traders
Market research	LI	LI	LI	LI	LI	LI	LI	LI
Product design	NI	NI	NI	NI	NI	NI	NI	NI
Branding	I	NI	I	NI	NI	NI	NI	NI
Training	LI	LI	LI	LI	LI	LI	LI	LI

Note: VI= Very important, I= Important, LI= Less important NI= Not important
(Source: Chapter six and chapter seven)

The response of the purchasing manager of Hans Textile is evidence for the above argument. When asked what his response would be if a manufacturer from Eritrea told him he could supply the right textiles to the European market, he said *"…we do not expect the Eritrean manufacturer to design a product that can be interesting for us. To avoid this problem we would give the manufacturer in Eritrea our designs and see what he/she can do with it. If he makes a good product out of it, there is a possibility of doing business."* Some buyers in the Netherlands do not make designs when the volume of the order is relatively small and in these cases trading companies in Southeast Asia fill the gap (see Table 10.2). The purchasing manager of Scapino said, "…*when we have a smaller order size we go to the export trading company. The export trading company is free to sell a similar type of footwear to wholesalers and retailers operating in markets other than the Netherlands. For that reason it can fulfil the minimum order requirement of the manufacturers."*

The internalisation of the market research and product design by the Netherlands wholesalers and retailers suits the Eritrean footwear and textile manufacturers as it reduces the need for scarce resources to finance transaction specific investments. In contrast to the Netherlands, our market study in chapter seven shows that the purchasing initiative of the middlemen in Uganda starts with a limited market study and without the production of footwear and textiles designs (see Table 10.2). No prior decision is made as to what type of footwear or textiles to buy and from whom. It is only when the design available in the spot market is appealing to the Ugandan wholesalers and retailers that they decide to buy. In this case the Eritrean manufacturers have to conduct a market study and produce a footwear and textile design accordingly. This leads to investment in market research and product design. To safeguard this investment and exploit the market opportunity better, direct entry to the Ugandan market becomes necessary.

-*Training*

Highly specialised and experienced domestic wholesalers, buying organisations, retailers and agents, dominate the Netherlands footwear and textiles markets. They invest in the training of sales people and promotion personnel to satisfy the requirements of their customers. Ultimately, by adapting to the requirements of the target market, they increase competitiveness. The purchasing manager of Scapino said, " *Although they are expensive we always buy footwear from wholesalers located in the Netherlands. The reason is that the wholesalers are nearer to the Netherlands market and have good knowledge of the fashion trend. They invest time and money to get footwear that is fit for the Netherlands market. Thus it helps us to cope with other competitors who buy footwear from the wholesalers*." If the Eritrean manufacturers are to enter the Netherlands market directly they must invest in training their sales personnel suitably for the market. Possibly hiring people could solve this problem, however, the cost is high and there is no guarantee for retaining the personnel for a longer period. Moreover, the Netherlands footwear and textiles export markets are sophisticated and there is less chance of the footwear and textiles manufacturers in Eritrea bypassing the aforementioned knowledgeable intermediaries. Thus selling to the wholesalers and retailers from the manufacturing site is the feasible alternative. The knowledge required in selling footwear and textiles in the Ugandan market is less demanding. The middlemen's purchasing decisions in Uganda are highly influenced by the attractiveness of the price. Lialigo Jamal, a textile trader in Muyinza trading company said "… *I am happy to buy textiles from Eritrea…but I must say that the price is the most important factor of the business component*." Moreover, as the list price is almost twice the selling price, the negotiation skill of the sales person is critical.

Table 10.3 Specific investments required for entering the Netherlands and Ugandan markets

Asset/market specific investments	*Netherlands*	*Uganda*
Market research	*Handled by wholesalers and retailers*	*Often handled by manufacturers/wholesalers*
Product design	*Often handled by wholesales and retailers*	*Often handled by manufacturers*
Training (learning) and branding	*Handled by wholesalers and retailers*	*Often handled by manufacturers*

(Source: Chapter six and Chapter seven)

-*Branding*

Branding is important for high fashion and classical shoes in the Netherlands Market. These shoes come mainly from European manufactures. They are also made in Southeast Asia under the supervision of the branded footwear wholesalers and retailers in the Netherlands. Retail chains and importers use fantasy labels and brands to distinguish their collections from those of competitors and also to target particular consumer segments. However, brand names are of little importance for slippers and other textile and plastic shoes. For a new, fashionable leather footwear manufacturer to play in the Netherlands export market, he/she has to build brand names, which are appealing to the buyer. Due to strict requirements in manufacturing and exclusive distribution brand names are transactions specific to manufacturers. However the wholesalers have many contacts and can sell the same brand to many retailers in the Netherlands. Consequently the branding cost is not a transaction specific investment to the middlemen. Compared to the Netherlands export market branding is less important in Uganda. Thus there are few branded footwear and textile traders in the market.

In conclusion, we note here that market research, design, training and branding costs are “transaction specific” to manufacturers. However, as the information gathered can be translated into different designs used for many transactions concluded in the home market these costs are not transaction specific to wholesalers. Moreover brand names are often given for several designs, which can be sold to several customers. As foreign manufacturers normally deal with a small number of selective and exclusive wholesalers and retailers, these costs are transaction specific to them. Thus, we conclude that dealing through wholesalers in the Netherlands who assume the market research, design, branding and training costs reduces transaction specific investments and therefore transaction costs. Unlike in the Netherlands, in Uganda there are no wholesalers, retailers and agents who can fill this gap. Thus, direct entry to the Ugandan market is the likely feasible entry strategy. Agents are not active in the Ugandan market due to high uncertainty, which will be discussed in the forthcoming section.

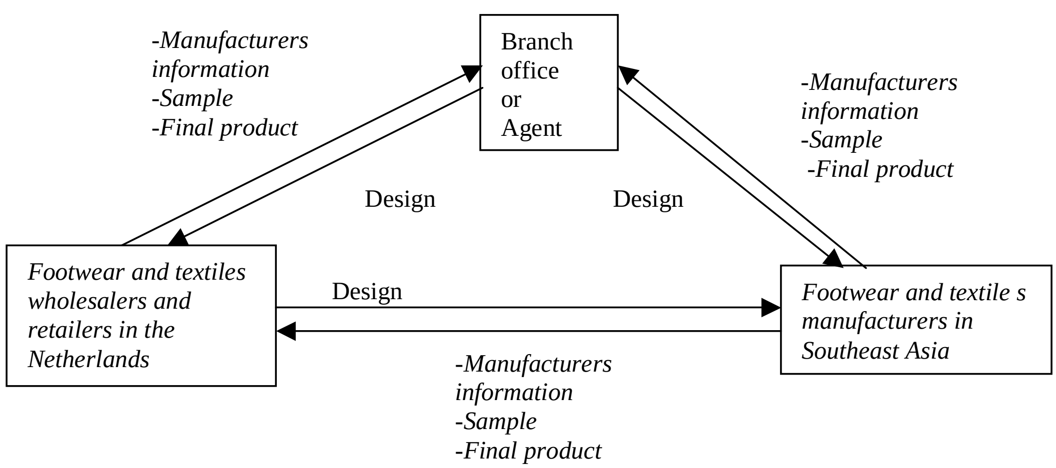
10.3 Uncertainty

The discussion in Chapter five reveals that four factors can decrease or increase the level of uncertainty in the footwear and textiles business. These are availability of information about the level of demand in the export market, level of trust between the transacting parties, availability of uncertainty-decreasing instruments and availability of courts of arbitration and litigation.

-Availability of information

The case studies in chapter six show that the footwear and textiles manufacturers in Southeast Asia depend on wholesalers and retailers in the Netherlands for market information (Table 10.3). The orders placed by the wholesalers and retailers in the Netherlands reflect the requirements of the Netherlands footwear and textiles export market. The orders contain information about the fashion trend and design, price and delivery time (Figure 10.1). The wholesalers, retailers and buying organisations deliver their requirements to the manufacturers in three ways. These are: (1) through an agent located at the manufacturing site (Comforta, Vadotex, Hans Textile etc) (2) through their branch office at the manufacturing site (Eegim shoe) or (3) directly from the wholesalers and retailers to the manufacturers (Intres). Direct delivery of the requirements is made when the wholesalers and retailers travel to the manufacturing site and negotiate with the manufacturers. The information helps the manufacturer to evaluate his production skills, purchase the right raw materials and plan the production and delivery time. However, as the Eritrean footwear and textile manufacturers can get this information from the wholesalers and retailers in the Netherlands while they are at home there is no need for direct entry to acquire this information.

Figure 10.1 Exchange relationships between wholesalers and retailers in the Netherlands and manufacturers in Southeast Asia



At the start of a new business relationship the manufacturer is required to give information about his competence. The information is mainly related to the manufacturer production capacity, the type of products he produces and the readiness in fulfilling promises (contractual trust). For example the general manager of Comforta said, " … *before we start business I would have to know the Eritrean manufacturer well. I have to be convinced that he has the capacity and skill to make the type of footwear I need to sell.*" The buyers in the Netherlands want to make sure that the manufacturer is competent enough to fulfil his obligations (competence trust) and will respect the agreement on exclusivity. In addition to the manufacturer's competence, the culture of the people and the business practices in the country where the potential manufacturer is located are also scrutinised. The purchasing manager of Scapino said, *"…it is important for us that we know the country first. Knowledge about the culture of the people, the business practices, the type of footwear manufactured, availability of footwear component producers, and the price level is important. If everything is Ok, I can*

place a trial order.” The exchange of information between the transacting parties can facilitate the trust building process and neutralises opportunism and ultimately uncertainty.
In the Ugandan market the buyers travel to the export market without solid knowledge of the footwear and textiles they want to buy. Consequently, the foreign manufacturer gets little or no information about the Ugandan market from the buyers. The unreliability of secondary data in the Ugandan export market and the lack of agents who can fill this gap make the uncertainty in the market high. Manufacturers do not appoint agents in Uganda because of the lack of trust in the exchange process and high monitoring costs. As a result, the direct presence of the manufacturer in the export market is necessary to view the export market from the inside and collect reliable first hand data.

-*Level of trust among the transacting parties*

The second factor, which influences the level of uncertainty in the exchange process, is the level of trust among the transacting parties (Table 10.4). Often the wholesaler in the Netherlands places an order to the footwear or textiles manufacturer in Southeast Asia after he secures an order from retailers in the Netherlands. In other words the footwear wholesaler in the Netherlands simply transfers the order from the retailers in the Netherlands to manufacturers in Southeast Asia. In this case there are two contracts. These contracts are a supply contract between the retailers and the wholesalers in the Netherlands, and a supply contract between the wholesaler in the Netherlands and the manufacturer in Southeast Asia. When the wholesaler in the Netherlands and/or the footwear manufacturer in Southeast Asia do (es) not fulfil their/his promise both of them face problems. The upshot is that the wholesaler in the Netherlands cannot supply the retailers in the Netherlands who are waiting for the shipment to arrive. The manager of Vadotex said “ *A few months ago a manufacturer from Bangladesh told us he would be shipping the textiles after a week. Two months later he told us the same story. This is something that we do not accept. Because not only we are losing the goods but also our programme is being disrupted...”*. This means the wholesaler faces the risk of losing the trust and potential business opportunities with the customers (retailers) in the Netherlands. Moreover, if the wholesaler in the Netherlands wants to find another supplier he has to make additional investment. The investment concerns activities to build trust and confidence with the new potential supplier. Time and money must be spent in gathering information about the new supplier and building competence trust. Finally, the news about his failure to supply the retailers in the Netherlands may spread rapidly and this can harm his reputation and future business opportunities with other footwear retailers in the Netherlands.

Table 10.4 Level of uncertainty in the Netherlands and Ugandan export markets

Uncertainties	*The Netherlands*	*Uganda*
Market information	*Handled by wholesalers and retailers*	*Often handled by manufacturers*
Trust	*Important*	*Not really important*
Contract enforcing organisations	*Well organised*	*Weak*

(Source: Chapter six and Chapter seven)

The most important consequence for the manufacturer of failing to fulfil his promise to the wholesaler in the Netherlands is that he is going to lose his long-term buyer. It is not easy for the manufacturer to find another customer and this may drive him out of business. Secondly, he faces the risk of losing the trust of other potential wholesalers and his reputation because information about his failure to fulfil his obligations can spread fast through the network. When both fulfil their promises, both gain from the business relationships. However, both lose when both fail to fulfil their promises. In this case we see a lot of interdependence between the buyer in the Netherlands and the manufacturer in Southeast Asia. For the buyer and manufacturer avoidance of dependence is not a priority, rather they like to build security out of it. In this respect the manager of Vadotex said, "*The important thing in business relationships is trust. If there is no trust between the parties, the written contracts have a lot of loopholes that either party can use to deceive the other. To answer your question directly we lose the money but we will not have any kind of business relationship with the manufacturer afterwards.*" Table 10.4 summarises the likely consequences.

The case studies in chapter seven reveal that the level of trust between the transacting parties in the Ugandan footwear and textiles export markets are in contrast with the findings in the Netherlands. The exchange process in the Ugandan footwear and textiles export market is characterised by lack of trust. A footwear importer in Uganda, Mary Thandle said, "*While we were exporting agricultural products from Uganda to Italy, an Ugandan customer asked us to bring a container full of footwear, which is about seven thousand pairs, for him. We accepted his request and we brought the footwear. However, our Ugandan customer refused to take the footwear and to pay the money. In this case we decided to sell the footwear ourselves. For this purpose we opened this shop and we are still importing and selling footwear from Italy*." This evidence reveals that the lack of trust in the exchange process forced Thandle to integrate the retail function. Moreover, Jjemba, a footwear wholesaler in Arafat Agencies said, " *We Ugandans lack trust. The lack of trust starts in the family. A husband and wife in the Ugandan family prefer to have different bank accounts, which you do not see in other African countries. This is mainly because they do not trust each other. This has an influence on the way we do business. For instance it is not common for a footwear trader in Uganda to give credit to his customers. Most of the customers who take credit do not pay back. Besides people do not want to use formal business practices such as a letter of credit as they want to evade taxes*."

Table 10.5 Consequences to the footwear and textile buyer and manufacturers in case of not fulfilling promises

		Footwear and textile buyer (wholesaler, retailer) fulfils his promise	
		Yes	No
Footwear and textile manufacturer fulfils his promise	Yes	-Both gain from the business relationship	-Manufacturer loses a customer -Long waiting period to get another long term buyer -Buyer loses his reputation
	No	-Buyer loses customers -High switching cost to find an alternative supplier -Manufacturer loses his reputation	-Both lose because they have to invest to establish a new business relationship

(Source: Chapter six and Chapter seven)

The Ugandan footwear and textile market is dominated by spot market price negotiation. Prior information exchange is rare. While in the Netherlands wholesalers and retailers buy footwear and textiles directly from manufacturers, the Ugandan wholesalers and retailers buy the footwear and textiles from wholesalers and retailers in the country of production or in a third country market (such as Dubai). According to Williamson (1985) the small order size of the Ugandan wholesalers and retailers does not justify direct entry. However, there is another way of enlarging the order size. By entering the market directly the manufacturers in Eritrea can even collect orders from the immediate consumers. Thus direct entry is still the plausible transaction governance structure.

-*Availability of contract enforcing institutions*

The third dimension that influences the level of uncertainty in the exchange process is the availability of contract enforcing institutions. Institutions are one of the sources of trust between the transacting parties. Our market study in the Netherlands shows that there are clearly laid down contract enforcing institutions that guide the business relationship between the footwear and textiles importer and the manufacturer. The first contract enforcing institutions in the Netherlands are the buying organisations. They give fourteen days guarantee of payment to the supplier any sales contract concluded between their member and a foreign supplier. Beside this quality inspection institutions, agents, and banks play a significant role in the smooth transfer of the footwear and textiles from the manufacturer to the buyer. The footwear and textile buyers in the Netherlands employ quality inspection institutions to certify the quality of the goods in the manufacturing site before they are shipped to the Netherlands. The certification is often made in reference to the footwear and textile design and other specifications forwarded to the manufacturer before production commences. Furthermore, buyer's agents certify the delivery of the right quantity and quality of footwear and textiles at the port of shipment. Banks control the availability of the documents necessary for the supplier to claim payment and for the buyer to claim the footwear and textiles. Moreover, although the transacting parties prefer to avoid going to court, when a need arises there are carefully laid down courts of litigation and arbitration. All the above-mentioned institutions contribute to the trust building process (neutralising opportunism) that reduces the uncertainty and therefore facilitate transaction between wholesalers and manufacturers.

Contract enforcing institutions in the Ugandan footwear and textile export market do not work well. Buying organisations in Uganda are informal social groups that are guided by personal relationships and family ties. The buyer makes the inspection of the footwear and textiles, receives the goods and conducts payment on the spot. Consequently, inspection institutions, banks, and agents play little role in facilitating the export transaction. The letter of credit barely works in the Ugandan market. Beside this due to the low level of trust exporters does not appoint agents. The legal system is unreliable and exporters always prefer to undertake the distribution function themselves. Indicating the ineffectiveness of the legal system, the manager of Allied Afri Trading house said, " *In Uganda you can get a person arrested not because he failed to honour his contract but because you are able to pay some money. The worst thing is even though you get him arrested by paying about $100, he only needs to pay $25 to the police to get out. The additional $25 is more important to the police than keeping him in prison."*

The Ugandan footwear and textile export market is full of uncertainty. This is mainly due to the weak legal system, corruption, lack of trust in the exchange process and lack of a culture of using uncertainty-reducing instruments (letter of credit, inspection institutions, agents etc.). These factors make it difficult for the footwear and textile manufacturer to appoint an agent in Uganda. In fact from the market study in Chapter seven we learned that appointing an agent is not common in Uganda. Consequently, the direct presence of the Eritrean footwear and textiles manufacturers in the Ugandan export market is critical to minimise the uncertainty that may arise from the opportunist behaviour of the traders and inefficiency of the contract enforcing institutions. In the Netherlands the exchange process is based on trust and long term business relationships. Thus, if the footwear and textiles manufacturers in Eritrea can offer enough information about their production capacity they can build competence trust and a transaction exchange process can be started thereafter. However, because competence trust is ascertained after inspection of the footwear and textiles, the presence of a strong agency organisation in Eritrea that can guarantee the quality of the footwear and textiles to buyers in the Netherlands is indispensable.

10.4 Volume and frequency of transaction

In Chapter five of this thesis we discussed the fact that the volume and frequency of the orders placed by buyers are among the factors that influence the choice of transaction governance structure in a certain market. Our market study in Chapter six reveals that the footwear and textile wholesalers and retailers in the Netherlands place large orders every six months. These orders are mainly related to the fashion and design trends in a certain season. However from our case analysis in the Eritrean footwear and textile manufacturing industry we learned that in the short run the Eritrean footwear and textile manufacturers can only sell a limited quantity to the Netherlands market. This is mainly because they have to improve their product quality to meet the requirements of the Netherlands buyers. Moreover, most of the footwear and textiles manufacturers in Eritrea are small in size and they produce small quantities. Even the larger ones have limited production capacity for each product line, as they produce different types of footwear and textiles. This makes product standardisation and co-operation in export among the Eritrean manufacturers necessary. Given the above reasons, in the short run direct entry of the Eritrean manufacturers to the Netherlands market is not feasible.

Table 10.6 Volume and frequency of transaction

Volume and frequency of transaction	*The Netherlands*	*Uganda*
Volume of transaction	*Large*	*Small*
Frequency of transaction	*Recurrent*	*Not recurrent*

(Source: Chapter six and Chapter seven)

In contrast to the orders placed by the footwear and textile buyers in the Netherlands, the order from an individual Ugandan footwear and textile buyer is small and trade relationships between buyer and seller are not recurrent (Table 10.6). According to the transaction cost theory this does not justify direct entry. Appointing agents in Uganda could solve this problem. However, this strategy does not work in Uganda due to lack of trust and high agent monitoring costs. Direct presence in the Ugandan export market enables the Eritrean manufacturers to enlarge orders by collecting every small order available in the market.

10.5 Organisation capacity and room for resource mobilisation

The basic indicators of the capacity of the organisation with regard to export are ability to finance exports, production capacity (machinery, raw materials, labour), and marketing knowledge. The production capacity problem has been discussed in the previous section. The other two indicators are discussed here.

Our studies in Chapters eight and nine reveal that the financial, human resource and knowledge capacity of the footwear and textile manufacturers in Eritrea is very limited (see Table 8.5, Table 10.5 and Table 10.7). Table 10.7 in particular shows that only the Bini shoe factory and the Asmara sweater factory have few market knowledge problems. Even in these organisations the market knowledge is concentrated in a single person who is acting as the general manager. The lack of specialised training institutions to prepare trained personnel for the footwear and textiles manufacturing firms aggravates this problem. Moreover the mobilisation of the young employees for national defence during the last four years has harmed the supply of human resources to the manufacturing firms. When asked about his capacity to produce asset specific designs forwarded by the buyers, the manager of the Asmara textiles factory said, “*Currently we produce T-shirts that are generic. Recently, we received an order from Germany with a superior product design. We did not accept the order because we do not have the capacity to do so*.” However, Erikog, which still operates in the local market and is highly supported by the government, thinks it has the human resource capacity to accommodate orders from foreign buyers.

Table 10.7 Organisational capacity of footwear and textile manufacturers in Eritrea

Capacity indicators	Footwear Manufacturers					
	Expo	Asmara	Negusse	Dahlack	Delux	Bini
Financial problems	VI	VI	I	I	VI	I
Human resource problems	VI	I	I	I	I	VI
Marketing knowledge Problems	VI	I	I	I	VI	LI
	Textiles Manufacturers					
Capacity indicators	Asmara Textile	Asmara sweater	Eritrea Textile	Barocko Textile	Erikog Garment	Ambesa Sweater
Financial problems	VI	I	VI	I	LI	I
Human resource problems	VI	VI	VI	I	LI	I
Marketing knowledge problems	I	LI	VI	I	VI	I

Note: VI= Very important, I= Important, LI= Less important, NI= Not important. (Source: Chapter eight and chapter nine)

The lack of capital investment in the manufacturing firms, except for a few, left them with obsolete machinery. Joint venture agreements with foreign investors may solve the financial and human resource problems. However, during the study no joint venture or subcontracting opportunities were found in the Netherlands and Ugandan potential export markets. The wholesalers and retailers only wish to conclude flexible supply contracts. Accordingly, for the Netherlands market the wholesaler, or retailer can handle the marketing activities. The only investment required is to train the manufacturers in Eritrea to produce standardised footwear and textiles. With the help of the designs coming from the buyers and their experiences the Eritrean manufacturers can improve their product quality. However, resource mobilisation is the key to realising entry to the Ugandan footwear and textile export markets as there are no wholesalers and retailers who can take the initiative for market research and product design functions.

Table 10.8 Organisational capacity of footwear and textile manufacturers in Eritrea in relation to export market requirements

Organisational capacity	*The Netherlands*	*Uganda*
Financial resource	*Not enough*	*Adequate*
Production knowledge	*Not enough*	*Adequate*
Marketing knowledge	*Not enough*	*Adequate*

(Source: Chapter six, Chapter seven, Chapter eight and Chapter nine)

In conclusion, because the Eritrean footwear and textiles manufacturers have limited financial and human resources, they cannot afford to raise the high financial and knowledge requirements to open a sales outlet and sell footwear and textiles in the Netherlands market (Table 10.8). Thus selling to wholesalers and retailers based in the Netherlands from the manufacturing site in Eritrea accommodates the financial, human resource and knowledge problems. However outsourcing marketing functions implies dependence. Flexible supply contracts with European distributors would normally concern large orders for the Eritrean manufacturers and this would lead to dependence. Discretional power can be specified in the contract, but knowing that the buyer controls the market research, this increases dependence for the manufacturer. We also observed that business relationships depend on past performance they often start with a small trial order. Reputation, trust and past performance are important assets in the marketing chain. We have already discussed the long lead-time and the interdependencies that result from it. This means that the dependence of manufacturers on the wholesalers involved in flexible supply contracts is high. This can be taken as an argument against these types of contracts as it may lead to opportunistic behaviour. However, wholesalers also depend on a trustworthy network of suppliers, as switching costs are also high for them. This serves as a safeguard for manufacturers and balances the dependency vis-à-vis the wholesalers. This is another factor that explains why flexible supply contracts are the dominant organisational form in co-ordinating exchange between manufacturers in developing countries and wholesalers in the Netherlands.

Due to the lack of trust, absence of wholesalers and retailers who can take the initiative for market research and product design, and the fact that only a few wholesalers and retailers in Uganda are willing to travel to Eritrea (see Chapter seven), direct presence of the Eritrean manufacturers in the Ugandan market is necessary in order to penetrate the market. For this purpose to raise the resources needed to open a sales outlet a horizontal business network among manufactures is needed. This is mainly because an individual manufacturer cannot do this alone.

10.6 Linkages

The strength of the business network relationship among manufacturers and buyers (wholesalers and retailers) in the export market are important factors for their competitiveness. This is mainly because of the importance of a smooth communication channel and trust. The lack of resources excludes the option for manufacturers to enter export markets on individual basis. Thus the manufacturers need to create linkages in order to get access to market knowledge and other resources. Joint ventures and subcontracting arrangements are interesting alternatives for the Eritrean manufacturers but the need for flexibility in the trade relationship implies that the distributors in the Netherlands are not interested in this type of relationships.

In the Ugandan market the business relationship is characterised as arms length. There are no long-term suppliers as well as buyers in the export market. Consequently the business relationship among manufacturers (suppliers), buyers (wholesalers and retailers) and immediate consumers is weak (Table 10.9). This gives the Eritrean manufacturers a chance of having a direct presence in the market for a reasonable investment. Sales from Eritrea to wholesalers and retailers in Uganda are not feasible as the volume of purchase is very small, documents such as the letter of credit are barely used by the Ugandan buyers and, finally, only a few wholesalers and retailers in Uganda are prepared to travel to Eritrea.

The strength of the business relationship between partners in the Netherlands and Uganda can be explained by two important concepts. These are security and flexibility. In Chapter five of this thesis we concluded that the higher the buyer's need for security the stronger the business relationship between the buyer and manufacturer and the more difficult it is for newcomers to enter the market. However, we also observed a willingness among retailers and wholesalers in the Netherlands to deal with new partners. These new business relationships are developed gradually and are based on trust and reputation. This provides opportunities for Eritrean manufacturers. It is recalled that institutions should be effective to strengthen trust building and to protect the interests of the partners involved in a flexible supply contract. Moreover we said that the higher the buyer's need for flexibility the weaker the business relationship between the buyer and the manufacturer and the higher the probability that the new entrant can penetrate the market. This fits the business relationship among the suppliers, wholesalers, retailers and consumers in the Ugandan market.

Table 10.9 Entry barriers in the Netherlands and Ugandan export markets

Entry barriers	*The Netherlands*	*Uganda*
Strength of supplier importer relationship	*Strong*	*Weak*
Strength of importer consumer relationship	*Strong*	*Weak*

(Source: Chapter six and chapter seven)[20]

In conclusion because the business relationships between the wholesalers and retailers in the Netherlands and their customers is strong it will be difficult for the Eritrean manufactures to win Netherlands customers. Consequently, it is better for the Eritrean manufacturers to sell the footwear and textiles to the incumbent wholesalers and retailers. This can help the Eritrean footwear and textiles manufacturers establish a link with the Netherlands market at a lower cost. However, the Ugandan buyers are highly flexible and the business relationship with their suppliers and customers is weak. With a better offer the Eritrean manufacturers can have the opportunity of entering the market directly at a relatively lower cost.

10.7 Conclusion

In the first chapter of this thesis, three businesses network alternatives were presented: subcontracting, joint venture, and flexible supply contracts. The export market study showed that no subcontracting and joint venture business opportunities were found. This is mainly because of two factors: first, there is no need for the importers in the Netherlands to make risky investments in manufacturing facilities. There are manufacturers who are capable of producing a product according to the importer requirements. The key issue is how to find a reliable manufacturer who can accommodate the orders. The wholesalers and retailers limit themselves to the marketing function by conducting market research, designing the product, training sales people and paying for branding costs. Often the technical aspects of production are left to the manufacturers and specialisation is becoming more important in Europe. Most of the importers like to remain as wholesalers or retailers rather than diversifying into production. Finally, the unstable political situation in developing countries makes investment more risky. Consequently, the case studies have shown that at present flexible supply contracting is becoming popular in the footwear and textiles business.

The general thrust of the discussion in this chapter is that the footwear and textile markets in the Netherlands and Uganda are different and require different marketing approaches. In fact our comparison acknowledges this difference and proceeds to identify the factors that differentiate the two export markets. Accordingly, the discussion in this chapter showed that footwear and textiles markets in the Netherlands and Uganda differ in the specific assets needed to enter the two markets, the uncertainties (behavioural plus environmental), and the volume and frequency of transactions placed by the respective buyers (table 10.10). Moreover, the two markets differ in terms of the resources needed by the manufacturers to

[20] Respondents were asked to rate the strength of their business relationship with their customers and suppliers. A comparison was also made between the two markets.

enter the markets and the linkages that prevail. Wholesalers and retailers are the main players active in the Netherlands footwear and textiles export market. Thus it is necessary for the footwear and textiles manufacturers in Eritrea to enter into the Netherlands footwear and textile export market through a vertical business network with wholesalers and retailers rather than bypassing them. The intermediaries in the Netherlands are well placed in the local target market, have considerable local market knowledge and crucial contacts with potential customers. However, to improve their product quality and expand their production capacity the Eritrean manufacturers need to establish a horizontal business network.

Table 10.10 Comparison of the two markets based on the variables that determine the governance structure

Factors that determine the export governance structure choice	*Netherlands*	*Uganda*
Asset specificity		
Market research	*Handled by wholesalers and retailers*	*Often handled by manufacturers/wholesalers*
Product design	*Often handled by wholesalers and retailers*	*Often handled by manufacturers*
Training and branding	*Handled by wholesalers and retailers*	*Often handled by manufacturers*
Uncertainties		
Market information	*Handled by wholesalers and retailers*	*Often handled by manufacturers*
Trust	*Important*	*Not really important*
Contract enforcing organisations	*Well organised*	*Weak*
Volume and frequency of transaction		
Volume of transaction	*Large*	*Small*
Frequency of transaction	*Recurrent*	*Not recurrent*
Capacity of Eritrean manufacturers to fulfil the requirements		
Financial resources	*Insufficient*	*Adequate*
Production knowledge	*Insufficient*	*Adequate*
Marketing knowledge	*Insufficient*	*Adequate*
Linkages		
Strength of supplier importer Relationship	*Strong*	*Weak*
Strength of importer consumer Relationship	*Strong*	*Weak*
Recommended network strategy	*Sales through wholesalers, retailers or agents*	*Direct entry (opening a sales outlet)*

(*Source: Tables 10.2…10.9)*

The high uncertainty in the Ugandan export market due to the lack of trust in the marketing chain, lack of reliable market data and inefficient contract enforcing institutions precludes the footwear and textile manufacturers from appointing agents in Uganda. Moreover, wholesalers and retailers in Uganda often travel to markets where they can find different varieties of footwear and textiles from which they can choose. They buy a limited volume of footwear and textiles from each design. According to the transaction cost theory this does not justify direct entry. However, direct presence in the Ugandan market can help the Eritrean footwear and textiles manufacturers to enlarge their sales by collecting orders even from the immediate customers. The quality and institutional structure in Eritrea is not yet ready for entering the Ugandan and the Netherlands markets and great deal has to be done. Chapter eleven discusses these factors.