

Summary of OTF Carpet Sector Activities

Overview

- The Afghanistan Competitiveness Project is a two-year project financed by the United States Agency for International Development (USAID) and implemented by the OTF Group. The objective of the project is to develop growth strategies for carpets, dried fruits and nuts, marble, finance and transportation.
- There are three core pillars of OTF's activities in Afghanistan: strategy development, institutional support, and competitiveness outreach.
- *Strategy*
 - Afghanistan's carpet exports were valued at \$140 M in 2004. Growing current exports will require increasing production volume as well as increasing the trade value captured in Afghanistan. The sector strategy therefore focuses on building capacity to address these needs.
 - Financing for increased manufacturing capacity and upgrading of current production can feasibly come from commercial sources. However, the ability of carpet producers to sustain local interest rates of approximately 15% is dependent on the ability to export directly to end-markets and sell for prices between 1.5 to 2 times of what they currently sell for. At current price points, they cannot afford commercial loans.
- *Institutional support*
 - The Afghanistan Carpet Committee by the Ministry of Commerce with support from the OTF Group. The Committee is the main leadership body of the carpet sector.
 - The Carpet Committee has spearheaded the following initiatives under OTF's leadership:
 - support for financing cut and wash facilities
 - supporting trade delegations to Germany and the US
 - cultivation of a design sub-sector.
 - The main challenges that the Committee is currently focusing on are:
 - access to land
 - access to finance
 - access to markets.
- *Outreach*
 - The OTF Group has been active in engaging carpet producers and traders in Kabul and beyond on behalf of the Afghanistan Carpet Committee.
 - Seminars have been conducted in Kabul, Mazar, Andkhoy, Maimana, and Herat in collaboration with carpet associations and the Afghan Chambers of Commerce and Industries.
- The sustainability of OTF's activities in support of the carpet sector is a serious concern. The Afghanistan Carpet Committee must take over from OTF to support the implementation of the carpet strategy and actively engage in initiatives to support the carpet sector. It is expected that the Committee will be able to rely on substantial support from the newly formed Export Promotion Center.

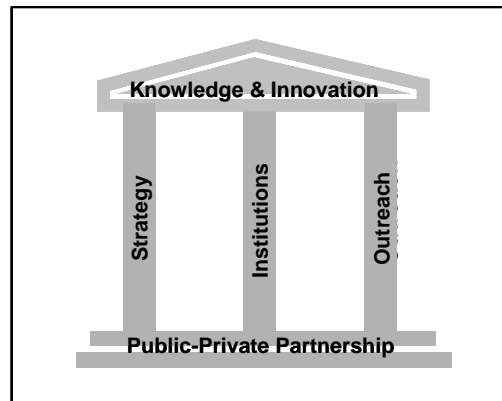


Background on the Afghanistan Competitiveness Project

The Afghanistan Competitiveness Project is a two-year project financed by the United States Agency for International Development (USAID) and implemented by the OTF Group.¹ The objective of the project is to develop growth strategies for 3 export-oriented sectors – carpets, dried fruits and nuts, and marble – and two enabling sectors – finance and transportation.

The strategies are based on the concept of forming industry ‘clusters.’ A cluster is a group of firms and related organizations that collaborate and compete at the same time to achieve a higher rate of innovation and productivity than they would otherwise achieve on their own. The strategies that the OTF Group develops with its partners require active participation from the private sector (the primary actor), government, business associations, related knowledge institutions and the donor community.

There are three core pillars of OTF’s activities in Afghanistan: strategy development, institutional support, and competitiveness outreach. The development of all three pillars is guided by a firm belief in the power of knowledge and innovation to change economic sectors, as well as the importance of public-private cooperation to address pressing business barriers. A summary of OTF’s activities for each of the core pillars is presented below.



Carpet Sector Strategy

Afghanistan’s carpet sector faces two major challenges: growing production volume and increasing the trade value captured in Afghanistan. The strategy therefore focuses on building capacity to address these needs.

The strategy envisions that new production growth comes from integrated production facilities, where the majority of the carpet processing is done on-site, in a factory-like facility. This allows for greater quality control, which will in turn allow producers more flexibility in design and new product development. This type of production also requires considerable investment in design and marketing, as both are essential to serving international buyers. Both design and marketing costs will be absorbed by private businesses, though public support is likely to be required as well.

Current production is primarily conducted through distributed networks of business and individuals. Carpet producers provide the capital and control design and sales. Most other processes are outsourced to other businesses or individuals. Currently over 90% of this production is sold to Pakistan, where it is then on-sold to wholesalers and retailers in end markets. The main thrust of the strategy with regard to this production is to divert more of this trade to Afghanistan. This will likewise require considerable investment in design and marketing, to replace the role currently served by intermediaries in Pakistan.

Situation analysis:

- Carpets are Afghanistan’s largest export, valued at \$140 M in 2005.
- Cutting and washing is undertaken almost wholly in Pakistan. Building a strong Afghan brand will require that carpets are cut and washed in Afghanistan and not finished in Pakistan.
- The carpet market, like all interiors markets, is constantly changing. Understanding trends, responding to them, and even leading them, will be key to Afghanistan’s success.

¹ The ACP was launched in September 2004 and concludes in August 2006. More information on the OTF Group is included in the annex.



Establishing goals:

- Good opportunities for growth exist. Despite a global market decline in value of 4% annually from 1998-2003, the market appears to be rebounding. Good growth figures are expected for 2005 and 2006.
- A combination of repatriation of weavers from Pakistan with increases in productivity over time can lead to average growth of the Afghan carpet sector of 11% annually.
- Changes to the current mix of products will be required as tastes shift and new carpet styles emerge.
- The growth of the cut and wash sector will add limited increased value but is key to increasing sales to end customers. Growth of the cut and wash sector will have to keep pace with the growth of end-market sales.

Carpet buyer survey:

- The product's aesthetics, quality of inputs, and value should form the foundations of a national carpet brand. According to wholesalers, focusing on 'unique Afghan attributes' is unlikely to have much traction.
- The data suggests that Afghanistan is well positioned with its production of hand-knotted, naturally dyed carpets. It should maintain and continue to improve its production of high quality *Chob Rung* carpets. However, the contemporary design market is an untapped opportunity for many Afghan producers. Entering it will require extensive learning and technical support to producers for both design and production.
- Supplier reliability and ease of transaction are what matter most to buyers. Afghanistan rates poorly as a supplier. The challenge lies in addressing this, while an opportunity exists in that Afghanistan is still a little known exporter.

Relative position:

- Focusing on the higher end of the market plays to Afghanistan's natural strengths in terms of good quality inputs and a tradition of carpet weaving. However, particular attention to quality will be required, as well as increased investment in building design capacity.
- Pursuing a differentiation-based strategy will require extensive education among all producers of customer needs. This will require substantial institutional capacity, in terms of: education about demand; ability to create designs that respond to demand; support services to facilitate buyer interaction.
- A strong brand will be key to supporting Afghanistan's differentiation. Addressing labor issues – for which neither India and Nepal were sufficiently prepared in the past – should be an important element of the brand creation.

Action guidelines:

- Financing for increased manufacturing capacity and upgrading of current production can feasibly come from commercial sources.
- However, the ability of carpet producers to sustain local interest rates of approximately 15% is dependent on the ability to export directly to end-markets and sell for prices between 1.5 to 2 times of what they currently sell for. At current price points, they cannot afford commercial loans.

Institutional Support

The Afghanistan Carpet Committee was established in May 2005 by the Ministry of Commerce with support from the OTF Group. The objective of the Carpet Committee is to address and resolve business barriers faced by carpet-related businesses through joint public and private sector cooperation.



The Carpet Committee comprises the following members:

- Government representatives: Ministry of Commerce (chair), AISA
- Business Associations: Afghan Carpet Exporters Guild, Kabul Carpet Manufacturers and Exporters Association
- Private business representatives: Yusuf Nabi Ltd., Rahmati Ltd., Khal Mohamad Ltd.
- Other organizations: OTF Group

The Carpet Committee meets on a regular basis to address specific issues. If necessary, it establishes working groups dedicated to addressing high priority concerns, such as special working groups on access to land and access to finance.

Carpet Committee meetings

1. May 2004 – Kick-off
2. June 2005 – Exhibition
3. August 2005 – Setting Goals
4. Sept 2005 – General Meeting
5. Dec 2005 – General Meeting
6. Dec 2005 – Finance
7. Feb 2006 – Access to Land
8. Feb 2006 – Export documentation (workgroup)
9. March 2006 – Access to Land (workgroup)
10. April 2006 – Finance
11. July 2006 – Atlanta Delegation

Quick-win Initiatives

The Carpet Committee has spearheaded a number of quick-win initiatives in collaboration with other partners to deliver short-term benefits to members of the carpet sector. These initiatives have been primarily led by the OTF Group. A summary of each is included below.

Initiative 1: Financial and Business Planning Support to Cut and Wash Businesses in Afghanistan

- Objective: Increase the capacity of the carpet cut and wash sector through providing access to grant facilities and business planning support.
- Implementing Partners: CNFA, UNDP, UNEP.
- Results to date:
 - Over \$115,000 of grant financing awarded to cut and wash sector as a direct result of the initiative.
 - Business plan template developed, allowing for easy replication.
 - Partnership model for cooperation among donor organizations established.
- Next stage: Improving access to commercial financing (i.e. non-grant) for cutting and washing facilities.

Initiative 2: Support for Carpet Producer Participation at DOMOTEX 2006

- Objective: Build producers' contacts with buyers in end markets, while also increasing their exposure to international product and competitive trends.
- Implementing Partners: AICC, CIPE, AISA and Cluster Pulse (India).
- Results to date:
 - 3 marketing consortia formed and coached on the consortia model. The methodology and approach are comparatively new to Afghanistan, and bound to have impact beyond the carpet sector.
 - Over 25 carpet producers attended the DOMOTEX Carpet Fair in Germany for the first time, expressing overwhelming support for the initiative, highlighting the importance of business contacts made and market learning generated.
 - All participants plan to attend DOMOTEX 2007.
- Next stage: Independent participation at Atlanta Carpet Fair in the USA in July 2006 (underway) and planning for DOMOTEX 2007.

Initiative 3: Stimulating the Growth and Innovation of a Local Design Sector



- Objective: Stimulate local capacity in Afghanistan to both drive and respond to global carpet design trends. A carpet design contest and award highlights the importance of taking a pro-active and market-based approach to carpet design.
- Implementing partners: AWBF, Aina Media and Culture Center, ACEG.
- Results to date:
 - ACEG awarded \$10,000 grant to establish a design reference center.
 - Design reference center launched and fully operational.
 - Highly successful contest launched, attracting over 30 designers and over 80 designs.
 - Design contest and award covered in the local and international media.
- Next stage: Continue to support the development of ACEG design center and publish a “Yellow Pages of Carpet Designers of Afghanistan.”

Current Focus

The main challenges that the Carpet Committee is currently focusing on are:

- *Access to land:* A working group has been formed to work with AISA to speed up the development of the Kamari Industrial Park and to support AISA in addressing and resolving development barriers.
- *Access to finance:* A working group has been formed to work with commercial banks to address how to improve the flow of both investment and working capital, and to potential lower interest rates charged to carpet businesses.
- *Access to markets:* A delegation of carpet producers is currently on a trade mission to the US. The Carpet Committee will work with this delegation and other producers to support their ability to export directly to end-markets. The Committee will also work with the Export Promotion Center to support delegations to travel to carpet fairs in Germany and the US in January 2007.

Post-OTF sustainability concerns

The sustainability of carpet sector activities is a major concern. OTF has made concerted efforts to involve other organizations in all activities that it has undertaken under the aegis of the Carpet Committee. However, at this point in time, it is highly likely that when OTF leaves virtually all of the activities that it has led will come to a halt.

It is therefore imperative that the Afghanistan Carpet Committee is further consolidated as a leadership organization for the carpet sector and develops the capacity to undertake the kinds of initiatives that OTF has led over the past 18 months. This will require the active participation of leadership from the Ministry of Commerce, as well as a full-time secretariat which will be able to support the Committee and manage initiatives that the Committee chooses to undertake. It is envisaged that the newly formed Export Promotion Center will play a key role in supporting the Carpet Committee in this manner.

Sector Outreach

The OTF Group has been active in engaging carpet producers and traders in Kabul and beyond on behalf of the Afghanistan Carpet Committee and in collaboration with carpet associations and the Afghan Chamber of Commerce and Industries.

Initial outreach seminars focused on general competitiveness issues and what it takes for firms to succeed in a global economy. Subsequent seminars focused on carpet-specific competitiveness challenges, and how public-private and inter-firm collaboration can serve to address them.

A summary of key outreach activities conducted to date is below.



1. Dec 2004 – Sector Kick-off Summit, Kabul
2. March 2005 – Regional Summit, Mazar
3. April 2005 – Regional Summit, Herat
4. May 2005 – Cut and Wash Seminar, Kabul
5. June 2005 – Sector Update Seminar, Kabul
6. Sept 2005 – Market Access Seminar, Kabul
7. Nov 2005 – Regional Summit, Maimana
8. Dec 2005 – Regional Summit, Mazar
9. Dec 2005 – Regional Summit, Andkhoy
10. April 2006 – Market Access Seminar, Kabul

Key Lessons Learned

The Afghanistan Competitiveness Project has been very well received. The efforts of the OTF Group in support of the carpet sector have been often praised by businesses and government alike. OTF believes that the foundations for the continuation of its efforts, under the leadership of the Afghanistan Carpet Committee, are also in place. However, there are two key corrections which, in hindsight, the OTF Group would have liked to have made to the project approach:

Parallel implementation

The most important lesson learned is the importance of combining strategy development with implementation components. This is important for a number of reasons:

- *Maintaining attention.* Sector-level strategies are of limited relevance to business owners, who make up the majority of the sector. They are more interested in what short-term benefit an outside actor will deliver to them as an individual business. Without this, it is not possible to engage the sector over a many month period.
- *Establishing credibility.* Outside organizations are often accused of writing reports but delivering nothing tangible as a result. High-impact, near-term gains are an important means by to generate credibility.
- *Testing ideas.* Through the implementation of initiatives, important experience is gained that can be incorporated into the strategy. The initiatives can be used to verify the relevance of ideas, test approaches/methodologies, and develop realistic goals and targets based on real experience.

In capacity poor countries, such as Afghanistan, much of the management of such initiatives will have to be borne by a lead agency, such as the OTF Group or the newly formed Export Promotion Center. This requires sufficient staff and budgetary allocation.

Seed capital

The efforts of the OTF Group with the carpet sector would have been strengthened by the establishment of a fund to provide seed capital to businesses, who are awarded small grants on a competitive basis. The fund can be used to test new business ideas and finance potentially high-risk but high-innovation initiatives. The fund would be used in conjunction with, and in support of, the implementation of sector initiatives.



Annex: Background on the OTF Group



Introduction

The OTF Group is the strategic business partner for regions and nations that are striving to build international competitiveness. Our work focuses on building competitiveness at the firm-level by developing winning strategies, fostering cooperation within clusters of firms, and facilitating productive dialogue between private and public sectors to promote innovation.

The OTF Group began its work as a leader in innovative thinking on competitiveness in 1991 as the Country Competitiveness division of the Monitor Company, an international strategy consulting firm. In 2000, backed by venture capital investors, OTF spun off from Monitor to focus its efforts on creating software tools and advisory services to help leaders think more strategically and to compete more effectively in global markets.

Our Clients

Our private and public sector client base spans North and South America, Europe, Asia, Africa and the Middle East. Among our recent clients are the leadership of Brazil, El Salvador, Bermuda, Jamaica, Rwanda, Serbia and Afghanistan. In addition, we have collaborated extensively with multilateral and bilateral development agencies such as the World Bank Group and the United States Agency for International Development (USAID). In the United States, we have advised regional economic development organizations in the states of California, Florida, Massachusetts, Texas and Washington and are a lead partner in the regional competitiveness efforts of the US Council on Competitiveness. We have helped develop competitiveness strategies in a broad mix of industry clusters, ranging from tourism and textiles to banking and biotechnology.

Our Competitiveness Practice

The objective of OTF's Country Competitiveness Practice is to advise leaders of private and public sector organizations on how to most effectively:

- Build a culture that supports innovation and entrepreneurship
- Increase the competitiveness of firms and clusters
- Facilitate significant, long-lasting change.

We offer a variety of services, including competitiveness leadership seminars, and comprehensive competitiveness building engagements. For these in-depth engagements, we develop a customized competitiveness program based on the specific opportunities and challenges faced by the region.