

De La Salle University

**AKI**

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for Business, Economics,  
Research, and Development

**Philippine Furniture Industry:  
Adjustments for the RP-US Trade  
Agreements**

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## **Abstract**

This paper is a descriptive study that attempted to identify the factors that helped the furniture industry in the Philippines survive in spite of pressures of globalization. This paper also tried to determine how the industry was able to innovate, develop skills, mix design, combine local manufacturing capability and global and local sourcing to become competitive in the high end, low volume markets. This paper likewise analyzed if the industry has the capability to capture the mid-range, high volume furniture niches. Finally, the paper also pinpointed adjustments the furniture industry has to perform, in the short and long run, to address this market niche. To analyze the industry problem, the Porter's Diamond Model Framework was utilized to determine the country's internal competitive advantage.

## **Philippine Furniture Industry: Adjustments for the RP-US Trade Agreements**

Despite resource constraints and international competition, the furniture industry (particularly in Cebu and Pampanga) was able to remain competitive through various factors in the last decade. Product innovation has helped the industry survive in spite of the pressures of globalization. This industry paper will attempt to find out the factors that helped the industry survive in the last decade. How was the industry able to foster innovation and develop skills, which changed the industry and transformed the image of the Philippines as the Milan of Asia in terms of design and artisanship?

This paper will try to identify how the local firms manage to mix design, local manufacturing capability and global and local sourcing to become competitive in the high end, low volume markets. If all of these can be sustained in the next ten years or so, then the Philippine furniture industry would be internationally competitive.

This paper will try to determine if the industry has the capability to capture the mid-range, high volume furniture niches. What adjustments will the furniture industry have to do to address this market? What will the industry have to do in the short and long run to address this market niche?

To analyze the industry problem, the Porters Diamond Model Framework will be utilized to determine the country's internal competitive advantage. Porter's work was driven by a belief that existing theories of international trade told only part of the reasons why industries succeeded or failed. For Porter, the essential task was to explain why a nation achieves international success in a particular industry.

Porter's model will further examine the four major areas of building a country's competitive advantage. What led to an industry having a competitive advantage other countries could not replicate. This will identify how the furniture industry addressed the issues of resource constraints and global competition and turned them into their favor. The four broad attributes of Porter's Diamond Model Framework will recognize the environment in which local firms compete and these attributes promote or impede the creation of competitive advantage. These attributes are the following: factor endowments, demand conditions, relating or supporting industries, and local firm strategy, structure, and rivalry.

Factor endowments is defined as the nation's position in local factors of production such as availability of skilled labor or the local infrastructure found or necessary to compete in a given industry. Demand conditions are the reasons for the home demand for the industry's product or service and how this influences or shapes the industry's direction. Relating or supporting industries discusses the presence or absence of supplier industries (backward integration) and related industries (forward integration) that make the industry internationally competitive. Finally, local firm strategy, structure and rivalry are local conditions governing how companies are created, organized and managed and the nature of domestic rivalry. These factors help shape the industry.

Porter's diamond speaks of these four attributes as a mutually reinforcing system. The effect of one attribute is linked to the state of the other. He asserts that firms are most likely to succeed in industries or industry segments (in this case the high end-low volume market) where the diamond is most favorable to it. For example, favorable demand conditions will not result in competitive advantage unless the state of rivalry is sufficient to cause firms to respond to them. Porter puts in two additional variables that can influence a nation's diamond in important ways: chance and government. Chance events are defined as major product innovation that helps reshape industry structure and provide the opportunity for one company to supplement the others in the industry. Government, by rules and regulations (in the Philippines, implementing guidelines) can improved or act as a detriment to national competitive advantage.

### ***Philippine Furniture Industry***

*PhilExport* (2004) gives a glimpse on the development of Philippine Furniture Industry. The furniture industry has transformed into a highly diversified manufacturing sector as seen both in the domestic and in the international markets.

#### ***Background/history.***

Tracing back to the Philippine furniture history, it was through the Galleon Trade when the furniture crafts were first introduced to the Philippines. The colonial merchants in the 16<sup>th</sup> century were the ones who discovered the possibilities of creating good furniture products using the Philippine hardwoods. Since wood is abundant during that time, cabinetmakers were brought in from Spain. Since then, the furniture skill was passed on to Filipino craftsmen, who learned from these cabinetmakers. During the same era, the Spanish friars built churches all over the archipelago. This broadened the design skill of these Filipino craftsmen. They learned not only the art of masonry but also of intricate carvings and adornments on doors and other church furnishings.

During the 18th century, European domestic furniture was brought in the country. As a result, new regional styles of furniture making emerged in the Philippines. From replicating to redesigning, the furniture industry prospered as the craftsmen built furniture to suit the local tastes and lifestyles.

By the time the Americans settled in the country during the early 1900's, values such as casualness, comfort, and practicality gave influence to the locals and had also an impact on the furniture industry. Due to this, the rattan furniture industry flourished and gave rise to the partnership between Mahitabel, Philippines and McGuire, U.S.A.

With continuous production improvement and product development, the furniture makers were soon able to export complete furniture pieces that attracted the attention of the international market. The value-added chain was completed by the late 1980s when the companies started

undertaking their own product development and design, manufacturing, assembly and final finishing.

The history of the industry is reflective of a rich craft heritage, eclectic influences, variety of locally available materials, and native artisans with excellent design flair and deft hands. These are the same reasons for the industry's subsequent growth and the wide acceptability of its products.

The Philippines now ranks as one of the world's best producers of fine furniture – from the traditional to the casual contemporary to the highly experimental. The furniture industry manufactures affordable products of exquisite craftsmanship that is the successful result of modern technology combined with human creativity and love of beauty.

From its prime position as the major source of creatively designed wicker and rattan furniture, the industry has successfully diversified into wood, metal, stone, bamboo, leather and mixed media furniture collections. Wrought iron and aluminum are principally used for metal furniture. Other inputs include fittings and finishing materials.

The industry utilizes wood, rattan, bamboo and other materials such as buri, metal, stone/marble and plastic, which are creatively and finely handcrafted into various products including: leg items for chairs, tables, beds, setters case goods such as cabinets, desks, chests of drawers, kitchen storage units, combinations for building/home fittings, shelves and ornaments. Furniture exports are divided into the following sub-groups: rattan, wood, bamboo, furniture parts, metal, plastic, other materials and furnishings.

Based on a research conducted by the Chamber of Furniture Industries of the Philippines (CFIP) in 2005, the Department of Trade and Industry (DTI) estimates that there are about 15,000 local furniture manufacturers comprising the furniture sector. According to the *PhilExport* as of 2004, the furniture industry is made up of 15,000 establishments with 481,500 direct workers and 300,000 others indirectly employed as subcontractors. Majority is dominated by small and medium-sized firms that are commonly composed of single proprietors and family corporations, thus 99% of the industry employs less than 30 workers.

## Local Furniture Industry Performance

### *Global Demand for Furniture*

The Chamber of Furniture Industries of the Philippines (2005) research states that the global demand and trade for furniture in 2004 amounts to an estimated US\$200 billion (based on UN data). Gross sales for 2005 are projected at US\$250 billion. The world ratio between import and consumption was 28.5% for 2002, significantly higher than the 18.5% ratio for 1995. The world's leading importer of furniture is the United States, followed by Germany, the United Kingdom, France, Japan, and Canada. Italy remains the world's top exporter, but in recent years, the largest export growth in furniture has been exhibited by China – about a US\$5 billion increase from 1995 to 2002.

In the past few years, Philippine exports of furniture have been erratic. From 1999 to 2003, exports were generally on the decline, posting negative growth rates of almost 5% yearly. The Philippines hold a marginal 0.2% of the world furniture market. Total furniture exports in 2003 were valued at US\$278 million. Wood furniture comprises the largest product line exported by the industry. The biggest market is the United States.

### *Philippine Furniture Exports*

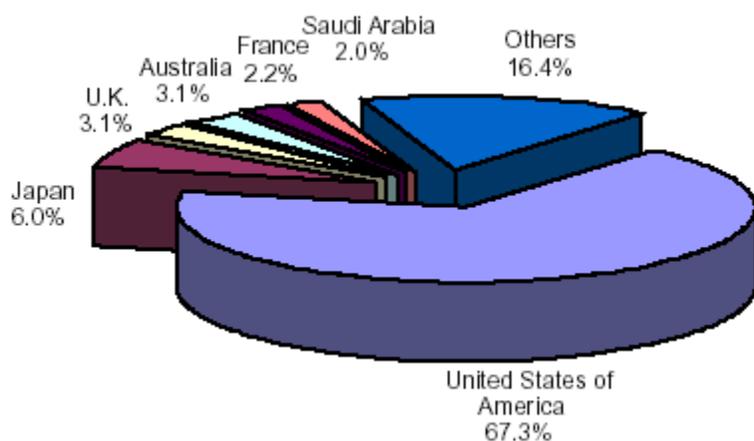
Found in DTI Tradeline Philippines (cited in CFPI, 2005), Figure 1 presents the Philippine furniture exports to the world fluctuated for the years 1998 to 2003. It is evident that the highest growth was during 2000, where the Philippine exports totaled US\$381 million. Philippine Furniture Export performance dropped from US\$381 million in 2000 to US\$297 million in 2001. Fortunately by 2002, furniture exports recovered to US\$316 million in revenue. However, this went down a year after to US\$278 million. As a whole, its growth rate from 1998 to 2003 was negative, dropping almost 5% every year.

*Figure 1.* Philippine furniture exports, 1999-2003 (in US\$ '000).

Year	Export Value (in US\$'000)	Growth Rate (%)
1999	352,523,833	-
2000	381,395,174	8.2
2001	296,772,062	-22.2
2002	316,015,625	6.5
2003	277,996,952	-12.0
Average		-4.9

Obtained from the National Census Office (NSO) (cited in the CFPI, 2005), Figure 2 shows that the United States was the primary market for Philippine furniture as of 2003, absorbing 67% of the total, followed by Japan (6%), the United Kingdom (3%), Australia (3%), France (2%) and Saudi Arabia (2%). Exports to the rest of the world constituted 16% of the total.

Figure 2. Philippine furniture exports by country 2003.

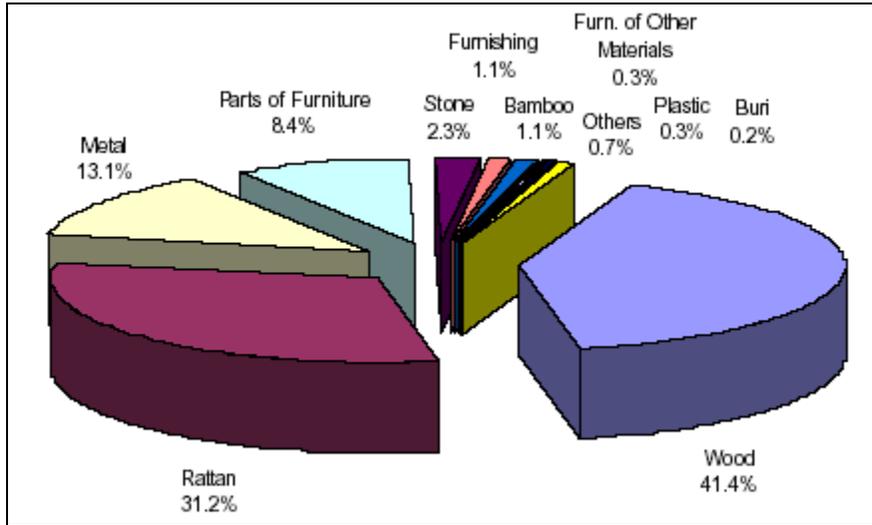


Year	Import Value (in US\$)	% Share
United States	179,011,624	67
Japan	15,839,996	6
United Kingdom	8,364,031	3
Australia	8,129,626	3
France	5,828,850	2
Saudi Arabia	5,334,539	2
Others	43,579,997	16
Total	266,088,663	100

Source: National Census Office (NCO)

Of the industry's product mix as illustrated in the DTI Tradeline Philippines, the wooden line has the largest contribution to the Philippine Furniture Exports in 2003. Figure 3 points out that wood contributed 41.4% of total export sales, and is followed by rattan furniture (31.2%), metal (13.1%), components of furniture parts (8.4%), furniture made with other materials (0.3%), and furniture from stone (2.3%).

Figure 3. Philippine furniture exports by product 2003.



Source: DTI Tradeline Philippines

### ***Domestic Industry Players***

PhilExport, *Opportunities Abound* (March 2004), cites the major producers in the Philippine Furniture Industry. Cebu, Metro Manila and Pampanga are the three major furniture making areas. Located in Cebu are the largest-sized rattan, stonecraft and metal furniture manufacturers. Currently, Cebu is the major destination for wood furniture due to the fact that quite a lot of rattan factories have already shifted to producing such products. On the other hand, rattan, wood and metal furniture companies are also found in Manila. In Pampanga, fine bone inlay work is what they are known for.

In order to include the production of contract furniture segment, these companies have diversified their capabilities. In progress, they have been recognized as preferred sources of furniture for hotels, restaurants, offices and other public institutions. In addition to this, contractors and interior design offices have become important clients since the industry tapped this segment.

### ***Philippine Designs, Inc. (PDI).***

Philippine Designs, Incorporated is engaged in Rattan furniture export. It exports in different countries such as the United States. 90% of its labor force is for export market and only 10% is for domestic market. 65% of PDI's export sales for United States only and the remaining 35% is for Japan, European countries and some Asian Countries. *According to the company, it gains competitive edge by identifying designs and the finished product.*

***Woodtech Corporation (WTC).***

Woodtech Corporation is a contract furniture company and engaged in furniture making demanded by the customers. 70% of its sales are domestic and the remaining 30% are allotted for export sales. Most of its domestic markets are the hotels, restaurants, and resorts. *According to the company, its competitive edge runs backward with production cost and they make sure that they deliver the products on time.*

***Furniture Ventures Inc.***

Furniture Ventures Incorporated is a company engaged in rattan, wicker and wrought iron works. Its major markets are the European countries like Spain, Germany, and United Kingdom. Its domestic market plays along shopping malls and their showroom. *According to the company, its competitive advantage amongst other players in the industry is that they do not tap the low end market.*

These major furniture producers are able to foster innovation and are able to gain competitive advantage through their quality and design. They were able to produce unique products by using indigenous materials such as rattan and other locally available materials. Some of the materials they used are sourced globally such as crushed bamboos. In addition, *they also import equipment such as sanding, paliner, compressor, polishing machines and finishing tools from Taiwan. On the other hand, labor is economical sourced* and the craftsmanship of the Filipino workers enabled them to be successful in the business.

Successfully, the company has captured the low volume market niche in other countries and is also trying to penetrate the local market niche. By maintaining their current market, they would be able to enjoy a better gross margin on their export products as well as the products they sell in the local market.

***Kinds of Products the Firms Produce***

***Product coverage.***

PhilExport, Opportunities Abound (March 2004), mentions the product coverage of the Philippine Furniture Industry.

Previously, the wooden furniture manufacturers were limited in exporting sanded products and Philippine-made wooden pieces were previously reproduction or period pieces only. However, as reflected in their progress, they have showcased local skills such as carving, marquetry, and inlaying that have now penetrated the global market. Together with this, several firms are now shifting in producing modern and contemporary style furniture by using particle boards and medium density fiberboards for panel furniture.

On the other hand, metal furniture is a combination of wrought iron with wicker, wood, seagrass and other indigenous materials. Furthermore, stonecraft pieces are composed of wooden carcasses and laminated with pieces of fossilized stones. These fossilized stones are commonly used in producing tabletops.

***Product classification.***

Figure 4 below shows the furniture product classification according to Harmonized System (HS) and Philippine Standard Commodity Classification (PSCC).

*Figure 4. Furniture product coverage/classification by HS and PSCC.*

PSCC	HS	DESCRIPTION
821.11-00	9401.10	Seats of a kind used for aircraft
821.12-00	9401.20	Seats of a kind used for motor vehicles
821.13-01	9401.50	Seats of bamboo
821.13-02	9401.50	Seats of rattan or cane
821.13-03	9401.50	Seats of buri
821.13-09	9401.50	Seats of osier or similar materials
821.14-00	9401.30	Swivel seats with variable height adjustment
821.15-00	9401.40	Seats, other than garden seats or camping equipment, convertible into beds
821.16-01	9401.61	Seats, n.e.s., with wooden frames, upholstered
821.16-02	9401.69	Seats, n.e.s., with wooden frames, not upholstered
821.17-01	9401.71	Seats, n.e.s., with metal frames, upholstered
821.17-02	9401.79	Seats, n.e.s., with metal frames, not upholstered
821.18-01	9401.80	Seats, n.e.s., of stone or marble
821.18-02	9401.80	Seats, n.e.s., of wood
821.18-03	9401.80	Seats, n.e.s., of metal
821.18-04	9401.80	Seats, n.e.s., of plastic
821.18-09	9401.80	Other seats, n.e.s., of other materials
821.19-01	9401.90	Chair controls
821.19-09	9401.90	Other parts of the seats of subgroup 821.1
821.3		Furniture, n.e.s., of metal
821.31-01	9403.10	Filing cabinet designed to stand on the floor, of metal
821.31-09	9403.10	Other furniture, n.e.s., of metal, of a kind used in offices
821.39-01	9403.20	Portable ice chests, fiber glass insulated, of iron or steel
821.39-02	9403.20	Music stands, of metal
821.39-03	9403.20	Beds, of metal
821.39-09	9403.20	Other metal furniture, n.e.s.
821.5		Furniture, n.e.s., of wood
821.51-01	9403.30	Filing cabinets, of wood
821.51-02	9403.30	Office tables, of wood
821.51-09	9403.30	Other furniture, n.e.s., of wood, of a kind used in offices
821.53-01	9403.40	Ice box, wooden
821.53-02	9403.40	Kitchen tables, of wood
821.53-09	9403.40	Other furniture, n.e.s., of wood, of a kind used in the kitchen
821.55-01	9403.50	Beds, of wood
821.55-09	9403.50	Other furniture, n.e.s., of wood, of a kind used in the bedroom
821.59-01	9403.60	Music stand, of wood
821.59-09	9403.60	Other wooden furniture, n.e.s.
821.7		Furniture, n.e.s., of other materials
821.71-00	9403.70	Furniture, of plastics
821.79-01	9403.80	Furniture, of stone or marble
821.79-02	9403.80	Furniture, of bamboo
821.79-03	9403.80	Furniture, of rattan
821.79-04	9403.80	Furniture, of buri
821.79-05	9403.80	Furniture, of glass
821.79-09	9403.80	Furniture, of other materials, n.e.s.
821.80-00	9403.90	Parts of the furniture of subgroups 821.3, 821.5 and 821.7

***Product use/s.***

According to Pearl 2 State of the Sector Report on Philippine Furniture 2003 (as cited in CFIP, 2005), the furniture in assembled or knock-down form are used in the following: Dining room furniture which includes tables, chairs, sideboards, buffets/dressers; living room furniture including seating elements, settees, wall storage systems, occasional tables, seasonal tables (coffee tables, etc.); bedroom furniture which comprises beds, headboards/bedstead ends, dressing tables, chests of drawers, wardrobes; and kitchen furniture, including storage units, kitchen tables and chairs.

***Production capacity.***

Information gathered in the PhilExport, Opportunities Abound (March, 2004), reveals the machines used for rattan and wood furniture production are 5-10 years old. Majority of wood furniture firms are investing in modern woodworking machines and increasing the application of specialized technology to streamline their production because of the growing need to improve their productivity. Existing firms accounting for 80% of total exports have capacities shown in Table 1 below.

Table 1  
*Registered Capacities per Year*

<b>Material Type</b>	<b>Registered Capacities Per Year</b>
Rattan/Wicker	2,603 x 40 ft. containers and 517,487 pieces
Wood	1,826 x 40 ft. containers and 185,853 pieces
Metal	1,255 x 40 ft. containers and 24,500 pieces
Stone	180 x 40 ft. containers and 73,000 pieces

***Factors of Production***

The factors of production are the following: raw materials, labor and packaging materials. The PhilExport, Opportunities (March, 2004) uncovers these factors.

***Raw materials.***

*Local.* For decades, Filipino furniture manufacturers have relied on rattan and wood as their basic raw materials. But in the face of severe supply constraints on such raw materials, producers have increasingly turned to stone, metal, plastics, bamboo, leather and even mixed media.

The industry has branched out from utilizing rattan, wicker and buri to using wood, metal, stonecraft, bamboo and plastic in production. New forms have also emerged with the

combination of two or more of these conventional materials, and their combination with other items such as grasses, shells, coconut lumber and leather.

Rattan poles, mainly those with a diameter of two centimeters or more, are either sourced locally or imported. Rattan furniture includes chairs, tables, headboards and casegoods constructed with rattan frames and combined with natural or colored wicker woven in myriad patterns. Items may also be made with wooden carcasses laminated with rattan splits and wicker. Styles vary from traditional and Victorian to contemporary.

While lumber is available in the domestic market, manufacturers have started using imported species. Lauan and tanguile are the commonly used types of wood that are locally-sourced. On the other hand, Honduras and Brazilian mahogany, pine, oak, beech, cherry and maple are imported by some manufacturers. Malaysia, Brazil and the USA are the largest suppliers of imported lumber.

Manufacturers have broadened their product range to include pieces using plantation species. Rubberwood and gmelina are being utilized at the moment. A priority concern of the industry is the development of tree plantations. The use of particle boards and medium density fiberboards for panel and office furniture and the manufacture of upholstered items are also gaining popularity among manufacturing firms. Fortunately, foreign and local buyers have been more than receptive towards these new products.

*Imported.* Approximately 60% of the industry's expenses are raw materials alone. Imported raw materials used in furniture making are: wood, rattan, leather, hardware supplies, etc.

#### ***Labor.***

Furniture manufacturers channel 32% of their expenses on labor. Some medium-sized and large companies subcontract a part of their operations to smaller firms, hence, industrial service provided by other firms account for 4.5% of the total cost. Investment on capital equipment and other fixed assets constituted a 3.5% of total expenses.

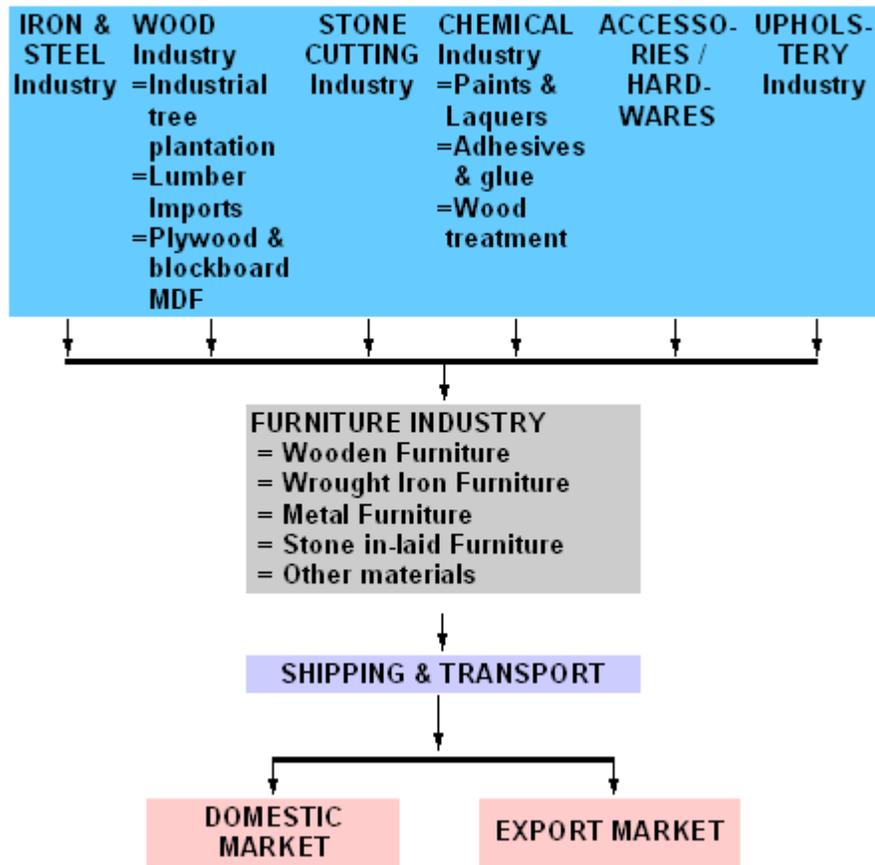
#### ***Packaging materials.***

Furniture manufacturers/exporters use the following packaging materials: double corrugated carton box with polyethylene tubes on critical points, kraft paper, abaca fiber straps, plastic bubble sheets, and styropor.

#### ***Flow/process chart of the furniture industry.***

Figure 5 illustrates how the furniture industry transforms raw materials and delivers the finished products to the market.

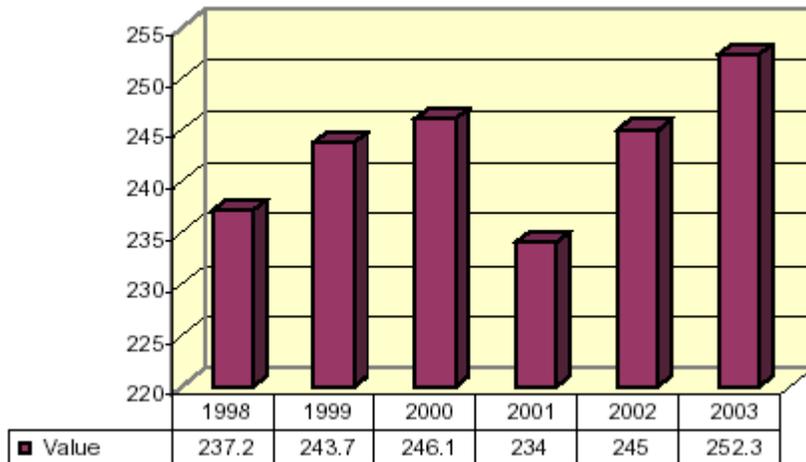
Figure 5. Furniture industry flow chart.



## Market for Furniture

Based on the Aktrin Home Furnishings Network (cited in CFPI, 2005) Figure 6 illustrates the world furniture production has been rising since 1998. However, in 2001, it had evidently dropped down to \$234 billion. That year was the 9/11 attack on the World Trade Center in New York, which caused disruptions in world trade. The following year, the industry recovered to \$245 billion. As of 2003, the global furniture production amounted to US\$252.3 billion.

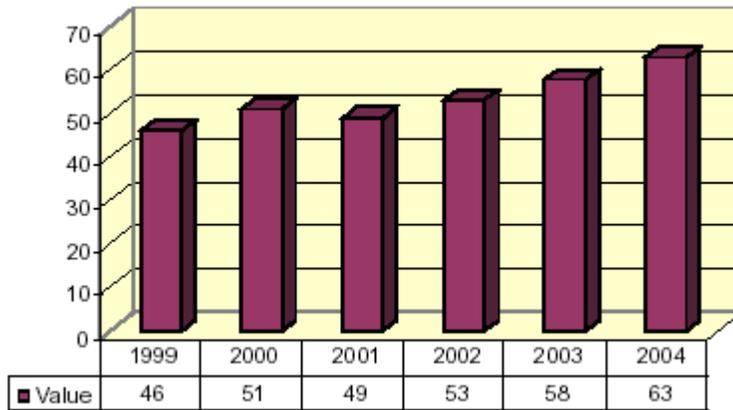
Figure 6. Global furniture production 1998–2003 (in US\$ billion).



Year	Value	Growth Rate (%)
1998	237.2	-
1999	243.7	2.7
2000	246.1	1.0
2001	234.0	-4.9
2002	245.0	4.7
2003	252.3	3.0
Average Annual Growth		1.3

Source: Aktrin Home Furnishings Network

Figure 7. World trade of furniture 1999-2004 (in US\$ billion).

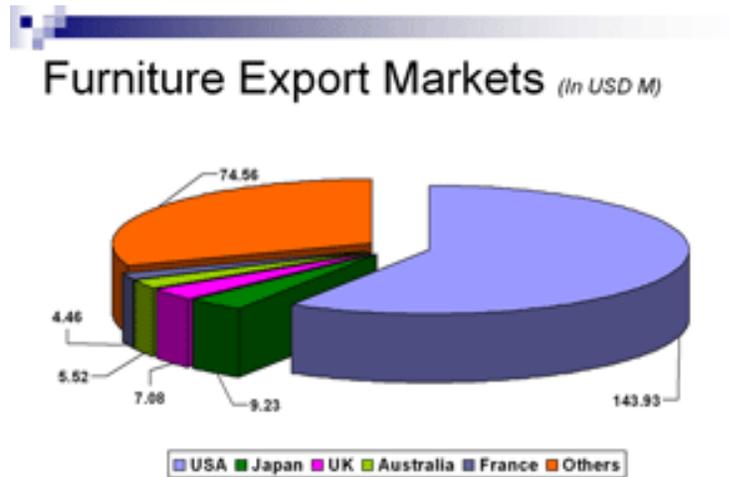


Notes: 2003 figures are estimated and 2004 figures are projected  
 Source: CSIL

As reported by the Center for Industrial Studies (CSIL) in Milan, Figure 7 presents the world trade in furniture from 1999 to 2004. Basing on the analysis of the research made by CFPI in 2005, the total projected gross sales are expected to top US\$63 billion in 2004. With the openness of the furniture markets, the world trade in furniture may be more robust.

Figure 8 shows that U.S. remains to be the largest market for Philippine furniture in 2004, with 59% of total or U.S. \$143.93M value of exports.

Figure 8. Furniture export markets industry performance (January – September 2004).



Source: DTI, National Census Office

## **Porter's Five Forces Analysis**

### ***Bargaining Power of Suppliers***

Suppliers are described to be individuals or companies that provide the direct and indirect materials for the product that the industry builds. They also render services such as direct labor. Direct materials are the things used to make the product complete; while indirect materials are the things used to make the product. Indirect materials; however, are not seen in the finished product. Other things that a supplier provides are the tools, supplies, machineries or equipment. These are necessary to create the finished product.

#### ***List of players per force.***

There are several suppliers needed in the industry, some of which are the following:

*Subcontractors.* Companies that specialize in making certain whole furniture products or certain portions of the furniture. They can influence or bargain up prices if demand increases and if they provide a specialized skill which other suppliers cannot do.

*Hardware stores.* Retail and bulk purchasers of key raw material and important components of a product for completion can be bought. Some hardware stores provide the necessary tools, supplies and equipment in making the product. They too can bargain up prices if demand increases.

*Direct importing materials companies.* Companies that have the financial capacity to import raw materials particularly wood, which is scarce in the Philippines because of the total log ban. Therefore, they can and influence prices upwards.

#### ***Analysis of force.***

*The market is not dominated by a few large suppliers of finished products.* In this industry, subcontracting has been a common practice among furniture companies. There are numerous subcontractors of equal size in this industry, some of which have staff salaried with regular pay, and some which receive a piece rate for finished parts or products. The question is whether the subcontractors are able to produce quality finished products. (Low.)

*The market is dominated by a few large suppliers rather than numerous fragmented sources of supply.* This is the case in raw materials, particularly "Rattan". The lack of readily available supply of the raw materials drives prices up as firms have to import to produce the finish product. Especially with the implementation of the total log ban, only large firms that have the importing and financial capacity would be able to supply sufficient raw materials just-in-time. (High.)

*The switching costs from one supplier to another can either be high or low depending on the scarcity of a particular material.* This will depend solely on the kind of furniture a particular company produces. If the company produces a product made of scarce raw materials, then the buyer has a high switching cost, but for those companies that rely on easily available kinds of raw materials their switching costs is relatively low. (Medium.)

Based on the analysis above, the bargaining power of suppliers seems to be balanced but has greater tendency to be low. Therefore it can be considered an opportunity rather than a threat because of the presence of a lot of subcontractors and numerous suppliers of imported raw materials and equipment.

### ***Bargaining Power of Buyers***

Buyers are individuals or group of people that purchase a product at the best possible price. Buyers may be grouped according to their gender, age, education, class, marital status, etc. to form a market. Sellers usually do this to determine their target market, a set or group of people that will most likely want to buy the product.

#### ***List of Players per force.***

*Working adults.* This group is composed of stable individuals who are either single or married. It is a fact that everyone will eventually own or rent a place as a place of residence, and designing their own home is where the purchasing of furniture comes in. It is usually more economical to buy Philippine made products than imported furniture.

*Homemakers or wife.* Homemakers include wives who do not work. However, there are a number of men now that want to be involved in keeping their homes organized. Homemakers are often active in searching for the best furniture and handicrafts that would fit their home and budget.

*Interior designers.* These are composed of arts students, architects, design engineers that are involved with the furniture industry. They are the ones who recommend, design, and visualize household products and interior projects.

#### ***Analysis of force.***

*Buyers do not purchase in volume.* Most of the time, buyers purchase only one set of furniture in staggered basis depending on budget availability. Unless these buyers are well-off and have a new house, acquiring a new set every year is an unlikely event. They can opt not to purchase for a long time too and just keep the old set in place.

*The product can be readily replaced by various substitutes.* There are many small, medium and large businesses that sell numerous types and kinds of furniture. They come in a

variety of designs, uses, sizes, prices etc. Therefore, buyers have unlimited options and they can choose furniture that would fit their taste, lifestyle, purpose and budget. They can switch at a low cost. (High.)

*People in the professional sector that do interior design may not recommend a particular type of furniture that the firm produces.* Since, furniture companies can produce basic and simple products or otherwise, they can recommend to buyers to find much simpler designs and cheaper products or vice versa. Interior designers can just opt to think about the current furniture mixing with their new acquisition and not care about the design or the quality of the product. The current trend of using old furniture sold in garage sales or thrift stores also poses a threat to the industry. (High.)

Based on the analysis above, the bargaining power of buyers is high; therefore it is deemed a threat rather than an opportunity.

### ***Threat of Substitutes***

Substitute products are considered to be things that have similar functions or purposes as those products in the industry. Since we are analyzing furniture, the substitutes are those used when the desired product is not available, expensive, unattractive and low quality.

#### ***List of Players per force.***

*Furniture.* There are several substitutes for designer furniture. These are plastic and fiberglass furniture which is called monobloc chairs and tables. This type of furniture is far simpler, inferior in quality and unilaterally designed, and a lot less cheap to produce than designer furniture. The proliferation of such inexpensive and practical monobloc furniture is evident in the various restaurants and offices in Metro Manila and the country.

#### ***Analysis of force.***

*Switching costs for customers is high.* With the current state of the Philippine economy today, customers are now more practical. Customers can just go directly to a subcontractor or an ordinary carpenter and commission them to make hand-made and home-made furniture instead of ordering through a furniture company. There are a lot of companies in the furniture industry, some of which already produce almost identical products with similar prices.

Based on the analysis above, the threat of substitutes in terms of cheaper alternative furniture seems to be high and is considered to be a threat.

### ***Threat of New Entrants***

New entrants are individuals or new companies planning to enter the furniture industry. They may have no experience at all in running a business or experienced entrepreneurs who plan to expand or diversify their present business. But in this industry, if the entrant has no experience in furniture manufacturing it would be a costly exercise.

#### ***List of players per force.***

*Subcontractors.* Subcontractors usually make the furniture components, or part of it as sub-components and through that they gain experience, and if given the capital they can compete with other existing companies they used to supply.

*Companies planning to integrate forward.* These are the existing companies that are partially already involved in the industry as suppliers of raw materials and might have had access to excess labor in the industry.

#### ***Analysis of force.***

*No strong brand preferences and customer loyalty.* Consumers do not have brand preferences or customer loyalty when it comes to purchasing furniture. Compared to shopping for clothes, shoes, cosmetics, food and so forth, buyers do not stick to just one brand or store when they buy furniture. People differ in not just taste but the look of their houses; some companies' designs might not be compatible with the design of the household.

*Inability to gain access to specialized technology.* In creating furniture, no special skill or equipment/tool/machine is needed. Rather, furniture requires creativity in creating one that uses good quality materials, attractive design and practical functions. Because of this, the industry is described to be highly domestic, intensive in labor requirements but with low capital requirement especially if the furniture is created out of non-scarce materials easily found in the country.

*Capital requirements and/or other specialized resource requirements.* Depending on the type of furniture that the company wants to create, capital requirement can range from small to medium.

Since the furniture industry is very flexible, it poses very low barriers to entry thus this becomes a threat rather than an opportunity. The current 15,000 SME's in the industry is proof of low entry barriers.

### ***Competitive Rivalry within the Industry***

Competitors can be described as those individuals or group of people who sell the same or similar products. These are the existing companies that manufacture furniture in the industry.

***List of players per force.***

*Local furniture companies.* These comprise the majority of the furniture industry who rely on imported raw materials and target market is Metro Manila or regions in the Philippines.

*Subcontractors.* These are firms who create complete furniture for companies and other sub-components of furniture and parts.

*Exporting companies.* Companies who compete in the global arena thru exporting.

***Analysis of force.***

*Lots of firms equal in size and capability.* There are about 15,000 furniture manufacturers as of the end of 1997, many of whom are small and medium enterprises with less than 30 regular workers. Because of this, there is fierce competition in this industry.

*Companies have high carrying costs on inventory.* Since there are numerous companies and firms who sell and manufacture furniture, the cost of carrying inventory forces firms to sell cheaply excess furniture not sold in regular season.

*Firms have diverse strategies, corporate priorities, resources and countries of origin.* Local and imported furniture is abundant in the Philippines. Likewise, small, medium and large sale businesses are able to manufacture and sell this. Because of such differences, firms often carry different strategies and priorities.

The rivalry among competitors in furniture industry is strong that is why this is considered to be a threat rather than an opportunity.

***Conclusion: 5 Forces Analysis***

Based on the 5-Forces Analysis conducted above, the following conclusions are observed:

- Low bargaining power of suppliers
- High bargaining power of buyers
- High threat of substitutes
- High threat of new entrants
- Intense competitive rivalry within the industry

In spite of the four negative implications of the five forces of the furniture industry, why are there still more furniture companies entering the industry in the Philippines?

## **Porter's Diamond Model Framework**

### ***Factor Endowments – Nation's Position in Factors of Production***

Below are established advantages the Philippines have already built in the furniture industry. The question remains, will the Philippines be able to sustain the two big advantages listed below in the future? How long will these advantages last before they become extinct?

#### ***Local wood processing technology – rattan, endemic varieties.***

Wooden furniture producers are currently giving special attention to the retooling and modernization of their facilities. The Philippine Furniture Training Center (PFTC) has been set up to improve the sector's productivity and enable the industry as a whole to develop its manpower resources through various training programs.

The PFTC's training curricula was a result of a study conducted in the country by the Skive Technical Institute of Denmark. It is the most comprehensive, one of its kind training schools in the Philippines that can approximate the level of those given in specialized schools in Europe.

Rattan companies are well-equipped with the machines necessary for efficient production while semi-mechanized production is the norm in wood furniture making.

#### ***Locally sourced good designs, world-class craftsmanship.***

A priority project of the CFIP is the conduct of an annual design consultancy program in line with the holding of the Philippine International Furniture Show (PIFS). This year, the association was able to obtain a grant from Canada to subsidize the cost of participating in this program.

Companies normally employ at least an in-house artist/designer to handle product development. "We tried to create opportunities out of the government's total log ban policy," said Emmanuel Padiernos, president of the Chamber of Furniture Industries of the Philippines (CFIP). "Since the ban is discouraging the export of rattan and timber, we see a growing use for wrought iron, metals and even wooden furniture. Timber, after all, can be easily imported whether in raw or processed form."

The problem in sourcing rattan, a major industry raw material, has also strengthened the use of mixed media, he added.

These two major factors have been the biggest supporting factors of the Philippine export furniture industry. Low-cost quality labor and innovative designs with the incorporation of mixed media has kept the export industry alive in the last 5-10 years. This will not hold for long because Vietnam and Thailand are trying to create in-roads into this part of the industry. Industry

news is that China has been hiring Filipino designers to help their furniture industry export segment by dangling attractive wages.

This part of the diamond is the key advantage the industry has at the moment.

### ***Demand Conditions***

Demand conditions pertain to the nature of home demand and external demand for the industry's product.

This part of the model assumes that the domestic demand plays a role in upgrading competitive advantage. Firms are generally sensitive to their closest customers. Thus, the characteristics of home demand are particularly important in shaping the attributes of domestically made products and in creating pressures for innovation and quality. The nation's firms gain competitive advantage if their domestic consumers are sophisticated and demanding. Such consumers pressure local firms to meet high standards of product quality and to produce innovative products.

As the data in this paper suggest, the pressure is not existent within the Philippine domestic market but externally, foreign buyers are the ones dictating on the local furniture producers. The local manufacturers' pressure is driven by the need to qualify to get external orders of furniture and serve this external market. In other words, it's the other way around in the Philippines. Our local market represents only 20% of the industry's volume, the rest is exported to the US and Europe.

### ***Country's export statistics.***

"Within the next two years, we plan to organize trade missions and commercial intelligence trips to assist in enhancing our local manufacturers' capacity and technology," said Emmanuel Padiernos, president of the Chamber of Furniture Industries of the Philippines (CFIP). "One of the international shows we will be visiting in Europe features suppliers and furniture manufacturers."

From the data gathered, the Philippine exports did not reach the targeted 500 million at the end of 2000. Volume of export will continue to be in increments because firms rely on personal company strategy only. The firms are reluctant to share technology or practical inputs because of secrecy concerns and usual crab mentality. Not all firms are capable of expanding capacity since the lack of qualified craftsmen and machinery hamper the possibility of firms from getting sudden huge orders from foreign buyers.

Data presented in the earlier part of this paper show that targeted export volume was not achieved, on the contrary it has been on a downswing for the last five years. An average of 5% according to data gathered at CFIP dated 2004.

External demand for high-end low volume furniture is great, but domestic demand is hardly noticeable. Colonial mentality is probably the biggest hindrance. Filipinos feel that foreign made products are better than locally produced ones. To pay a high price for domestically produced furniture is out of the question for certain markets in the Philippines. Italian and American made furniture is held in high value as manifested by brisk sales of Ikea furniture and other importers of foreign made furniture.

This part of Porter's diamond does not reinforce the country's strategy. Changing the colonial mindset will take some time. This makes one wonder why anyone in the country would want a genuine leather sofa given its two-season climate.

### ***Relating or Supporting Industries***

Relating or supporting industries pertain to the presence or absence of supplier industries and related industries that are internationally competitive.

The benefits of investments in advanced factors of production by related industries can spill over an industry, thereby helping it achieve a strong competitive position internationally. This model also assumes that this related industries form clusters that help and support one another.

In this instance, as stated below, the Bureau of Domestic Trade Promotion (BDTP) had to make a survey to identify key regions in the country that produce the various types of furniture because Philippine furniture companies except for the Cebu companies do things by themselves without help from the others. Below is what the BDTP did in 1996 and the findings:

Of all the regions surveyed, Region 2 ranks highest in terms of number of producers with 18 percent share followed with 11 percent each. This may be attributed to the abundant supply of raw materials, particularly narra, which is plentiful in Region 2. Region 9 on the other hand, has a wide variety of raw materials such as lauan, mahogany and gmelina which is necessary in the manufacture of furniture. Although it is common knowledge that Region 7 specifically, Cebu and the National Capital Region have a thriving furniture industry, survey results did not validate this as far as the number of suppliers and producers are concerned.

In Region 2, Cagayan and Isabela have the largest number of producers with Cagayan accounting for 38.5 percent and Isabela, 27 percent. Of the four provinces surveyed in this region, Cagayan and Isabela also have the widest range of product lines. In Region 9, Zamboanga City accounted for almost 50 percent of the total number of producers in Region 3. In Region 8, Northern Samar and Eastern Samar contributed the biggest percentage share of producers with 26.2 percent and 25.2 percent respectively.

Raw materials used in the production of furniture range from various woods such as bamboo, narra, tanguile and wicker to such media as wrought iron. Material such as pinewood is only available in Baguio, Bontoc and Mt. Province while gmelina can only be sourced from the Mindanao areas. Although narra can be found in some parts of Mindanao and the Bicol region,

its major source is Region 2 which area is in fact the top producer of narra furniture. Buri, on the other hand, is produced in Ilocos Sur, Pangasinan and Southern Leyte.

Skills utilized in the production of furniture include carpentry, carving, dyeing, sanding, varnishing and welding, among others. Region 3, 2 and 8 employ the most number of workers with 4,196, 2,193 and 1,568 permanent and temporary workers and subcontractors, respectively.

This part of Porter's diamond is what this paper is trying to improve on. This can be solved by getting the firms related and supporting in a clustering model.

Porter defines clusters as geographic concentration of interconnected companies and institutions in a particular field. Clusters encompass an array of linked industries and other entities important to competition. They included, for example, suppliers of specialized inputs such as components, machinery, and services, and by providers of specialized infrastructure. Clusters also often extend downstream to channels and customers and laterally to manufacturers of complementary products and to companies in industries related by skills, technologies, or common inputs. Finally, many clusters include government and other institutions – such as universities, standards-setting agencies, think tank, vocational training providers, and trade associations – that provide specialized training, education, information, research and technical support (Porter, 1998).

The need to form clusters in the furniture industry in the different parts of the country will harness built-in advantages of the regions. Advantages such as local raw materials sourcing, availability of skilled labor and local technology will be strengthened if the clusters are managed by a government organization like PhilExport or BDTP or a professional organization like the Chamber of Furniture Industries of the Philippines (CFIP). Clustering builds value chain advantages bigger than a firm's value chain because shared resources can be used to build other advantages. Or clusters can purchase technology and share costs.

### ***Local Firm Strategy, Structure, and Rivalry***

This factor deals with the conditions governing how firms are created, organized and managed and the nature of domestic rivalry.

Data shows that out of 150,000 or so companies in the industry, 90% of Philippines furniture companies are small and family-owned. Most have a workforce of 30 or less. Since they are small and family-owned, the type and level of management will be paternalistic and personal. Meaning, each firm is like an extended family model where everyone waits for the CEO or President in this case the head of the family ( in most cases the father ) for decision making or strategy decisions.

## **Current Issues**

### ***Reasons Why New Firms Enter the Furniture Industry***

There are reasons why new firms enter the furniture industry. First is the high profitability per unit of this industry. It will attract aggressive entrepreneurs to enter and to capture a share in the furniture market. Firms have various cost structures in the industry with an average profitability per unit of designed furniture of over 100% per unit.

Second is the opportunity to capture international customers, which could bring a higher level of profitability. Some firms that used to supply the local market enter export market by being sub-contractors of larger furniture companies. Data that was presented earlier indicates that the furniture industry is still the fifth largest in Philippine export. However, due to current economic situation in the country, it is now facing a lot of challenges and its cost structures have increased as compared 5 years ago.

Third is availability of good quality labor at reasonable prices. Firms that have recently closed down resulted to surplus of furniture workers in the country. The export labor market cannot absorb these displaced workers.

Fourth is the alternative use of native raw materials such as buri and seagrass. These native endemic raw materials and the use of such in mixed media furniture allow the industry to be exciting and increase the value of such materials.

A new entrant of the industry will have to deal with all these factors. Determining the right strategy for the firm and making use of market opportunities will be the key to profitability. The firm's ability to come out with new product innovations through creative designs and the use of various forms of endemic materials will be the key for the future of the industry.

### ***Current Issues According to Firm Owners***

According to firm owners, there are current issues in the furniture industry. First, firms generally agree that they would have a hard time in capturing the mid-range, high-volume furniture niches. The lack of capital and technology are key reasons for the apprehensions.

Second, the other apprehensions stem from the general notion of not being able to match prices and quality of cheap imports of this type of mid-range high volume niches.

Third, many companies believe that it will require a lot of adjustments to cater to the high-volume market niches and it would be better if the company would focus on their current high-end, low volume market niche.

## ***Short Run and Long Run Problems of the Industry***

### ***Fierce international competition.***

International competition is the biggest problem faced by the furniture industry. This is the competition posed by the country's neighbors such as Malaysia, Indonesia, Thailand and Vietnam. These countries have doubled the Philippines' share, except for Vietnam which has a bigger international market share than the Philippines. It is the inability of the local producers to match the price and quality standards of these countries in the mid-priced and high volume market which has led to the continued downswing in our furniture exports. For the past decade, the Philippines has been producing mixed media type of furniture. Slowly, Vietnam and Thailand have been entering into this media type of furniture, which is becoming a threat to the country's industry.

The long run target is Taiwan's export market size, which is three times the Philippines share. China's share of the global business has grown tremendously in the last 5-6 years. This is beyond comprehension to even look at them as a competitor in this industry. Their pressure to bring the prices of export furniture lower will be the challenge of all furniture exporters globally.

### ***Outdated technology.***

Most machines in the factory line are 10-15 years old already. The furniture companies have to import updated modern machines to cope up with increasingly shorter finishing times. The ironic thing though is that the available updated machines in the market today are those produced in Taiwan and China, the country's major competitors in the furniture business.

### ***Intense domestic rivalry.***

Local competition is intense because of numerous companies of equal size and capital. The fact that these companies are fighting for the small local market share only intensifies the rivalry. Domestically the prices of furniture are determined by their sizes, the quality, cost of materials and the areas where they are acquired.

There is the so called "*crab-mentality*" that is present among some companies. Pulling other furniture companies' reputation thru word-of-mouth or downplaying the difficulty of manufacturing products among local customers cannot be stopped.

Local companies are very secretive of their designs or copying of market selling designs is a very big issue that is why some companies are reluctant to join Philippine trade fairs and exhibitions.

***Availability of cheap imported furniture undermines the local manufacturers.***

Imports of furniture from Italy, US, and Asian countries like Thailand, Korea, India, Indonesia, Vietnam and China are the reasons why the furniture industry is experiencing dwindling local market sales.

Low domestic sales is the biggest stumbling block to the internal growth and development of the furniture industry. Vigorous domestic sales is a requisite for growth in any industry.

***Scarcity of raw resources for production due to total log ban.***

Firms have to result to importing wood from Brazil and Honduras like oak, maple, mahogany and the like. If the entire industry relies on imported wood, any sudden price increase in raw material will make Philippine furniture uncompetitive against other countries exports.

***What Adjustments have to be made in the Philippine Furniture Industry?***

***Raw materials inventory build-up nationwide.***

The country should build a massive base or source of endemic or prized Philippine raw materials wood, shell, or stone. Backward integrate into these industries plus research on enhancing these materials by identifying the hard to sourced materials such as wood and be able to have an alternative like the use of mixed media.

If the BDTP was able to identify the furniture companies in the various regions (relating, supporting industries; porters diamond), then the supply advantage of endemic raw materials can be easily identifies in these regions. Organizing these clusters of suppliers in these regions can contribute to the growth of the furniture industry in the Philippines.

The country should also build a cluster of supplier; sourcing these materials and that can do simple value-added processing like finishing the stones or seagrass.

***Furniture design strengthening through formal / informal education.***

The government should strengthen the design aspect of the local designers by offering scholarships and courses in the country or abroad.

Another adjustment would be to build on the project of the Philippine Furniture Training Center by linking up as a satellite institute of a world class design center or create a national institute for furniture design similar to the Denmark institute. Then, offer this service via the national associations or government agencies so that the smaller companies have access to the new designs.

***Import manufacturing technology.***

Technology upgrading of the production and fabrication system will increase collective efficiency and maximize output. Through imported manufacturing systems, volume production will increase and will not rely on too much product innovation as the major source of competitive advantage. The company technology situation at the moment is that most machines are 10-15 years old. Updated machines have to be imported to compete in the high-volume-mid range market.

***Industry clustering of furniture companies / furniture cities.***

Clustering aims to build local linkages in order to build competitive advantages for export industries. To further define the meaning of clustering, Schimtz (1995) clarifies that it is a geographical agglomeration of specialized enterprises wherein the SMEs, who are collectively efficient, benefits thus becoming competitively advantageous to the economy.

Developing clusters of furniture centers in the different regions of the country similar to the example of the Cebu furniture firms and finding regional advantages that could be shared with other regions are some adjustments the country can make to improve the status of the furniture industry. Through clustering, advantages in labor/skill, raw materials surpluses of firms, sharing of equipment and expertise, might help bring cost down and would increase profit.

***Creation of satellite export offices in host countries.***

Major trading partners of the country will need an export satellite office that will facilitate documentation handling of Philippine products. Various industries can share in the cost of such satellite office for instance, furniture with fashion accessories and garments. Small fees can be charge for handling goods shipped to these countries.

Furniture inspection, retouching, rework/repair, and possible handling problems can be done by the satellite office. This ensures that Philippine exports are always delivered to final customers. This will eliminate extra freight expenses.

The Satellite Office can be used as a marketing tool for all firms in the industry. Appropriate fees can be collected for such function. Market intelligence and market information can also be another function.

***Creation of furniture export commission.***

Representatives for the Furniture Export Commission can be selected from DTI, PhilExport, BDTP, and CFIP. The Commission's tasks will include selection of firms to join the

cluster or Furniture Cities. This includes the mechanics of how firms will be selected in joining the cluster. They will be responsible for monitoring activities in clusters or Furniture Cities.

The Commission will be responsible for lobbying of incentives for the industry and filing of appropriate import tax for competing furniture products of the industry. It will also be tasked to look for long term contracts of Philippine firms. Huge contracts can be divided/shared among furniture companies located in the Furniture Cities or Clusters.

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