



NEEDS AND CHALLENGES FOR TRACEABILITY BY BRAZILIAN TANNERIES

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JANUARY 2021

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1. TARGET

The purpose of this report is to record the results of the third stage of the BEEF ON TRACK PROGRAM - LINE OF ACTION OF THE LEATHER VALUE CHAIN.

The overall objective of the line of action is to encourage Leather Platforms to incorporate the criteria of the Accountability Framework Initiative (AFi) into their certification schemes.

This stage specifically aims to identify and qualify the needs and challenges for traceability by the main tanneries considering the concept of deforestation- and conversion-free chains established by CFA and AFi.

This document first describes the structure of the tanning industry in Brazil so that the reader can understand the complexity of the industry and its main intra and intersectoral relationships. It then shows the method used in this stage and the outcome.

In the final section, the opportunities and challenges are identified from the tanneries' point of view so the proposal, that will give direction to the actions, can be constructed considering a production chain "free of deforestation".



2. STRUCTURE OF THE TANNING INDUSTRY IN BRAZIL

This chapter aims to give an overview of the structure of the tanning sector, highlighting its heterogeneity in relation to production processes and access to raw materials.

2.1 Production structure

The leather sector in Brazil has 244 industrial plants belonging to 207 business groups ranging from multinationals to family businesses. The sector employs some 30,000 workers and trades more than \$2 billion each year (CICB, 2019).

All these companies are known generically as tanneries but they have several productive structures, which make them significantly different when it comes to establishing their markets and supply relationships within the production chain. The "integrated tannery", which performs all production processes to turn hide into finished leather, was common until the 1970s. The leather industry has been dismembered in the past 50 years due to two fundamental factors: the migration of the herd to the northernmost regions of the country and the need for greater speed in the delivery of finished leather, mainly for the footwear industry.

As a result, it is now common to see 'wet-blue tanneries', which process raw hides (fresh or salted) to the point of chromium tanning and are located close to meat processors and 'finishing tanneries', which transform wet-blue into finished leather and are located close to consumer hubs (footwear). Some tanneries can still get raw or tanned leather to the semi-finished stage (without final finishing). Annex A shows a leather production flowchart with the processing stages and the steps for all the leather types mentioned above. Table 1 shows the amount of companies that operate in each of the leather production stages.

Table 1 - Number of companies by type of leather produced

Process	Number of companies	Share
Raw to tanned leather	39	18.8%
Raw to crust leather	9	4.4%
Raw to finished leather	36	17.4%
Tanned to crust leather	17	8.2%
Tanned to finished leather	89	43.0%
Crust to finished leather	17	8.2%
Total	207	100.0%

Source: CICB, 2019



Most tanneries focus on the production of finished leather (68.6%) and are located close to footwear manufacturing hubs, especially those in Vale do Sinos in Rio Grande do Sul state and Franca in São Paulo state, and are typically small companies. Wet-blue tanneries, on the other hand, are characteristically larger and spread over several states, mainly in the south-eastern and midwestern cattle ranching regions (ABDI, 2011). Figure 1 shows the geographical distribution of tanneries in Brazil.

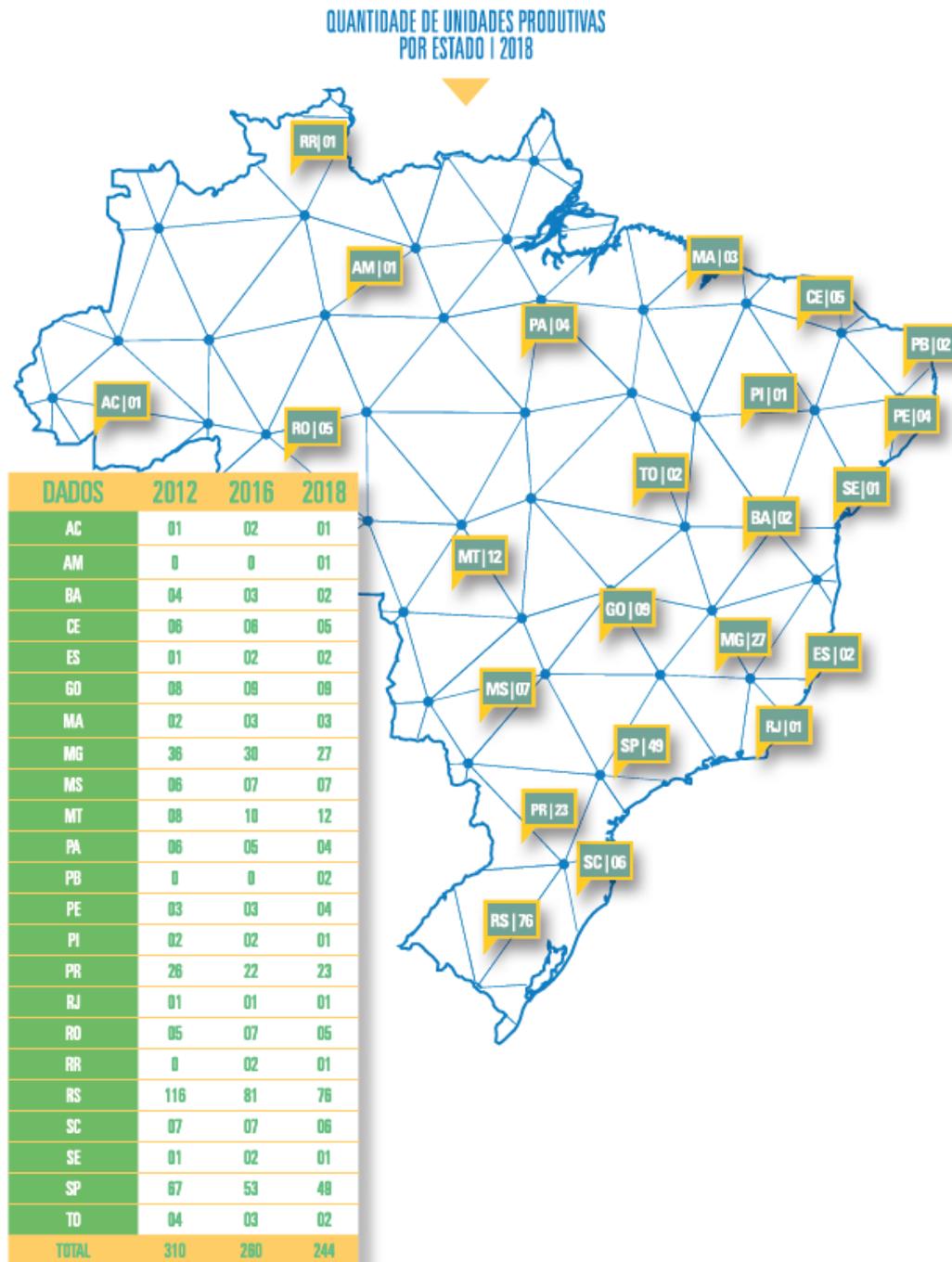


Figure 1 - Distribution of tanneries by State

Source: CICB, 2019



2.2 Access to raw material

Brazilian tannery production is mostly focused on bovine leather. According to the data in the Study of the Leather Sector in Brazil (CICB, 2019) and based on the meterage produced, 97.2% of hides are bovine, 1.4% are ovine, 1.1% are caprine and 0.3% derive from other sources.

Data from the Brazilian Statistics Bureau (IBGE) (2019) shows that 64.2% of the leather comes from large slaughterhouses or meatpacking plants, 27.4% is provided by third parties, 6.2% by dealers, 1.8% comes from municipal slaughterhouses, and 0.5% from other sources.

The raw material access structure is also heterogeneous and three tannery groups were used for the analysis proposed in this study:

- **Group A:** Vertically-integrated meat processors, which have direct access to the livestock production plant and process the hides in their own or outsourced units. This group is composed of a few companies but accounts for a significant share of Brazilian leather production.
- **Group B:** Tanneries that work with raw material purchased from slaughterhouses or dealers but that do not have direct access to livestock units. These tanneries may be small, medium or large and total around 80 companies.
- **Group C:** Tanneries that work with tanned leather acquired from tanneries in the previous groups or from dealers. These are mostly small and medium enterprises and total around 120 companies in Brazil.

In regard to production process, 78.4% of tanneries have their own production, 14.4% outsource their production and 7.2% are service providers (CICB, 2019). It is worth mentioning that service provision is most common in finishing tanneries. In this case, the raw material (tanned leather) is purchased by the customer (notably footwear industries), usually without any concern about its origin. This makes it even more difficult to deal with traceability issues in this trade modality.



3. METHODOLOGY

In-depth interviews were carried out for this study with representatives of selected companies belonging to the three groups mentioned in the previous section. The selection of companies was made for convenience purposes based on previous knowledge of the companies/interviewees and their relationship with the specific subject of traceability.

The interviewees were contacted and the interviews were scheduled and conducted remotely. The script used for the interviews was the following.

Point 1 - How the tannery handles the matter of raw material traceability. Understand the process used by the tannery.

Guiding questions:

- What is the company's policy with regard to the traceability of a raw material?
- How does the tannery control traceability: physical, documents, system?
- What is the extent of control (percentage of hides/tracked leathers)?
- What is current customer demand for full traceability?

Point 2 - Identify the tannery's difficulties.

Guiding questions:

- What is the tannery's main difficulty with regard to the traceability of a raw material?
- Is there data available for the tannery to perform a comprehensive check? Is the data accessible? Is it verifiable data? If not, what are the difficulties?
- What costs are involved in the traceability system today (percentage in end product)?
- Are there plans to invest more in this area to maintain customers and markets?
- What aspects are not covered by the traceability system and are (or may be) questioned or required by customers/markets?

Point 3 - How the issue of deforestation and conversion are addressed.

Guiding questions:

- Are there strategic trade differences depending on the biome (Amazon and/or Cerrado) from where the raw material is sourced? For example: preferences, raw material price or guarantees on raw material origin?



- What are the challenges or difficulties considering deforestation within the scope of selection of raw material suppliers?
- To what extent do customers already require or signal the possibility of requiring "deforestation-free leather"?
- What does the tannery think of the possibility of reputational risk turning into operational risk?

Point 4 - Interaction with certification systems (CSCB, LWG, ICEC).

Guiding questions:

- What certifications does the tannery possess and how does it stay active?
- What is the level of compliance with the traceability requirement (compliance with the CSCB indicator, LWG or ICEC traceability score)? Does the market consider these indicators valid?
- How is the certification and traceability of raw materials disclosed to the customer?
- H1. What does the company think of the possibility of making the traceability requirement mandatory to obtain certification (extending the scope of certification)?
- H2. What does the company think of the possibility of a separate certification for traceability?
- H3. What does the company think of the possibility of a separate certification for the deforestation-free supply chain "deforestation-free leather certification"?

Final considerations for the interviewee.

Guiding questions:

- What other aspects would you like to leave on record regarding the company?
- Any other comments or suggestions?
- Acknowledgements.

The interviews were recorded and broken down so they could be analysed for the consolidation of results shown in the next chapter. The identity of the interviewees and the companies is not shown since the respondents were ensured confidentiality.



4. INTERVIEW RESULTS

The results of the interviews are shown below and cover the four points addressed above.

4.1 Treatment of traceability of raw materials

Traceability is included in the daily routine of tanneries. Tanneries connected directly to meatpackers are very aware of this issue because of its importance in the beef industry. Large meatpackers use information generated from geomonitoring systems to ensure the origin of the animals and consequently the raw material delivered to the tanneries. Even tanneries that are not linked to the meat industry have some kind of traceability policy in place, most often required by certification systems and by customers, especially those in the foreign market.

It is clear how easy it is to operate traceability systems for tanneries connected to meatpackers (Group A). Tanneries that buy the hides from other meatpackers (Group B), however, find it difficult depending on the system used by the meat processing plant to guarantee the origin of the animals. The interviewees further stated that in larger meatpackers, particularly those that export, taking into consideration the origin of the animal at the time of purchase is a usual procedure; however, when the concern is smaller meatpackers, it becomes harder to commit and to acquire the data to establish a robust traceability system.

The finishing tanneries (Group C) are the most scrutinised by customers, especially those in the foreign market. It has been pointed out by the companies in this Group, however, that the requirements are more in terms of certification (especially LWG) than more specifically in regard to the issue of traceability. On the other hand, they are the entities that find it hard to ensure the traceability of their raw materials to their origin.

All the tanneries interviewed said they were able to trace the hides produced up to their direct supplier (tannery or meatpacker) internally. The tracking systems are physical and document-based, i.e., the hides are identified by means of stamps and the related documentation refers to in-house Production Orders (or Service Orders). However, the exact identification of the origin of the animals can be guaranteed only by the tanneries of Group A. The tanneries that represent Group B require their suppliers (meatpackers) to meet this requirement and perform periodic audits to ensure the system's operation. Group C tanneries, on the other hand, accept the statement of suppliers (tanneries of the other two Groups) that have traceability systems and do not use farms where problems related to deforestation, use of child or slave-like labour or embargoed areas have been detected. However, as a rule, there is no systematic monitoring or auditing system.



Normally, when a customer requests specific information about the purchased leather, a request is made to the suppliers, who send the information needed.

According to the tanneries, requests by customers for information regarding the origin of raw materials has become more frequent but is still "niche" and occurs mostly with some footwear manufacturers. Most customers seek information related to the existence of the traceability system, not "leather-to-leather" traceability.

4.2 Difficulty of tanneries

When asked about the 'main difficulty with regard to the traceability of raw materials', the answers of the three groups of tanneries was significantly different.

For Group A tanneries, the greatest difficulty lies with indirect suppliers; in other words, getting reliable and transparent data regarding the origin of the animals up to their birth. The tanneries of this Group made a point of mentioning the efforts made by their companies in this sense and believe that it will still take some time to gain access to this information, although some initiatives are currently being put in place.

The tanneries of Group B, on the other hand, highlighted the "cultural difficulty of dealing with trade issues with meatpacking companies". This difficulty is greater with meatpackers that work in the domestic market since tanneries that export are more structured and are used to disclosing information about the origin of their raw materials.

The tanneries of Group C stated that their main difficulty was "reaching the farm". This is because not all wet-blue tanneries have systematised traceability information. Since the system of these tanneries relies on the statements of their suppliers, the system bases itself more on trust than on information systems. There is also the issue of the origin of "picked" hides, i.e., those that do not come directly from meatpacking plants but are acquired from small meatpackers or slaughterhouses through dealers. This raw material is still quite common, in particular for the production of fur-lined leather.

All the interviewees agreed that the transactional nature of trade relations within the sector was also a problem. In other words, the matter of price is mandatory in the purchase and sale of leather especially when wet-blue is involved since it is, after all, a commodity.

This runs contrary to the costs involved in implementing and operating traceability systems. These costs are ultimately borne by the tannery (regardless of the production stage) because the customer does not pay more for traceability. Nevertheless, all the interviewees considered traceability a premise that needs to be met, regardless of the cost involved.



The tanneries mentioned the need to consider integrating the entire chain to fully improve traceability. Despite not being intense yet, customers' demands have been driving this process.

4.3 The issue of deforestation and conversion

The issue of deforestation is not yet explicit within the requirements of the tanneries. It ends up being incorporated into the scope of traceability of the raw material. This topic of conversation does not yet appear in discussions among the tanneries and only makes an appearance when deforestation is discussed.

Some clients, particularly Europeans, are beginning to question the specific issue of deforestation as a result of the coverage the international press has been giving to the wildfire problem in the Amazon in recent years. This biome has become the centre of attention.

Due to the possible risks involved, and also due to the difficulty of some international clients to understand the issue of the Legal Amazon, some tanneries choose to work with suppliers who operate outside this biome to serve specific clients who require a guarantee that the raw materials are not sourced from the Amazon region.

The matter of data transparency comes back to the fore when tanneries are questioned about difficulties related to this specific topic. Some international buyers are already talking about "deforestation-free leather"; however, they are restricted to the niches mentioned above, mostly footwear brands.

4.4 Interaction with certification systems

All tanneries interviewed are or have been LWG certified. Most have or are implementing the CSCB. There is a certain lack of knowledge by the tanneries in regard to the ICEC. Reiterating what was said above, the existence of certification is more relevant than the specific issue of traceability. For example, it is more important to be awarded Gold in the LWG or CSCB than to meet the traceability requirement.

In this part of the interview, three cases were presented to the interviewees regarding the issue of traceability and deforestation and the certification systems:

- H1. Make the traceability requirement mandatory for certification (extending the scope of the certification)



- H2. Have separate certification for traceability.
- H3. Have separate certification for the deforestation-free supply chain.

With regard to H1, the tanneries stated they were very open to this possibility. One of the interviewees said that "traceability should be a prerequisite for certification". They pointed out that currently there may be some difficulty involved in the availability of information but that it would be a viable solution and would be very important for the certifications since this would make them more transparent.

The second case (H2) was not well received because it involves an extra cost for a new audit. This cost could be covered by the current certifications, which aligns with the preference for H1.

The previously mentioned difficulty of how to ensure information about the indirect producer came up often in reference to case 3. As such, it does not relate to the tannery since it is a requirement that needs to be met by the breeder. If the control and monitoring systems do not evolve, the interviewees considered this case infeasible.

4.5 Considerations of interviewees

In their final statements, the interviewees reiterated the importance of traceability for the tanning industry primarily when speaking of it becoming a possible technical-trade barrier for Brazilian leather sourced from the Amazon (mostly) and Cerrado biomes.

The integration of the production chain has also been highlighted, given that the tanneries - especially those that are further downstream in the production process and consequently closer to the end consumer - depend on all the upstream links (other tanneries, meat processors and cattle breeders).



5. OPPORTUNITIES AND CHALLENGES

Based on the experience of the tanneries, working on a traceability system integrated with the certification program provides some opportunities and large challenges.

OPPORTUNITIES

- Traceability is a common topic in tanneries at various stages of the production chain.
- Certifications already include traceability as an important requirement, despite it not being mandatory.
- There is an understanding that meeting this requirement is now very important if the company wants to gain and maintain a market slice and this will only increase.
- Despite the greater maturity of the foreign market, there are indications from Brazilian companies that this topic will become increasingly more important.
- Large retail brands are concerned with how the origin of the leather can affect the reputation of their products.
- Tanneries are looking for ways to report their best practices to the market and traceability is included in these practices.

CHALLENGES

- Increase the availability and transparency of information throughout the entire production chain*.
- Show customers/markets the value of this information and the additional costs required by all processes in the chain.
- Evolve from the transactional model (price-based) to the relationship-based model in the trade processes of the production chain.
- Include traceability as a mandatory requirement in certification systems.
- Establish an integrated system among the certifiers to meet this requirement.
- Extend traceability systems upstream from the chain (dependent on livestock and the meatpacking industry).
- Disseminate the technical understanding of biomes with regard to permissible breeding possibilities.

* This core challenge can be explained differently depending on the group of tanneries under assessment.

Group A: reliable and transparent data from indirect suppliers (farms).

Group B: obtain reliable information from meatpacking companies concerning the origin of the hides.

Group C: have an information system in place that extends to the origin (dependent on the previous groups).



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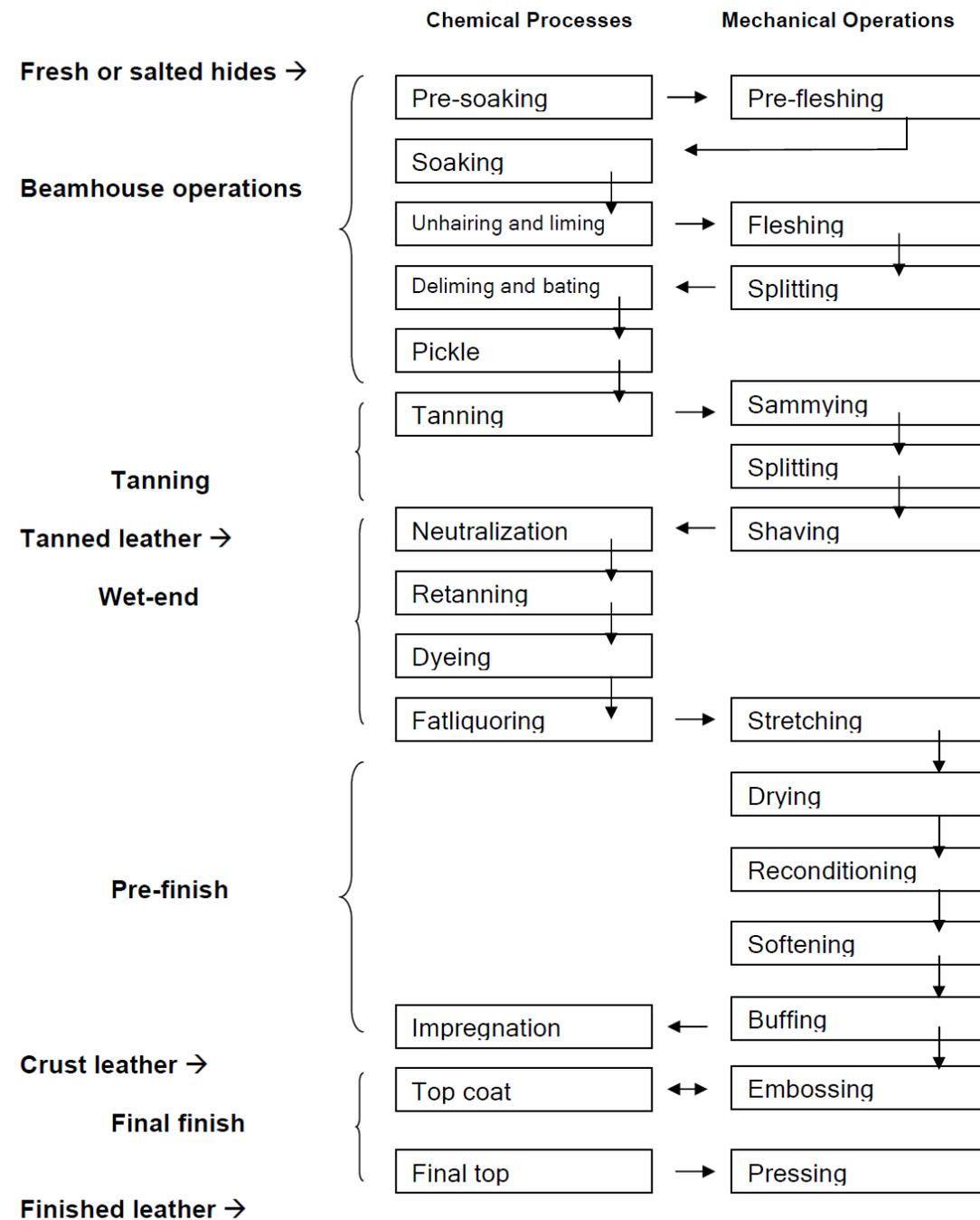
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ANNEX

Annex A - Leather production process



Source: ABNT, 2020

