

# SWOT Analysis for the Value Added Tea Industry in Sri Lanka

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## ABSTRACT

Tea has been the major plantation crop in Sri Lanka for more than a century. This was also the leading sector in Sri Lankan economy in terms of foreign exchange earnings, government revenue and employment generation.

Being a commodity trader of tea in the international market, Sri Lanka exports about 64 percent of tea annually in the form of bulk. The price fluctuations, difficulties in marketing and low profit margin are the crucial problems for the exporters in the industry as a consequence of exporting bulk tea. This has resulted in loss of valuable foreign exchange earnings and depletion in the foreign reserves. The problems faced by exporters and the other stakeholders as commodity traders can be minimized through value addition of tea. The average price of 1 kilogram of value added tea gains a higher price in the market, than that of bulk tea. Exporting of value added tea allows exporters to establish brand loyalty among consumers and secure market share in the long run. However, at present, only 36 percent of total products are exported as value added teas. The main objective of this research study is to identify perceived strengths, weaknesses, opportunities and threats in relation with investment of value added tea sector in Sri Lanka. Descriptive, tabular and frequency analyses were used for data analysis.

Weaknesses of the internal environment are identified as to energy availability, research and development, access of information and marketing capabilities. At the same time labour regulations, exchange rate regime and tax regime are the prevailing threats for the industry. Therefore the requirement of proper credit policies is emphasized for the convenience of such firms involving in value addition of tea, which are in need of higher capital requirement. The study has highlighted the necessity of overcoming weaknesses and capitalizes on strengths in order to encourage investment in value added tea sector and thereby to survive highly competitive global tea export market.

**KEYWORDS:** Tea Export, Value Addition, SWOT Analysis, Marketing

## INTRODUCTION

The establishment of tea industry has gone back to 138 years. The first commercial tea plantation was started in Loolukandure estate, in year 1867. Sri Lanka is known as a producer of some of the finest teas in the world (Anon, 2003a).

At present Sri Lanka is among the major exporters. The world tea export share of Sri Lanka was 20 percent in 2003. In Sri Lanka 91 percent of manufactured tea are exported and the rest is consumed domestically. Three main channels are identified in marketing Sri Lankan teas. They are public auction, private sales and direct sales (Anon, 2003a). In composition of the exported tea of Sri Lanka, 64 percent is in the form of bulk while 30 percent is in the form of packets. The higher value added forms of tea such as tea bags, instant tea and green tea accounts for the rest of the exports which is less than 6 percent (Anon, 2003a).

The expected benefits through an increase of the supply of bulk tea would not be acquired due to the deterioration of tea prices. Fluctuation of price of tea is the other problem that tea exporters face. The tea prices in Sri Lanka have shown a fluctuating trend with more years of depression. This is one reason why Sri Lanka deficit in balance of payment has increased causing depletion of foreign reserves. The resulted low profit margin created by price fluctuation and low price situation highly affect to the tea plantation sector, tea factory owners and small holders. Therefore the value of tea as a commodity is declining in real terms and furthermore it will continue to decline as long as it is traded as a commodity in the competitive international beverage market (Abeywickrame 1996).

Tea producing countries are now attempting to overcome the uncertainties of commodity prices and low margins, by gradually developing exports of tea in value added forms that command a high profit margin. But Sri Lanka still performs as a exporter and is not a tea marketer in the real sense. Even though Sri Lanka has stepped in to value addition, it has not been able to have a greater impact in the international market or has not reached a satisfactory level like other competing tea exporters such as Kenya, who export all of it's tea in value added forms. Therefore the local producers are unable to obtain the best value for their efforts. Instead the benefits are being enjoyed by overseas middlemen who add value on it. There is a remarkable gap between the prices of value added teas and bulk tea per 1kg.

Export of value added tea products might also allow exporters to establish brand loyalty among consumers. It also enables exporters to secure market share in the long run. This research study is focused on identifying the strengths, weaknesses, opportunities and threats in value added tea industry in Sri Lanka and to study the factors including their position according to the perception of the major exporters.

## MATERIALS AND METHODS

A SWOT Analysis is a strategic planning tool used to evaluate the Strengths, Weaknesses, Opportunities and Threats involved in a project or in a business venture. Strengths and weaknesses are internal to an organization or industry. Opportunities and threats originate from outside the organization or industry. A SWOT analysis, usually performs early in the project development process, helps organizations

to evaluate the environmental factors and internal situation facing a project (Anon, 2005).

**Table 1-Price and quantity of different teas exported in year 2002 and 2003:**

Type of tea	Year 2003		Year 2002	
	Quantity MT	FOB price Rs. kg	Quantity MT	FOB price Rs. kg
Bulk tea	175,951	176.41	188,134	175.16
Tea packets	82,680	573.95	68,915	221.45
Tea bags	15,500	767.67	14,139	491.12
Instant tea	1,324	332.9	1,298	645.59
Green tea	1,473	212.35	1,054	505.14

Source: Annual Report, Sri Lanka Tea Board, 2003

First internal and external set of factors affecting the value added tea industry were identified using secondary data and formal discussions conducted in identified major tea exporting companies.

The identified factors were classified in to strengths, weaknesses, opportunities and threats according to the perception of major tea exporters. A semi-structured questionnaire was used to assess the perception. Eighteen companies were selected purposively as the sample, from major 25 tea exporters. The directory of major companies engaged in tea exportation was drawn from Sri Lanka Tea Board. Telephone conversations and mails were used in addition to interviews. Descriptive, tabular and frequency analysis were used for data analysis.

**Table 2 -List of surveyed exporters**

Number	Name of the company
1	Akbar Brothers Group
2	Stassen Group
3	MJF Group
4	Unilever Group
5	Van Rees Ceylon Ltd.
6	Expolanka teas (pvt) limited
7	James Finlay Group
8	Tea Tang Ltd.
9	Qualitea Ceylon (Pvt) Ltd.
10	Imperial Tea Exports (Pvt) Ltd.
11	Fern Tea Group
12	Jaferjee Brothers Group
13	SKS Exports (Pvt) Ltd.
14	Union Commodities (Pvt) Ltd.
15	Standard Trading Company (Pvt) Ltd.
16	Commercial Exports Company (Pvt) Ltd.
17	Mabroc Teas (Pvt) Ltd.
18	Empire Teas (Pvt) Ltd.

## RESULTS AND DISCUSSION

The results are used as a technique that takes the findings of the survey and categorizes key points as strengths, weaknesses, opportunities or threats. This also brings together the internal and external environmental scanning to identify the internal strengths and weaknesses and external opportunities and threats of the business. The analysis has provided information that is helpful in matching the resources and capabilities to the competitive environment in

which firms operate. The identified factors are evaluated according to the perception of the exporters (Table 3).

**Table 3 -Perception of the exporters towards the identified SWOT factors**

Factor	Response percentage		
	Weak	Average	Strong
<b>I.Strengths</b>			
Quality and availability of human resources	22.22	50.00	27.78
Quality management	0.00	0.00	100.00
Technological strength	27.78	61.11	11.11
<b>II.Weaknesses</b>			
Energy availability	72.22	27.78	0.00
Research and development	66.67	33.33	0.00
Access to information	66.67	16.67	16.67
Marketing capabilities	83.33	16.67	0.00
Capital strength	16.67	61.11	22.22
<b>III.Opportunities</b>			
Incentives and subsidies	11.11	33.33	55.56
Key market size	11.11	27.78	61.11
Price structure in niche markets	5.56	44.44	50.00
<b>IV.Threats</b>			
Labour regulations	83.33	16.67	0.00
Exchange rate regime	55.56	44.44	0.00
Tax regime	50.00	33.33	16.67

### 1. Strengths

Strengths are the resources and capabilities that can be used as a basis for developing a competitive advantage in value added tea industry.

#### 1.1 Quality and availability of human resources

Availability of educated and energetic workforce that is familiar with modern production techniques and having a level of trainability were the factors considered in this case. According to the perception received by the tea exporting companies 50 percent of the respondents had an average perception in this aspect (Table 3). It was estimated that labour cost is more than 55 percent of total cost of production of tea. The workers in the plantations were demanding higher wages in the face of the rising cost of living. On the other hand Sri Lanka has faced a future labour crisis in tea estates, where the younger generation was shifting out of estates.

#### 1.2 Quality management

Sri Lanka tea board is the regulatory body to control quality of tea manufacturing and exporting. Lion logo was given only to those exporters dealing with high quality pure Ceylon tea. ISO 3720 was the minimum quality standard stipulated by tea board and it was a physical standard where a visual examination showed a maximum crude fiber level of 10.5 percent (Anon, 2002).

According to the Table 3, 100 percent of the respondents had a strong perception about existing quality management system of value added tea. It was believed that tea industry in Sri Lanka enjoys comparative advantage in quality and success of the industry depends greatly on the quality reputation.

### 1.3 Technological strength

Availability and use of new technological techniques, equipments and knowledge in Sri Lanka to expand value added tea sector were considered. According to the results (Table 3) prevailing technology in Sri Lanka was beneficial, as the exporters used advanced technological techniques and equipments through which they could achieve high production efficiency as well as low cost of production by reducing man power involvement. For instance some companies used vacuumed packs to gain advantage in global competitive market.

### 2. Weaknesses

The absence of certain strengths may be viewed as weakness or it may be the flip side of strengths. It is also may be considered as a weakness, if a large investment in manufacturing capacity prevents firms from reacting quickly to the changes in the strategic environment.

#### 2.1 Energy availability

Availability of reliable power supply sources, stability of power supply and the cost of power were considered in relation to the energy availability. According to Table 3, it was observed that 72 percent of the sample exporters perceived that the energy availability in Sri Lanka affected weakly on investment opportunities in value added tea sector. As the value added tea industry uses various machineries which depend highly on various energy sources mainly electricity and diesel. Greater extent of electricity power in Sri Lanka is generated from hydro energy (around 67 percent) and greatly depends on weather conditions for a constant supply. Therefore the instability and higher unit cost were the main constraints. Recently, the price of diesel had hiked by higher amounts. Therefore it was found difficult to compete in the international market due to the higher cost of production. On the other hand the final quality was affected due to the instability of electricity power supply.

#### 2.2 Research and development

Research and development plays a dominant role in being qualitatively superior, innovative and diversified in the value added tea industry in order to compete in the international tea market. It is recorded that (Table 3) the exporters perceived that the existing research and development were weakly affecting on investing towards value addition. Research on improving the existing manufacturing and processing techniques to produce better teas more efficiently, devising new techniques to produce new types of products and new packaging techniques and surveys to identify changing needs of potential consumers were in negligible level compared to other competitive countries.

#### 2.3 Access to information

There were 66 percent of respondents who had weak perception on impact of extension to expand investment on value added tea sector (Table 3). This implies that the current information system is a barrier for the development of value added tea sector. The

flow of research outputs to the end user and getting the feedback from them was important. Otherwise the objective of research and development would lose. Exporters who were constrained by lack of information on the demand for specific tea related products might find it difficult to survive in the international market. Therefore it was important to make such information available to all exporters and make market forecasts periodically and effectively.

#### 2.4 Marketing capabilities

As the table 3 portrays, 83 percent of total regular exporters considered, the current promotional strength would be inadequate to encourage investment in value added tea sector to be survived in a highly competitive global tea export market. The Sri Lanka Tea board was focused on assisting the industry by conducting promotional campaigns in foreign markets and giving financial assistance to companies undertaking their own brand marketing. But it was found inadequate due to the limited budget of tea board.

It was needed for local exporters to develop their own brands, because future of Sri Lankan tea would depend on brand marketing. As individual companies were unable to bare a high cost that needed for the promotion activities in overseas market.

#### 2.5 Capital strength

Value addition was demanding high capital to purchase the costly machinery and establishment of hygienic working environment. According to the results (Table 3) it was a barrier to the industry. Firms involved in value addition are harassed with higher capital requirement. Therefore it is to be emphasized the government involvement in policy making to facilitate value adding firms with credit. Encouraging joint venture projects with the approval from BOI where a foreign partner shares the costs and the risks is another alternative for this. The packaging industry in Sri Lanka was in a better position compared to regional competitors. Advanced packing systems like vacuumed pillow types were also in operation.

### 3. Opportunities

An opportunity is an attractive arena for industry in which the firms would enjoy a competitive advantage. The external environmental analysis may reveal certain new opportunities for profit and growth. In some cases, the firms can overcome weaknesses in order to prepare itself to pursue a compelling opportunity in the industry (Anon, 2005).

#### 3.1 Incentives and subsidies

Fifty five percent of the sample exporters have realized the present incentives and subsidies as a desirable policy measure in terms of investing for value addition. Some incentives and subsidies are available for the value added tea sector. One policy measure is for Tea bagging machines in which 75 percent of the interest of loans obtained to purchase new tea bagging machines is met by the tea board. The export development and investment support scheme is

granted for the exportation of value added tea. Offering the sponsorship to participate in trade fairs by financing 50 percent of the total cost for brand promotion and generic promotion (Lion logo), for the highest exporters is another favorable policy measure. Importation of tea bagging machineries at zero tariff and interest free loans were given for brand promotion can be identified as a better policy measure to promote this industry.

**3.2 Key market size**

The greatest potential for value added tea now centers on East and Central European countries. The leading buyers of Sri Lankan tea in packets were CIS countries whilst Australia maintains the leading position for imports of tea bags.

Based on the perception of exporters existence of key market size and growth rate was strongly affecting as an opportunity for investment expansion (Table 3). Producing countries are now attempting to enhance their market share by gradually developing exports of tea in value added forms that has a growing demand in international markets. Today consumers are experiencing busy life styles, which make them to demand more convenience products. Therefore value added teas are having a good potential for development in local and international market. According to tea committee in London approximately 60 percent of all tea in the world has been consumed by tea bags. In USA 90 percent of all tea consumed was in the form of tea bags and in continental Europe this comes to almost 100 percent (Jain 1999).

**3.3 Price structure in niche markets**

The price position for Sri Lankan value added tea in relation to competing countries was considered. It was identified that Sri Lanka enjoys the present high price of value added tea at the international market (Table 3). Most of the tea exporters commented that Sri Lankan tea had a good price position in the international market because of the positive attitude for "Quality Ceylon tea". For example the average unit of FOB value at which trading had taken place in 2003 reflects improvement of 13.6 percent over the previous year (Anon, 2003a). So value addition was identified as an area needed to be further improved to obtain higher price and profit margin in the future global market.

**4. Threats**

A challenge posed by an unfavourable trend or development in the external environment that would lead the absence of purposeful marketing action to the erosion of the industry is what meant by threats.

**4.1 Labour regulations**

Manufacture of tea in Sri Lanka was highly labour intensive and, it was a major component of the cost of production. At the same time strict labour rules and standards were prevailed in Sri Lanka. Therefore it was important to consider the effect of prevailing labour regulations on investment expansion in value added tea sector. Among the respondents 83 percent had weak perception on the effect of labour regulations for investment expansion in value added tea sector

(Table 3). It was pertinent to mention that the improved labour regulation was an important prerequisite for the growth and restoration of viability of the tea industry in Sri Lanka. And hence appropriate labour regulations were to be adopted to ensure industrial peace and protection of worker rights.

**4.2 Exchange rate regime**

Fifty five percent of the respondents had weak perception for the effect of exchange rate regimes on the investment expansion in value added tea sector (Table 3). The increased sector deficit and the continuous declining international reserves exerted pressure on the rupee to depreciate faster during the second half of 2002. The rupee depreciated by 9.9 percent against the US dollar during 2003 as compared with 6 percent in 2002 (Anon, 2003b). The recent devaluation of rupee had increased the cost of import of goods such as tea chests, tea bag paper and flavouring caused the uncertainty in the industry. It was also criticized that the rupee that was kept overvalued in order to regulate inflation had contributed much towards the reduction of rupee revenue for the tea exports and decline in tea prices at the auctions. Therefore, it would be more useful to review this policy in the light of the crisis the sector was facing.

**4.3 Tax regime**

Tax consists of cess and duty. Cess is a levy imposed on all of the teas exported from Sri Lanka to finance the research, fiscal, regulatory, marketing development and promotional activities undertaken in the tea sector (Anon, 2003a).

The prevailing concessionary export duties and tax in tea sector were as follows

- 1. Export duty
  - Bulk teas -Rs. 1.50 per kg
  - Tea packets -Rs. 1.00 per kg
  - Tea bags -Rs. 0.50 per kg
  - Instant tea -Rs. 6.50 per kg
- 2. Tea Cess -Rs. 2.85 per kg

source: Anon, 2004

The stake holders in tea sector enjoyed the duties and tax. And they were said to be in a better position to lower their prices against some competing countries. Therefore profit margins after tax were highest in Kenya followed by Sri Lanka. But in India profit margin was reduced to a very low levels, as a result of high taxes.

**CONCLUSIONS**

Dissatisfaction with the traditional methods of marketing tea had arisen because of the fall in real prices of tea resulting a lower profit margin. Therefore the main thrust of export strategy in Sri Lanka is to switch over from the export of teas in bulk form to the export of value added tea products. The study had highlighted the necessity to focus on overcoming weaknesses and capitalize on strengths in order to encourage investors in value added tea sector to survive in a highly competitive global tea export market. In this case the government has an important and constructive role in creating policies. But the firms

in the tea industry have to influence the government in shaping policies and must adhere their support behind constructive government programmes. It needs assistance for the innovations and improvements within the industry and create a better environment in which firms can upgrade their competitive advantage. Other than that it is important for the government to pay much attention on deregulation of the labour market, development of financial market for the companies cannot find investment capital and expansion of investment to improve activities of Tea Research Institute with relation to value addition. It is required to formulate a dynamic tea promotional programme and franchising of the Lion logo to use only in packs with minimum quality standards to popularize Sri Lankan tea worldwide.

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