International Labour Organization

FROM OBLIGATION TO OPPORTUNITY

the LAB
MARKET SYSTEMS DEVELOPMENT FOR DECENT WORK

A MARKET SYSTEMS ANALYSIS OF WORKING CONDITIONS IN

ASIA'S GARMENT EXPORT INDUSTRY

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GLOSSARY

Apparel The range of sewn products including wearable clothing, household and industry apparel

Downstream Supply chain roles closest to retail and end users

Fast fashion A model of quick and inexpensive garment production based on short product life cycles and an increased number of seasons

Garments Wearable clothing produced by the readymade garment industry

Global value chain The range of activities located across different countries required to bring a product from its conception, through design, raw material sourcing and production, to marketing, distribution and retail to the final consumer

Lead times The duration from receiving an order to shipping it to the buyer

Outsourcing Transferring portions of work to outside suppliers rather than completing it internally

Offshoring The practice of moving a company's operations, supply base or to a country where costs are cheaper

Reshoring The return of some work to factories based in the country where most sales are made

Sweatshop A working environment considered to be unacceptably difficult or dangerous

Textiles The design and production of cloth and woven fabrics using natural or artificial fibres

Trim Materials used in sewing other than fabric, such as threads, buttons, lining, zippers and labels

Upstream Supply chain roles closest to raw material extraction and production

NOTES

On terminology and data consistency. This report uses the terms 'garments' and 'clothing' interchangeably. Secondary sources often present statistics for garments together with related products such as footwear, apparel and textiles. We have noted where such multi-sector figures are used, since some countries have a significant textile industry which affects data comparability. Much of the data about the garment industry is inconsistent and uses assumptions or proxies. Where contradictory figures exist, range estimates have been provided based on the most generally accepted secondary sources. Finally, as different institutions have slightly different methods to account for trade flows, for the sake of consistency we have used World Trade Organization figures wherever possible.

On confidentiality. All data collected through primary research have been made anonymous so that individual brands, agents and factories cannot be identified. Instead, we refer in generic terms to 'some buyers' or 'a garment manufacturer in Vietnam'. Company names are only used in reference to good practices where these are already in the public domain (e.g. in published articles or sector analysis documents), or, where not already public, if permission has been sought from the company in question.

On report limitations. Asia a vast continent encompassing many different countries with a range of policies, practices and cultures[1]. A degree of generalisation has therefore been necessary. Given the relatively narrow research window, the large geographic scope and supply chain complexity - alongside limitations in the quality and consistency of data presented in secondary sources - this analysis is just a piece in the puzzle of understanding the underlying reasons that inhibit better working conditions. This report also focuses on garments produced for global export, not for domestic markets. Finally, as a vast academic and practitioner literature already exists on the garment sector in Asia, the report should also be read alongside other key resources[2].

1. For the purposes of this report, Asia is defined as Southern Asia, Eastern Asia and Southeast Asia.
2. The 3 key reports which are drawn on heavily throughout this document are the World Bank publications from 2016 "Stitches to Riches? Apparel Employment, Trade, and Economic Development in South Asia", and 2012's "Sewing Success? Employment, Wages, and Poverty following the End of the Multi-fibre Arrangement" alongside the 2017 Friedrich-Ebert-Stiftung report "The missing link in the chain? Trade Regimes and Labour Standards in the Garments, Footwear and Electronics Supply Chains in Vietnam"

EXECUTIVE SUMMARY

The Lab (www.ilo.org/thelab) carried out an analysis of the garment supply chain in Asia to understand the dynamics of value addition and the market incentives to provide better working conditions[3]. This report, along with two complementary reports on industrial relations and environmental sustainability, is part of the scoping phase for a regional project on "Decent Work in the Garment Sector Supply Chains in Asia", funded by the Regional Development Cooperation Section at the Embassy of Sweden in Thailand. The programme seeks to address improvements in decent work, environmental sustainability, and gender equality in the garment sector in Asia[4].

Export-oriented apparel production is the quintessential global value chain. Different stages of production – as raw materials are transformed into retail products – are carried out in different countries, involving complex and fast-changing buyer demands and drawing on diverse industries such as agriculture, textiles, and footwear[5].

The global value chain structure helps link local producers to international markets, facilitating knowledge spillover and new skills for workers. For emerging economies, garments are considered a gateway to globalised manufacturing exports[6]. The sector is also a critical absorber of low-skilled labour: On average, garment production accounts for half of manufacturing employment in the main clothing exporting countries in Asia[7]. For poor labourers, it is often the most attractive industry after agriculture. Garments are also an important driver of economic empowerment, with women accounting for a larger share of the workforce compared to other sectors[8].

However, working conditions in Asia's factories remain a key concern. The nature of the modern garment industry —relying on labour-intensive inputs with short lead times — carries a high risk of human rights and environmental violations. While employment conditions vary greatly across countries

3. The research was conducted by an ILO Lab team made up of Shelvy Arifin, Callie Ham, Auret van Heerden, Ba Lam Nguyen and Matt Ripley. The views presented in this paper are those of the authors and do not necessarily represent those of the ILO.
4. For further background on the scoping phase and the regional validation meeting, see http://www.ilo.org/asia/events/WCMS_571308/lang--en/index.htm
5. EPRS (2014)
6. World Bank (2016)
7. An average of 40% across SAARC countries (World Bank, 2016). Includes both garment and textile sectors.
8. World Bank (2016), p.19

and companies, instances have been reported of child labour, discrimination, forced labour, work-related injury and ill health, violations of the right of workers to establish or join a trade union and to bargain collectively, non-compliance with minimum wage laws, and wages that fail to meet basic needs of workers and their families[9]. The production process and materials used in garment manufacturing also increase the risk of environmental hazards, including dangerous chemicals, excessive water consumption, water pollution and greenhouse gas emissions.

The sector has received significant international attention, in large part due to a series of high-profile media stories concerning industrial disasters and serious labour rights violations[10]. Numerous initiatives have been launched by governments and development agencies to try and promote a more sustainable garment industry, including through 'top-down' policy channels, 'bottom-up' interventions on the factory floor, and 'outside-in' campaigns seeking to leverage public and consumer pressure.

This report uses a market systems approach to identify the set of actors and factors that influence how garment factories behave. A market systems analysis seeks to identify the 'systemic' constraints to pro-poor sector growth, such that business innovations can spread and be sustained across an industry – and not just confined to the few firms that development programmes partner with[11]. It recognises that no enterprises exist in isolation: Rather, their commercial and social performance relies on an ecosystem made up of many interconnected market actors, from suppliers to buyers, and a range of supporting services such as access to appropriate technology, capital and know-how[12].

The **first part** of the report focuses on the regional context. Based on desk research, it synthesises key existing documents and data to present region-wide challenges, production trends, purchasing practices, and the role of intermediaries. It includes a mapping of the chain from primary producers to end users, setting out where value is created at each stage. Special attention is paid to issues of gender equality and environmental sustainability.

The **second part** takes a deeper dive into the drivers of poor working conditions. It is informed by market systems scans in Vietnam and Indonesia, where primary research was undertaken to investigate the under-performing functions and rules which inhibit both better working conditions *and* improved business performance. The aim was to identify strategies that not only encourage companies to better comply with core human and labour rights, but also help them realise that good working conditions can often be good for business; in short to see decent work as an opportunity, not just an obligation.

The identified systemic constraints are:

- *Shortfalls in the effectiveness of public and private regulation* are caused by an inability to monitor complex supply chains, and misaligned incentives. Despite significant progress over the past decade, both regulation and 'beyond compliance' mechanisms are hindered by hidden subcontracting and (a lack of) supply chain transparency. As a result, many subcontractors and lower tier suppliers are 'sandwiched' between complying with labour standards, and meeting the time-pressured orders of international brands. Brand social responsibility teams are often structur-

9. OCED (2017)
10. The Guardian Newspaper (2017)
11. For more information see the BEAM Exchange (https://beamexchange.org/market-systems/what-market-system/)
12. Kramer and Pfitzer (2016)

ally removed from the sourcing decision-makers in their company whose buying behaviour increases the risk of unauthorised subcontracting.

- *Sub-optimal human resource strategies and inefficient in-factory management practices* constrain both business performance and improved labour standards. However, the link between productivity and better working conditions is neither automatic nor uni-directional. Efforts to build a 'business case' for manufacturers to improve working conditions have focused on demonstrating the 'returns', but not on the investment and risks side of the equation. Given slim factory margins that can be eroded to selling at cost, there are questions about how receptive the majority of factories will be to the opportunity argument. Instead, the carrot of efficiency improvements needs to go hand-in-hand with sector-wide upgrading strategies, particularly for those companies deploying a 'cost control' and survival-based business model.

- *Equitable access to finance*. Foreign investment can facilitate knowledge spillovers in the long-term, but can create closed networks based on nationality in the short-term, which limit opportunities for domestic upgrading. Local suppliers need access to growth capital, but often face significantly greater challenges to accessing affordable credit than their foreign-invested counterparts. This constrains working capital and creates a risk averse attitude towards investing in working conditions. Development and 'impact' finance can help bridge the gap, but significant private capital will be needed to achieve scale.

- *Over-reliance on imported inputs* can impact on lead times and create additional pressure on workers, resulting in excessive overtime and abuse. Yet there are questions about the strength of the commercial and environmental case for countries to develop backward linkages. Textile production requires significant capital, good infrastructure and above all is energy-intensive. However, there are proven opportunities for significant efficiency savings which can reduce the environmental impacts of textile production and free up resources to improve working conditions.

- *Slow-to-adapt skills systems*. Garment production has long been a low-skilled, low-paid, labour-intensive industry – and the source of Asia's comparative advantage in production. High staff turnover rates are generally accepted as a 'cost of doing business' as labour supply has historically been plentiful, but in some countries the emergence of other more attractive sectors such as electronics is creating new pressures on factories. Skills upgrading will be vital as the industry modernises and many of the traditional entry-level jobs, held mostly by women, might be lost. The use of intelligent technologies – the so-called Fourth Industrial Revolution – means that many workers will no longer be required to control machines. Buyer demands for full service production emphasise the importance of upskilling the workforce. However, vocational training is not widely demanded, links to industry can be poor, and the quality of

supply is generally low. Professional recruitment services are not developed, and the medium-term market capacity to absorb skilled workers is uncertain.

The **third** and final part zooms back out to lay the foundations for a series of regional-level actions. Based on the study's mandate to go beyond tried and tested tools to identify more integrated models, it thinks critically about which arguments and pressure points may lead to systemic change across the supply chain. There is a particular focus on measures to go beyond the 'tip of the iceberg' and reach the lower tiers of the global supply chain, which is where the most precarious working conditions can be found. The following actions are recommended, based on a framework for sector collaboration set out by the OECD:

- Pool information: Sharing information can help increase the awareness of specific risks in the sector and bring attention to emerging risks – and opportunities – more quickly than would be possible for most individual enterprises. Good data are essential to help highlight problems that several countries share, and provide the platform to explore where solutions best can be found in regional cooperation. Potential activities include:
  - *Regional statistical benchmarking*. Develop standards for comparable data on decent work in the garment sector.
  - *Share the business case*. Compile and quality control differentiated business cases for working conditions, environmental sustainability and gender equity into an open-source repository.
  - *Understand the audience for evidence*. Agree on a framework to understand what evidence will be most persuasive for different types of brands and factories.

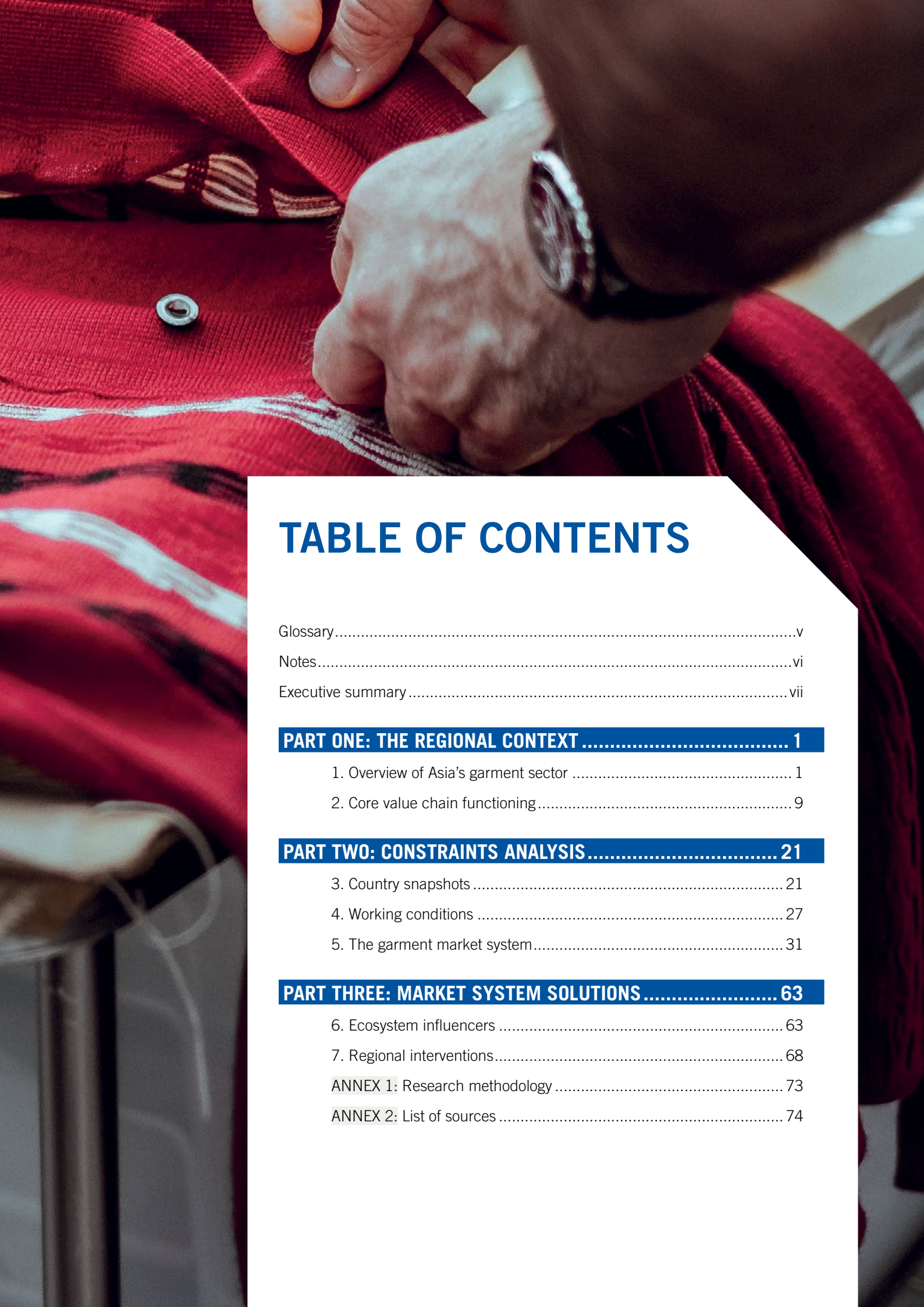
- Increase leverage: There are many reasons why individual enterprises may lack leverage on their own, such as a small size or relatively insignificant buying power. Where a single enterprise lacks leverage, a group of enterprises operating together may wield greater leverage by participating in forums or seeking alignment of their activities, timelines and follow-up measures. Potential activities include:
  - *Engage buyers on responsible sourcing*. Build the capacity of NGOs, unions and business associations to interact with sourcing teams on the buying practices that ultimately drive many of the working conditions deficits.
  - *Replicate sub-regional models*. Encourage adoption across the region of methods and models that have proven successful at a sub-regional – or even country-level in extending compliance to 2nd tier suppliers and subcontractors.

- Scale-up successful measures: Collaboration can help play a role in scaling-up solutions (e.g. policy, training, capacity building, etc.) that have been demonstrated to be effective. Scaling-up can also crowd-in SMEs that may have more limited resources and are more risk-averse to initially investing in pilots. Potential activities include:
  - *Accelerate the journey from seed to scale*. Scan the market to see which pilot programmes are addressing systemic constraints, and pro-

vide a platform to discuss their success – then share and disseminate proven solutions across the region.

- Increase sector transparency: Collaboration can help facilitate the disclosure of aggregate information which increases the transparency of the sector. Making public the information about suppliers, compliance assessments, and any corrective action(s) taken not only shows how brands are making demonstrable progress, but also allows third parties to independently verify and observe how working conditions are improving. Potential activities include:
  - *Supercharge supply chain transparency*. Encourage the spread of common standards for the public disclosure of supplier lists and real performance data.

Annex I sets out the research methodology and **Annex II** lists the key source documents.



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The regional context

PART 1 The regional context

1 OVERVIEW OF ASIA'S GARMENT SECTOR

1.1 REGIONAL PRODUCTION AND EXPORT

Global trade in garments is dominated by a small group of exporters: In 2015, ten countries produced 87% of the world's exports[13]. Asia is the so-called clothing factory for the world, accounting for 60% of global exports of garments, textiles and footwear[14].

Table 1 shows the top 15 global clothing exporters by value. While 11 of the 15 largest clothing exporters are from Asia, there is far from an equal split of market share across the region. With $175 billion of garment exports in 2015, China alone counts for about 40% of global clothing exports by value, making up over 60% of all garments exported by Asia's ten largest manufacturers[15]. Rising costs of production in China – especially labour, where wages have increased by 124% in the last ten years[16] – coupled with an economic transformation to focus on higher value-added sectors means the likely longer-term importance of garment production in the country will decrease. However, at least in the short term, China remains the dominant player. Productivity has increased with wages, meaning unit labour costs have remained competitive. China's market share is currently holding steady, and buyer confidence is growing: The 2017 State of Sourcing Survey showed a rise in the number of brands looking to increase orders from the country in the upcoming year[17].

13. WTO World Trade Statistics 2016
14. ILO (2015), 2014 figures
15. US175 out of US286 (2015) figures
16. Fashion Unite (2013)
17. Just Style (2016)

After China, the largest garment producers in the region are Vietnam and Bangladesh, exporting a combined $48 billion of clothing in 2015. **Figure 1** shows the average annual percentage change in clothing export volumes from 2010-14. Alongside Cambodia, Vietnam and Bangladesh are the fastest growing exporters: Over the past five years they recorded average annual garment export increases of 18%, 17% and 13%, respectively. The latest 2015 data cement this trend, albeit at a slower pace: Increases in export value took place in Vietnam (+10%), Cambodia (+8%), Bangladesh (+6%) and India (+2%). All other major exporters saw stagnation or a decline in their export values[18].

Figure 2 sets out changes in the share of the world clothing market for Asian exporters between 2000 and 2015. Bangladesh, Vietnam, India and Cambodia have significantly increased their share of the world clothing market, while Indonesia, Pakistan, Sri Lanka, Malaysia and Thailand all lost ground.

Table 1:
Top 15 global clothing exporters by 2015 figures (Asian countries in bold)

Rank	Country	Value ($, billion)	Share (%)
1	**China**	**175**	**39.3**
2	European Union (28)	112	25.2
3	**Bangladesh**	**26**	**5.9**
4	**Vietnam**	**22**	**4.8**
5	**Hong Kong, China**	**18**	
6	**India**	**18**	**4.1**
7	Turkey	15	3.4
8	**Indonesia**	**7**	**1.5**
9	**Cambodia**	**6**	**1.4**
10	United States	6	1.4
11	**Pakistan**	**5**	**1**
12	**Sri Lanka**	**5**	**1**
13	**Malaysia**	**5**	**1**
14	Mexico	4	0.9
15	**Thailand**	**4**	**0.8**

Figure 1:
Average annual percentage change in clothing export volumes, 2010-14

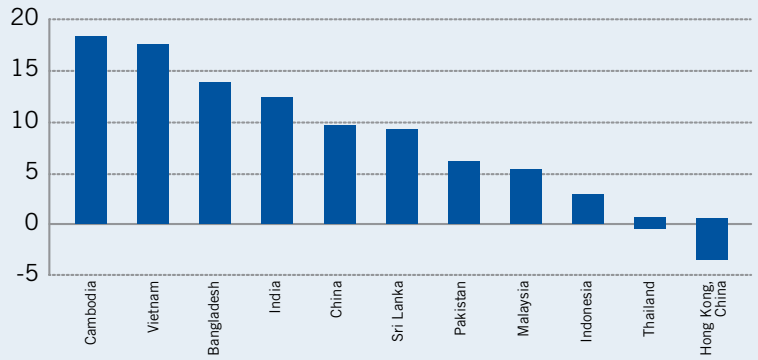
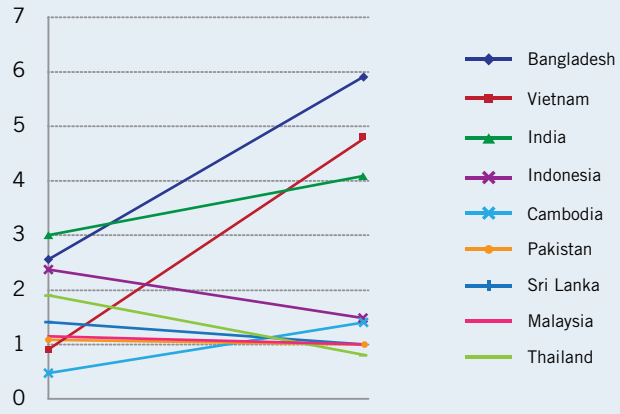


Figure 2:
Share of world clothing export market, selected Asian countries (excluding China) in %, 2000 and 2015



18. WTO World Trade Statistics 2016

1.2 PRODUCTION LANDSCAPE

1.2.1 Global trends

The value of export trade in clothing fell from $483 billion in 2014 to $454 billion in 2015 – the first time since the global financial crisis that world garment markets recorded negative growth[19]. This comes against a backdrop of renewed uncertainty about the policy environment and the macro-economic climate that shapes trade.

Buyers continue to strive to rationalise their supply chain by looking for fewer places and firms for outsourcing. Such consolidation aims to reduce sourcing complexity (and associated management/monitoring overheads), while securing larger and more capable strategic suppliers who can offer a range of services at competitive prices[20]. At the same time, buyers are also looking for opportunities to diversify supply. Three quarters (72.1%) of buyers who responded to the 2017 global sourcing survey say they are actively looking for alternative sources of supply. Growing concerns about compliance and corporate social responsibility – as well as rising raw material and labour costs – have led some buyers in Europe and North America to look for new suppliers outside Asia[21]. Popular emerging sourcing destinations include Central America and Kenya, whose attractiveness as commercially viable suppliers has improved due to a combination of cost (competitive wages, a supply of skilled workers) and infrastructure factors (significant water supplies, decreases in electricity costs, improved port efficiency)[22].

Brands and retailers also list exchange rate volatility as a major concern[23]. Asked about expectations for the coming year, 69% of survey respondents expect overall sourcing costs to rise, compared with 54.5% last year[24]. The primary reasons for this are fluctuating exchange rates, demand for higher quality products and more complex compliance requirements. Margins in the sector (see section 2.3) remain squeezed – so foreign exchange fluctuations in particular can have significant effects on competitiveness[25]. Emerging market currency shifts are likely to continue in the future in a prolonged period of volatility risk. This presents a challenge for countries like Myanmar, where strong growth in apparel export volumes has been offset by a depreciation of the kyat, resulting in a drop in the dollar value of garment earnings[26].

Competition for global buyers remains intense. In response, some garment manufacturers have begun to diversify their own end markets to mitigate the risk of over-reliance on the European Union and the United States. Expanding consumer classes in Asia – and the purchasing power of a growing middle class – provide opportunities closer to home for some of the world's largest garment producers[27]. Outside of Asia, the world's fastest growing consumer markets include Brazil, Russia, Saudi Arabic and the United Arab Emirates[28].

19. WTO International Trade and Market Access Data, Clothing Exports, 2015
20. Interview with IDH Sustainable Trade
21. ITC (2016)
22. ITC (2016)
23. Just Style (2016)
24. Sheng Lu (2016)
25. Economist Intelligence Unit (2016)
26. Economic Intelligence Unit (2016). Note that for buyers, while currency volatility is a problem, depreciation makes a country more attractive for buyers.
27. ILO (2015),
28. World Bank (2016), p. 48

The highest performing clothing exporters have started to build capabilities across the value chain, often supported by sectoral policies and industrial development strategies. This includes investing in adding both front-end (design) and back-end services (logistics) so companies can move into higher value-added activities such as design and marketing, as well as developing backward linkages closer to raw material supply. With countries continually vying to capture market share, there is a sense that companies need to 'move up the value chain just to hang in'. In Asia, however, the most successful exporters in recent years have tended to occupy the 'fast fashion' side of the garment export market. In countries like Bangladesh and Vietnam, which rely on bulk orders of lower-quality clothing, the garment sector has bucked the trend of an overall decline in merchandise exports. This, however, is likely a result of the unique situation caused by China stepping out of the low-end market segment[29].

Trade policies and agreements have long played an important role in shaping global garment production. The phase-out of the multi-fibre arrangement (MFA) in 2004 – which imposed a system of quotas on import volumes – drove down retail prices and opened up the market to greater cost competitiveness[30]. More recently, preferential market access schemes have been instrumental in dictating the winners and losers of trade. Garment sector growth in countries like Kenya has been in part spurred by the market access provided under the American Growth and Opportunity Act (AGOA)[31]. For low-income countries, the European Union's Everything But Arms (EBA) and Free Trade Agreements have included reduced tariffs for apparel products. Yet the direction of travel of future governance of global trade is uncertain, particularly following recent decisions in major destination countries such as the USA and the de facto death of the Trans Pacific Partnership, which was set to have significant implications for both textile and garment industries across Southeast Asia.

Figure 3:
Share of garment exports which are cotton-based, 2012 (World Bank, 2016)

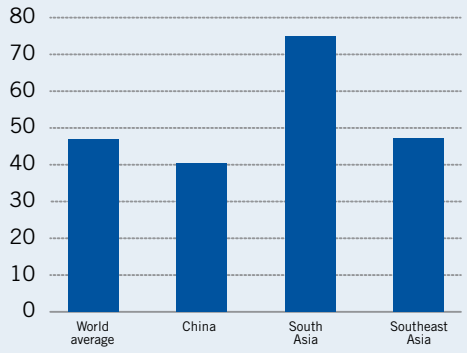
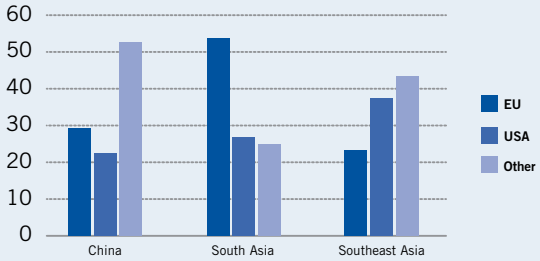


Figure 4:
Share of exports to the EU, US and other by value (based on World Bank, 2016 using 2012 data, EU-15 only)



29. Bangladesh, for example, has seen growth without significantly changing its market structure or export composition
30. World Bank (2012)
31. ITC (2016)

1.2.2 Sub-regional and country comparisons

The garment industry in Asia can be broadly divided into three sub-regions – each with important differences in product lines, source materials and end markets. These are:

- China, as by far the largest exporter both regionally and globally
- South Asia, including India, Bangladesh and Pakistan[32]
- Southeast Asia, including Cambodia, Vietnam, Indonesia, Myanmar

South Asian countries produce more cotton-based garments, while those in Southeast Asia make greater use of man-made fibres (MMF). **Figure 3** shows that South Asia has almost double the world average share of cotton-based apparel exports. This share of output is largely driven by input availability: India and Pakistan have large textile industries, and are fully self-sufficient in terms of their cotton sourcing needs.

South Asia exports a greater share of garment products to the European Union, while Southeast Asia exports a greater share to the USA. As in **Figure 4**, China has the most diversified end markets, with half of garment exports going to non-USA and non-EU destinations.

Southeast Asia is more economically integrated through the Association of Southeast Asian Nations (ASEAN), and the recently agreed ASEAN Economic Community. It is worth noting, however, that intra-regional trade in garments is minimal: Less than 1% of total apparel exports from South Asia, for instance, are exported to other South Asian countries[33]. So while we can speak of Asia's garment sector, in terms of market structure it is more a global than a regional value chain.

At the country level, Asia's garment exporters have emerged from their own unique historical circumstances. While all countries share in the importance of garment production as a labour-intensive source of employment, the relative significance of the sector to their economies varies greatly. **Table 2** shows that in Bangladesh, garments make up over 80% of all manufacturing exports, and in Cambodia and Sri Lanka this figure is near the 50% mark. In all other countries the garment share of manufacturing exports is 20% or below, reflecting either a nascent clothing sector or a more diversified industrial base.

Due to the global nature of garment production, foreign firms have often played a pivotal role in developing domestic apparel sectors, particularly in Cambodia and Sri Lanka. Foreign investment can provide access to new technologies and buyers, with related learning and upgrading opportunities[34]. On the other hand, there is some evidence to suggest that foreign ownership can also place barriers to local innovation, potential for nationals to advance to managerial positions, and developing domestic inputs, such as textiles and trim[35].

In terms of product differentiation, Asia's garment exporters can be split into two groups. In broad terms Bangladesh, India, Pakistan, Cambodia and Vietnam produce low-cost basic commodity items, while Sri Lanka, Myanmar, India (embroidered garments only) and China produce (or aspire to produce) higher value-added technical items. This is reflected in the range of products

32. Sri Lanka has markedly different products and inputs from other South Asian countries, so is excluded here
33. World Bank (2016)
34. World Bank (2016)
35. Cho and Chi (2017)

mostly commonly exported by each country, as set out in **Table 3**, below.

Table 2:
Production comparison, compiled using data from Business Innovation Facility (2016), World Bank (2012), World Bank (2016), Wage Indicator (2016), and own research

	Sri Lanka	India	Pakistan	Bangladesh	China	Myanmar	Vietnam	Cambodia	Indonesia
Estimated number of exporting factories (2014/16)	800	1,200	5,000#	5,000[36]*#	100,000[37]	210[38]	2,500	1,000	3,000
Share of manufacturing (%)[39] (2014)	43.5	5.5	20.2	80.9	8.0	8.9	13.0	54.3	4.4
Range estimate for number employed in sector[40] (2012/2014)	267,000 - 280,000	1.8 million*[41]	1-2m	2.7-4.2m	4.5-10.8m*	126,000-280,000[42]	2.5m (VCCI)	400,000-700,000	1.1-1.3m
Firm ownership[43]	80% Joint ventures and locally owned	Majority local	Less than 2% foreign owned	90% local	65% local[44]	75% foreign owned or joint ventures	Foreign (75%), rest domestic	93% foreign	Mixed, approx. half local
Role of FDI	Historically high	Low	Low	Low	Medium	Medium	Medium	High	Medium

Key: *G,T&F figures, #Large number of firms are cottage industry, small and informal.

Table 3:
Product specialisation table (World Bank, 2012, and own research)

Country	Specialisation/export products
Bangladesh	Basic commodity items, including trousers, knit and woven shifts, sweaters/sweatshirts (mostly cotton)
India	Cotton products, including knit and woven tops, skirts, men's bottoms and embellished and embroidered apparel
Sri Lanka	Niche and fashion-oriented items such as intimate apparel, trousers and footwear – equally divided between cotton and MMF
Pakistan	Basic cotton, woven, denim and chino trousers, low-priced knitwear such as polo shirts and t-shirts, and fleece sweatshirts
Vietnam	Cotton knit shirts, MMF knit shirts, MMF trousers. Jackets are of greater importance in the EU market, while t-shirts have greater significance in the U.S. market.
Cambodia	Highly concentrated in trousers, sweatshirts, and t-shirts
China	Full range of technical and fashion products
Indonesia	Cotton knit sweaters, pullovers, & vests; men's/boy's cotton shirts; cotton trousers; women's/girl's man-made fibre shirts and blouses, sports jerseys

36. Business Innovation Facility (2016)
37. Sheng Lu (2016)
38. Business Innovation Facility (2016)
39. WTO World Trade Statistics 2015, using 2014 figures
40. ILO (2015) and EPRS (2014)
41. Fashion United (2013)
42. Business Innovation Facility (2016)
43. World Bank (2016)
44. EU SME Centre (2011)

1.3 WORKING CONDITIONS, GENDER AND ENVIRONMENTAL SUSTAINABILITY

Garment production in Asia has provided an opportunity for millions of low-skilled informal workers to transition to formal jobs[45]. However, the nature of the modern garment industry and the ever-increasing pressure from 'fast fashion' to reduce lead times means the sector carries a high risk of human and workers' rights violations.

Working conditions vary greatly across countries and companies, with key issues including long hours, low wages, insufficient occupational safety, abusive practices and the harassment of women[46]. All 20 of the largest apparel exporting countries have a minimum wage, and most have regulations on working time, but non-compliance is high. While aggregate wages across the region are slowly rising, according to recent ILO research, excessive working hours remain common in the garment industry[47]. In Cambodia, half of all garment sector employees worked more than the allowed 48 hours per week. In Pakistan and Vietnam, more than 40% work excessive hours.

Over the past decade, it is estimated that at least 1,500 people have died and 3,000 people have been injured in fires or collapsed buildings in textile factories[48]. These tragedies are exacerbated by inadequate fire escapes, alarms, first aid or fire-fighting equipment. Other physical hazards include repetitive strain injuries from repeated spinning and cutting; as well as exposure to steam and hot fluids during processing and finishing operations that contribute to cardiovascular and communicable diseases. The widespread lack of personal protective equipment (PPE) can result in exposure to chemical hazards, leading to skin and respiratory disorders[49].

In the absence of effective public regulation, private regulation has stepped in. Global buyers and brands have sought to exert influence over suppliers by requiring adherence of codes of conduct and conducting regular (albeit often pre-announced) audits. However, labour standards are routinely violated, and the impact of private regulation rarely extends beyond first tier suppliers. Even in factories that have participated in the Better Work programme in Indonesia and Vietnam, 25-35% of factories are still non-compliant with national legislation[50].

Although garments and textiles are critical from a **gender perspective** to attract women into the workforce, there are differences in the ratio of male to female employment across countries. This is partly due to the context-specific nature of male and female relations and cultural norms shaping respective roles within society, as well as overall female labour force participation[51]. **Table 4** sets out estimates of the share of female employment in the garment sector against benchmark labour force participation rates. In Sri Lanka, Myanmar and Cambodia, women comprise the vast majority of all garment industry employees. Given that India and Sri Lanka have similarly low female labour force participation rates, the share of female employment in the garment sector in Sri Lanka is remarkably high (at 75-87%).

45. ILO (2015)
46. Tufts (2016)
47. ILO (2015)
48. J. Safra Sarasin (2014)
49. J. Safra Sarasin (2014)
50. Tufts (2016)
51. ODI (2004)

Table 4:
Female share of employment in the garment sector (World Bank, 2012, VGCL and ILO, 2017[52]).

	Sri Lanka	India	Pakistan	Bangladesh	China	Myanmar	Vietnam	Cambodia	Indonesia
Range estimate (%) of female employment in garment sector (2013-5)	75-87	22-38*	28-30*	62-80	69	80-95	67-87	82	64-65
Female labour force participation rate (2017)	30	27	25	43	63	75	74	76	51

Key: *Garment and textiles

Women consistently lag behind men in terms of earnings. ILO research (2015) indicates that, when controlling for demographic, educational, geographical, subsector and occupational differences between the sexes, there is a significant wage disparity in favour of men: Female garment workers earn an average of 11% less than their male peers, rising to as high as 48% less in Pakistan and 39% in India. Indeed, aside from Bangladesh, women earn less than men on an hourly basis in all countries in the region[5253].

Beyond wages, women face additional gender-specific barriers, including more limited access to education and training programmes and childcare solutions[54]. Gender-related job segregation is also prevalent, as female labour is concentrated in jobs such as weaving and sewing, while men are employed mainly in more technical and skilled positions such as machine supervisors[55]. There is a glass ceiling to career progression: In a recent survey in Bangladesh, 4 out of every 5 production line workers was female, while just over 1 in 20 supervisors was a woman – meaning 95% of the managerial talent in factories emerges from 20% of the workforce[56]. It also places women at greater risk of redundancy, as new technologies mean more manual jobs are made redundant. In Bangladesh, the female share of employment has actually decreased since the 1990s, as the sector modernized[57].

The production process and materials used in garment manufacturing have negative **environmental impacts.** The nature of these concerns, however, varies at each stage of product transformation, with the greatest risks found in upstream suppliers. The interconnected industries of textiles and tanneries have the highest use of polluting chemicals and, along with cotton growing, have the most water intensive processes such as dyeing/printing and finishing, where critical decisions are made about the temperature and frequency that fabric is washed at[58]. In the clothing assembly-to-retail segment, greenhouse gas emissions arise from transportation and packaging. A separate Environmental Sustainability Scoping Study covers these issues in more detail – the focus in this analysis is on links between environmental sustainability and enterprise performance[59].

52. Labour force participation rate from ILOSTAT, modelled rates 2017
53. ILO, Phu Huynh (2015)
54. ILO and IZA (2014)
55. ODI (2004)
56. International Growth Centre (2014)
57. World Bank (2012)
58. OCED (2017)
59. To read this report, visit http://www.ilo.org/asia/events/WCMS_571308/lang--en/index.htm

2 CORE VALUE CHAIN FUNCTIONING

Garment production is a buyer-driven chain. Brand owners and retailers – usually in the United States and Europe – dictate key functions such as marketing, sales and design. The actual assembly of clothes is outsourced to a decentralised network of third party suppliers, largely offshored to Asia.

The garment supply chain is made up of the physical transformation of raw materials into final products, while the value chain consists of activities that add economic value to the product at each stage. Together, they make up the global value chain for garments[60].

2.1 THE GARMENT SUPPLY CHAIN[61]

Figure 5 sets out a simplified and generic garment commodity supply chain, depicting the flow of inputs through to retail. The chain is organized around five main parts: *Raw material* supply, including natural and synthetic fibres; provision of *components* for garment assembly, such as the yarns and fabrics manufactured by textile companies alongside trim; *production* networks made up of garment factories that conduct cutting, sewing, trimming, ironing – including their domestic and overseas subcontractors who conduct wet processes, printing, dyeing and washing; *export* channels made up largely of trade intermediaries; and marketing networks which *retail* to the final consumer[62].

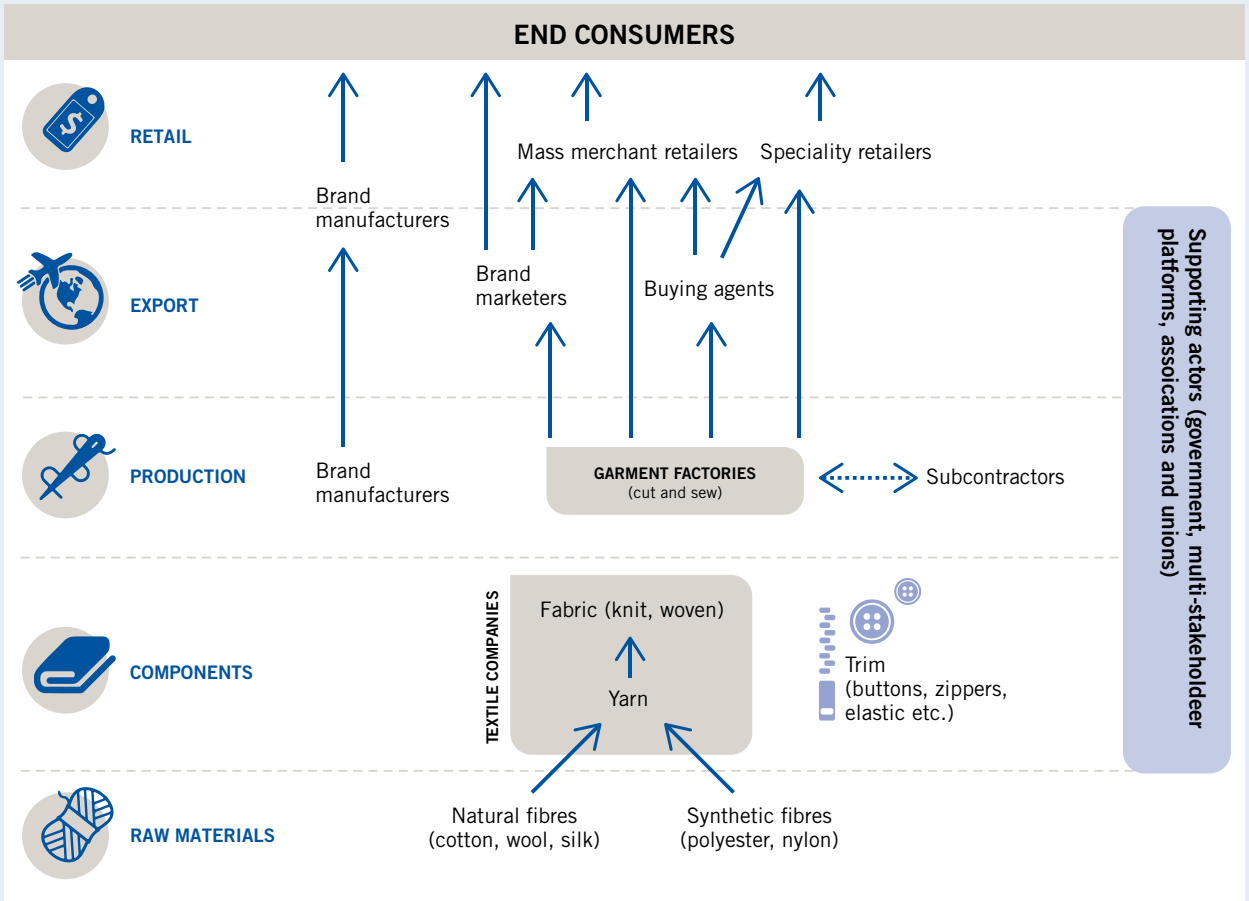
60. World Bank (2012)
61. The garment supply and value chain has been written about extensively. This section is based on a number of key source documents: including the World Bank (2012 and 2016) and UNIDO (2003)
62. Adapted from UNIDO (2003) and World Bank (2012 and 2016)

Lead firms are the buyers who control access to the most profitable resources, such as product design, new technologies, trademarks and consumer demand. In the garment sector, these firms operate downstream and closest to the end customer. The two groups of lead firms are brands and retailers.

Brands have their own distinctive clothing line, complete with unique logos and other visual elements, which are sold at discount or department stores, or sometimes through specialist retail outlets owned by the brand themselves. There are two types of brand owners: *marketers* who control branding and marketing but contract out manufacturing capabilities, and *manufacturers* who own production plants and coordinate textile sourcing, in addition to controlling marketing and branding activities[63]. **Table 5** sets out the supply chain distribution in Asia for selected major brands.

Brand marketers are known as 'manufacturers without factories' and include companies such as Nike, Adidas, Polo Ralph Lauren and Calvin Klein, as well as the well-known luxury and designer brands[64]. These companies have focused their competitive edge on design and branding, leaving overseas contractors to manage the whole production process. Brand manufacturers such as Hanesbrands (and until recently, Fruit of the Loom), on the other hand, have an integrated supply chain and tend to have larger operations. Over the past decades, the numbers of brand manufacturers has markedly declined.

Figure 5:
The garment supply chain



63. Increasingly brand manufactures also contract out (parts of) production
64. Also known as garment merchandiser

Table 5:
Supply chain distribution of selected major brands – share sourced from Asia by country by number of factories (2013 unless otherwise indicated, based on Wage Indicator, 2016)

Brand	Location of HQ	Total suppliers (global, all products)	Bangladesh	Cambodia	China	India	Indonesia	Pakistan	Sri Lanka	Vietnam
GAP*	USA	900[65]			26%					
G-Star*	USA	28	35%		23%	18%				13%
H&M^	Sweden	1882	73%[66]							
Inditex^	Spain	4312	31%		23%	7%				
Levi Strauss#	USA		2%	2%	34%	9%			4%	5%
Mango	Spain	264	6%		42%	5%			4%	
New Look	UK	917	12%	14%	48%	3%		2%		2%
Next	UK	2118	7%		44%	9%			8%	
Nike*	USA	669	1%	3%	21%	3%	19%	2%	3%	35%
Pimkie	France	161	5%		37%	12%				
Puma	Germany	203			33%	10%				21%

***2016**
^2015
 # 2011

Retailers develop clothing product lines which are sold only via their retail locations. Retailers used to be the main customers of brands, but have now become their competitors as retail stores have turned to developing their own labels. The two types of retailers are *mass merchants*, which sell a wide array of consumer products in addition to articles of clothing, and *speciality apparel stores*, which only sell their own private label. Both types of retailer fully outsource garment production. Mass merchant retailers are mostly large department stores such as WalMart, Tesco, Mark & Spencer, Sears and Carrefour, which are able to reap economies of scale and secure the lowest prices. The strength of these retailers rests in marketing and branding, and they tend to have more limited know-how to design and make the products they are procuring. Speciality apparel stores are generally the international chains such as Gap and H&M, and will likely be engaged in product design, fabric selection and procurement and even monitoring contracted out sewing operations.

Agents – also known as buying houses, vendors or trading companies – are intermediaries who act on behalf of retailers to coordinate a network of garment suppliers. Agents locate, qualify and inspect overseas garment producers, negotiate orders with them, and sometimes conduct quality control and monitoring against the retailers' standards and codes of conduct[67]. As retailers prefer agents capable of building and selling the entire range

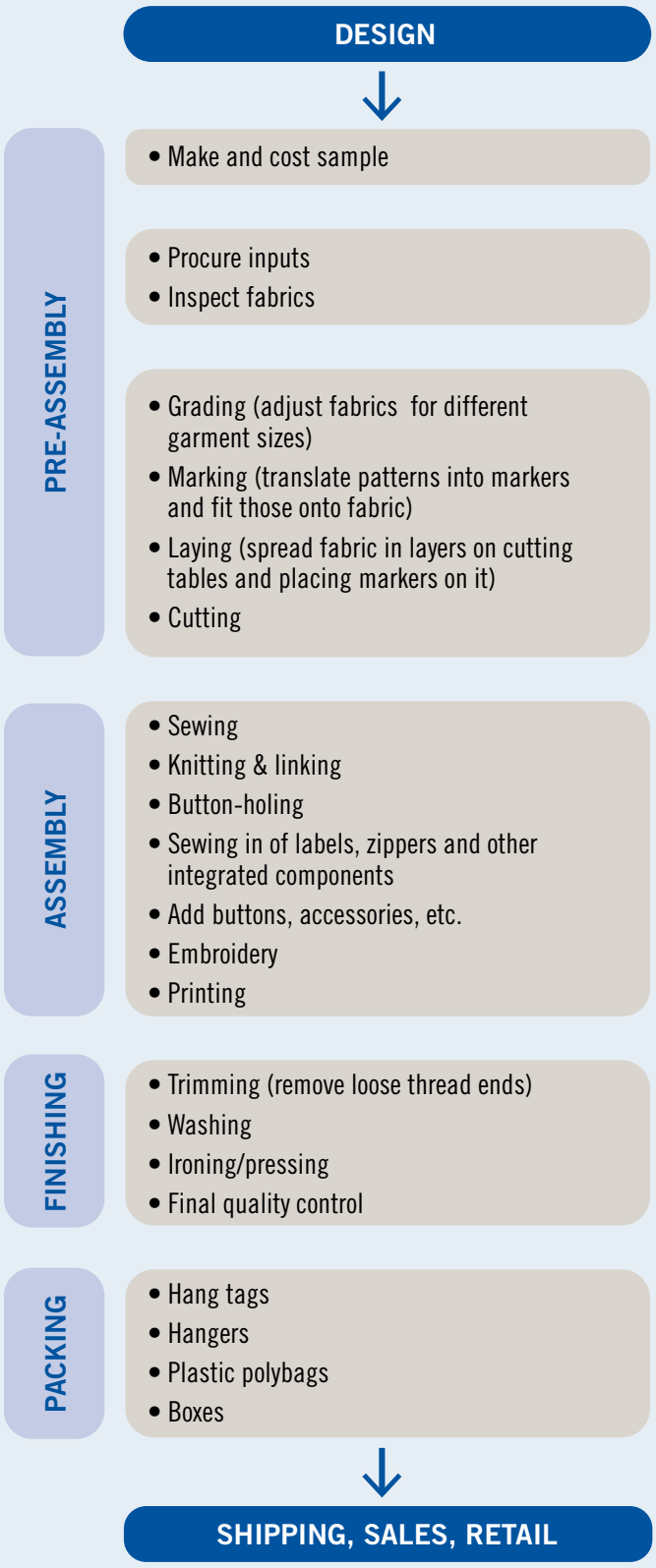
65. ETI (2016)
66. For a detailed list of suppliers, see http://sustainability.hm.com/en/sustainability/downloads-resources/resources/supplier-list.html
67. ODI (2004)

of manufacturing and logistics, buying agents tend to be relatively large, and have expertise in garment production. Examples of agents include Li & Fung from Hong Kong, South Island from Malaysia and Mitsubishi from Japan. Some agents have their own brand and retail outlets such as in E-land in South Korea[68]. Since agents occupy a position between producers and buyers, they can exercise a degree of governance over other segments in the chain, through selection, inspection and capacity building of factories[69].

Factories manufacture garments by assembling textile and trim inputs into a finished product ready for export and retail. **Figure 6** sets out the simplified stages of the garment production process[70]. Factories may use **subcontractors** to fulfil all or part of the order. Part-process subcontractors provide services such as printing and embroidery (part of assembly) and washing (part of finishing), which often require specialised staff and equipment.

Garment factories, in turn, source their materials from **component suppliers** such as textiles (fabric and yarn) producers and accessories manufacturers. These 'suppliers of suppliers' can often be part of a vertically linked supply chain – where spinning, weaving and dyeing factories are located nearby clothing factories. Bangladesh and Vietnam have invested heavily in building such backward linkages, to the extent that Bangladesh is now capable of producing approximately two-thirds of its fabric needs, which are mainly cotton[71]. Garment producing countries without a raw material base, or that have neither the capacity nor the incentive to invest in upstream textile plants, which are energy and capital-intensive, rely on imports. China, the European Union

Figure 6:
Simplified garment production process based on ODI, 2004)



68. Another category of intermediary is licensees, who are licensed to produce a specific branded product line for a specific customer. They organise their own supply chain.
69. ODI (2004)
70. Adapted from 2004
71. World Bank (2016), p.56

and India are the top three exporters of textiles, and together account for almost two-thirds of world exports[72]. The Republic of Korea, Chinese Taipei Hong Kong and Pakistan also have significant textile exports.

Finally, **supporting actors** shape the enabling environment for garment production by providing an array of business development services and value chain governance functions. These can be national governments, non-governmental organisations, associations or representative membership organisations. In recent years, given the level of attention in the sector on working conditions and compliance, an array of multi-stakeholder initiatives has been set up. **Table 6**, below, outlines some of the most prominent and active initiatives across the region. These stakeholder schemes often seek to partner with buyers to provide an overall assessment of factory compliance to improve working conditions, while paying particular attention to workers' rights, health and safety, and environmental impacts.

Table 6:
Multi-stakeholder initiatives active in Asia's garment supply chain (source: ILO 2017 and own research)

Name	Current scope of work
IndustriALL Global Union	Signed global framework agreements with Tchibo, H&M, Inditex and Mizuno for collective bargaining on wages, social benefits and working hours in their companies and across the industry
IDH Sustainable Trade Programme	Multi-donor initiative that seeks to align standards and prove the business case for social and environmental responsibility in apparel manufacturing. Partners with the Sustainable Apparel Coalition. Active in China, Vietnam and Pakistan.
Better Cotton Initiative	Promotes better standards in cotton farming and practices across 24 countries. The initiative now represents around 12% of global cotton production worldwide. Partner retailers include H&M, Gap, IKEA, and Levi Strauss.
Better Work	Partnership between the ILO and IFC bringing together governments, global brands, factory owners, and unions and workers to improve working conditions in the garment industry and make the sector more competitive. Active in Bangladesh, Cambodia, Indonesia and Vietnam.
Clean Clothes Campaign	An alliance bringing together trade unions and NGOs to educate and mobilise consumers, lobby companies and governments, and offer direct solidarity support to workers on rights and working conditions.
Ethical Trading Initiative	Brings together companies, trade unions and NGOs to promote respect for workers' rights, with a particular focus on living wages and working conditions in the garment sector. Partners with the ILO's SCORE programme in China on in-factory improvement training.
International Apparel Federation	International trade association consisting of apparel associations from more than 40 countries representing over 150,000 companies that provide products and services to the apparel industry.
Sedex	Helps member companies simplify and share responsible sourcing data, with a range of platforms designed specifically for buyers and suppliers.

72. WTO World Trade Report 2016

Name	Current scope of work
Sustainable Apparel Coalition	Forum for collective action in the garment industry, focused primarily on standardisation: both for auditing labour conditions and social impact, and supply chain measurement through the Higg Index, which creates a common language and helps factories formulate a program for continuous improvement.
Action, Collaboration, Transformation (ACT) initiative	First global framework on living wages in the garment sector that brings together global brands and retailers and trade unions to improve wages in the industry by establishing industry collective bargaining in key garment and textile sourcing countries, supported by world class manufacturing standards and responsible purchasing practices.
Core Labour Standards Plus (CLS+)	A regional initiative of the Friedrich-Ebert-Stiftung (FES) and partners in Asia that advocates to actively enforce binding and enforceable labour and social standards, guarding against inequality and in support of a stronger role for workers along supply chains – including in garments.
Fair Labor Association (FLA)	Represents a collaborative effort of socially responsible companies, colleges and universities, and civil society organizations. FLA holds participating companies accountable for monitoring 100% of their own supply chains to ensure that they meet FLA labour standards. In addition, FLA conducts independent assessments of a random sample of companies' supplier factories.
OECD Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector	Comprehensive guidance for multinational enterprises, developed through a multi-stakeholder process to support a common understanding of due diligence and responsible supply chain management in the sector.
Better Buying	A new dialogue and rating platform that is being created to highlight areas for improved purchasing practices. Created by the University of Delaware with technical support from the Fair Factories Clearinghouse.
Fair Wear Foundation	Multi-stakeholder initiative working with brands, factories, trade unions, NGOs and sometimes governments to verify and improve workplace conditions in 11 production countries in Asia, Europe and Africa
Social & Labor Convergence Project	Initiative led by manufacturers, brands, retailers, industry groups, (inter)governmental organizations, service providers and civil society organizations, to develop a common assessment framework and data collection system, which aims to dramatically increase industry efficiency and reduce audit-related costs.

2.2 VALUE ADDITION

Beyond the physical transformation of raw materials to finished article, a series of 'intangible' activities adds economic value to clothing products[73]. **Figure 7** overlays the four main value-adding activities onto the supply chain: product development and design, textile sourcing, logistics and distribution, and branding and marketing.

These activities are largely controlled by the buyers, since they require higher capacity, extensive global networks and have high barriers to entry. However, to varying degrees value addition is carried out by garment factories themselves, depending on the model of supply chain organisation. There are four main categories of production, which are set out in **Table 7**.

Garment factories can therefore have a range of functional responsibilities, from direct production to input sourcing, logistics and distribution – which reflect different levels of involvement in value addition. Global apparel buyers often prefer to work with suppliers who have OEM capabilities, so that they can outsource not only assembly but also wider supply chain management activities[74].

Full package production fundamentally changes the relationship between buyer and supplier, and the complexity of the chain. An OEM arrangement does not necessarily mean that the manufacturer keeps the actual garment production in-house: They, in turn, may subcontract out the labour-intensive activities such as cut, make and trim to a network of second-tier supplier factories.

When manufacturers move up the value chain from assembly to own brand, this tends to mirror a country's industrial development from

Figure 7:
Value added activities mapped on the garment supply chain (source, Sewing Success and UNIDO)

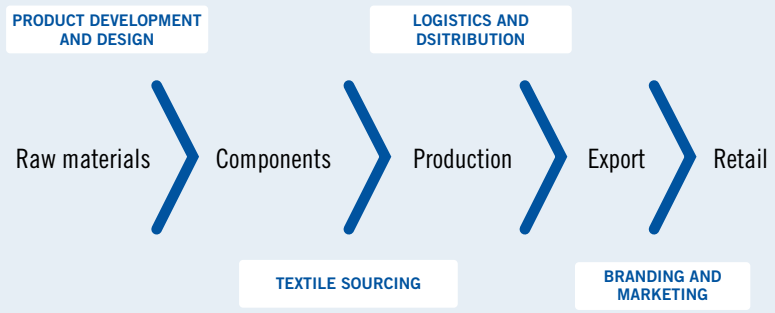


Table 7:
Categories of garment production (source, World Bank 2012 and 2016 and UNIDO, 2003)

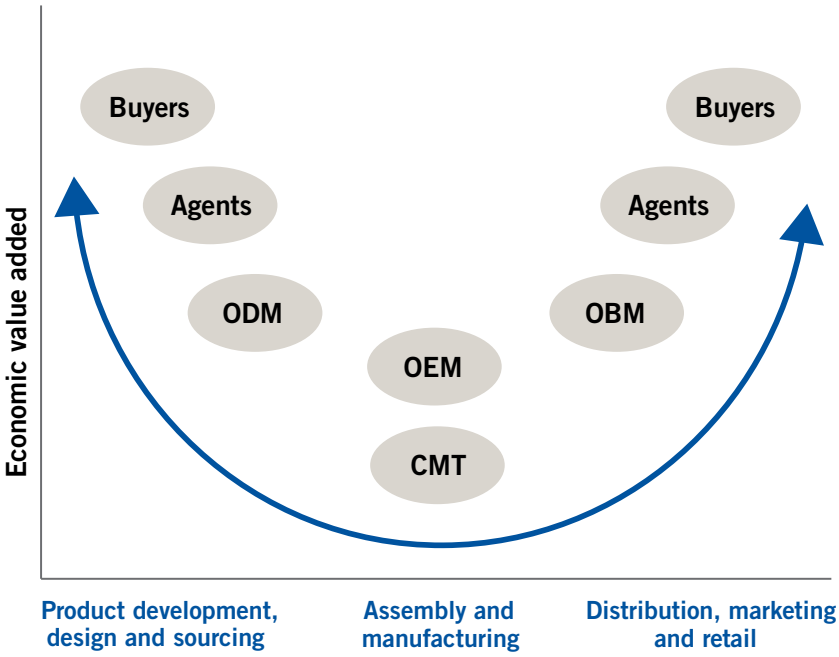
Cut-make-trim (CMT)
The factory is responsible for cutting the fabric, and making and trimming the garments. The buyer will provide product specifications and the inputs (fabric). Factories are often paid a processing fee rather than a price for the product. Most common in export processing zones (EPZs)
Also known as: Assembly
Original equipment manufacturing (OEM)
The manufacturer purchases (or produces) the textile inputs and provides production services, finishing and packaging for delivery to the retail outlet. The buyer provides the design and often specifies the textile suppliers.
Also known as: Fee on board (FOB) or full package
Original design manufacturing (ODM)
The manufacturer is also involved in the design and product development process, including approving the samples and the selection, purchase and production of required materials.
Original brand manufacturing (OBM)
The manufacturer brands and markets the final products. This can be on a contract basis on behalf of a buyer, or mark the transition from apparel supplier to lead firm, where the manufacturer has their own brand – typically in domestic or regional markets.

73. See World Bank (2012)
74. World Bank (2016), p.55

product producer to a service hub that invests and coordinates regional or global networks. The Republic of Korea, for example, was a dominant garment exporter in the 1970s and 1980s, but as wages rose and other sectors gained in importance, assembly was offshored and manufacturers shifted from carrying out to coordinating full-package production, often as intermediaries[75]. Hong Kong has followed a similar trajectory. Despite significant differences between companies, in Asia the current exporters with majority CMT production are Cambodia and Myanmar. Bangladesh, Indonesia, Vietnam and Pakistan have OEM capabilities, and China and Sri Lanka – and to a certain extent India – have OEM and are pushing into ODM.

The garment value chain, therefore, reflects the archetypal 'smiling curve' of Stan Shih – set out in **Figure 8** – where the greatest economic value can be found at the edges, in conception and marketing, rather than in the actual production. Lead firms have retained higher value added portions of the value chain, recognising that the "true value in making something is no longer in making it"[76].

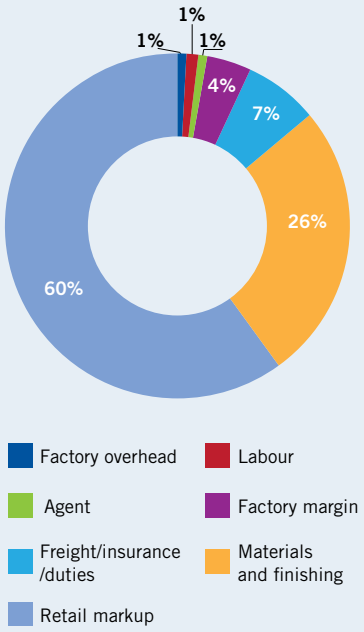
Figure 8:
The relative position of market actors on the garment sector 'smiling curve' (source, Cho and Chi, 2017 and own research)



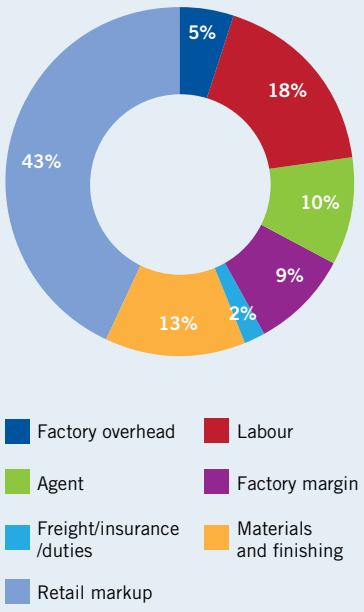
75. UNIDO (2003)
76. Bloomberg Businessweek (2017)

Figure 9:
Retail cost breakdown based on real-life cases in Bangladesh and India (Source: Ecouterre,2013 and Kick-starter, 2017)

Bangladesh: Budget T-shirt



India: Niche childrenswear



2.3 VALUE CAPTURE

Accurate, comparable and region-wide financial data is not readily available. Nonetheless, it is possible to obtain a general picture of the relative value capture by different actors in the garment supply chain.

Figure 9 shows the retail cost breakdown for two very different types of garment, a generic $14 dollar t-shirt manufactured in Bangladesh and sold in Canada, and an artisanal $70 children's dress manufactured in India and sold in the USA.

Mark-ups – just like retail prices – vary widely depending on type of product and end market location. According to the Wall Street Journal, typical mark-ups on designer fashion labels range from 55 to 62% in the USA, but can be as high as 100 to 350%, with some items such as jeans frequently found at the upper end of the range[77].

Retailers use a pricing technique known as keystone mark-up, which multiplies the cost basis of an item by a factor two. The $14 budget t-shirt made in Bangladesh, for example, cost $5.67 to actually make. Generally speaking, keystone can be applied twice: once as brands sell to retailers, and again as retailers sell to consumers – but this will depend on the type of sales channel, as set out in section 3.1, and whether they operate retail outlets that incur 'bricks and mortar' rental and staff costs[78].

It is important not to mistake mark-ups for margins. **Table 8** sets out key financial metrics for lead firms. While initial mark-ups may be high, gross margins are usually lower due to the cost of markdowns (price reductions to move merchandise unsold at full price) and stockouts (lost sales due to sellouts of popular styles) and unsold stock[79]. After taking into account overheads, operating costs, interest and taxes, final net profit for garment retailers is in the low single digits[80]. This, however, can vary greatly with some fast fashion companies posting markedly better figures. Zara, for instance, is estimated to capture a consistent 16% return due to supply chain flexibility and shorter lead times.

Intermediary buyers apply a range of mark-ups to reflect their coordination and aggregation services. In the example in **Figure 9**, agent fees are 3% of the cost of producing a garment in Bangladesh, and 19% in India. Industry insiders verify that trading companies do routinely take a margin of up to 20%[81]. Some intermediaries also own a stake in their supplier factories, although this is thought to be a minority.

Garment manufacturers operate with thin margins and a small share of the retail price. As a rule of thumb, the costs of garment pro-

Table 8:
Key financial ratios for retailers (source: Sourcing Journal, 2015)

Ratio	Definition	Metric (%)
Mark-up	Increase in purchase price to cover profit and cost of doing business	60
Gross margin	Revenues minus costs of goods sold	40
Net profit/income	Revenues minus all costs of doing business	Generally <10

77. WiseBread (2010)
78. Forbes (2012)
79. Forbes (2015)
80. Sourcing Journal (2015)
81. Quality Inspection (2017)

duction are two-thirds raw materials and inputs, one fifth labour, and the remainder rent and utilities[82]. Net profits vary widely, but according to a recent survey in Bangladesh, a third of managers claimed their profit rate had been between 0 and 2%, half claimed between 2 and 5% and most of the remaining managers between 5 and 7%[83]. To improve commercial performance, factories have been forced to lower their prices to get business, or rush production to make a small profit. As the majority of costs incurred in garment production are direct costs like raw materials, managers control the variable costs that they can – often leading to unskilled (cheap) labour, long hours and minimal quality control[84]. This is particularly the case for CMT suppliers and subcontractors.

But as the next section shows, low costs alone are no longer a sufficient advantage in apparel export. In an increasingly crowded marketplace, many manufacturers have concluded that the only option is to upgrade – either developing backward linkages into the textile sector for greater control and shorter delivery times, or forward linkages to be entrusted with larger portions of the value chain and increased sell-side responsibilities, which may include form development of styles to final delivery in the buyers' stores[85].

2.4 COMPARATIVE ADVANTAGES BY COUNTRY

There is intense competition between garment manufacturers firms as they vie for a piece of the export market. Successful manufacturers, according to the World Bank, will be "those who can introduce new processes, work organisation and technology and can respond to fast changing apparel industry remands – and not just those who offer low costs"[86].

Buyers are looking for a variety of products at competitive prices, at a consistent quality, with reliable delivery, sufficient lead times and the capability to offer full package; in short, buyers want a broad range of both manufacturing and non-manufacturing capabilities. While in

Table 9:
Buyers' perspective of competitive comparison between countries (source: World Bank, 2016)[87]

	Sri Lanka	India	Pakistan	Bangladesh	China	Myanmar	Vietnam	Cambodia	Indonesia
Cost	*	**	***	***	*	**	*	***	**
Speed	**	*	*	*	***	*	***	**	***
Compliance	***	*	*	*	***	*	***	**	***
Quality	***	*	*	**	***	**	***	**	**

***least competitive, ***most competitive**

82. World Bank (2016)
83. According to Frenkel et al, 2017. 31% of managers claimed their profit rate had been between 0 and 2%, 47% between 2 and 5% and most of the remaining 22% between 5 and 7%
84. Quality Inspection (2017b)
85. The Financial Express (2015)
86. World Bank (2016)
87. This does not include an assessment of nonmanufacturing capabilities. If OEM production, then this would also involve the ability to source own inputs, and if ODM, then product development and design are important comparative advantages. For all manufacturers, adequate distribution and inventory capacities are critical.

theory there are many important objective differences within countries and across firms, including specialisation by clothing product, in reality, market access is shaped by buyers' perceptions. **Table 9** sets out how buyers rank countries against key criteria of cost, quality, lead time and compliance.

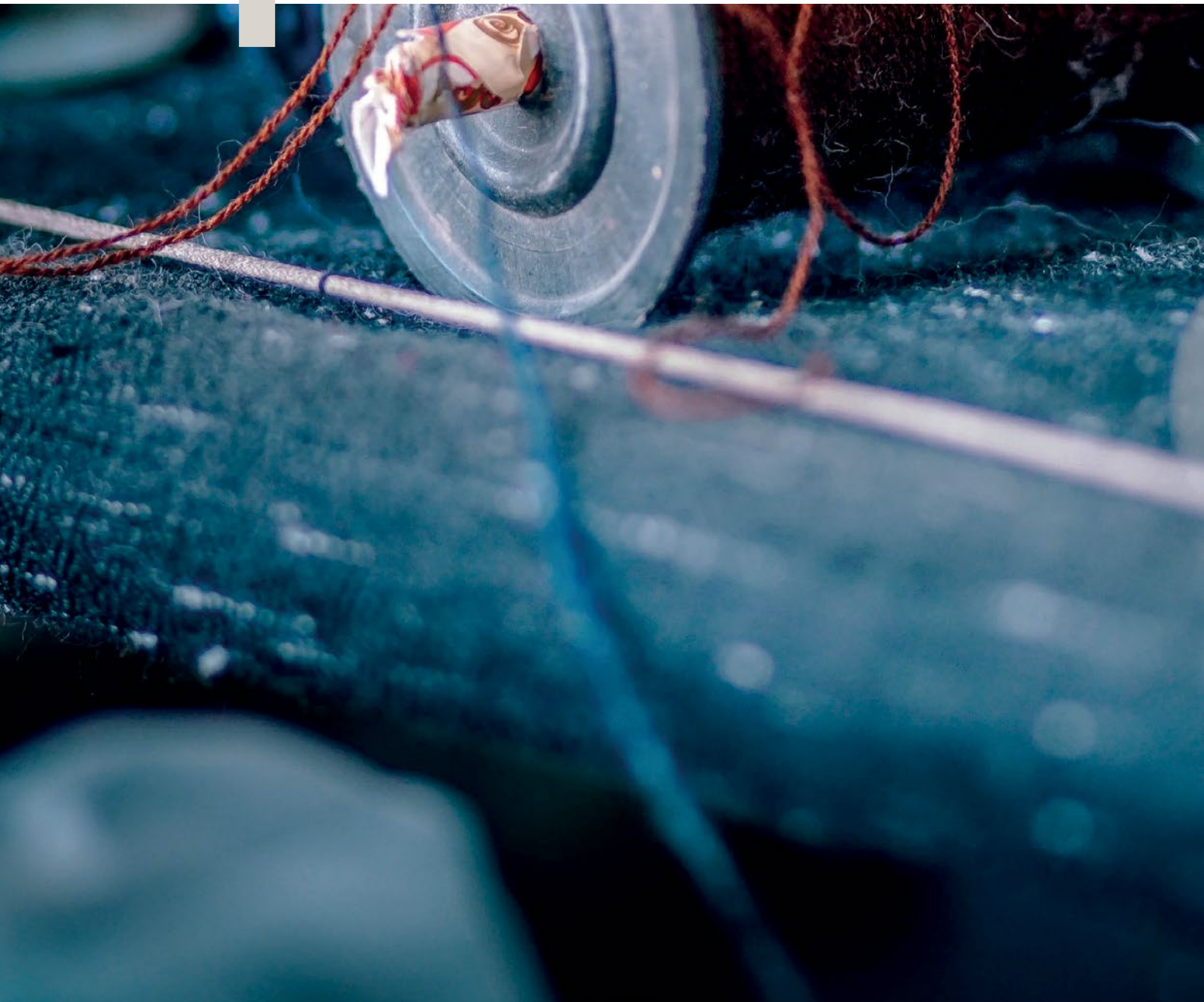
Cost represents the fee on board price, which – as we have seen – is largely determined by access to textile inputs and can account for approximately two-thirds of the costs of production. Quality is influenced by the raw materials, the skill level of the sewing machine operator and the quality control team. Lead times reflect productivity and efficiency of firm level processes, and how well the supply chain segment is organised – including transportation and infrastructure. Social compliance in recent years has become an increasingly important criterion for image-conscious brands. **Table 10** summarises key comparative advantages and disadvantages by country.

Table 10:
Summary headline comparative advantages and disadvantages by country (source: World Bank 2016, and own research)[88]

Bangladesh	Low wages, capable of large bulk orders, low and mid-market specialisation. Scores low in compliance, quality, and reliability. Self-sufficient for majority (2/3rds) of fabric sourcing needs.
China	Produces a vast range of goods and services, high levels of productivity in short lead times, ability to deliver on non-cost factors.
Cambodia	Surging wages threaten FOB prices. Scores low in compliance, with low unit values, lacking in product diversity and mid-range quality.
India	Scattered supply chain made up of small informal producers, with low product diversity. Full capabilities for cotton production but lacking in synthetic fibres. No trim suppliers, instead relying on Hong Kong
Pakistan	Competitive prices but highly concentrated in cotton and with a lack of product diversity. Low reliability and political instability.
Sri Lanka	Higher priced, higher value niche products. Imports almost all textile inputs from elsewhere in Asia, scores well on social compliance.
Vietnam	Ability to deliver on non-cost factors – and has recorded strong growth despite higher unit values. Invested heavily in backward linkages
Indonesia	Low to moderate product value, has a positive image with buyers, substantial textile plants and a good skills base.

88. It should be noted that garment production can be highly specialised even within the different regions and districts of a given country, but such local/sub-national dynamics are beyond the scope of what is feasible to cover in this overview.

PART 2
Constraints analysis



PART 2 Constraints analysis

3 COUNTRY SNAPSHOTS

This section focuses on the drivers of poor working conditions in Asia's garment sector. It is informed by research undertaken in Vietnam and Indonesia[89]. A 'market systems' approach was used as a lens to view the systems of regulation, information and delivery that shape incentives for businesses to uphold labour rights, and the private and public market failures which could be addressed through regional action[90].

It asks: W*hat* are the working conditions deficits; *where* are they found in the supply chain; and *why* do they persist? It starts by describing how workers work and how businesses perform, and then goes on to analyse the underlying causes of workplace abuses beyond the factory floor, which are deeply bound up with global supply chain dynamics[91].

A systems approach seeks to grow markets that operate efficiently for everyone, but especially for disadvantaged workers[92]. A market systems analysis identifies constraints at the intersection of both economic *and* social upgrading. There is no guarantee that if companies move to higher value chain roles and improve their commercial performance, improved social outcomes – including better wages and working conditions – will follow. On the other hand, just securing better wages and working conditions, which often require firms to invest in people, processes and equipment, without – or at the expense of – business growth is unlikely to be aligned with commercial incentives, and therefore would not be sustainable. A market systems approach looks for 'win-win' ways for more inclusive and equitable growth.

89. These two countries were selected by the Industrial Relations Study Team. They are a purposive sample and not representative of regional dynamics. However, the constraints analysis draws in experience from other countries to attempt to build up a generalizable picture of the garment sector across Asia.

90. This is not a comprehensive analysis of all constraints. Rather, the country specific analysis only considers national level challenges that have potential to be addressed by improved regional collaboration and strengthened capacity of regional actors.

91. As noted by Tufts (2016)

92. See the Operational Guide to the Making Markets Work for the Poor Approach

3.1 VIETNAM

Vietnam, a relative latecomer to garment exporting, has seen rapid growth since the early 2000s, primarily driven by buyers from the United States. The country has a large working age population and developed its export apparel sector around high-volume, low-margin production of basic items. However, labour costs are now rising faster than productivity and faces stiff competition from countries such as Bangladesh. **Figure 10** sets out the current destinations of Vietnam's apparel exports.

Vietnam initiated a number of important labour reforms in order to qualify for the Trans-Pacific Partnership (TPP) and attracted considerable amounts of investment in anticipation of the TPP. While the country has also invested heavily in developing backward linkages with textile spinning, weaving and dyeing factories, over 70% of the materials used in producing export-grade garments are still imported, mainly from China[93].

Figure 11 lists some of the largest brands and retailers sourcing from Vietnam, which include Nike, Adidas, Levis, Gap, Mango and Inditex. These companies enter into direct relationships for full package (FOB) production either with 1st tier garment manufacturers (based overseas or in Vietnam), or buying agents (always headquartered overseas, but often with local offices). Buying agents then contract manufacturers in Vietnam for CMT production, often providing them with (imported) raw materials. In many cases the FOB manufacturers subcontract out a part of production to smaller suppliers, either due to specialisations or to meet rush orders.

Table 11:
Key facts and figures about Vietnam (source: World Bank Country Profile, Friedrich-Ebert-Stiftung, 2017, and ERC, 2017)

Population
93 million (2016)
GDP per capita
2,185 USD
Human Development Index Rank
115 (medium)
Labour force
55.9 million
Poverty rate
13.5% (2014)[93]
Global garments export rank
4th
Total export value garments
$22.81 billion
Major garment producing regions
Hai Phong, Da Nang, Ho Chi Minh City, Binh Duong, Dong Nai, Long An

Actors use a variety of different methods to classify supplier tiers, which are relative to where they sit in the chain. **Figure 12** sets out a common framework of three different tiers from cotton farms to finished goods. This includes both direct sourcing where manufactures contract with brands for FOB production, and indirect sourcing through agents.

There are an estimated 6,000 garment manufacturing companies, of which around 2,500 produce for export. Almost 70% of firms are garment manufacturers and their subcontractors, and the remainder are component producers: 8% yarn spinning, 17% weaving, 4% dyeing and 3% trim[95].

93. Vietnam Textile and Apparel Association: Fabric imports come from China (50%), South Korea (18%) and Taiwan (15%)
94. National poverty line
95. FES Survey of Garment and Footwear Enterprises (2015)

Figure 10:
Destination of Vietnam's apparel exports, by value (Friedrich-Ebert-Stiftung 2017, based on Vietnam customs office, 2015)

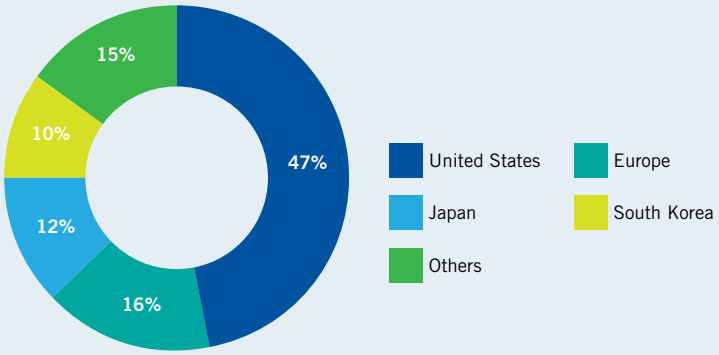


Figure 11:
Biggest buyers sourcing in Vietnam, by total number of suppliers (interviews with brands, August 2017

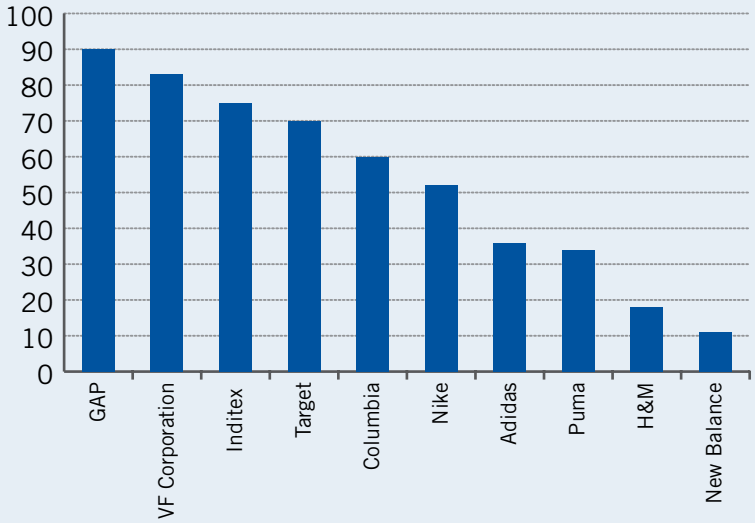


Figure 13 shows the ownership of factories involved in the supply chain, and the relative contribution of foreign direct investment and the domestic sector to Vietnam's total export value in 2015. While almost two-thirds of companies are domestic private companies, the foreign-owned firms dominate the first tier of production – hence the value-added activities[96]. Across all sectors, Foreign Direct Invested (FDI) enterprises contributed 63% of Vietnam's total export value in 2015,

96. Foreign firms account for 79% in fact of Better Work Vietnam's participating factories

but the share of FDI value is even higher in garments at 76.6%[97]. Domestic firms make up approximately three-quarters (75%) of 2nd tier suppliers and subcontractors[98].

Most (65%) garment manufacturers produce on CMT contracts. A further 25% produce full service, 9% ODM and 1% OBM. In the first tier of production, the number of employees is usually in the range of 500-1,500, but the average export garment factory size in Vietnam is just 255 workers[99].

Figure 12:
Supplier tier framework used by major brands (J. Safra Sarasin, 2014, and own research)

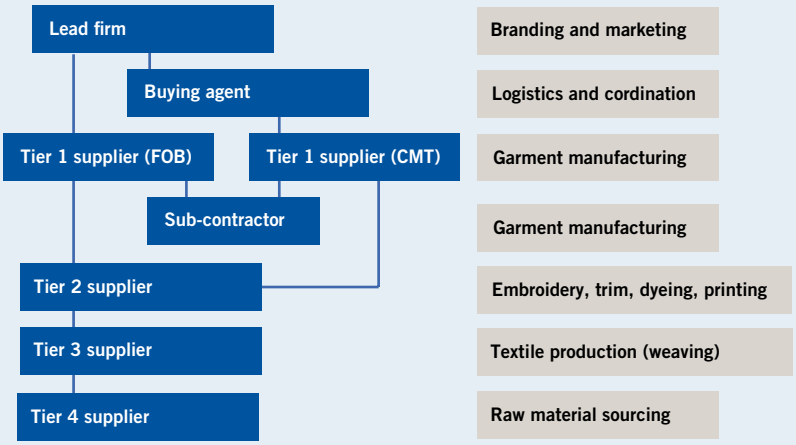
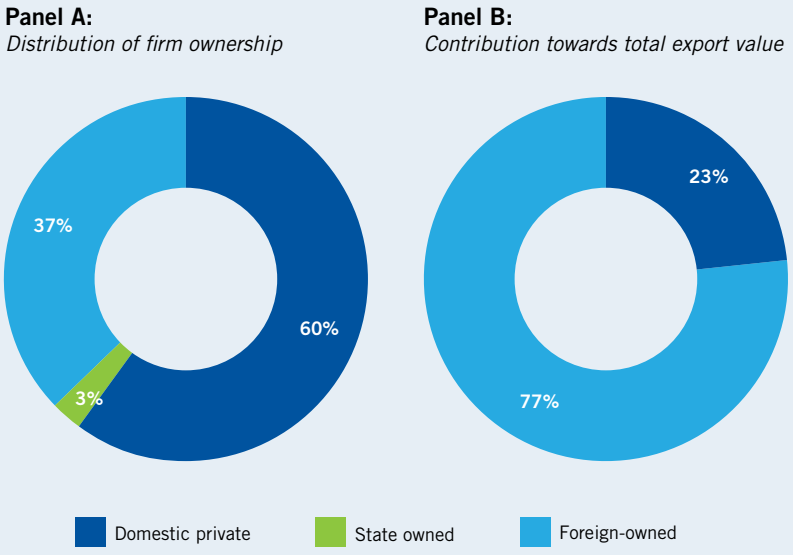


Figure 13:
Distribution of firm ownership and contribution towards total export value (2015) (Source: Friedrich-Ebert-Stiftung 2017)



97. Friedrich-Ebert-Stiftung (2017). Some factories – mostly foreign-invested ones – are located in Industrial Zones (IZs). These IZs often have waste water treatment facilities and provide a range of on-site services such as fire-fighters and clinics.
98. ERC (2017)
99. Better Work (2013)

Table 12:
Key facts and figures about Vietnam (source: World Bank data, UNDP, CLS WTO, BWI Industrial Profile, and own research)

Population
261 million (2016)
GDP per capita
3,570 USD (2016)
Human Development Index Rank
113 (medium)
Labour force
127.4 million (2016)
Poverty rate
11.3% (2014)[100]
Global garments export rank
8th (2015)
Total export value garments
$7 billion
Major garment producing regions
West and Central Java, Greater Jakarta and Batam

3.2 INDONESIA

Indonesia's garment sector was born in the 1970s in an expanding domestic market amidst export-oriented trade policies. By the 1980s, the rapid growth of the industry led to significant foreign exchange earnings and job creation, particularly for women and low-skilled workers. With the expiry of the MFA, however, the country began to face heavy competition from other producers in the region, particularly China and Vietnam.

Despite its earlier reputation for low labour costs, the minimum wage made significant jumps starting in the 1990s. In 1996 it rose by 30%,[101] rising again by 30-40% in 2002, and more than doubling in certain regions between 2012 and 2017[102]. Buyer prices, however, remained constant. Many garment manufacturers therefore opt to save on production costs by moving to regions like Central Java, where the minimum wage is lower. The earlier large jumps in the minimum wage also appear to have accelerated an employment shift from smaller firms to larger factories[103].

There are over 170 foreign brands in Indonesia's garment and textile sector[104]. Among the biggest buyers are Nike, GAP, Adidas, Walmart, H&M, PVH Corp, American Eagle, M&S, and New Balance.

For the most part, brands and buyers work directly with full service suppliers, particularly larger ones capable of handling large orders, but tend to go through agents when sourcing from factories performing primarily CMT functions. However, this is not always the case, as many factories in Indonesia have adapted to provide mixed services – full service or CMT only, through an agent or directly to the lead firm – depend-

100. At national line
101. Kian Wie Thee (2009)
102. Wageindicator.org (2016) and Trading Economics (2017)
103. Rama (1999)
104. Clean Clothes Campaign (2015)

ing on the needs of the buyer. While local firms or 'vendors' tend to be one and the same as the factories, foreign-owned firms own several factories operating under a single vendor. In these cases, the vendor coordinates production between its factories and is the point of contact for either a buyer or agent.

As of 2013, there were about 3,000 garment factories in Indonesia.[105] The sector employs approximately 2.2 million people, with over 516,000 working in large and medium sized firms that are largely linked to the export market.[106] The Ministry of Industry estimated that roughly 60% of enterprises are CMT factories linked to the export market.[107] Workers are primarily young women.[108]

The exact division of firm ownership is difficult to assess. The majority of firms are registered as Indonesian companies and are managed and run by Indonesians, but many receive heavy foreign investment, with very little share actually going to Indonesia.[109] **Figure 15** below shows the division of ownership of Better Work factories, with a majority owned by South Korea. However, while specific figures were not obtainable for all factories in-country (including non-exporting garment manufacturers, subcontractors, and component producers), interviews and past studies suggest that Indonesian ownership actually represents a greater piece of the pie.

Figure 14:
Destination of Indonesia's apparel exports, by value (Textile Outlook International (2015))

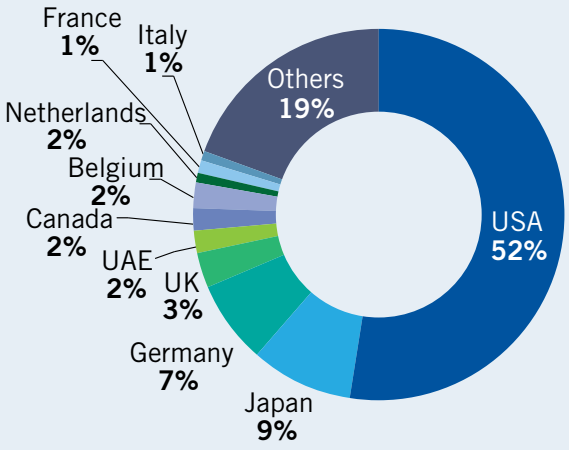
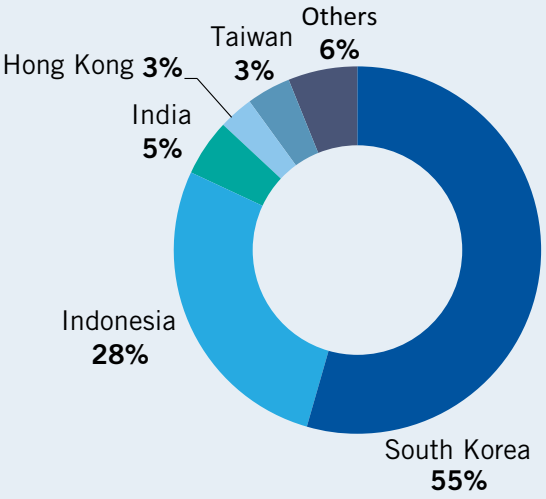


Figure 15:
Distribution of foreign ownership (Better Work data from surveys and factory registration 2016)



105. Textile Outlook International (2016)
106. Better Work Indonesia (2015), Synthesis Report
107. Interview with the Ministry of Industry (2017)
108. Better Work (n.d.), Guidelines for Employers
109. Interview with KBN Cakung.

PART 2 Constraints analysis

4 WORKING CONDITIONS

There is a wealth of information on working conditions in garment manufacturers based on Better Work's comprehensive impact assessments and audits. In **Vietnam**, the highest compliance with national labour law and international standards was found in the areas of child labour, forced labour and discrimination. Factories are noncompliant in the areas of freedom of association and collective bargaining, compensation, contracts and human resources – although some progress had been made since early audits. The greatest problems were found in occupational safety and health and working time, where the majority of firms were noncompliant. In **Indonesia**, the highest compliance with national labour law and international standards was also found in child labour and forced labour, but, in addition, it performed significantly better in the categories of freedom of association and collective bargaining, albeit with room for improvement, as non-compliance with collective bargaining still remains high at 24% of firms. **Indonesia** was found to be generally compliant concerning discrimination as well, with the exception of a rule that 1% of the workforce be workers with disabilities. Where Indonesian firms struggled the most was in occupational safety and health, followed by compensation, contracts and human resources. Concerning working time, Indonesian firms did somewhat better than those in Vietnam when it came to overtime regulations, but significantly worse at granting leave.[110]

However, these data largely cover 1st tier firms, and the problems are thought to be more severe further down the supply chain[111]. Subcontractors and 2nd tier suppliers are subject to less oversight and, in the case of component suppliers, the risks of exposure to dangerous substances is far higher than in 1st tier suppliers. Fabric manufacture involves significant use of chemicals. During washing, practices such as sandblasting denim are

110. Better Work Indonesia (2015), Synthesis Report

111. SOMO (2015)

associated with occupational health concerns[112]. Smaller companies often produce both for domestic and export markets, have less bargaining power with buyers, and are subject to even greater pressure on prices and delivery times[113]. In interviews with 1st tier factories in **Vietnam**, they stated it was a struggle to find quality subcontractors (for washing and printing) that could also meet their compliance requirements. Interviews with 1st tier suppliers in **Indonesia** and **Vietnam** revealed that main factories often needed to train subcontractors themselves in order to get them up to par in terms of social compliance.

Persistent violations of basic working conditions can result in industrial action. In **Vietnam**, the garment industry is the most strike-hit sector in the country, accounting for 40% of all national strikes. According to a recent report commissioned by the ILO, two-thirds of these strikes occurred in domestic garment companies, which in turn make up the bulk of lower-tier suppliers[114].

4.1 WAGES

Although factory workers are often paid in line with (or slightly above) minimum wages, this compensation often falls short of living wage benchmarks. Salaries are increasing – but not enough, as in most cases wage increases are lower than inflation and cost of living rises. In a competitive environment where buyers exert downwards pressure on unit prices, rising labour costs put garment manufacturers in a difficult position. In **Vietnam**, for example, a recent study found that prices for CMT production have not increased in the past five years but the minimum wage in Vietnam has increased at a rate of 12.3% per year over the last decade[115]. Similarly in **Indonesia**, wages have increased at an average of 11-13% per year,[116] [117] and with unchanging CMT prices squeezing margins, firms are relocating from higher minimum wage regions, such as Jakarta, to lower ones, like provinces in Central Java.[118]

4.2 WORKING TIME

Excessive working time is a major issue – with 80% of clothing manufacturers in **Vietnam** and 88% in **Indonesia** exceeding daily limits on overtime hours worked[119] [120]. Overtime is often necessary to meet rush orders, and accepted by workers as a strategy to boost their take-home pay. According to a study commissioned by the Friedrich-Ebert-Stiftung (2017), "excessive overtime is [also] one of the biggest problems found during Fair Wear Foundation audits of suppliers to European garment brands in Vietnam. Particularly during peak seasons, working hours are found structurally between 65 and 75 hours per week." In systematically non-compliant factories there are often two parallel records

112. RobecoSAM (2016)
113. As noted by Friedrich-Ebert-Stiftung (2017), "The 2012 ILO-MOLISA Survey on Child Labour found that there were 47,343 workers under 18 years old employed in garment workshops, mostly household businesses…most of these workshops are unregistered and manufacture low-cost garment products for the local markets"
114. ERC (2017)
115. Friedrich-Ebert-Stiftung (2017). Three of the seven suppliers the study spoke to admitted that the CMT prices have even decreased by 5-10%/year over the past few years. Taking into account compulsory social contributors together with overtime and bonus pay, when the minimum wage increases by 1 Dong, the supplier has to pay an extra 1.48 Dong per worker.
116. Trading Economics (2017)
117. ILOSTAT (2017)
118. Allen and Kyloh (2016)
119. Tufts (2016). Overtime as measured in 3rd and 4th audits. The national legal limit is 200 overtime hours per year (or 300 hours in special cases)
120. Better Work Indonesia (2015). Labour reforms in Indonesia

of work hours – one for internal use and a different one for auditors[121].

4.3 SAFETY AND HEALTH

Better Work audits[122] in **Vietnam** recorded the highest non-compliance in occupational safety and health (OSH), with more than 70% of manufacturers falling short of acceptable standards across the vast majority (6 out of 8) compliance points. In **Indonesia,** the same is true for more than 75% of manufacturers. On the factory floor, the most common persistent problems are:[123]

- The need to offer comprehensive first aid training and ensure the use of personal protective equipment (PPE) and first aid materials at all times
- Inadequate storage of chemicals and non-provision of emergency eye-washing facilities
- Not providing a sufficient numbers of lockers, changing rooms, showers, and adequate accessible toilets for employees
- Dangerously exposed electrical wires and machinery
- Blocked or not clearly marked emergency exits
- Non-assurance of building safety
- A lack of proper guards installed on machinery
- Non-compliance with ergonomics requirements
- A lack of a fire detection equipment, fire-fighting equipment, and a trained fire management team
- The need for an adequate eating area

For workers, poor safety and health can translate into headaches, followed by backache, dizziness and fatigue. Workers also complain about factory temperatures, which are often cited as too hot with inadequate ventilation. Chemical smells and poor quality or unpleasant-tasting drinking water are other common complaints for between 3-10% of workers. In terms of the safety of the building structure itself, in third-cycle Better Work assessments, 100% of surveyed factories in **Indonesia** were still found to be non-compliant with ensuring the building is safe and maintaining legally required permits.[124] While some buyers have requested it, local regulation does not stipulate a specific mechanism or standard for issuing building safety certificates, nor are there clear rules on which institution is responsible.

4.4 GENDER

Reports of gender-based violence and sexual harassment in garment manufacturers vary between countries. In **Vietnam**, 97.6% of workers report no concerns with sexual harassment. Occasional verbal abuse (such as shouting, using vulgar language) was reported by one in 10 workers, though there are no indications this is targeted at female workers any more than male workers[125]. In **Indonesia**, however, the picture looks quite different, where during the first audit, only 15.6% report *no* concerns related to sexual harassment.

In **Vietnam**, while men and women work an equal number of hours (after controlling for age, education, position, promotion history, etc.),

121. Better Work (2013)
122. These figures represent aggregated findings from factories that vary in the length of time they have participated in the Better Work program, so while figures are high, factories that have been in the Better Work program for longer do show clear improvements in occupational safety and health.
123. Better Work Indonesia (2015) Synthesis Report and Better Work (2013)
124. Tufts (2016)
125. Better Work audits and the Tufts (2016) impact assessment

women earn about $5.32 less per week than men[126]. In **Indonesia**, the gender pay gap stands at 16.6%,[127] but in a Better Work study, after controlling for demographic characteristics and job, women in garments were found to earn more or less equal to men[128]. There is also a raft of gender-specific implications resulting from OSH non-compliance: the inadequate provision of changing rooms for female workers, failure to provide adequate accessible toilets or showers, and insufficient lockers for employees' personal belongings. While in many countries the majority of senior management in garment manufacturers are men, the majority of employees are women, meaning that decision-makers often do not take into account the workforce gender composition when making decisions. According to the Friedrich-Ebert-Stiftung (2017), in **Vietnam** female workers account for over 80% of the labour force but the number of toilets for men and women are the same, leaving many female workers unable to access toilets during working hours.

Finally, Better Work audits found inadequate implementation of maternity-related benefits. Half of factories participating in Better Work Vietnam do not settle claims for sick leave and maternity leave within 3 working days[129]. In **Indonesia**, the majority of women reportedly are denied rights to maternity protection, despite it being required by law[130].

126. Tufts (2016)
127. OECD (2014). Achieving stronger growth by promoting a more gender balanced economy
128. Tufts (2016)
129. However, this is a noticeable improvement from early audits, where 94% of factories were non-compliant.
130. Better Work (n.d.). Guidelines for Employers

PART 2 Constraints analysis

5 THE GARMENT MARKET SYSTEM

Bad working conditions are the physical manifestation of a deeper malaise. If excessive hours, low pay and unsafe workplaces are the symptoms, what are their underlying causes? In market systems jargon, the decisions that companies make about how to treat their workers are directly influenced by an array of 'supporting functions', such as access to information, technology and services; along with social norms and standards which constitute the 'rules of the game' shaping acceptable firm behaviour.

A systems approach zooms out to identify the pressing problems in the business ecosystem. Addressing these constraints may look like a long-term and even intractable challenge, but by chipping away at the 'root causes', programmes can achieve a more sustainable impact, which is capable of enduring without the need for continued donor support. Such systemic change requires collective action: Looking beyond just the *capacity* of market actors to pay close attention to the material or purpose-oriented *incentives* driving behaviour, and the organisations that shape attitudes toward risk and reward[132].

> ***"We've all spent too much time tackling the symptoms of workers' rights abuses - be it child labour, forced labour, poor health and safety, or discrimination - and not getting to the root causes of poor standards and abuse."*** [131]

131. ETI (2011)
132. See the Operational Guide to the Making Markets Work for the Poor Approach

Figure 16:
The market system shaping working conditions in garment manufacturers

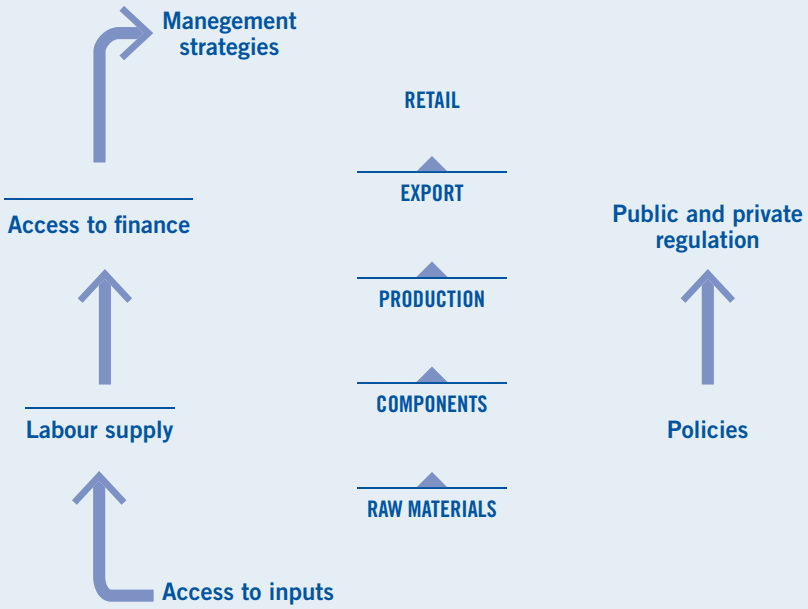


Figure 16 depicts the market system for garment production[133]. The remainder of this section examines the important functions and rules, ending by identifying additional constraints to gender equity[134].

5.1 PUBLIC AND PRIVATE REGULATION

A comprehensive set of international labour standards exists to inform and harmonise national legislation[135]. These standards are designed to ensure a level playing field in the global economy, guarding against 'race to the bottom' practices where governments and employers lower labour standards to give them a greater comparative advantage in international trade.

However aligned national laws are with the international legal framework, many countries struggle to enforce basic labour standards. In the garment industry, in particular, there is also an argument that some governments are not interested in improving conditions for employees as it "would bump up costs for employers and might encourage outsourcing companies to take their business elsewhere"[136]. In the fast-paced global export market, the competitive environment is largely shaped by the relative *absence* of

133. Constraints related to social dialogue are not repeated in this report

134. Context-specific social norms (the rules of behaviour that are considered acceptable in a group or society) are also an important constraint but too complex to be covered in this scan. Such social and cultural factors are therefore important in determining how managers perceive and provide for their workers, and what conditions workers are willing to tolerate. This applies to all actors in the value chain, from buyers to agents to suppliers. Some brands, for example, are known to be stringent in their compliance requirements, while others are not. In Vietnam, the perception is that European buyers are most attuned to working conditions, with North American buyers slightly less so, and Japanese and other Asian brands either unconcerned or just 'going through the motions'. Indeed, many agents from South Korea and Taiwan have offshored production to countries such as Vietnam "precisely because they want to be freed from labour constraints (Better Work, 2013)

135. This includes a comprehensive system of instruments on work and social policy, backed by a supervisory system.

136. J. Safra Sarasin (2014)

government action, hence profitability is determined by pure competition between firms[137].

Even if producer countries had sufficient incentive to enforce labour standards, they often lack the basic capacity to do so. In **Vietnam**, for example, a recent ILO study found that labour inspectorates were overloaded, with many provinces relying on enterprise self-assessments and others only intervening if industrial action lasts more than two days[138]. Better Work has boosted the soft and technical skills of Ministries of Labour, helping to put in place mechanisms to guard against 'zero tolerance' issues such as child labour. However, capacity constraints at both national and provincial levels remain pressing.

Private regulation has stepped in to plug the gap, with buyers developing their own codes of conduct (CoC) and standards[139]. Over the years some audits have shifted from firm-specific to multi-stakeholder initiatives, with the most progressive attempting to move "from traditional social compliance auditing to a process of cooperation between brands and supplier"[140]. In two separate interviews in **Indonesia**, brand representatives indicated that social compliance monitoring responsibilities were being shifted to main factories through capacity building programmes. Programmes such as Better Work have sought to rationalise the social audit process, with many global buyers now accepting Better Work audits instead of their own, reducing the audit fatigue and burden for suppliers and brands alike.

While the last 20 years have seen a paradigm shift in how brands engage with their supply chain, challenges remain[141]. For starters, there are limitations which derive from the complexity of the supply chain, with some brands sourcing from many hundreds of suppliers, meaning "brand inspectors and third-party monitors – even those that are diligent and professional – are at best able to visit factories periodically and for short periods"[142]. There are also questions about how far into the supply chain such social audits can penetrate, with most only touching the upper tier of suppliers. Tier 2 suppliers – fabric production and finishing – have traditionally not been part of the scope of work for social responsibility (CSR) teams[143]. In an interview with a brand manager in **Indonesia**, it was revealed that the brand considered social compliance of second tier suppliers the responsibility of first tier factories, even when the suppliers came from the brand's pre-approved or "nominated" supplier list and even when the product was imported. Meanwhile, factories reported that if suppliers were from the brand's nominated supplier list, the responsibility lay with the brand, and not the factory. One factory manager said that the factory was absolved of risk, which is inconsistent with brand responses, leaving a monitoring gap.

137. Musacchio and Werker (2016)
138. ERC (2017)
139. Suppliers are often categorised by buyers using A, B, C or D grades. Those receiving the lowest grade (D) are not eligible to be a supplier. Brand social responsibility teams (or outsourced third parties) orientate and audit factories on an ongoing basis.
140. BSR and UL (2014)
141. Oka (2016)
142. Human Rights Watch (2017):" The quality and accuracy of third-party monitoring reports depend largely on the methodology used in the assessments, the independence of the assessors from the factory and the apparel company, and the weight given to testimonies from workers and other interested parties"
143. Instead they are dealt with by sourcing teams

The responsibility for monitoring labour practices in subcontractors is usually left to the 1st tier suppliers and agents, rather than the brands themselves[144]. First tier suppliers are expected to carry out internal audits of their own suppliers, but with the burden of managing their own compliance, they have limited capacity to do much more than checking that there are no serious labour violations in their suppliers[145].

We find the effectiveness and reach of private regulation further constrained by two inter-related factors:

- Subcontracting practices; and
- Supply chain transparency.

5.1.1 Subcontracting

Suppliers often outsource elements of CMT production to meet peak short-term demand. According to the European Union, practices such as multiple subcontracting are widespread. In **Vietnam** and **Indonesia** we found that many factories made use of subcontractors to fulfil specific functions such as embroidery and printing. By some estimates, in **China**, up to 25% of CMT orders are outsourced by the contracted supplier[146].

Subcontracting, however, has been termed the "Achilles heel of code of conduct implementation", since it sometimes takes place on an unauthorised basis to meet tight deadlines and complete unanticipated orders, and in some countries smaller subcontractors may be informal and not registered[147]. As a result, subcontracting factories are at higher risk of falling outside of legal and regulatory frameworks. They are also likely to be smaller enterprises with less professional management, engaging in water-intensive activities such as washing or using chemicals in printing.

Almost all brands require their agents and 1st tier suppliers to seek pre-approval before subcontracting in order to ensure minimum sustainability requirements are met[148]. In reality, the extent of subcontracting in practice is not always visible to major brands. In **Vietnam**, while some brands interviewed could give accurate lists of authorised subcontractors, others were unclear whether their suppliers actually used any subcontractors as their sourcing decisions were all made through intermediary agents, or were the responsibility of their first tier[149]. Others worked on an assumption basis: That because their 1st tier suppliers were thought to have enough production capacity to meet order volumes, subcontracting would not occur.

Authorised subcontracting can fulfil a legitimate and essential requirement for factories: either to provide surge capacity, or because it simply makes business sense to outsource specialised tasks[150]. If unauthorised subcontracting does take place and suppliers are caught, most brands have punitive measures in place, culminating in business termina-

144. ERC (2017). First tier factories submit the names of their suppliers and subcontractors to brands, along with relevant internal audit reports.

145. Such as child labour. The most effective 1st tier monitoring of their suppliers seem to occur in vertically integrated chains, where subcontractors and 2nd tier is either part of the same group, or at least in the same physical location (such as an industrial zone)

146. Quality Inspection (2017)

147. Frenkel et al (2017)

148. Friedrich-Ebert-Stiftung (2017): Outsourcing production through subcontracting does not exonerate a multinational enterprise of its responsibility under UN and OECD guidelines for responsible business.

149. Illustrating the complex nature of the global supply chain, the CSR unit of a number of the brands based in Vietnam we interviewed did not have insight in sourcing practices as these were handled by a sourcing team who were based in China or Hong Kong or at their headquarters in the US or a European country, or even by the brand's agent, based in Korea.

150. Outsourcing also helps mitigate the risk that machines do not run under capacity during low season of spring and summer

tion[151]. **Table 13** lists measures put in place by selected major brands to mitigate the risks of unauthorised subcontracting. However, beyond resource-intensive spot-checks, it is extremely difficult for brands to actually find out if illicit subcontracting is taking place. In a recent study in Vietnam, two foreign-owned 1st tier suppliers and one domestic 2nd tier supplier admitted that not all subcontracting activities were reported to the relevant brands. The director of one supplier said: "*When the orders are too big, we have to transfer a part to the subcontractors. Subcontractors must be approved by the buyers but sometimes we had to do it secretly…If the buyers know, we will be sanctioned*"[152]. In **Indonesia**, all interviewed garment manufacturers said that subcontracting work for surge capacity is strictly forbidden, but not for supporting services like print, wash, and embroidery, as long as the subcontractor is either on a pre-approved "nominated" list by the brand or is guaranteed by the manufacturer to comply with the brand's social standards. Interestingly, one printing subcontractor used by at least two of these manufacturers said that when lead times are reduced, it regularly shares the work with other printing companies in the area to meet the order. In these cases, it reports its own 'surge capacity' subcontracting to the manufacturer, but it is highly unlikely that this in turn gets reported back to the brand.

This is a challenging situation for buyers – but in many ways it is exacerbated by their own sourcing decisions. A recent report by SOMO, the Dutch NGO, listed a number of buyer demands that directly increase the risks of unauthorised subcontracting, including[153]:

Last-minute changes. After samples have been approved, buyers may change designs, production volumes and production schedules without adjusting prices or timeframes, thereby putting more pressure on the manufacturer. This may even happen after the production for a specific order has already started.

- **Short lead times.** The most profitable clothing brands and retailers are those that are able to offer the newest trends in stores within the shortest timeframe. Production timelines are often short. If manufacturers cannot meet the deadline for transporting the ordered goods by boat, they may be forced to send the goods via air at a much higher cost. Equally, the buyer may be in the position to demand a discount as a penalty, which affects the already tight profit margin of the supplier.
- **Low FOB prices.** Unrealistic FOB pricing forces 1st tier suppliers to subcontract in order to reduce costs, thus increasing the price pressure on lower-tier suppliers. With brands looking for shorter lead times at lower prices, competition is intense and some suppliers adopt a policy of accepting whatever orders they can (no matter how low and unrealistic the prices) to ensure sufficient work.

Subcontracting can therefore become less about choice and more about necessity for suppliers. According to reports, not meeting shipping deadlines can lead to a 5% discount, eroding suppliers' already thin margins. So in order to meet deadlines and avoid penalties, manufacturers may resort to ad hoc subcontracting to ensure orders are finished.

151. J. Safra Sarasin (2014): "Where proven instances of subcontracting will be reported to Primark's senior Directors and may lead to the termination of business"
152. Friedrich-Ebert-Stiftung (2017)
153. SOMO (2015)

Compliance audits cannot take place in segments of the supply chain that are invisible to buyers. While precise information is difficult to obtain, it is thought that many subcontractors are where the worst working conditions can be found, especially as they are more likely to include unregistered, informal enterprises where no taxes are paid[154]. A survey conducted in **Bangladesh**, for example, found that 32% of the garment factories were informal subcontractors, and 91% of these informal factories produced at least partly for export[155].

Subcontracting also impacts on power dynamics in the supply chain. There has been significant attention on the influence of brands on their first tier suppliers, but studies have found that the pressure of agents and 1st tier suppliers on their subcontractors is even higher[156]. Subcontractors are generally paid by piece rate, provide lower-value added services, and exist in an even more crowded marketplace where like-for-like substitutes are relatively easy to find. Brands do not intervene in how much subcontractors are paid: The agents and 1st tier suppli-

Table 13:
Selected brand strategies to mitigate the risks of unauthorised subcontracting (Source: RobecoSAM ,2016)

Primark
Primark's purchasing teams manage a system for assessing supplier capacity. Factories are asked to report their capacity and the auditors use this information to cross-check what they see in factories. Where necessary, weekly production management meetings are set up with the suppliers, combined with unannounced spot checks to check for any illegal night shifts or subcontracting.
Inditex
Inditex's IT system maps the entire supply chain and the flows of materials that make up the final products. This enables the company to identify where it is exposed to risk in operations along the supply chain. The monitoring system is integrated into the commercial team's procurement system to match supplier capacity. All suppliers have been trained to work with this system. Inditex trains and educates its suppliers extensively to ensure that they are all compliant with the policies and standards required by Inditex. It also requires suppliers to apply those policies and standards to their own supply chains.
M&S
With local teams on the ground, M&S actively monitors the production c1apacity of all factories to avoid the risk of subcontracting. Every subcontractor is pre-approved and it claims never to source from any subcontractor that is not known. The company is confident that its processes are robust enough to prevent its suppliers from engaging in any illegal subcontracting without M&S approval.

154. SOMO (2015)
155. EPRS (2014)
156. Friedrich-Ebert-Stiftung (2017)

ers can shop around to get the lowest price possible[157]. As the owner of a factory doing fully outsourced CMT production in **Vietnam** told the Friedrich-Ebert-Stiftung (2017) study: *Some South Korean brokers came to us with the orders at very low prices [...]. Our normal price is 1.5 USD/unit but they offered only 0.9 USD. They said if you don't want this price, we can find suppliers who will agree with even 0.7 USD. To have enough work for the workers, sometimes we had to swallow the anger and accepted that low price*"[158]. And according to an interviewed printing company in Semarang, **Indonesia**, "[*Sometimes], we don't get any profit at all. The price from the factory is just enough to pay the production cost. However, we manage our profit from other orders.*" Agents and 1st tier suppliers therefore can exert considerable power to maintain downwards pressure on prices[159].

Any support received by the brand when it comes to training on social compliance, new technology, or productivity strategies, also generally stops at the 1st tier supplier. In **Indonesia**, all brand representatives interviewed indicated that this was the case. Some have tried to increase efforts to support main factories in this regard, but engagement with subcontractors or the 2nd tier is limited to auditing only.

5.1.2 Transparency

Private regulations – just like public ones – require effective oversight. However, this has been hindered by a lack of supply chain transparency. This is not only due to the challenges of hidden subcontracting, but also because of the difficulty of tracing the origin of a garment back to its raw material source[160]. The intermediated and tiered nature of the global garment supply chain means buyers often only have direct (contractual or business) relationships with their 1st tier suppliers or buying agents[161]. In many cases even brands have little insights into the lower tiers of their supply chain – or such insight is scattered across different business units.

The recent OCED Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector calls on multinational companies to develop a full understanding of their supply chain, including second and further tier suppliers, subcontracted units, down to the informal sector. If brands are sourcing indirectly through agents, this calls for brands and their agents to work closely together to map out suppliers and develop a shared approach to risk mitigation.

157. Friedrich-Ebert-Stiftung (2017)
158. Friedrich-Ebert-Stiftung (2017)
159. Wage Indicator (2016)
160. Frenkel et al (2017). In Vietnam, for example, it is common for US-based brands to use Korean agents who source textiles from China (produced in cotton fields) for their Vietnamese-based firms to assemble garments, who use imported chemical and trim inputs and the services of domestic washing and printing facilities
161. J. Safra Sarasin (2014)

Many brands already voluntarily share information with competitors (including suppliers' names and audit reports) through closed databases such as the Fair Factories Clearinghouse and Sedex. Other brands have gone further with public disclosure, such as Adidas, Levi Strauss, Nike, Patagonia, and Puma. **Figure 17**, for example, is an extract from the M&S public database that lists the names and addresses of Vietnamese suppliers, along with the number of employees by gender, and trade union status. However, this has mostly been limited to 1st tier and, in some cases, direct 2nd tier suppliers. Few of the brands we interviewed in **Vietnam** and **Indonesia** saw any intrinsic benefit or use of public disclosure – and those that had disclosed did so because they were under civil society pressure.

However, if more brands publically disclose the names, addresses and other relevant information about supplier factories, this could help[162]:

- Determine whether a brand has sufficient leverage or influence in a particular factory or country to achieve remediation of workers' rights abuses.
- Sector- or region-wide collaboration, as many enterprises in the garment and footwear sector source from the same countries and suppliers – and most suppliers sell to multiple buyers. Sharing information can help increase the awareness of specific risks in the sector and bring attention to emerging risks more quickly than would be possible for individual brands[163].
- Guard against unauthorised subcontracting – workers and other third parties would know which factories are authorized to produce for the company and which are not.

Some brands cite commercial confidentiality as a reason for not publically disclosing their suppliers[164]. In 2016, nine labour and human rights organisations endorsed the 'Transparency Pledge' as a minimum standard for supply chain disclosure. Systematic uptake and adherence to such industry-wide standards for acceptable informa-

Figure 17:
Extract from M&S supplier database (source: M&S website)

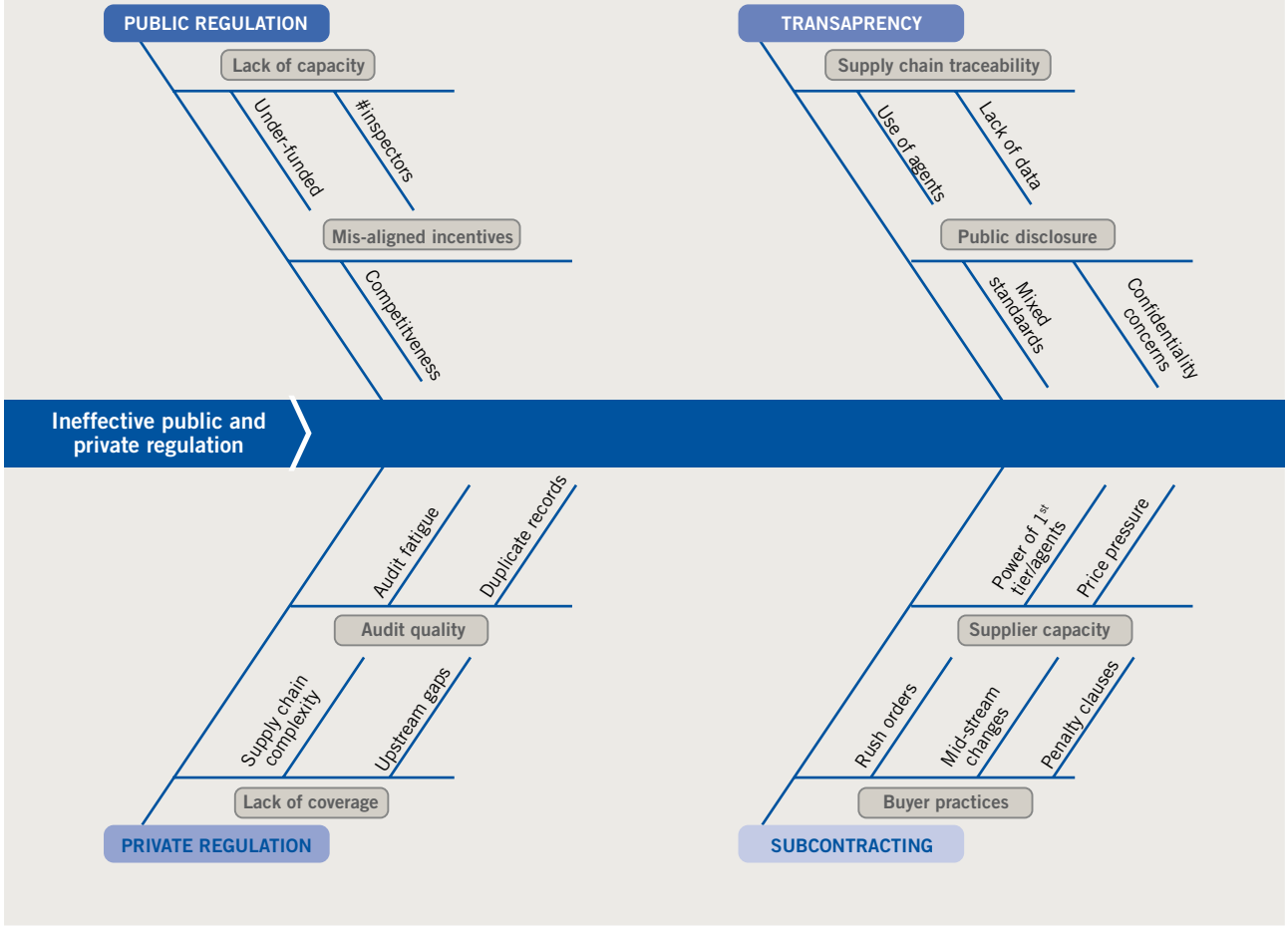
162. Human Rights Watch (2017)
163. OCED (2017)
164. Human Rights Watch (2017)

tion disclosure would create the impetus for brands to continue to develop a fuller understanding of their supply chain, and arm third parties with critical information needed to monitor progress.

Constraint conclusion:

Shortfalls in public and private regulation are caused by a lack of capacity to monitor complex supply chains, and misaligned incentives[165]. Despite progress over the past decade, both regulation and oversight mechanisms alike are hindered by weak subcontracting and supply chain transparency. As a result, subcontractors and 2nd tier suppliers are precariously 'sandwiched' between complying with labour standards, and meeting the time-pressured orders of international brands[166]. **Figure 18** below depicts the root cause analysis using a 'fishbone' visual.

Figure 18:
Analysis of causes of ineffective public and private regulation



165. See the conclusions of the 2016 International Labour Conference discussion on global supply chains for further information about the global governance gap

166. Friedrich-Ebert-Stiftung (2017)

5.2 FACTORY MANAGEMENT

Poor working conditions can be considered, above all else, a human resource problem. Management teams in manufacturing enterprisers make rational choices not to invest in their employees: For example by cutting costs in building safety, not providing protective equipment, or verbally abusing staff to meet order shipment dates.

There is a wealth of research that shows good human resource practices, by contrast, can be positively associated with outcomes such as productivity, innovation, staff retention and customer satisfaction[167]. So why is progressive management not always practised? This section looks past basic capacity constraints to consider the underlying business models and incentives at play in garment manufacturers.

5.2.1 Productivity, efficiency and wages

While labour costs are a fraction of total production costs, and an even smaller portion of retail costs, according to the World Bank "buyers are generally not prepared to accept proportional increases in prices despite CSR efforts"[168]. If anything, as we have seen, the pressure is to drive prices downwards. In a scenario where minimum wages are failing to keep pace with cost of living, the commercial case for better wages rests on increasing productivity.

There are vast differences across Asia in terms of productivity levels. In **Vietnam**, the volume of exports produced by the garment industry has significantly increased over the past decade, but value-added in manufacturing has almost halved[169]. In fact, Vietnam has the fourth lowest labour productivity growth rate in all of ASEAN, holding steady at 3.4% per year for the past five years[170]. This ranks Vietnam as a 'mid-table' performer, along with **Indonesia** – where value addition in manufacturing has fallen more steadily since the mid-90s (21% in 1994 to 11% in 2013) – and **Cambodia**. **Bangladesh** and **India** have performed the worst. **China** has performed the best: Despite a decade of wage rises, the average price of Chinese apparel exported to the United States in 2015 was lower than it was in 1990[171].

In-factory productivity is measured by the 'efficiency rate' – the ratio between actual versus targeted production[172]. This is determined by a range of factors, including work organisation (supervision, processes and systems), labour (quality, turnover and motivation) and access to supporting services such as credit, technology and infrastructure[173].

Boosting operational performance and productivity is a sound business goal, and essential for value chain upgrading. But the direction of causality between productivity and working conditions (including wages) is not simple. If productivity rates rise, workers can be rewarded with better working conditions; but in reverse, better working conditions can lead to better motivated workers, who improve their productiv-

167. Better Work (2013) and ILO (2013)
168. World Bank (2016)
169. World Bank development indicators. Value added is the net output of a sector after adding up all outputs and subtracting intermediate inputs. In Vietnam this fell from 20.3% to 13.2% between 2006 and 2013
170. Friedrich-Ebert-Stiftung (2017). Labour productivity is defined as gross value added in current prices per employed persons,
171. World Bank (2016) and key informant interview
172. Tufts (2016)
173. World Bank (2016)

ity. If the former, however, there is no guarantee that the labour share of productivity gains is passed on to the workers, hence the importance of developing mechanisms for social dialogue and worker representation[174]. If the latter, how can factories be persuaded to make investments that may only pay off in the longer-term? Making this argument means paying attention to the specific enterprise context, and, in order to penetrate beyond the first tier, to many other constraints facing SMEs.

The larger, mostly foreign-owned 1st tier exporters have access to a range of brand- and multi-stakeholder capacity building initiatives, while lower tiers, which face high barriers to break out of the cycle of low value-addition, have a relative paucity of support[175]. The 1st tier, as we have seen, is largely responsible for auditing their 2nd tier suppliers and subcontractors – but frequently does not offer support to lift standards if shortfalls are discovered. Interviews in **Vietnam** cited a lack of public or private programmes to support washing, printing, embroidery services or smaller CMT producers[176].

As a result, domestic garment producers in particular lack the necessary experience and expertise to meet production capacity, efficiency, quality, sustainability standards and delivery times[177]. Additional hurdles facing SMEs in accessing finance and labour supply are covered in future sections. Here, we turn to the issue of management systems.

5.2.2 Management style and systems

Just as working conditions vary considerably across countries and companies, so do management strategies. The proliferation of modern management concepts and methodologies is outside the scope of this paper, but some of the most popular in garment manufacturing (as in manufacturing more widely) are Six Sigma – a data driven approach to eliminate inefficiencies – and lean production, a systematic approach to eliminating waste while boosting productivity[178].

There is a relative lack of research in the garment sector about which management systems, and related human resource strategies, optimize commercial performance while improving working conditions. Better Work has noted the positive correlation between management professionalization and business outcomes, where "factors such as the capacity for worker engagement, a willingness to experiment with new ways of improving operations, the amount of training given to workers and the robustness of a firm's organisational structure can all contribute to better labour standards"[179]. On the other hand, some central tenets of lean manufacturing, for example 'just in time' production – which reduces the amount of goods and materials a company holds in stock and emphasises individual worker performance assessments – have

174. A common assumption is that lower tier suppliers in particular have low profit margins, leaving them little room to increase wages or improve working conditions. However, data from the 2017 Friedrich-Ebert-Stiftung study in Vietnam do not support this conclusion, instead finding that working conditions and wages do not necessarily go in line with the value added or the profit margin that the supplier receives in the supply chain – and that serious labour violations were just as likely to be found in foreign-invested firms where margins were highest.

175. In Vietnam, a range of ethical trade and business development services are active at both the region – such as Elevate (http://www.elevatelimited.com/), Impactt (https://impacttlimited.com/), Vectra (http://www.vectra-csr.com/Vietnamese/index.htm) and national levels such as OneStep (http://www.onestepvietnam.com/GL/en/home/).

176. During interviews, only one Japanese brand was cited as organising capacity building training (on quality assurance and modern management methods) for subcontractors

177. ERC (2017)

178. ILO's SCORE programme for SMEs, active in both Vietnam and Indonesia, is inspired by the lean manufacturing technique

179. Better Work (2013)

been cited as contributing to decent work deficits[180].

Beyond technical systems, an important determinant in the success of management strategies is the quality of supervisors and senior leadership. In **Vietnam**, some studies have found that although foreign-invested firms enjoy access to more advanced technology and know-how, this does not always translate into improved efficiency. The studies found that strikes were more likely in southeast Asian- and east Asian-owned firms, where foreign companies unfamiliar with the local circumstances employed Korean or Taiwanese managers who often had little knowledge of culturally appropriate ways to manage and motivate the workforce[181].The same studies noted that in **Cambodia**, foreign-invested firms often hired an additional layer of local managers to "deal with union leaders and resolve labour-related issues in a more reserved and locally appropriate way"[182].

There is also an important gender consideration in labour management. Garment production absorbs a large number of unskilled female workers, but few get promoted from the factory floor. While in **Vietnam** there is very high share of female line leaders (92%), this is not always the case across Asia[183]. Even in Vietnam, a recent survey of a representative sample of factories found that all workshop management positions in every factory were held by men[184]. This inhibits more gender-sensitive management decision-making which could lead to better working conditions – such as decisions to place an equal number of male and female toilets even where the employee headcount is heavily dominated by women. And while recent evidence from **Bangladesh** shows that while female trainee supervisors have lower *initial* performance than their male counterparts (because they face initial resistance as supervisors) after approximately four months in the role, both perceptions and performance of female supervisors catch up with those of males – suggesting a relatively short but sharp period to overcome cultural and social norms.[185] A recent Better Work evaluation found that when women were trained as line supervisors, it resulted in a 22% increase in productivity in the lines they supervised, making a business case for promoting women in the sector[186]. Interviews with factory managers in **Indonesia** indicated that the majority of supervisory positions were filled by women, but this was only the case in factories that had upgraded to provide more full service functions that also had majority women managers. One OEM factory manager expressed that women were generally more responsible and trusted to perform managerial tasks. This suggests a possible correlation between upgrading capacity and management practices that are less discriminatory towards gender.

180. WIEGO (2017) Verified in interviews with CSR experts in Vietnam, who cite lean production as a 'nightmare' for compliance: toilet breaks are carefully monitored, and individual employees singled out when their outputs are sub-standard.
181. Vixathep & Matsunaga (2012) and Wage Indicator (2016)
182. Vixathep & Matsunaga (2012). This is now also happening in Vietnam, with Korean and Taiwanese firms increasingly using local managers.
183. VGCL (2017)
184. Vietnam General Confederation of Labour. Factories are sub-divided into workshops. In Vietnam, anecdotal evidence points to state owned factories having more women in upper management roles
185. Frenkel et al (2017)
186. Better Work (2016). Supervisory Skills Training Impact Evaluation.

5.2.3 Impact of sourcing practices

In economics jargon, the structure of the garment industry is a monopsony: Where a small number of global buyers control the market as the major purchasers of goods, and as such, can exert considerable influence on prices and how suppliers participate in the value chain[187].

Better Work impact assessments have found clear evidence that sourcing practices of global apparel brands are "associated with higher rates of non-compliance with working hours and with workplace safety and health"[188]. Remember the last-minute changes and short lead times that were a driver of subcontracting? In **Vietnam**, uncertain orders are the single biggest problem that factories report: Almost half of all firms report uncertain orders, late penalties, changes in technical requirements and defect penalties as serious business challenges[189]. This, in turn, contributes to supervisor stress which increases the likelihood of verbal abuse[190]. Subcontracted firms in **Indonesia** also divulged that last-minute requests for repairs or 're-dos', which were sometimes even demanded in a single day, were one of the most difficult challenges to manage. Better planning in general was reported to be desperately needed by subcontracted firms. One printing company in Central Java said that when it is initially contracted by a manufacturer, it is given a certain number of days within the total allotted lead time stipulated by the buyer, but if the manufacturer is late in delivering the garment to the printing factory, it is the subcontracted printer that must manage the reduced timeframe, which typically includes a significant reduction in the originally quoted time allowance.

Incentives to cut corners on worker health and safety often start at the top[191]. This includes practices such as 'forum shopping', where brands change suppliers frequently to force down prices and shorten delivery times[192]. Developing more stable relationships – while maintaining the supply chain flexibility which is critical to the modern garment retail industry – requires close and collaborative partnerships between brands and suppliers to encourage value-sharing, learning and innovation[193]. A number of recent well-publicised cases – such as Nike, among others – have shown the transition from "poster child for irresponsibility to a leader in progressive business practices" is not impossible[194].

Importantly, however, sustainable solutions require moving beyond name-and-shame 'brand bashing' to recognising the structural issues that mean that while many brands do care about job quality, both internal and external commercial pressures make it difficult for these good intentions to translate into impact on the ground.

The disconnect between social compliance and sourcing within brands is reflected in departmental structures, with CSR teams often removed – both physically and organisationally – from procurement decision-making, which often takes

187. Friedrich-Ebert-Stiftung (2017).
188. Better Work
189. Tufts (2016)
190. Tufts (2016): "Variations in technical requirements, variations in social compliance requirements, late delivery penalties, changes in technical requirements, defect penalties, replenishment orders and uncertain orders are all moderate drivers of manager reports of supervisor stress"
191. Subramanian (2016)
192. EPRS (2014)
193. Better Work (2013)
194. Better Work (2013) and Zadek (2006)

place at headquarters[195]. In **Vietnam**, for example, most in-country CSR teams had little insight into their brand's sourcing practices, which as we have seen, are a key driver of poor working conditions. Approval for subcontracting and textile sourcing are almost exclusively the responsibility of other business units such as production and merchandising. While some brands have sought to link CSR performance of suppliers directly to order volume, Better Work has noted a particular conflict in the area of excess overtime, with some buyers even rewarding longer hours with larger orders[196].

This echoes a wider concern about 'Base of the Pyramid' (BOP) initiatives that seek to combine commercial motivations with development objectives. Some commentators find that the "locus of corporate interest in BOP has steadily shifted away from the profit-and-loss side of the business to the philanthropic and social responsibility departments". This is also reflected in participation in multi-stakeholder initiatives and programmes such as Better Work, where the majority of brands send their CSR teams rather than the commercial decision-makers. Yet the root causes of incentives shaping poor labour standards and abuse are deeply embedded in the core business activities of buyers[197].

Information asymmetry is another factor inhibiting better sourcing. Most brands have limited capacity to understand a growing network of suppliers, where production is spread thinly across many different factories, who in turn, may be selling to many different buyers. According to recent research in **Vietnam**, while social responsibility audits do check compliance with minimum wages, the actual wages of workers are highly unlikely to be a factor in price negotiations between suppliers and buyers[198]. This is because suppliers are resistant to open costing, believing it puts them in a disadvantaged position in price negotiations. As a result, brands have limited leverage or insight into labour costs.

5.2.4 The business case for better working conditions

So where does this leave the so-called 'business case' for garment producing factories to invest in better working conditions?

Repeated studies have shown a clear business return from introducing better conditions for workers. This includes:

- In **Vietnam**, Better Work factories where workers report good working conditions reach their daily production targets up to 40 minutes faster than similar workers who are working in factories with worse conditions. These factories received a 5.9% boost in profitability if workers perceive improvements in 'sweatshop' working conditions, and a 7.6% boost if workers experience a comfortable environment and trusting workplace.
- In **India**, textile suppliers recorded a 17% increase in productivity where managers received previously unavailable information on international best-practice management techniques, such as quality control and inventory tracking[199].

195. This is gradually changing. In 2016, recognising sustainability and business go hand-in-hand, Puma changed the setup of their sustainability department and embedded it into their International Trading team, creating an Executive Sustainability Committee at the corporate level.
196. Friedrich-Ebert-Stiftung (2017). H&M and Inditex have participated in voluntary initiatives for triangular bargaining with their suppliers and the trade unions in the exporting countries. Nike's Manufacturing Index gives sustainability equal weight alongside quality, cost and delivery to rate suppliers.
197. Simanis (2013)
198. Friedrich-Ebert-Stiftung (2017)
199. Better Work (2015)

- In **Bangladesh**, absenteeism reduced by 33.7% after participating in Impactt's Benefits for Business and Workers (BBW) Programme, and worker turnover was down by 52.2%[200].
- In **Cambodia, Haiti, Indonesia, Jordan, Lesotho, Nicaragua, and Vietnam**, as mentioned above, empowering women through training them to be line supervisors increased productivity in Better Work factories by an average of 22%.

If the benefits are clear, what about the costs? Programmes such as Better Work and BBW charge fees for the services they provide to factories[201]. But these pricing levels are heavily subsidised – and do not represent the true cost for factories to access the information and expertise needed to adopt better practices. They thus provide a solid reason for factories to participate in programmes – but do not tell us much about the business case for garment manufacturers, in general, to invest in better working conditions.

Scaling-up a business case beyond donor subsidised programmes requires evaluating the benefits, costs and risks that provide justification for an enterprise to start an undertaking. However, the costs and risks side of this equation are often over-looked, or not well-understood. Commercial return on investment (ROI) decisions require examining potential benefits relative to both their costs and alternative options – which means taking into account other uses of the same investment capital (opportunity cost), the time value of money (depreciation), and internal rates of return (hurdle rates).

The potential business case – and the time horizon for pay-off – will vary significantly depending on the different types of working condition 'investment'. Some innovations such as incentive-based pay, team work, communication and problem-solving may have shorter-term benefits, while others such as occupational health may require 'patient' capital – involving significant up-front costs, with effects only felt over the longer-term. Since businesses are also dynamic entities, there are also spillover risks: That a positive improvement in one dimension of job quality will impact negatively on another. In **Vietnam**, for example, there is evidence that as firms increased wages in line with rises in the minimum wages, they became less compliant with other aspects of labour legislation, and changed the composition of the workforce towards less skilled workers, often switching to more temporary and fixed-term contracts[202].

There is also question as to how scalable the business case might be. In both **Bangladesh** and **Myanmar** there is qualitative evidence that many factory owners believe that better worker welfare will not improve productivity or profits, and that making such investments simply results in additional costs[203]. This attitude can be found not just in suppliers, but in buyers as well. According to a European brand manager in **Vietnam**, "*For us, there is hardly a linkage between labour standards and business performance or profitability. Violations of labour standards are the risks that we have to prevent*"[204]. In other words, social responsibility measures are geared towards managing reputational risks, and do not represent a compelling competitive

200. Impactt (2017)
201. For reasons of cost-recovery and to ensure appropriate incentives of participants. Factories contributed the equivalent of £2,000 to participate in the BBW programme
202. Vixathep & Matsunaga (2012). Also see http://english.vietnamnet.vn/fms/business/184884/companies-warned-about-massive-layoffs-of-workers-over-35.html#
203. Business Innovation Facility Burma (2016)
204. Friedrich-Ebert-Stiftung (2017)

return on investment. This suggests labour standards are not systematically embraced within business models across value chain actors because: they do not have access to locally appropriate information; the case does not exist (or actors do not believe it); their commercial performance is doing just fine regardless of how workers are treated[205].

5.2.5 Business models

The business models used by garment manufacturers largely determine how responsive they will be to arguments about working conditions – whether coming from the 'carrot' of a business case, or the 'stick' of brand pressure.

Broadly, we can consider two types of business models: value maximising strategies, and low-price cost-saving strategies (which are the most prevalent). **Table 14** sets out the different characteristics for Type A and Type B business models.

Manufacturers make different decisions depending on whether their production is geared towards Type A or Type B. Factories can also have a blend of both business models, depending on who they sell to[207].

Under the pressure of rising costs of production (including labour) but stagnant unit prices, in order to maintain profit margins Type B factories are more likely to resort to cost-cutting measures, such as lowering the production line headcount coupled with greater work intensity, including excessive overtime and negative motivational techniques such as abuse[208]. They are also more likely to cut costs by 'cheating' on audits or 'faking' ISO certification – practices which are rife across Asia[209]. Excessive cost control measures, in turn, place more pressure on the remaining workforce, increasing the chances that poor working conditions will boil over into strikes. These strikes may then force suppliers to halt production, creating a vicious cycle that further ratchets

Table 14:
Business models used by garment manufacturers (Source: own research, inspired by Friedrich-Ebert-Stiftung, 2017)

	Type A	Type B
Functions[206]	Full service, OBM and CMT	CMT or subcontractor
Brand relationship	Direct, more likely to be stable	Indirect, more switching
Decision-making	Longer-term	Short-term
Buyer relationship	Technology transfer and upskilling	Transactional
Profit maximising strategy	Value creation	Cost control

205. Business Innovation Facility Burma (2016): "Following the Rana Plaza tragedy, it emerged that many owners feel that they are doing fine without investing in welfare or productivity, and indeed that many factories will become so un-competitive if they adopt better labour standards that they will have to close (leaving aside factories that have had to close because of building safety issues)"

206. There is no automatic relationship between the size of firm and business model. In Sri Lanka, for example, many Type A full service could be considered SMEs, such as Ocean Lanka which has 700 employees.

207. In the Friedrich-Ebert-Stiftung (2017) study, one Vietnamese manufacturer was selling to both a fast-fashion American brand and a Japanese brand specialising in more sophisticated products. While the Japanese buyer was important to their business, the factory still needed orders from the American brand to ensure sufficient work for its labour force.

208. Friedrich-Ebert-Stiftung (2017). Shift work is uncommon

209. Larsen (2013)

up the pressure to meet tight turnaround times. While Type A factories can also exercise short-term cost controls, they are more likely to be receptive to efficiency initiatives, such as improving workers' skills to raise labour productivity, and reducing unnecessary management costs and energy waste.

With less stable shorter-term relationships with buyers, Type B factories are likely to try and take on simultaneous orders from multiple clients to ensure a constant flow of business. 'Hedging' behaviour mitigates the risk that orders can fall through before contracts are signed. Factories would rather be over-capacity than under-capacity and eat into already thin margins. However, this can lead to unrealistic production schedules, requiring the use of rush subcontractors to deliver on time. Type B companies are also likely to have less control over the arrival of inputs as these are sourced and shipped by brands or their agents. If inputs are delayed, manufacturers may have to resort to unethical treatment of workers, or subcontract orders in whole or in part in order to meet the contractual shipping deadline[210].

Business models based on the 'low-road' of Type B are less likely to result in genuine efforts to uphold labour standards – or for such efforts, even if introduced, to be sustained in the face of the next rush order. Type B factories tend to be *reactive*, focusing on immediate outcomes rather than preventative investments that pay off in the longer term. Interviews in **Vietnam** confirmed that the majority of garment factories were not pro-active in making factory improvements, only

Table 15:
Types of economic upgrading and feasibility for social upgrading (source: adapted from World Bank, 2012)

Type of economic upgrading	Description	Feasibility for social upgrading
Functional	Increasing the range of functions or changing the mix of activities to higher-value tasks; for example, moving beyond direct production-related activities to input sourcing, logistics and distribution, product development, design, and branding	A core component of Type A production, associated with upskilling and higher labour compliance. However, requires a range of supporting services such as adequate know-how, technology and investment.
Supply chain	Establishing backward manufacturing linkages within the supply chain, in particular to the textile industry	See section 5.4. There are mixed opinions about the commercial case for developing backward linkages; however, this may help to reduce import delays to take pressure off meeting tight shipment dates for both Type A and B.
Channel	Diversifying to new buyers or new geographic or product markets	Depends on the type of buyers. Many Type B simply prefer to find more 'low road' buyers who, in turn, have lower labour standards.
Product	Shifting to more sophisticated products with higher unit prices.	Closely associated with the working conditions benefits of functional upgrading, but depends heavily on ability to access quality raw materials and the buyer-base (channel upgrading) that values product sophistication.
Process	Reorganizing the production system or introducing new technologies to gain efficiency	Unlikely to have a sizeable effect on working conditions in Type B models unless it goes hand-in-hand with other types of upgrading (functional/product)

210. Friedrich-Ebert-Stiftung (2017)

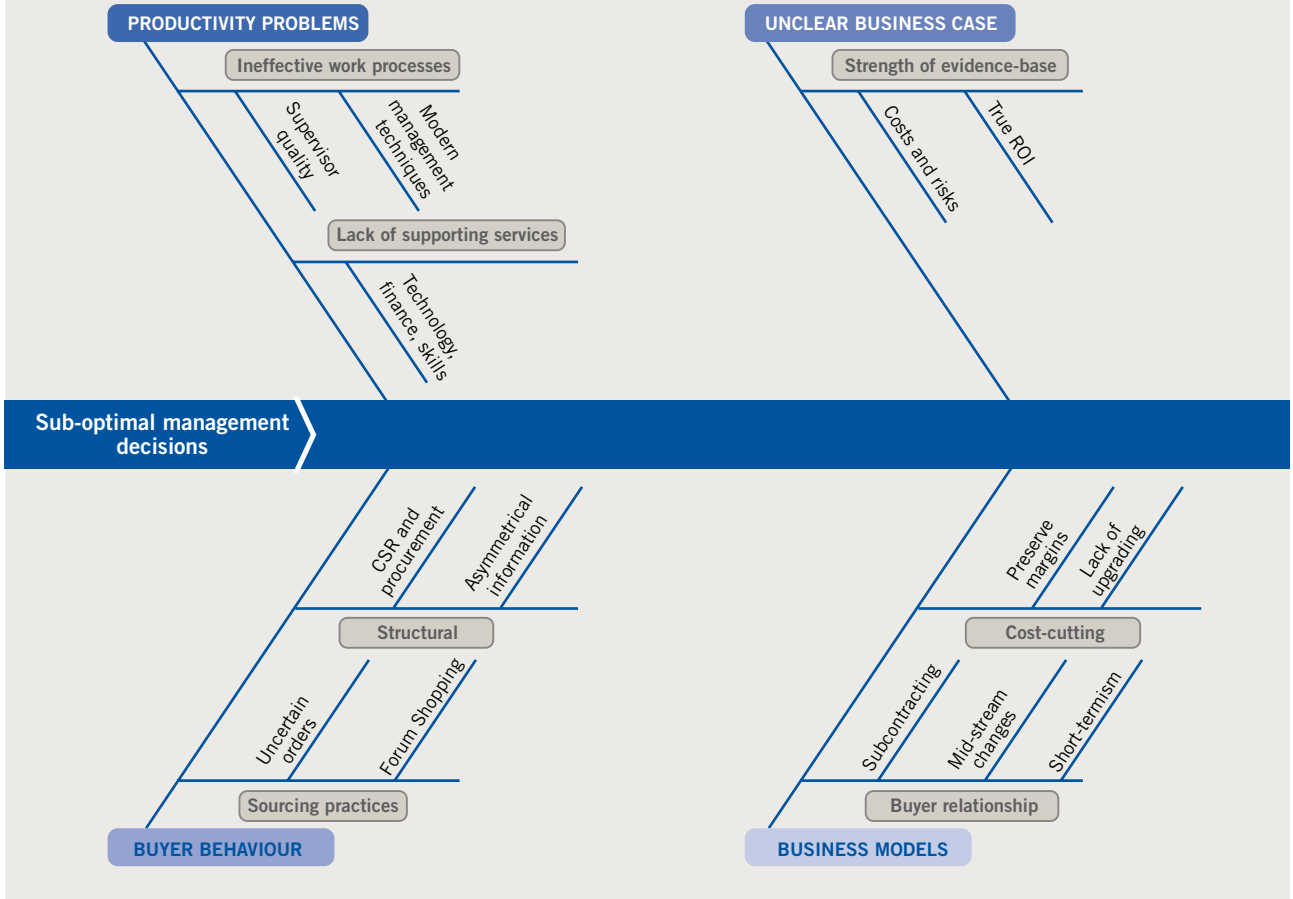
adopting new business practices when pushed by buyers[211].

Moving from compliance obligations to arguments about commercial opportunity will only go so far – and likely be superficial, particularly for Type B factories – without shifting their underlying business models. It is therefore not simply about boosting productivity and profitability, but paying attention to the quality and nature of upgrading. **Table 15** sets out variety of strategies for economic upgrading, and the feasibility of social upgrading, taking into account the A/B categorisation. Even if firms are motivated to upgrade (and many are not, content with their place in the chain), they face a range of constraints – such as access to investment and inputs, and the policies and social norms shaping the business environment – which we now turn to in the remainder of this section.

Constraint conclusion:

Sub-optimal human resource strategies constrain both business performance and improved compliance with labour standards. However, the link between productivity and better working conditions is neither automatic nor uni-directional. The type of business models and management strategies used by manufacturers are largely driven by buyer sourcing practices, which can be subject to conflict between a corporation's commercial and social interests. The costs and risk side of the business case for better jobs in factories is not as well-understood as the proven benefits; leading to

Figure 19:
Analysis of causes of sub-optimal management



211. Brands have also started to differentiate between suppliers, recognising that it is difficult to persuade all factories to make working conditions improvements. Rather than treating all factories the same, brands select 'strategic partners' where they engage in continuous improvement activities.

questions about how effective the business opportunity argument is for the 'squeezed middle' of subcontractors and lower-tier suppliers, unless this goes hand-in-hand with upgrading strategies. Buyers do not link orders to better working conditions, and it is generally the opposite – orders go to cheaper suppliers who are not investing in better working conditions.

5.3 ACCESS TO FINANCE

In **Vietnam**, the majority of garment manufactures who supply directly to brands and their agents are foreign-invested. **South Korea**, the dominant player, is one of Vietnam's biggest trading partners, with textile materials making up the single largest category of South Korea's imports into Vietnam[212]. This is reflected in the participation in programmes such as Race to the Top and Better Work, where almost half (46%) have South Korean ownership, 14% are from Taiwan, and 6% each from Japan and Hong Kong[213].

There is, firstly, the network effect of firm ownership – companies from the same country are more likely to supply, sell and subcontract to each other[214]. This was largely the case in **Indonesia**, where Korean-invested firms were said to primarily source from and subcontract other local Korean-invested firms.[215] Studies have shown that the network effect is particularly strong in emerging garment industries, but over time, foreign-owned firms engage in more knowledge transfer activities and increase local sourcing of materials[216]. In **Vietnam**, however, knowledge sharing – resulting in upskilling and increased productivity - between the foreign-invested sector and the domestic sector remains relatively weak[217].

There is also the issue of access to capital. Foreign-invested firms by definition have attracted outside investment, which is crucial for growth and to economically upgrade. In **Vietnam**, this has been aided by national and provincial policies that incentivise foreign direct investment (FDI): Corporate tax is reduced for projects over $300million – a ticket size too big for most domestic investment – and Thai Nguyen province has halved its tax rate and offered exemption from land rent for overseas electronics manufacturers[218].

By contrast, domestic suppliers struggle to access affordable finance. In **Indonesia,** local banks consider garments to be a risky industry, and the loans they do provide are at prohibitively high rates,[219] making it difficult to purchase modern machinery. One large trim supplier in Indonesia shared that it will sometimes provide machinery as in-kind payment to its subcontractors handling its overflow orders, as these smaller subcontractors cannot otherwise secure a loan to purchase the machinery themselves. This is not the case for foreign-invested firms, which have their national banks located near industrial zones that help facilitate capital investment. According to a manager of a medium-sized factory in **Vietnam's** commercial hub of Ho Chi Minh City: *"In order to become a first-tier supplier to international brands and produce on FOB, we must invest a lot in upgrading our machinery, [and] factory infrastructure…we do not have such a budget, so we have*

211. Better Work (2013)
213. Better Work Vietnam
214. In Vietnam this is particularly the case for Korean firms
215. Interview with KOGA (2017).
216. Better Work (2013)
217. ERC (2017)
218. ERC (2017)
219. Global Business Guide Indonesia (2014)

to accept smaller orders through vendors"[220].

Even if the appropriate skills and contacts are in place, double-digit interest rates have made it prohibitive for some domestic firms in Vietnam to acquire credit for FOB contracts[221]. Some firms upgraded to full service production but had to stop due to difficulties in accessing bank credit. As another factory owner told the Friedrich-Ebert-Stiftung study: *"Before 2012, around 30 per cent of our production was FOB, but then the interest rates were increased too high for us to access, usually around 12-15 per cent/year, even higher than our profit. Without bank credits, we could not have enough of a budget to purchase materials for the FOB contracts. We had to go back to CMT".*

If firms moving to the cusp of 'Type A' production are struggling, the credit crunch hits Type B firms even harder. Squeezed by agents and upper tier suppliers, subcontractors have seen profit margins slip below the cost of borrowing. This backs smaller suppliers into a corner during negotiations: If they do not accept the low prices on offer, they will have no work – putting them at risk of default and, at worst, going bankrupt[222].

There are currently no mechanisms tying access to concessional finance to improved working conditions in **Vietnam**[223]. With credit and working capital being major constraints to firms simply surviving, making the case for investments in better working conditions – that may only pay off over the longer term – is even more difficult.

More promising is the nascent interest in garment and textiles factories from socially-responsible investment, where recent cases have shown that even if 'impact' finance cannot mitigate all risks, at least it can be part of a faster, more transparent response to potential industrial disasters. For instance, in early 2017, a section of the factory floor collapsed at Ananta Apparels Ltd in Dhaka, **Bangladesh** – a top supplier of GAP, H&M and Next – and the recipient of investment capital from both the Dutch and British development finance institutions[224]. The Ananta Fashion & Apparels Workers Union (AFAWU) called on workers to evacuate the building. As factory management, supported by the Ministry of Labour and the garment exporter's association, recognised that building safety is an important issue, workers' demands were quickly and fairly responded to: Five days after the collapse, urgent structural repairs were completed and employees returned, having been paid for the days the factory was closed[225]. With stringent requirements on environmental, social and corporate governance standards – often coupled with capacity building support to help meet these standards – long-term patient capital offered through development finance can help professionalise factory management. Socially-driven investors, however, have largely steered clear of corporate supply chains until now, despite this being cited as one of the four top impact investment opportunities for

220. Friedrich-Ebert-Stiftung (2017)

221. Friedrich-Ebert-Stiftung (2017)

222. Friedrich-Ebert-Stiftung (2017)

223. The IFC has worked with Vietinbank and Sacombank to develop financing options for domestic SMEs, but these are loans for energy efficiency and cleaner production investments. The IDH Sustainable Trade Initiative is currently exploring a scheme for supplier financing, with pilots soon to begin in India, Bangladesh and Vietnam. A fund will be set up to re-risk innovation and productivity investments for both garment and textile factories; an anchor investor has been secured, and the IFC will provide a first-loss guarantee. In Vietnam, IDH's Race to the Top programme has also worked with the IFC to organise investor forums, linking to local financial institutions through the Global Trade Supplier Finance programme

224. CDC (2013)

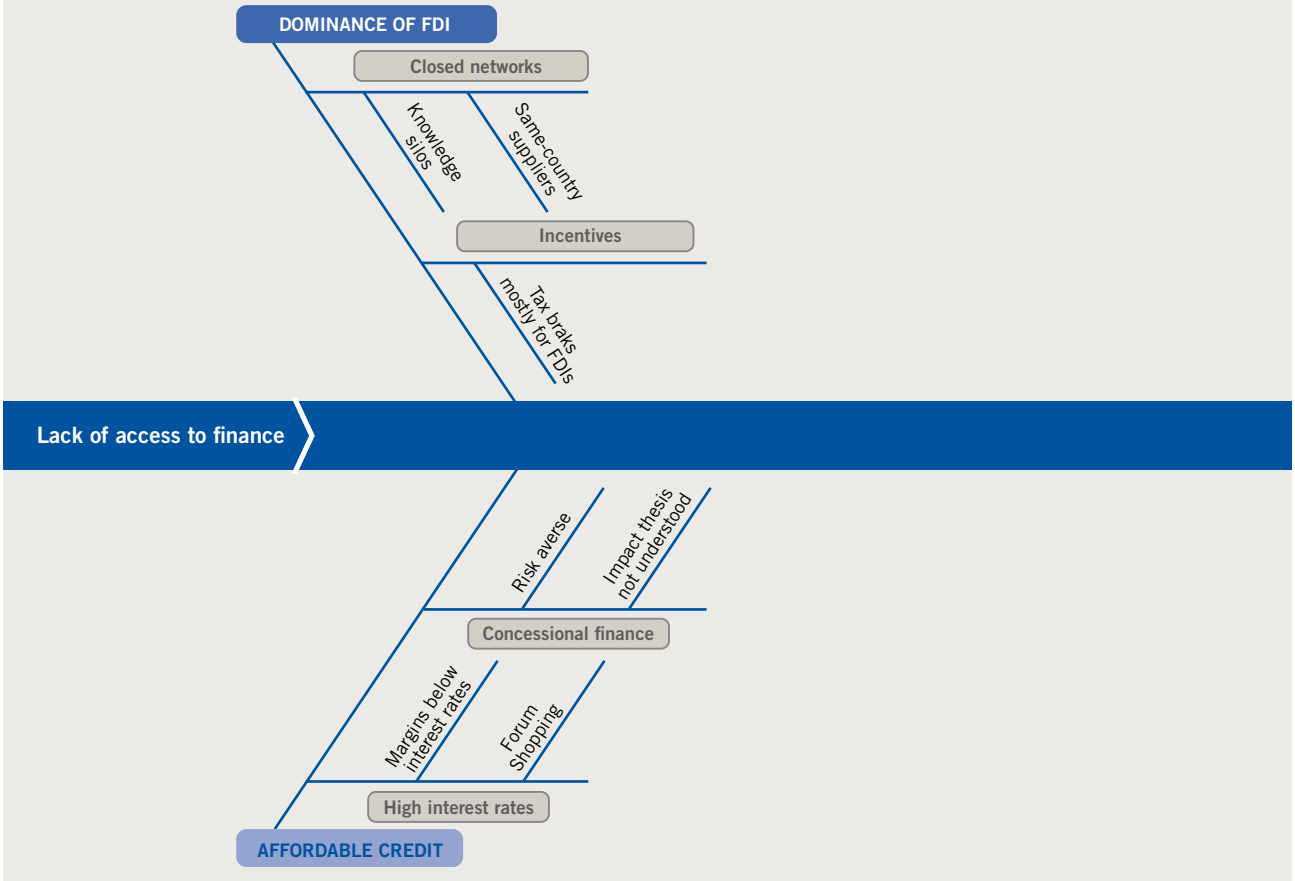
225. IndustriALL (2017)

2016[226]. Outside of Asia, as the CEO of a garment factory in **Liberia** that provides life and business skills to its women workers has said, an impact thesis related to empowerment and employment is a more difficult sell than creating a tangible product for the poor: "*There are a lot of impact investors that won't touch our company because the final product is …a pair of pants that is going to be sold in Macys"*[227].

Constraint conclusion:

Foreign investment can facilitate knowledge spillovers in the long-term, but 'closed' networks based on nationality may slow the pace of this upskilling. CMT suppliers (which are often domestic SMEs) need access to growth capital to upgrade, but often face significant challenges to accessing credit – not least high interest rates. This constrains working capital and creates a risk-averse attitude towards longer-term investments in working conditions. Development and 'impact' finance can help bridge the gap with a focus on environmental, social and governance (ESG) considerations, but significant private capital will need to be catalysed to achieve scale.

Figure 20:
Analysis of causes of lack of access to finance



226. Martin (2016). Exceptions include Unitus Impact
227. Alliance Magazine (2014)

5.4 ACCESS TO INPUTS

The extent to which suppliers can control textile sourcing is a key determinant of how much value they capture from the final retail product price. Textiles can make up to 70% of production costs, and without the ability to negotiate fabric and material prices, factories can only negotiate by adjusting their labour costs[228]. According to Friedrich-Ebert-Stiftung (2017), for example, the fabric for a denim shirt if purchased from a U.S-based manufacturer cost of $5/unit in 2013, but a Bangladesh supplier could buy the fabric for $3.3/unit from a different supplier (CNN 2013)[229].

A number of countries in Asia have therefore set out to develop backward linkages into the textile sector, such that clothing factories have easy access to nearby spinning, weaving and dyeing facilities. Over-dependence on imported materials leaves garment factories at risk of changes to trade patterns and tariffs, resulting in unstable supply and volatile prices. If imports are delayed, manufacturers may struggle to meet shipment deadlines. In **Bangladesh**, one of the two most common reasons factories breach contractual delivery dates are strikes that hamper transporting fabric from the port city of Chittagong to a plant in the capital city of Dhaka[230].

Taking control, however, does not always mean onshoring material production but being an OEM supplier who makes decisions about where and at what price to import inputs. The commercial case for a 'dirt to shirt' industry has been questioned since textile production is capital-intensive, employs relatively few people, and requires excellent infrastructure[231]. Textiles also need to be of consistently good quality: **Vietnam** imports almost three quarters of materials used in exported garments, and despite recent significant investments in upstream textiles (in anticipation of the TPP), Vietnamese fibres and MMF textile products are both too small in quantity and low in quality to satisfy the standards of the international fashion brands[232]. The same holds true in **Indonesia**, where domestically grown cotton is only able to satisfy an estimated 0.3% of the market.[233] Stakeholders suggested that the climatic conditions for producing cotton are not favourable and that much of the textiles produced with locally grown inputs develop mould, resulting in inconsistent quality. Dyes, yarn, and a variety of fabrics are also mainly imported, increasing production costs and reducing price competitiveness.[234] There is also no automatic connection between domestic sourcing of textiles and working conditions: **Sri Lanka** imports its entire fabric needs, and has one of the highest compliance rates in Asia, while **India** and **Pakistan** are largely-self-sufficient but have lowest compliance.

Textile production, above all, is extremely energy-intensive. The greatest environmental impact in the global garment value chain is found in 2nd tier suppliers and below, particularly through excessive water use if dyeing and finishing activities are not carefully controlled[235]. There is also more use of hazardous chemicals. While this presents a potential threat to the country's natural environment, the good news is that there are proven good practices in

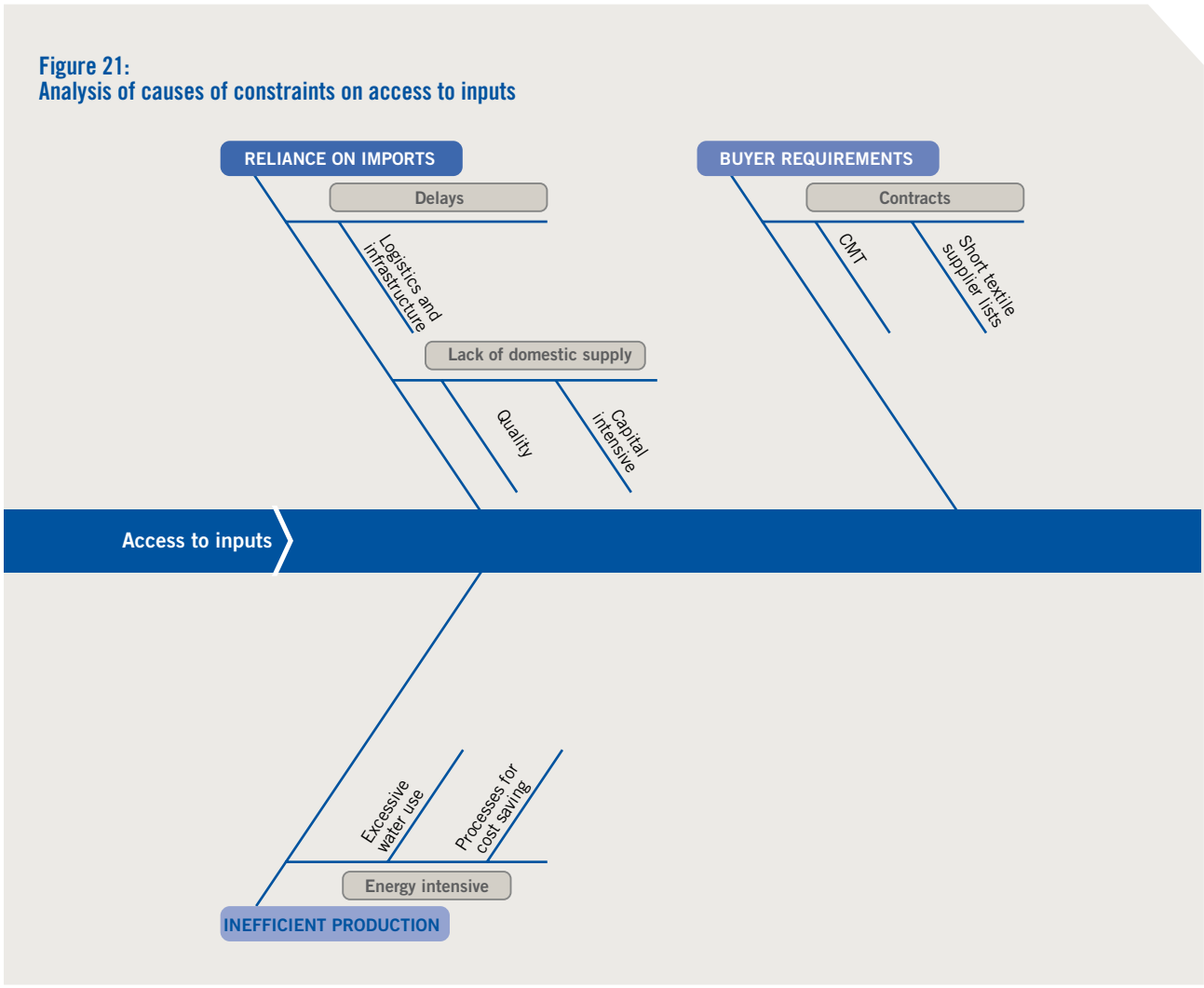
228. World Bank (2016) and Friedrich-Ebert-Stiftung (2017)
229. Friedrich-Ebert-Stiftung (2017)
230. SOMO (2015)
231. Flanagan (2014)
232. Friedrich-Ebert-Stiftung (2017)
233. Textile Outlook International (2016)
234. Interview with the Indonesia Investment Coordinating Board (BKPM)
235. Interview with IDH

sustainable manufacturing which can overcome many of the risks.

According to research, the typical South Asian textile factory "could save up to 20% of chemical inputs, 40% of energy, and 50% of water in their wet-processing operations—improving the environmental footprint without raising unit costs"[236]. In Vietnam, the *Race to the Top Initiative* is working to transfer best-in-class milling and dyeing practices based on NRDC's 'Clean by Design' programme in **China**. This includes energy efficiency, air emissions and wastewater treatment. The first three mills in the pilot programme in Vietnam have saved between $445,000 and $1.5 million in annual electricity, natural gas and water costs, with a predicated break-even on investment after 18 months[237]. However, there is little current coordination between the many brand and development agency initiatives to support energy efficient production. In **Vietnam** a vertically integrated manufacturer complained that such initiatives had led not just to overload (since there is an opportunity cost to participating) but also to overlap, since many programmes have similar content.

In **Indonesia**, government regulation (No. 70/2009) provides incentives for improved energy management, including tax deductions, import duty assistance, low-interest funds for investing in energy efficient machinery, and energy audit support.[238] Interviewed factories reported that

Figure 21:
Analysis of causes of constraints on access to inputs



236. Martin (2016)
237. Interview with IDH
238. International Energy Agency (2015)

energy efficiency gains did help to some degree compensate for some of the rising production costs, but that proper waste treatment and disposal generated additional costs. It is mandatory for factories to install wastewater treatment facilities, which third parties from the local government will pick up and dispose of for a charge. Buyers may demand monthly purity tests costing between 100,000 ("simple") and 1,000,000 IDR ("complex"), which are also incurred by the supplier. For solid waste, the factory pays certified collectors from the local environmental agency to pick up leftover material cuttings, but this can also be sold for a net gain to handicraft producers who convert the scraps to new products.

Constraint conclusion:

There are questions about the strength of the commercial, social and environmental case for developing backward linkages. At the same time, over-dependence on textile imports and those of other inputs can create barriers to upgrading. Textile production requires significant capital, good infrastructure and above all is energy-intensive. However, there are proven opportunities for significant efficiency savings that can reduce the environmental impacts of textile production and free up resources to improve working conditions.

5.5 LABOUR SUPPLY AND SKILLS

Garment production, by and large, requires a low-skill labour force. Indeed, the main reason for Asia's competitiveness in global garment production is the mix of plentiful labour supply, low wages, and high informality which makes even poorly-paid factory jobs attractive.

The Faustian pact, then, is that workers tolerate bad jobs as better than the alternative, but when they have had enough, businesses in turn tolerate a high turnover – because they can readily find new staff. While there is no doubt that vulnerability on the labour side has meant many businesses treat workers as a commodity, a number of emerging trends in labour supply and skills demand make the future direction less certain.

Turnover rates vary by country and factory – in **Myanmar** it is estimated at 8%, in **Bangladesh** at 10% and **India** at 12% per annum. Absenteeism rates are 4, 8 and 14%, respectively[239]. In **Cambodia**, some reports suggest nearly half of the workforce quits each year[240]. Such high turnover has been shown to reduce the incentive for factories to invest in their workers because managers do not expect workers to stay long[241]. Replacing these workers is not usually a problem. Eighty percent of workers are recruited to the factory floor with no relevant skills at all – they are trained on the job[242]. A sewing machine operator, for example, requires 4-6 weeks of training, with education up to primary level being more than sufficient[243]. Factories also do not have to expend much money or investment to find new staff: employee referrals and recruitment notices on the factory gates are the most common methods. Advertisements are only placed in local dailies to find supervisors, and occasionally head-hunters or recruitment agencies are used for senior management positions[244].

239. Business Innovation Facility Burma (2016)
240. 44%. Rodrigo (2017)
241. Better Work (2013)
242. Vietnam Chamber of Commerce and Industry
243. World Bank (2013)
244. Interviews with Better Work Vietnam

In **Vietnam**, however, growing labour shortages in major cities have become a hurdle to further expanding the garment industry[245]. The causes of such shortages are complex, but are thought to result from a combination of increasing wages, government policies to encourage factories to relocate to more remote provinces, and rapid development of other sectors (electronics, for example, has overtaken garments as the biggest foreign exchange revenue earner, largely thanks to recent investment from Samsung)[246].

There is also evidence that workers are becoming more discerning. In **Vietnam**, migrant workers who had moved to the industrial cluster surrounding Ho Chi Minh City are starting to move back to their home provinces, since workers prefer to stay with their families as soon as employment is available in their neighbourhood. Outside of Asia, a recent high-profile academic study of industrial employment in the **Ethiopian** garment sector found almost two-thirds of new workers quit within a year. What is more, workers went back to their previous livelihoods of agriculture, construction or selling goods in the market, which made them as much money, often with fewer hours and in better conditions[247]. Workers, however, remain largely ignorant about the risks or reality of factory work before they start. Even once they are on the factory floor they are unaware of their labour rights and are not always conscious of health and safety issues.

The truism of low-skilled labour demand is no longer holding true as factories start to compete on more than simply price. Increasingly, industry buyers are seeking to purchase a full service, from design to stock delivery, but "countries with low-skilled textile workers face difficulty to meet these demands"[248]. **Vietnam** is investing in management and design as part of a strategy to shift to more OBM and ODM production. There are a number of public – and increasingly privatised – vocational training centres in the major cities and provinces where workers can learn about cutting, sewing and other factory skills[249]. Yet demand for these courses is low. People enter the garment industry as a necessity, rather than as a career choice, and choose not to invest in vocational training in the same way as they would higher education. The quality of the training is also sub-standard: focusing too much on theory not practice, and with weak links to companies and few traineeship schemes[250]. In **Indonesia**, some factories reported having to retrain workers that came to them after completing the government-run training programme, which includes a traineeship, but due to varying levels of technological advancement between firms, there is typically a period in which new workers have to be trained to use new machinery. Finally, brand- and factory-specific technical requirements mean that workers will often still need additional on-the-job training even if they have a formal certification.

Skills upgrading will be vital as the industry modernises and many of the traditional, entry-level jobs, held mostly by women, might be lost. The use of intelligent technologies – the so-called Fourth Industrial Revolution – means that workers will

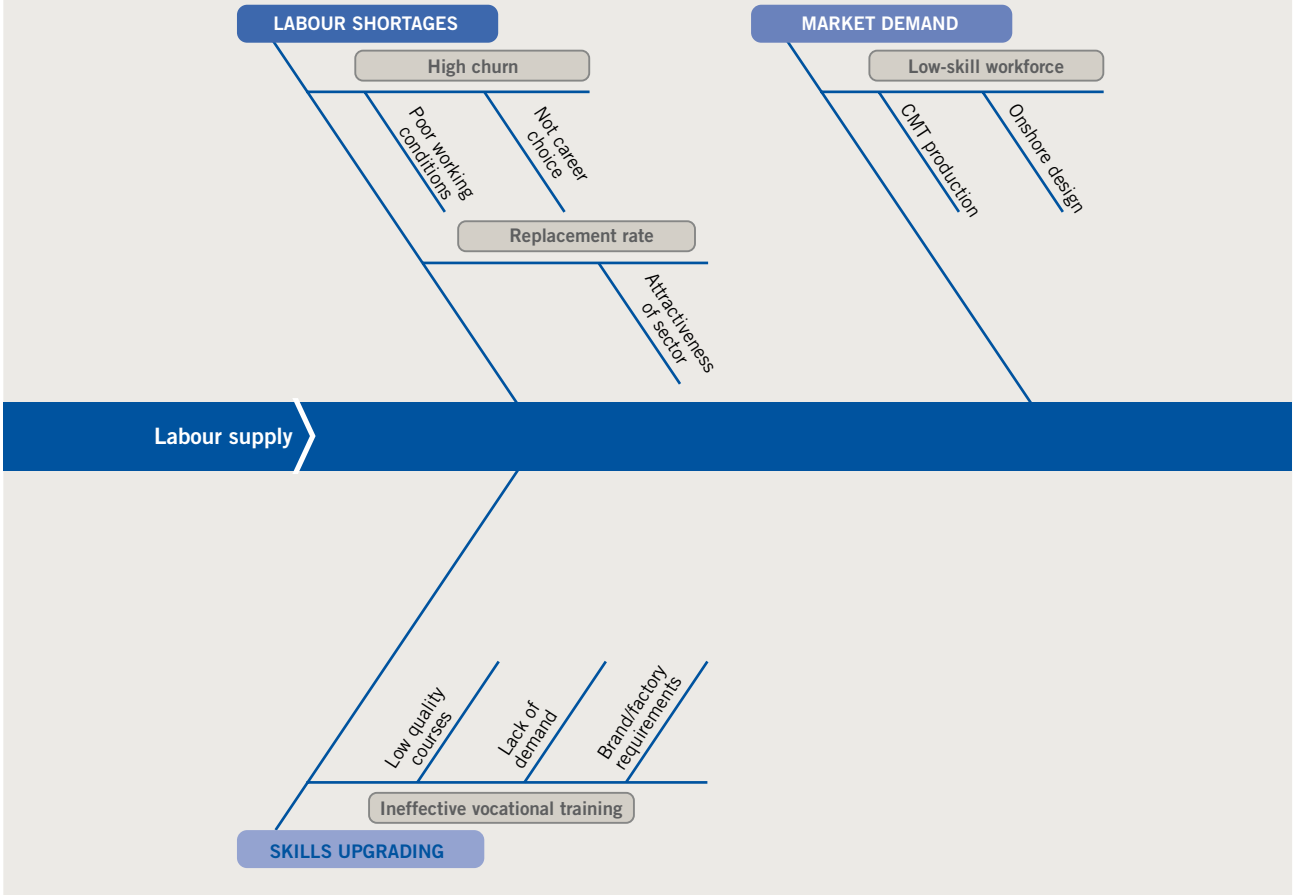
> ***"I actually have never read my labour contract…only when I have some problem…same with other documents…I believe my colleagues do the same…we are struggling with more than 10 hours at work before going home with family…we don't have time"***
>
> **Experience of an embroidery worker in Vietnam (Source: RespectVN)**

245. Wage Indicator (2016)
246. Vietnam Chamber of Commerce and Industry
247. Blattman and Dercon (2017)
248. ILO (2016)
249. For higher skilled design and management roles there are also polytechnic universities, some of which have entered into partnership with garment factories for internship programmes
250. Training is also not rewarded: In Vietnam, workers with a vocational certificate can expect to earn a 5% salary premium for his or her qualification. However, this same premium is given to workers after completing on-the-job training, which takes around 6 weeks, during which they will have also been paid a salary (and not have to pay for training).

no longer be required to control machines[251]. The ILO recently calculated that 85% of jobs in **Vietnam's** textile, garment and footwear sector are vulnerable to being replaced by robots (the figure is 65% in **Indonesia** and 88% in **Cambodia**). The Chairman of Vietnam's textile and apparel association (VITAS) has estimated that a textile factory now employing 450 workers would require just 30 labourers to accomplish the same production volume. The precise impact of mechanisation will vary along the supply chain, with the highest value-added segments, such as design, being more impervious due to the need to be sensitive to intangibles such as changing consumer fashion tastes. In Vietnam, stakeholders worry that the speed to adapt to new technology of the garment industry is slow, and the upskilling of workers to meet these changing needs will take many years[252].

However, a lingering concern is whether the global market demands wholesale upskilling. While brands are looking for capabilities for higher-quality technical production, they continue to need a base for low-price bulk-order production. Indeed, this is the very reason that buyers offshore production in the first place. Buyers have historically been unwilling to push for upgrading skills in any given country as they have so

Figure 22:
Analysis of causes of constraints on labour supply



251. Vietnam News (2017)
252. Interviews with VCCI, CSR experts and VINATEX

many options to move "new investment to different countries...rather than upgrade in an economy where they already operate"[253]. "The main challenge of small companies here are human resources…As a (unnamed brand) manager, I was often sent to a workshop overseas. They give opportunities to everyone in the company to grow, however, many locals don't see the opportunities."[254] Buyers and agents have flexibility to exit to lower-cost destinations within (and outside of) Asia. In **Vietnam**, some foreign-owned enterprises are looking to relocate because of rising labour costs, and see domestic firms upgrading to FOB as a competitive threat.

Constraint conclusion:

Garment production continues to be a low-skilled, labour-intensive industry. While turnover rates are generally accepted as a 'cost of doing business', in some contexts, this can stunt growth. Both buyer demands for full service production and the potential use of intelligent technologies emphasise the importance of upskilling the workforce. However, vocational training is not widely demanded, and the quality of supply is generally low. Professional recruitment services are not developed, and the market capacity to absorb a wave of more skilled workers is uncertain.

5.6 POLICIES

Trade agreements play important roles in shaping national garment industries, both in terms of products (specialisation and material sourcing) and markets (export destinations). **Vietnam's** Bilateral Trade Agreement with the USA in 2002 and accession to the WTO in 2006 led to garment exports growing at double digit rates for almost a decade. Vietnam was due to be a major beneficiary of the Trans Pacific Partnership (TPP), which is now considered defunct following the withdrawal by the United States. The TPP contained comprehensive clauses on tariffs, investment, intellectual property rights, labour and environmental sustainability. It also included a 'yarn forward' Rule of Origin (ROO), which required TPP nations to use a TPP member-produced yarn to receive duty-free access for the eventual apparel product. While on paper Vietnam remains committed to TPP-related reforms (including freedom of association), in practice, key informants said that reforms were effectively frozen. Investors are on a cautious footing and not making further investments into backward linkages.

In lieu of the TPP, **Vietnam** is now seeking to pursue a bilateral free trade agreement with the USA. However, the threat of a protectionist trade strategy from the new U.S. administration – and with it the possibility of higher import tariffs – is a risk to Vietnam's garment sector, given it relies on the USA as the top export destination[255].

253. Better Work (2013)

254. Interview with an ex-brand manager (anonymous).

255. Credendo (2017)

In contrast, **Vietnam** has successfully negotiated a free trade agreement with the EU (EVFTA), which is due to enter into force in 2018. This has been called the most "ambitious free trade agreement the EU has thus far concluded with a developing country" and eliminates at least 90% of tariff lines of Vietnam's exports to the EU, including duties for some textile and garment products over a 5-7 year period[256]. Instead of a strict 'yarn forward' ROO, the EVFTA includes a double transformation rule, meaning the production steps of weaving and sewing need to be carried out in Vietnam to benefit from customs advantage. This is intended primarily to prevent China from obtaining duty-free access to the European market for its textile products by way of indirect access via Vietnam, but to allow Vietnam to import fabrics from South Korea (largest source of imports, including textiles)[257]. As a result, Vietnamese exports of textile, clothing and footwear to the EU are expected to more than double by 2020 because of the FTA – potentially leading to a significant reshaping of export markets[258].

For **Indonesia**, a Framework Agreement on Comprehensive Partnership and Cooperation (PCA) with the EU entered into force in May 2014, providing the legal framework for different policy fields and the basis for higher level engagement and bilateral relations. In 2016, negotiations for a free trade agreement (CEPA) were launched, which are expected to come to a head in 2019.[259] According to the president of the Indonesia Textile Association (API), the FTA could triple Indonesia's garment and textile exports over the next five years.[260] The EU intends to gradually work towards a future EU-ASEAN agreement. [261] A Trade and Investment Framework Agreement (TIFA) between Indonesia and the U.S. was formed in 1998 as a forum to discuss trade and investment, but a free trade agreement has yet to materialize.

Within the region, **Indonesia** has formed bilateral trade agreements with Japan (Japan Economic Partnership Agreements), which came into effect in 2008, leading to tariff cuts on over 92 percent of goods, and Pakistan (Pakistan-Indonesia Preferential Trade Agreement), which came into force in 2013, leading to preferential tariffs on over 200 products. As a part of the ASEAN Free Trade Area, Indonesia enjoys zero tariffs on the majority of goods traded between members. ASEAN trade agreements affecting Indonesia include those with China (ASEAN-People's Republic of China Comprehensive Economic Cooperation Agreement), Australia and New Zealand (ASEAN-Australia and New Zealand Free Trade Agreement), India (ASEAN-India Comprehensive Economic Cooperation Agreement), Japan (ASEAN-Japan Comprehensive Economic Partnership), and Korea (ASEAN-Korea Comprehensive Economic Cooperation Agreement).[262]

National policies provide the enabling environment which allows a country's garment sector to thrive. Access to infrastructure, skills and investment are – as has been shown – important determinants of how companies are able to economically upgrade and add value. In **Vietnam**, the Socio-Economic Development Strategy (SEDS) is a master plan that governs Vietnam's industrial policy framework for ten years. Monetary

256. Friedrich-Ebert-Stiftung (2017)
257. Friedrich-Ebert-Stiftung (2017)
258. Working conditions are less integrated into the EVFTA, as they were thought to be covered by the TPP
259. European Commission (2017)
260. Rodrigo (2016)
261. European Commission (2017)
262. Global Business Guide Indonesia (2016)

policy on inflation and interest rate targets provides important incentives (or dis-incentives) for foreign investment and domestic borrowing; while fiscal policy and stimulus packages can develop sectors and supporting services. However, industrial policy has largely been reactive – to respond and prepare *within* countries for wider international trade agreements (such as Vietnam investing in domestic textile production). The competitive environment for garment production, particularly *between* countries, remains driven by market forces and multi-sectoral trade agreements[263].

In **Indonesia,** the government encourages greater exports in bonded zones by offering tax free imports of raw material if the factory exports one hundred percent of its production. The government is also seeking to ease the administrative burdens for entrepreneurs. MOT Regulation No. 08/2017 was recently passed, waiving fees for company registration certificate renewal,[264] which was flagged by an interviewed agent to be especially helpful for smaller companies.

In terms of skills, the **Indonesian** government also sponsors a vocational training programme for high school students, *Sekolah Menengah Khusus*, to help them transition into the workforce. For garments, this includes a practical internship traineeship in which students get hands-on knowledge. Factories can then hire them directly once they have graduated. For older workers wishing to develop new skills, the *Balai Latihan Kerja* training school exist, also provided by the government[265].

5.7 SPECIAL FOCUS: GENDER

Economic empowerment can only happen if both women and men are able to participate in, contribute to, and benefit from, growth in a way that recognises the value of their contributions[266]. As most workers in the garment industry are women, and because of inequitable social outcomes, brands and civil society have paid significant attention to gender-specific workplace policies and practices. However, this external pressure has led to a 'compliance culture' in some factories, where measures are introduced to ensure boxes are ticked on audits, rather than truly addressing the discrimination and barriers to decent work.

One example of this is the buyer-mandated mother's rooms, which aim at accommodating breast feeding women. However well-intentioned the policy, in many contexts, mothers do not bring their babies to factories as the infrastructure does not exist to ensure that children are looked after – and as a consequence "mothers' rooms…are either locked and left to collect dust or used a store rooms"[267]. Encouraging mother-friendly workplaces, in contrast, would mean incentivising suppliers to provide childcare facilities, and providing for longer maternity leave.

While garment factory work can provide the wages which are critical to livelihood coping strategies, there are questions about the extent to which it can increase women's agency – the power to think and act freely and exercise choice. Academic literature shows that while factory work for global markets can open up important income-earning

263. ERC (2017)
264. Indonesia Company Law (2017)
265. Interview with the Ministry of Industry (2017).
266. OECD (2017)
267. Yap (2017). Instead, once their maternity leave ends, women generally leave their babies at home with their grandparents

avenues, it also creates new forms of gender subordination: For example, "though some women may gain greater autonomy from male members of their household, female employees' subjugation to male factory managers and employers may intensify"[268]. In **Vietnam**, Better Work's baseline analysis found that women who were more highly educated tended to be more dissatisfied and vocal about concerns with wages and career aspiration. Women are less likely to be promoted or receive training than men: Despite women being employed, on average, at the same factory longer than men, less than 14% of women have been promoted compared with about 25% of men[269].

The glass ceiling creates a self-perpetuating cycle where women are less likely to be promoted due to entrenched gender, cultural and social norms. In **Vietnam,** more women than men list the relationship with their supervisor as the main obstacle to promotion[270]. This, in turn, increases the chances that the predominately male management fails to address the gender-specific needs of their workforce. A 2015 survey found that female workers have distinctive issues such as high rate of gynaecological diseases due to limited toilet breaks and poor hygiene – especially for pregnant workers – and the lack of representation of female workers on the board of the enterprise unions[271].

BOX 1: SELECTED PROGRAMMES DEALING WITH WORKPLACE AND COMMUNITY EMPOWERMENT

BSR is a global non-profit business network and consultancy for sustainability. The BSR aims at increasing awareness of basic health issues among female factory workers with the objective of bringing the knowledge back to their communities. Factory workers are trained as so-called Peer Health Educators and they then teach their co-workers. Modules cover topics such as waterborne diseases, nutrition, reproductive health etc. Each module begins with an informative portion, and then goes through preventative methods and proper treatment of the symptoms.

A leading Asia-based agent has started to pilot ways to leverage smartphone technology to improve worker engagement. Through an app, workers not only have access to digitalised human resource tools (such as the ability to request and track leave), but they can also access a range of e-learning materials concerning women's health. The agent is also able track worker satisfaction (and address issues before they escalate) as employees can use 'emojis' to indicate how happy they are with the work environment.

Outside of Asia, a garment factory in Liberia exclusively employs women, most of them internally displaced people (IDPs), using a social enterprise approach. The 300 employees are provided with both business and life skills training and encouraged to start their own micro-enterprises. Two other factories in the country have now started to copy the model.

268. Fontana and Silberman (2013) citing Elson and Pearson (1981)
269. Fontana and Silberman (2013)
270. Fontana and Silberman (2013). Statistically significant at 38% compared with 31%
271. ERC (2017): The 2015 survey was conducted by Marie Stopes International into 9 footwear exporting firms in the South of Vietnam

Addressing the barriers to advancement is critical since women often occupy the lowest-skilled roles in garment production, such as sewing, which are most vulnerable to automation and the 'fast fashion' search for ever-lower-cost sourcing destinations. Box 1 sets out a number of programmes that have started to address empowerment issues – the challenge now is to mainstream these across the sector, and move beyond compliance to gender-responsive business practices.

PART 3
Market systems solutions

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PART 3 Market systems solutions

6 ECOSYSTEM INFLUENCERS

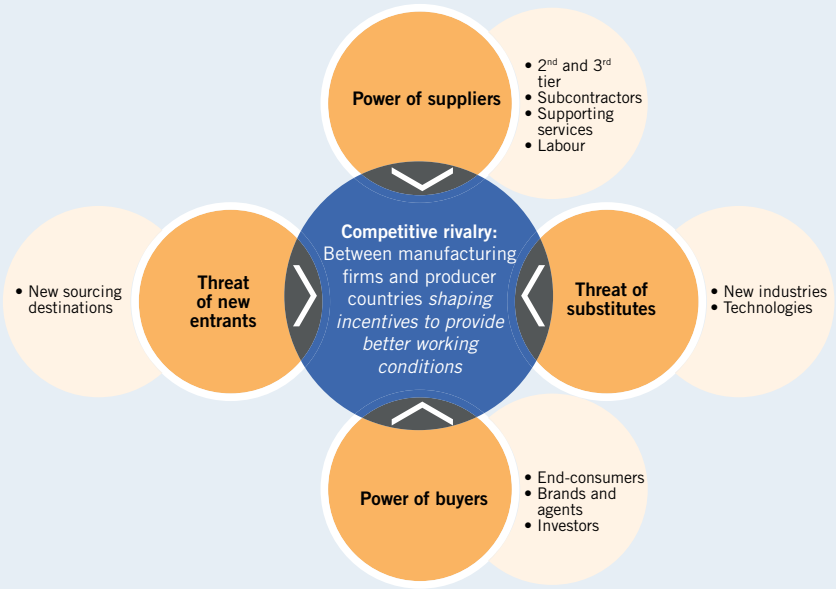
This section focuses on the challenges and opportunities for a regional programme on decent work in the garment sector in Asia. To achieve sustainable impact at scale on the conditions for millions of workers, it will be important to address the structural barriers – including to supply chain transparency, improved buying practices and human resource management – standing in the way of better business and social performance.

Market forces will not eliminate 'low-road' practices in the garment industry, and in many instances are themselves the root causes of workplace abuses[272]. Systemic solutions seek to make a contribution to overcoming such private and public failures through better cooperation, knowledge sharing and partnership coherence. We start by depicting the 'ecosystem' influencing garment manufacturers, before setting out possible options for regional collaboration.

272. Tufts (2016)

Measures to incentivise garment manufacturers to provide good working conditions can be deployed by a range of different stakeholders. Pressure for change may come from competitor rivalry, from suppliers, buyers and end-consumers, or from market dynamics such as the threat of new entrants and substitutes. **Figure 23** visualises the actors and factors shaping the competitive environment for garment production, based on Porter's five forces, a common business analysis tool. What follows is a brief summary of the likely leverage points for positive change that can be harnessed at the regional level.

Figure 23:
A graphic representation of Porter's Five Forces for working conditions in Asia's garment industry



Competitive rivalry

Garment manufacturing companies operate in an atmosphere of intensive competition. Product differentiation is low and firm concentration is high – resulting in a scenario of almost pure competition where profit margins are eroded away. However, and perhaps because of the industry's nature, rival firms do collude to maintain aspects of industry competitiveness. In Vietnam, for example, companies coordinate with each other to prevent the spread of wildcat strikes and prevent wage competition[273]. This can take place through informal networks based on geographic location (in the same province) or ownership structure (same nationality), or through formal dialogue in **business associations** and **foreign chambers of commerce**, although there is little connection between country activities, and they lack capacity and voice.

At the country-level, **national governments** have been largely unwilling or unable to regulate the garment sector, in part recognising that they are in direct competition with other countries for market share. However, government policies play important roles in shaping the business environment, not least on minimum wages and the infrastructure and finance required for domestic firms, in particular, to move to full service production. The implication of such policies on social outcomes is not always considered: such as the interplay between different aspects of working conditions – with evidence that wage gains can be offset by backpedalling on safety and health measures – or the link between the various types of economic and social upgrading.

The **general public** in producer countries has had limited interest and influence on working conditions practices. However, this may change as the ease of communication and connectivity increases[274]. Workers are growing more aware of which factories have a bad reputation for providing poor conditions, increasing the incentive for workplaces to reform to attract new workers. To-date, this has relied on word of mouth rather than more explicit

273. ERC (2017)

274. Such as through mobile phones, and particularly smartphones. Social marketing and awareness campaigns have been rolled out in emerging economies to address a variety of social policies, but so far used to limited degree for worker awareness activities

'name and shame' information or rating systems, accessible to potential employees to help them make more informed decisions about where to choose to work.

- Assessment of leverage: *Medium.* Intense competition has resulted in some firms colluding to maintain competitiveness (and ensure a ceiling on working conditions and wages); while national governments struggle with both the incentive and capacity to enforce standards.

Threat of new entrants

The pressure to drive down prices means there is the ongoing threat posed by new **lower-cost sourcing destinations**, both within Asia (like Myanmar) and globally. This creates a sense of constant competition – where national garment industries have to upgrade to survive; to 'step up' just to 'hang in'. Agents, in particular, have networks of factories across the region, and are prepared to shift sourcing locations based on hard-nosed commercial decisions. In Vietnam, for example, despite extensive and long-standing investment into the country, Korean firms are reportedly looking for alternatives as Vietnamese labour costs are rising faster than productivity[275]. Individual garment manufacturers are largely unsighted of these macro-level trends, thinking more about meeting shipment dates and next quarter performance, rather than with a longer-term lens.

At the firm-level, the extremely low barriers to entry to become a **new garment manufacturer** – which in most basic form requires a few sewing machines – mean there is always the threat of new entrants to the market. However, these entrants largely service local and regional demand, with very few able to access the networks and investment to export[276].

- Assessment of leverage: *Medium.* Economic upgrading is essential just to maintain market share; and with wages in Asia likely to further rise, the success of a country's garment industry will be determined less by low-road strategies and more by the ability to transition to higher-value added segments of the supply chain.

Threat of substitutes

While global demand for readymade garments is unlikely to decline anytime soon, at both a regional and country level the emergence of **new industries** can affect both public policy attention and labour supply. As has already happened in many countries in Asia, when economies develop they diversify and drop garment production – shifting to higher value-added manufacturing and service industries[277]. In Vietnam, the electronics sector has now overtaken garments as the biggest foreign exchange earner, and is attracting workers who may have previously sought jobs on the factory floor. While this may be an incentive for factories to provide better benefits to retain and recruit workers, any gains are likely to be offset by the decrease in labour demand caused by **mechanisation**, and the (likely) eventual replacement of unskilled manual labour by intelligent technologies.

- Assessment of leverage: *Low.* Longer-term trends in mechanisation and shifting consumer tastes are unlikely to influence incentives for better working conditions in the short- to medium-term.

275. No alternative viable destinations have yet emerged
276. Aside from intermittent subcontracting
277. Hong Kong and China

Power of suppliers

In a buyer-driven value chain, suppliers have very little power. Suppliers of **raw materials** (3rd tier), **components** (2nd tier) and **subcontractors** do not exert influence on the 1st tier, either because these transactions are pre-determined by buyers, or because substitute suppliers can be easily found. Excess labour supply has traditionally been the source of Asia's comparative advantage in the garment sector, leaving individual workers with little bargaining power. However, as **labour** is one of the key cost components that garment manufacturers need to control and manage to turn a profit (and meet order obligations), workers can exert strong influence – particularly through strikes which halt production. This leverage point was explored by a simultaneous ILO study on industrial relations and thus has been omitted from this study.

- Assessment of leverage: *Low-Medium.* Suppliers are uniquely disadvantaged in terms of their influence on the chain, but given the importance of labour, there is potential to strengthen mechanisms for self-organisation and autonomous action that can influence working conditions from the bottom up.

Power of buyers

As the dominant group in the value chain, significant attention has been placed on the way in which brands play a controlling role in shaping incentives for garment factories to provide good working conditions. But what influences brand behaviour? Many **brands and agents**, in line with overall movement towards responsible business, have 'baked in' social responsibility as an intrinsic part of the way they do business. As Li & Fung observe, the days of shopping around for simply the lowest-cost are over: "today, sustainability is just as important as product price and quality – maybe more"[278]. Brands are seeking to reflect ethical values as a part of their product and company, proactively embracing closer collaboration with factory and worker communities[279].

Part of the reason for this is that **end-consumers** tend to view brands as responsible for the products, irrespective of how they actually manage their supply chain, and who actually made the clothes[280]. This is thought to appeal particularly to new market segments such as millennial customers, who make consumer decisions based on factors beyond simply quality, price and fashion. However, there is evidence the "reason that brands are so focussed on labour standards is not really about the ultimate consumer"[281]. In fact, while there is a growing number of people who are aware of the origin of their clothing and will make purchase decisions accordingly, this does not apply to the majority of consumers. Exports from Bangladesh to the USA actually *increased* after the Rana Plaza disaster; there has not been any concerted consumer action (such as large-scale boycotts) which has led to changes in business models; and fast fashion labels have recorded record sales, despite the negative media stories. Consumers are simply not aware of, or not prioritising, social considerations. The end-consumer ethical pressure also tends to come from European or American markets, with the rest of the world – and some of the fastest growing apparel retail markets,

278. Sourcing Journal (2015)
279. Sourcing Journal (2015)
280. J. Safra Sarasin (2014)
281. Business Innovation Facility Burma (2016)

such as India – significantly less focused on ethical buying.

Instead, brands are very attuned to **civil society** attention – from NGOs and rights groups – not only because it helps shine a light on possible poor practices in their supply chain, but because they come under investor pressure to act. **Investors** are much more aware and sensitive than consumers, both due to environmental and social criteria which are often obligatory to report on to institutional clients, and because of the impact of negative events on returns[283]. Investor research has found that in a sample of three clothing brands, after news broke of 'controversial events' (including factory accidents, failure to comply with standards and sourcing from controversial countries, such as cotton from Uzbekistan), over one third of the time (37%) the brand's share price dropped over a 2-4 week period compared to the sector index[284]. They conclude that negative events can have a negative impact on the enterprise value, even if this valuation is also influenced by a variety of other factors, and in the long run, it means the "company is not only likely to be operating at a disadvantage (through damage to its image and brand, for example), but also risks missing out on a number of clear benefits, such as greater flexibility and efficiency in production." Shareholders in garment brands – the vast majority of which are publically traded companies – have both a commercial case and a fiduciary obligation to mitigate supply chain social and environmental sustainability risks[285].

- Assessment of leverage: *High.* Garment production is a buyer-driven chain, and incentives for working conditions start from the top down. Buyers are most likely to respond to civil society and investor actions, rather than consumer pressure.

Table 16:
What investors can ask brands to do[282]

Working condition problem	Investor recommended action
Mass fainting of workers	Provide snacks and canteen on site, as well as free seated transport to work
Deaths through fires	Insist on better audits that include offsite worker interviews, increase safety training
Child and forced labour	Invest in deeper unannounced audits and never send solo auditors; join industry collaborations
Worker strikes	Use balanced scorecard to reward factories that balance a decent wage with price, quality and shipping time; support capacity building in factories

282. Larsen (2013)
283. Business Innovation Facility Burma (2016)
284. MSCI Consumer Discretionary Index, from J. Safra Sarasin (2014)
285. http://investsnips.com/list-of-publicly-traded-companies-with-apparel-brands/

PART 3 Market systems solutions

7 REGIONAL INTERVENTIONS

The below four ***components can be considered for inclusion in a regional programme on Decent Work in the garment sector*** in Asia. They are based on:

- A recognition that the intense focus on Asia's garment industry has resulted in a multitude of initiatives; so any new activities should add value to existing platforms rather than create new ones.
- The need to go beyond the 'tip of the iceberg' and reach the lower tiers of the supply chain, which is where the most precarious working conditions can be found.
- An established framework for sector collaboration, set out by the OECD, which calls for pooling knowledge, increasing leverage, and scaling-up effective measures across the region.
- The conclusion of the previous section that buyers have the greatest leverage and incentives to drive decent work improvements, and that they, in turn, are most likely to respond to civil society and investor actions.

Component 1. Pool information

Many enterprises in the garment sector source from the same countries and suppliers. They therefore face many of the same challenges to improving working conditions, environmental sustainability and gender equality.

Sharing information can help increase the awareness of specific risks in the sector and bring attention to emerging risks – and opportunities – more quickly than would be possible for most individual enterprises. Good data are essential to help highlight problems that several countries share, and provide the platform to explore where solutions best can be found in regional cooperation.

Activities include:

- **Regional statistical benchmarking.** Develop standards for comparable data on decent work in the garment sector. Recognising that there will always be limitations on data availability, this should be an action-oriented rather than an academic exercise, engaging buyers, national stakeholders (governments, employers and workers) and multi-stakeholder initiatives to explore what information sources and definitions will be acceptable to reach a common understanding of region-wide challenges[286]. This could result in the development of an authoritative public database to serve as a reference point for interested actors. At the moment, the difficulty in separating data fact from fiction hinders both the identification of issues, and effective action to address them. In Bangladesh, for example, the widely-reported figure that 80% of the garment sector workforce are women is likely incorrect; the number is now closer to 60%. As a result, initiatives have continued to focus on gender mainstreaming measures, rather than also seeking to understand why women are transitioning out of the sector[287]. A global sourcing representative of one brand said that having a central database of information would be key to improving private regulation and allowing local enterprises to adequately self-regulate[288].
- **Share the business case**. Compile the business cases for working conditions, environmental sustainability and gender equity into an open-source repository. This would help transition from anecdotal 'case studies' towards a coherent regional dataset that would be of sufficient size and rigour to capture buyer and investor attention. Putting business cases – as far as commercially allowable – in the public domain would also help improve coordination, mitigate the risk that resources are spent 'proving' very similar cases, and expose them to valuable third party review and critique. The repository (hosted by a body such as the ETI or SAC) would need to quality assure the data to ensure adequate reward, risk and costs coverage to allow decision-makers to clearly understand return on investment calculations. This would also not be a single generic business case – but broken down by aspect of working condition (wages, gender, overtime etc.) or sustainability. This could also provide the launchpad for a debate on how 'strategic investments' (i.e. donor or philanthropic subsidies) could help unlock (or distort) the business case[289].
- **Understand the audience for evidence.** Agree on a framework to understand what evidence will be most persuasive for different types of brands, investors and factories. Enterprises respond in different ways to evidence about the benefits of moving 'beyond compliance' depending on their organisational structure, business model and culture. At the moment, there is a limited under-

286. While brands have often expressed a willingness to share data, few end up doing so. The Fair Factories Clearing House and SEDEX, despite being widely used, have limited datasets. This component should carefully consider how trust and data reliability barriers to information sharing can be overcome.

287. The ILO and UN Women are currently commissioning a study to understand why women are leaving jobs in Bangladesh's RMG sector.

288. According to interviews, the SAC is already working on how to do this (trying to develop the tools and agreements on accountability, transparency, who is responsible, etc.)

289. Including admitting where no business case exists

standing of the factors that make some enterprises more amenable to evidence than others. Yet there is growing recognition that to influence social outcomes we not only need to collect evidence, but to also ensure the evidence is *relevant and persuasive* for those we want to influence[290]. Just as programmes like Better Work are moving to provide differentiated services to factories depending on their size and supply chain tier, evidence should be differentiated based on what 'stage' an enterprise is in its journey towards social responsibility. A sample framework is included in Table 17, below, based on work that AccountAbility conducted with Nike. This framework could be further refined by value chain role (buyer/supplier), type of product (CMT, FOB), and tier – as well as type of business model (Type A or B).

Component 2. Increase leverage

Leverage refers to the ability of stakeholders to influence buyer behaviour. Stakeholders can be public programmes, or other enterprises in the chain – both suppliers and buyers who influence other buyers. There are many reasons why individual enterprises may lack leverage on their own, such as a small size or relatively insignificant buying power. Where a single enterprise lacks leverage, a group of enterprises operating together may wield greater leverage by participating in forums or seeking alignment of their activities, timelines and follow-up measures.

Activities include:

- **Engage buyers on responsible sourcing.** Build the capacity of NGOs, workers' organisations, and investor and business associations to address the buying practices that ultimately drive many of the working conditions

Table 17:
Five stages of corporate responsibility (Adapted from Zadek, 2006)

Stage	What organisations do	Why they do it	Most persuasive evidence
Defensive	Deny practices, outcomes, or responsibilities	To defend against attacks on their reputation that in the short term could affect sales, recruitment, and the brand	Focus on risk aversion and the costs of non-compliance (unlikely to respond to opportunity-based evidence)
Compliance	Adopt a policy-based compliance approach as a cost of addressing ongoing reputation and litigation business risks	To mitigate the erosion of economic value in the medium-term	
Managerial	Embed the societal issue in their core management processes	To mitigate the erosion of economic value in the medium-term and to achieve longer-term gains by integrating responsible business practices into their daily operations	
Strategic	Integrate the societal issue into their core business strategies	To enhance economic value in the long-term and to gain first mover advantage by aligning strategy and process innovations with the societal issue	Focus on opportunities to gain a competitive edge (productivity, worker satisfaction) and embrace more sophisticated models of 'shared value'
Civil	Promote broad industry participation in corporate responsibility	To enhance long-term economic value by overcoming any first mover disadvantages and to realize responsibility gains through collective action	

290. Uraguchi (2017)

deficits[291]. This could include training and information sharing about: How to meaningfully participate in buyer forums; good practice models that weight sourcing criteria of cost, quality, labour and environmental concerns; strategies to overcome commercial confidentiality and anti-trust considerations; and language to use with more commercially-minded non-CSR units in brands, such as their sourcing and merchandising teams. Collaboration would build on successful country cases, informed by the work of initiatives such as Better Work and Better Buying.

- **Replicate sub-regional models**. Encourage adoption across the sector of methods and models that have proven successful at a sub-regional or country level in extending compliance to 2nd tier suppliers and subcontractors. On paper, brands are held responsible for conditions along their whole supply chain, but putting this into practice has been a challenge, so brands are seeking solutions to help manage risk in their lower tiers. The Hong Kong-based *Apparel & Footwear Brand Coalition Forum (AFBCF)*, for example, is a network of around 20 brands that convene periodically to engage on social and environmental sustainability. The AFBCF is currently taking the initiative to share how respective brands define their subcontractors, and has completed a mapping to identify the top 10 fabric mills they collectively source from – as initial steps to explore how to extend social responsibility to 2nd tier suppliers[292]. Regional replication could be encouraged through either direct (engagement with stakeholders in selected countries) or indirect methods (case studies, promotional materials etc.).

Component 3. Scale-up successful measures

Collaboration can help play a role in scaling-up solutions (e.g. policy, training, capacity building, etc.) that have been demonstrated to be effective. Scaling-up can also crowd-in SMEs who may have more limited resources and are more risk-averse to initially investing in pilots.

Activities include:

- **Accelerate the journey from seed to scale.** Scan the market to see which pilot programmes are addressing systemic constraints, and provide a platform to discuss their success – then sharing and disseminating proven solutions across the region[293]. This could include building on a range of current programmes such as Better Work, the ACT initiative on living wages, NRDC's 'Clean by design' programme on environmental sustainability and the ILO's SCORE programme for productivity and working conditions in SMEs. Topics for future innovation could include:
  - Digital HR management / worker engagement platforms
  - Gender-responsive workplace practices
  - Providing job seekers with information about working conditions in factories [294]

291. Better Work already offers training for buyers (through the Better Work Academy) in countries where the programme is not active
292. AFBCF is a private forum, but frequently invites NGOs and multi-stakeholder platforms to talk about their work. As a buyer-driven initiative, it has been successful in engaging other business units within brands, and Sourcing Directors have attended meetings.
293. This could include the possibility of using seed funding to replicate solutions that have been proven in one country context to another
294. Rodrigo (2017): "This could help reduce recruitment costs for well-managed factories while increasing recruitment costs for poorly performing plants"

- Methods to formalise the recruitment process (demand-supply intermediation)

Component 4. Increase sector transparency

Collaboration can help facilitate the disclosure of aggregate information that increases the transparency of the sector. Making information public about suppliers, compliance assessments, and any corrective action(s) taken not only shows how brands are making demonstrable progress, but also allows third parties to independently verify and observe how working conditions are improving.

Activities include:

- **Supercharge supply chain transparency**. Encourage the spread of common standards for the public disclosure of supplier lists and real performance data. As has been shown, transparency is critical to extend social outcomes to upstream suppliers and process subcontractors. But some brands face challenges in understanding the full extent of their true supply chain. The regional programme could explore how to accelerate the uptake of – and build on – the *Transparency Pledge*, a set of minimum standards for supply chain disclosure drawn up by the Civil Society Coalition[295]. This could include measures to draw on good practice from other global supply chains (such as electronics, and Apple Inc.'s decision to publish hours of work performance of supplier factories), to leverage the interests of regional investor networks and business associations, as well as to support supply chain mapping where barriers to brand disclosure are caused by 'hidden' supply chain segments[296].

295. Which consists of 9 labour and human rights organisations including global unions such as IndustriALL, the ITUC and UNI Global Union.

296. Investor networks include those hosted by UNPRI (https://www.unpri.org/network/asia) and Endeavor (http://endeavor.org/network/investor-network/) and the Asia Investor Group on Climate Change (*aigcc.net*) and apex associations such as the Confederation of Asia-Pacific Chambers of Commerce and Industry (https://www.cacci.biz/)

ANNEX

1 RESEARCH METHODOLOGY

Research consisted of a literature review and primary stakeholder interviews, which were conducted in Vietnam and Indonesia. A full list of documents consulted is set out in Annex II. The report draws heavily on secondary sources for the regional overview in particular. As part of the literature review, key informant interviews were held with ILO headquarters colleagues in Better Work, SECTOR and the SCORE project.

During the in-country research, meetings were held with:

- *Industry associations*. Vietnam: VITAS (the Vietnam Textile and Garment Association), and VCCI (the Vietnam Chamber of Commerce and Industry) as well as KOCHAM (the Korean Chamber of Commerce). Indonesia: KADIN (the Indonesian Chamber of Commerce); the Ministry of Industry – Directorate of Textile, Leather, Footwear, and Multifarious Industry; the Indonesian Synthetic Fiber Producers Association (APSyFI); BKPM (the Indonesia Investment Coordinating Board); and KOGA (the Korean Garment Association in Indonesia).
- *Development projects*. Vietnam: IDH, UNIDO and Better Work; Indonesia: Better Work
- *Brands and agents*. Vietnam: 12 major European and US-based brands and their agents were interviewed. Indonesia: 7 major primarily US-based brands and their agents were interviewed. Company names are not included to preserve the confidentiality of responses.
- *Garment and textile factories*. Vietnam: 6 factories producing readymade garments, fabrics and supporting services such as printing and embroidery were interviewed. Indonesia: 7 factories producing readymade garments, trims, and supporting services; and 1 representative from a large industrial bonded zone. Company names are not included to preserve the confidentiality of responses.

The research took place over May to September 2017. The in-country research took place over a two-week period in August.

ANNEX

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