International Labour Organization

Building resilience during and after the COVID-19 pandemic

COVID-19 guide & action checklist

For medium-sized factories & managers

Reducing costs

This guide helps factory managers and manufacturers navigating the COVID-19 pandemic reduce costs to ease financial liquidity and cash flow pressures on their factory operations.

Getting started

Includes: Spreadsheet template for costs, action checklist

In this guide:

- Why managing costs are essential during the pandemic
- Types of costs in the manufacturing sector
- 8 ways factories can reduce costs in a socially responsible manner

1. Why managing costs are essential during the pandemic

The COVID-19 outbreak has most likely put your factory in a challenging financial position. With orders being cancelled and fewer payments coming in, the financial pressures in your factory are going to be multifaceted. Settling invoices for your ordered supplies such as raw materials or packaging could prove challenging, if not impossible. Factories, such as free-on-board (FOB) factories, which undertake significant additional expenses before receiving payment, are particularly exposed to this type of financial pressure.

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Paying your workers' salaries may be difficult in times of low liquidity. A further challenge could be paying your utility bills for water, electricity or gas. While you may need to reduce costs to safeguard your business in the near future, the COVID-19 pandemic also provides an opportunity to make your operations more cost-efficient in the longer term.

The recommendations in this guide will help you to reduce costs in a socially responsible manner. In doing so, manufacturers can ultimately:

- Focus on maintaining operations and minimize strain on the factory in the long-run
- Build resilience during and after the COVID-19 outbreak

Increase their competitiveness over time

2. Breaking down costs in your sector

Before taking action, it is important to know what your costs are and how they can potentially impact your business and factory operation in a pandemic situation. Manufacturers face a wide range of costs that typically can be separated into three main categories:

Materials cost: Depending on the sourcing model, factories may cover the costs for materials used in production, as well as shipping and duties expenses.

Labour costs: Wages of workers involved in the production process, such as operators and machinists.

Overhead costs: These are costs needed to keep the factory running, but that are not directly linked to your factory's production, such as rent and utilities.

What makes up the bulk of costs in your factory?

Factory costs can also be divided into fixed and variable costs:

- **Fixed costs** do not change with fluctuations in your production volume. No matter how much your factory produces every month, your fixed costs will remain the same. Fixed costs include e.g. the rent of the factory building, property taxes, insurance, security, machinery and equipment costs, compliance costs, etc.
- **Variable costs** are, to the contrary, directly linked to the decrease / increase in your factory's production. Variable costs include e.g., the wages of your workers, utilities, chemicals

Costs also depend on the location of the factory, the factory itself, the types of materials used and the sourcing model that it is operating under. For factories that purchase their own raw materials, material costs can make-up a significant portion of overall costs.

3. Getting ready for action

Now that you've reviewed the types of costs involved in your operation, the next section will provide some concrete steps on managing costs and doing so in a socially responsible manner.

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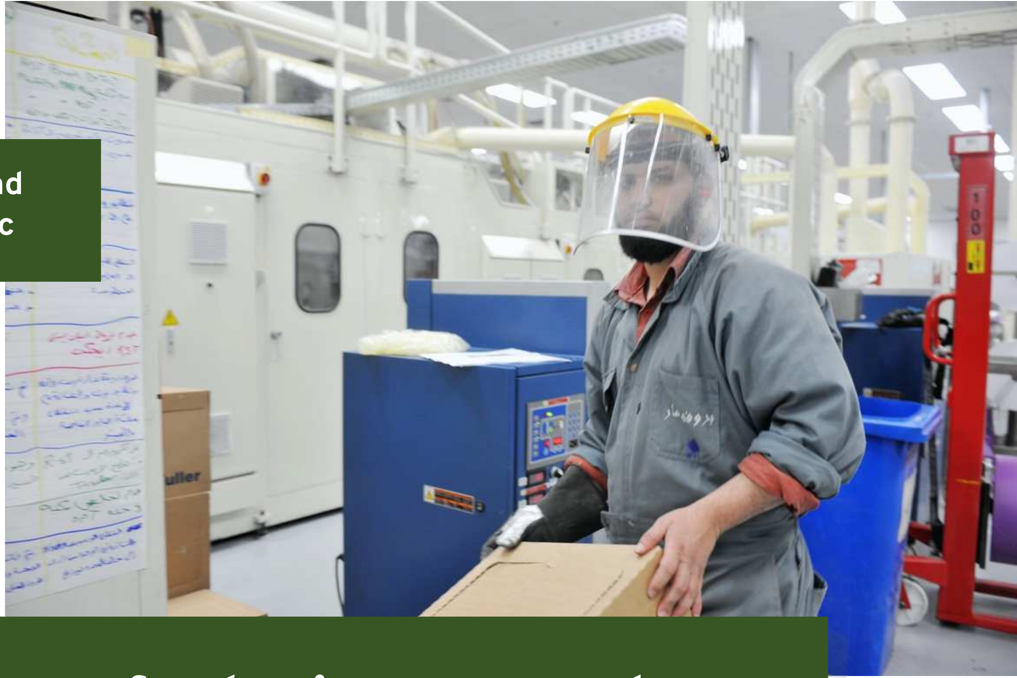

8 ways factories can reduce costs in a socially responsible manner

01	**Review your costs** Develop a clear, detailed picture of spending.
02	**Focus on the low-hanging fruit** Identify costs you can easily and immediately reduce.
03	**Eliminate what does not add value** Cut back on non-essentials
04	**Reduce material costs** Look for savings on materials.
05	**Rationalize and reinvent your inventory** Keep it at a minimum and look for alternatives to storage .
06	**Seek ways to cut overhead costs** Reduce monthly expenses and negotiate fixed costs such as rent
07	**Mitigate impact on workers** Consider all alternatives to lay-offs and keep employees informed.
08	**Support each other** Work together with other factories, associations and stakeholders.

Putting the measures in action: Factory checklist

1. Review your costs

Start by taking some time to go through your financial records. You cannot reduce costs if you don't know what they are. **Useful tip:** Use the attached cost worksheet template (at right) to help you lay out your costs.

Factory_Cash_Flow Template.xlsx

Action	Ease of implementation	Timeline	Check ✓
For reviewing your fixed costs, go through your financial records with the following questions in mind: ▶ On what do we regularly spend every month that is independent of our production? ▶ How much do we spend on each of these items monthly?	✓✓✓	⋙ Short-term	☐
For reviewing your variable costs, go through your financial records with the following questions in mind: ▶ Which costs vary with our output? As stated above, this could be wages of your workers, utilities or chemicals, etc. ▶ How much do you spend for each product?	✓✓✓	⋙ Short-term	☐

2. Focus on low-hanging fruit

As a second step, we will focus on quick-wins your factory can achieve. For this, try to identify those cost items that you can easily cut or reduce immediately

Action	Ease of implementation	Timeline	Check ✓
In your financial statement or completed template, identify what costs are not essential for your factory to maintain operations or not linked to critical activities. These costs may include costs for equipment, office supplies etc.	✓✓✓	⋙ Short-term	☐
Find a way to reduce or cut non-essential costs as soon as possible.	✓✓	⋙ Short-term	☐

3. Eliminate what does not add value

If necessary, you should also look at eliminating activities that have not been profitable in the past.

Action	Ease of implementation	Timeline	Check ✓
Review your product lines and activities in the factory for their profitability.	✓✓✓	⋙ Short-term	☐
Take a look at your product lines and calculate the financial returns per item for each order. Eliminate the product lines and activities that have not been as profitable as others in the last six months, and do not hesitate to do so, as it will become harder and harder to financially recover from this crisis the longer you wait to respond.	✓✓	⋙⋙ Mid-term	☐

4. Reduce material costs

If your factory purchases its own materials, it is likely this comprises a substantial part of your total monthly costs. Reducing material costs should therefore be a priority for you as you continue or resume factory operations.

Action	Ease of implementation	Timeline	Check ✓
Ask for a discount. Always negotiate to get the best deal possible.	✓✓✓	››› Short-term	☐
Ask several suppliers (up to five, for example) to send you quotations when sourcing materials.	✓✓	››› Short-term	☐
Look at techniques to reduce material waste in your production (e.g. look at your factory operations – improve floor layout, increase efficiency %, increase material utilization %, etc.).	✓	››› Short-term	☐
Consider if you can use alternative (cheaper) material without comprising product quality.	✓✓	››› ››› Mid-term	☐
Build long-term relationships with your material suppliers, which are built on mutual understanding and partnership. A good relationship will create a win-win situation for you and the suppliers, in which you will be able to source materials for a lower price and the suppliers have a long-term customer.	✓	››› ››› ››› Long-term	☐

5. Rationalize and reinvent your inventory

In the time of COVID-19, many factories have been left with cancelled or suspended orders or large inventories. While purchasing materials is costly in itself, the expenses associated with storing products e.g. staff, insurance, stocktaking, electricity and maintenance will also result in growing costs over time.

Action	Ease of implementation	Timeline	Check ✓
Keep your storage organized. This will make your operations more efficient and will help reduce unnecessary costs by avoiding damage to expensive materials and products.	✓✓✓	››› Short-term	☐
If you have leftover materials or products from cancelled orders, discuss with your buyers how you could use these materials or products and not let them go to waste. Contractual arrangements can vary in this regard, but you should push your buyers to allow you to maximize benefits in order to stay viable in these exceptional times.	✓✓	››› Short-term	☐
If you cannot re-use leftover materials, consider re-selling or recycling them. There may be opportunities to re-sell or recycle materials through various platforms. Talk to your industry association about existing opportunities in your country (including producing items for the local market, but first check on regulations).	✓✓	››› ››› Mid-term	☐
If you cannot re-use, resell or recycle your materials, try to dispose of them in an environmentally friendly manner, as they will take up space in your storage and cost money over time.	✓✓	››› ››› Mid-term	☐

Start applying models that will help you carry an optimal level of inventory, such as JIT (Just-In-Time) and/or EOQ (Economic Order Quantity).	✓	»» »» »» Long-term	☐

6. Seek ways to cut overhead costs

Regardless of whether your operations are constrained or even suspended, you will still have to pay your fixed costs. Take time to re-negotiate your fixed costs. Look for both short-term solutions, such as temporarily lowering or deferring your rent, as well as long-term solutions.

Action	Ease of implementation	Timeline	Check ✓
Reduce your utility costs by using less electricity, water and gas (e.g. use machines with direct drive motors, use push or foot water taps as appropriate, turn off the lights in empty rooms, install translucent roofing sheets for natural lighting, etc.).	✓✓	»» Short-term	☐
Contact your landowner and ask to renegotiate or temporarily freeze the rent.	✓	»» Short-term	☐
Call your insurance provider to see if they have a better offer for you.	✓	»» Short-term	☐
Ask your industry association for guidance related to government taxes and other government programmes / subsidies that were introduced during the outbreak.	✓✓	»» Short-term to mid-term	☐
Talk to your bank to see if they can offer lower rates for their financial services, such as letters of credit or loans.	✓	»» »» Mid-term	☐

7. itigate impacts on workers

The COVID-19 outbreak might result in you having to reduce your workforce. If this is the case, make sure that you do so in a socially responsible manner. Layoffs will have potentially devastating consequences for your workers, and you should consider how you can mitigate such to the extent possible. For more guidance on how to deal responsibly with retrenchments during the COVID-19 outbreak, click here.

Action	Ease of implementation	Timeline	Check ✓
Seek advice from your industry association on what possibilities you have before proceeding with any layoffs or scaling down operations.	✓✓✓	»» Short-term	☐
In all cases, businesses must adhere to national legislation and regulations as well as international labour standards.	✓✓✓	»» Short-term	☐
Consult with workers and their representatives before taking any measures related to layoffs.	✓✓✓	»» Short-term	☐
Provide relevant information to workers' representatives and engage in a dialogue regarding measures to avoid termination of contracts as well as mitigation of effects.	✓✓✓	»» Short-term	☐
Ensure your factory has information about government measures, social protection schemes and support for workers and communicate this information to workers.	✓✓✓	»» Short-term	☐

8. Support each other

Working together with other factories and your associations can help you to lower your costs and to project a common industry position to buyers, the government and other stakeholders.

The COVID-19 pandemic will take a hard toll on your factory as well as that of your peer factories. This is a time to act in solidarity, and for the sector to overcome this crisis by working together with other factories.

Action	Ease of implementation	Timeline	Check ✓
Communicate with your peer factories to understand their situation and to explore how you can work together	✓✓✓	Short-term	☐
Source materials jointly to be able to purchase at a lower price.	✓✓	Short-term	☐
Purchase materials and other inputs from each other if possible to mitigate the impact of cancelled orders leaving factories with leftover materials.	✓✓	Short-term	☐
Explore opportunities to barter with each other to acquire needed equipment.	✓✓	Mid-term	☐
Engage together in the work of your industry association to strengthen the competitiveness and resiliency of your country's sector.	✓✓✓	Mid-term	☐

This guide was developed by the ILO Enterprises department for the **Decent Work in the Garment Sector Supply Chains in Asia** project, funded by the Government of Sweden.

For more guides and resources to help you navigate the global COVID-19 pandemic, visit:

- ilo.org/covid19

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A better world starts here.