

▶ Building resilience during and after the COVID-19 pandemic

 COVID-19 guide & action checklist

 For garment factories & managers

Reducing costs

For garment manufacturers navigating the COVID-19 pandemic, this guide helps factory managers reduce costs to ease financial liquidity and cashflow pressures on their factory operations.

Getting started



Includes:
Spreadsheet
template for
costs, action
checklist

In this guide:

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



1. Why managing costs is 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 materials such as fabric, trim or packaging by your supplier could prove challenging if not impossible. Factories, such as FOB factories, which are procuring the fabric themselves, are particularly exposed to this financial pressure.

Building resilience during and after the COVID-19 outbreak.



Paying your workers' salaries will also be difficult in times of low liquidity. A further challenge could be to pay your utility bills for water, electricity or gas. While you therefore 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, garment operators 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, and
- ▶ Increase their competitiveness over time.



2. Breaking down costs in the garment sector

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



Materials cost: Depending on the sourcing model, e.g. fee on board/full package (FOB) or cut-make-trim (CMT), factories may cover the costs for materials used in production.



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





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 etc.

Costs also depend on the location of the factory, the factory itself and the sourcing model that it is operating under. For factories that purchase their own fabric, material costs typically make-up approximately two-thirds of total costs while labour and overhead costs account for one-sixth each, as shown below.

For garment manufacturers that operate under a CMT model and use materials provided by their customers, labour costs account for approximately 50 to 60 percent of the cost while overhead costs make up between 30 and 40 percent (as shown below). Accessories, such as thread, needles and zippers account for the remaining 10 percent.

Cost breakdown of a typical FOB model factory



Cost breakdown of a typical CMT model factory



3. Getting ready for action

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



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 fruits**
Identify costs you can easily and immediately reduce
- 03 Eliminate what does not add value**
Cut back on the non-essentials
- 04 Reduce material costs**
Look for savings on materials and fabric
- 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 industry



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
<p>For reviewing your fixed costs, go through your financial records with the following questions in mind:</p> <ul style="list-style-type: none"> ▶ 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	<input type="checkbox"/>
<p>For reviewing your variable costs, go through your financial records with the following questions in mind:</p> <ul style="list-style-type: none"> ▶ Which costs vary with our output? As stated above, this could be wages of your workers, utilities or chemicals, etc. ▶ Next, you need to know how much you spend for each product. 	✓✓✓	>>> Short-term	<input type="checkbox"/>

2. Focus on the low-hanging fruits

As a second step, we will focus on the 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 costs which are not essential for your factory to maintain operations but linked to non-critical activities. These costs may include costs for equipment, office supplies etc.	✓✓✓	>>> Short-term	<input type="checkbox"/>
Find a way to reduce or cut the costs as soon as possible.	✓✓	>>> Short-term	<input type="checkbox"/>


3. Eliminate what does not add value

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

Action	Ease of implementation	Timeline	Check
Review your product lines and activities in the factory for their profitability.	✓✓✓	>>> Short-term	<input type="checkbox"/>
<p>Take a look at your product lines (tops, bottoms, jackets, t-shirt, etc.) and calculate the financial returns per item for each order.</p> <p>Eliminate the product lines and activities, which have not been as profitable as the others in the last six months and do not hesitate to do so, as it will become harder and harder to recover from this crisis the longer you wait to respond.</p>	✓✓	>>>> Mid-term	<input type="checkbox"/>


4. Reduce material costs

If your factory purchases its own fabric, it's 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 
Never be afraid to ask for a discount. Always negotiate to get the best deal possible.	✓✓✓	»»» Short-term	<input type="checkbox"/>
Ask several suppliers (for example up to five) to send you quotations when sourcing materials.	✓✓	»»» Short-term	<input type="checkbox"/>
Look at techniques to reduce material waste in your production (e.g. look at your cutting room operations - systematic laying, increased marker efficiency %, increased fabric utilization %, etc.).	✓	»»» Short-term	<input type="checkbox"/>
Consider if you can use alternative (cheaper) fabric without comprising product quality.	✓✓	»»»» Mid-term	<input type="checkbox"/>
Build long-term relationships with your material and trim suppliers, which are built on understanding. 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	<input type="checkbox"/>












5. Rationalize and reinvent your inventory

In the time of COVID-19, many garment factories have been left with cancelled or suspended orders. This has led to a lot of materials which cannot be used. While purchasing materials is costly in itself, additional costs for e.g. staff, insurance, stocktaking, electricity and maintenance will result in costs growing 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.	✓✓✓	»»» Short-term	<input type="checkbox"/>
If you have leftover material from cancelled orders, discuss with your buyers how you could use these materials and not let it go to waste. Contractual arrangements can vary in this regard, but you should push your buyers to allow you to maximize benefits (ship more than the allowed 3% or 5%) in order to stay viable in these exceptional times.	✓✓	»»» Short-term	<input type="checkbox"/>
If you cannot re-use the leftover material, consider recycling it. There are opportunities today to recycle materials through various platforms. Talk to your garment association about existing opportunities in your country (produce items for the local market but first check on regulations).	✓✓	»»»» Mid-term	<input type="checkbox"/>
If you cannot re-use or recycle your fabric, try to dispose it in an environmentally friendly manner, as it will take up space in your storage and cost you a lot of money over time.	✓✓	»»»» Mid-term	<input type="checkbox"/>
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	<input type="checkbox"/>












6. Seek ways to cut overheads

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

Action	Ease of implementation	Timeline	Check 
Cut your utility costs by using less electricity, water and gas (e.g. use the 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	<input type="checkbox"/>
Contact your landlord to ask to renegotiate or temporarily freeze the rent.		 Short-term	<input type="checkbox"/>
Call your insurance provider to check if they have a better offer for you.		 Short-term	<input type="checkbox"/>
Ask your garment association for guidance related to government taxes and other government programmes / subsidies, which were introduced during the outbreak.		 Short-term to mid-term	<input type="checkbox"/>
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	<input type="checkbox"/>

7. Mitigate impact 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 garment association on what possibilities you have, before proceeding with any layoffs or scaling down operations.		 Short-term	<input type="checkbox"/>
In all cases, businesses must adhere to national legislation and regulations as well as international labour standards.		 Short-term	<input type="checkbox"/>
Consult with workers before taking any measures related to layoffs.		 Short-term	<input type="checkbox"/>
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	<input type="checkbox"/>
Ensure your factory has information about government measures, social protection and support for workers and communicate this information to workers.		 Short-term	<input type="checkbox"/>

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 brands, the government and other stakeholders of the industry.

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	<input type="checkbox"/>
Source materials jointly to be able to purchase at a lower price.	✓✓	»» Short-term	<input type="checkbox"/>
Purchase materials and other inputs from each other if possible, to mitigate the impact of cancelled orders leaving factories with leftover fabric.	✓✓	»» Short-term	<input type="checkbox"/>
Explore opportunities to barter with each other to acquire needed equipment.	✓✓	»»»» Mid-term	<input type="checkbox"/>
Engage together in the work of your garment association to strengthen the competitiveness and resiliency of your country's garment sector.	✓✓✓	»»»» Mid-term	<input type="checkbox"/>



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

Decent Work Technical Support Team for East and South-East Asia and the Pacific

United Nations Building, 10th Floor

Rajdamnern Nok Avenue,

Bangkok 10200, Thailand

Tel.: 662 288 1234 Fax. 662 288 3058

Email: BANGKOK@ilo.org

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A better world starts here.