

Inclusive Labour Markets, Labour Relations  
and Working Conditions Branch

***Redistributing value added towards labour in apparel  
supply chains: Tackling low wages through purchasing  
practices***

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## Abstract

Efforts to redistribute value added in favour of apparel production workers are made complex by a structurally asymmetrical value chain where the potential for wage increases may be compromised by a footloose, buyer driven, outsourced system of production. Measuring change in the distribution of value added to capital and labour within such parameters is virtually impossible. However it is possible to deconstruct the capturing of gain at the level of an individual apparel product. This is the starting point and the methodological basis for this working paper which attempts to deconstruct labour costing in different national and product contexts. The paper demonstrates that there is room within buyer margins for a redistribution of value added. A critical assessment of existing individual buyer attempts to address their code of conduct commitments with respect to a 'living' wage highlights the limits and possibilities of such efforts and points towards collective buyer efforts - specifically plans for industry wide bargaining mooted, for instance, by the 'Action Collaboration Transformation' initiative (ACT). The establishment of industry-wide collective bargaining in key garment and textile sourcing countries, supported by world class manufacturing standards and responsible purchasing practices, is likely to require a degree of collective intra-organisational negotiation between buyers and suppliers to agree on a labour minute value which can deliver any new wage increase within manufacturing standards geared towards improving efficiency. The implementation of such industry wide bargains at the level of the firm could have serious implications for workers in terms of job security and work intensification, issues for which organised labour will need to prepare.

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## Abbreviations

ACT	.....Action, Collaboration, Transformation
AFW	.....Asia Floor Wage
BDT	.....Bangladeshi Taka
BGMEA	.....Bangladeshi Garment Manufacturers' and Exporters' Association
BKMEA	.....Bangladeshi Knitwear Manufacturers' and Exporters' Association
CBA	.....Collective Bargaining Agreement
CCC	.....Clean Clothes Campaign
CCM	.....Macedonian Trade Union Confederation
CMT	.....Cut Make Trim
DSP	.....Designated Supplier Programme
ETI	.....Ethical Trading Initiative
FLA	.....Fair Labor Association
FLO	.....Fairtrade Labelling Organisation
FOB	.....Free on Board
FWF	.....Fair Wear Foundation
GSD	.....General Sewing Data
GTZ	.....Gesellschaft für technische Zusammenarbeit
GMAC	.....Garment Manufacturers' Association of Cambodia
GVC	.....Global Value Chain
ILO	.....International Labour Organisation
LBL	.....Labour Behind the Label
MSI	.....Multi-stakeholder Initiative
MOSHA	.....Macedonian Occupational Health and Safety Association
NMW	.....National Minimum Wage
OECD	.....Organisation of Economic Cooperation and Development
RMG	.....Ready Made Garment
SAM	.....Standard Allowed Minute
SMV	.....Standard Minute Value
SKU	.....Stock Keeping Unit
WRC	.....Workers' Rights Consortium

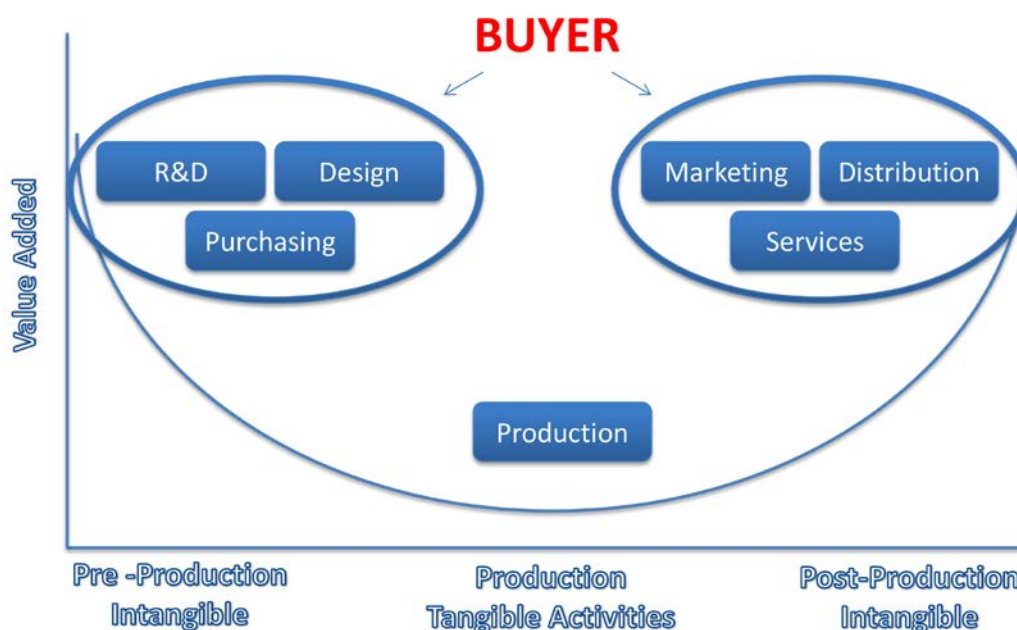




## Introduction

The distribution of value added across global apparel value chain continues to be skewed towards OECD economies, with pre and post manufacturing services capturing more gain than actual manufacturing (Fredericks 2010; Banga 2014). This asymmetrical distribution can be depicted by what has been termed a ‘smiley curve’ of value added distribution (Frederick *ibid*) (See Figure 1). Structurally speaking, apparel exporting countries are ‘locked in’ at the foot of this curve and locked out of those downstream parts of the industry which generate higher rents. This is the context in which the discussion about the redistribution of value added towards labour in the apparel sector has to be assessed. Given the complexity of the value chain and the specific ownership structures of capital in the sector it is virtually impossible to establish a macro level overview of the share of relative profit and wage in the industry both at a national as well as international level. It would be ambitious indeed even to attempt to establish the share of profit and wages in terms of a single brand across its value chain. What is however possible and measurable is the distribution of value added across individual apparel products. This is the starting point and the methodological basis for this working paper. Deconstructing the costs and the costing of specific apparel items assists us in establishing the relative values afforded to the factors of production and is critical for an analysis of wages in the industry which continue to remain in a parlous state (ILO 2014, pp. 15-20; Vaughan-Whitehead 2010; Center for American Progress 2013; Miller 2014).

**Figure 1: Curve of value added in the textile supply chain**



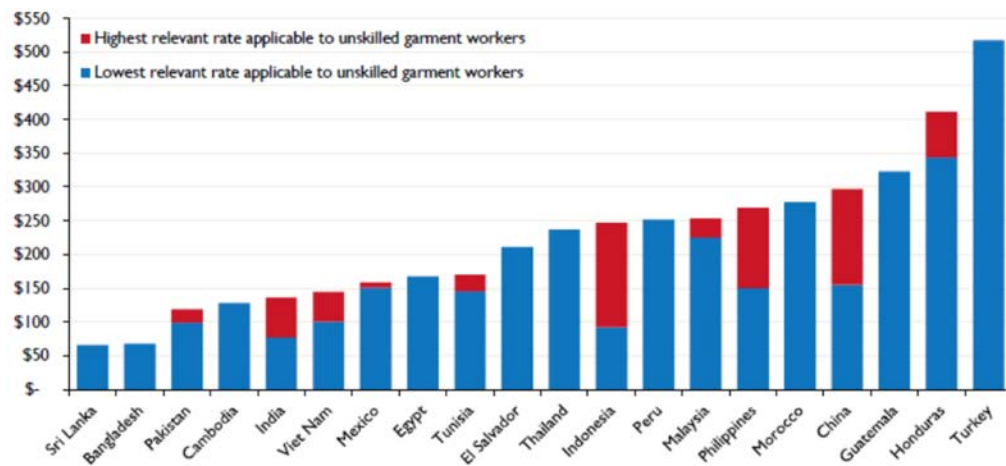
Graphic based on (Frederick, 2010)

As we await due diligence guidance on wages from the ILO/OECD in respect of the UN Guiding Principles<sup>1</sup> and the determination of possible solutions to the redistribution of

<sup>1</sup> OECD 2016 OECD Due Diligence Guidance for Responsible Supply Chains in the Garment and Footwear Sector Draft version, February 2016, <https://mneguidelines.oecd.org/public-consultation-guidance-for-responsible-supply-chains-in-the-garment-and-footwear-sector.htm> [accessed 10 March 2016].

value added across the sector, brands and retailers continue to be the targets of sustained NGO campaigning on the issue.<sup>2</sup> Figure 2 below shows the monthly minimum wage for workers in the key garment exporting countries as of January 2015. One of the campaign groups' central demands calls for an increase in the labour cost part of the FOB (INCOTERM "free on board") price paid to manufacturers. Quite apart from a persistent downward trend in FOB prices, buyers have been dogged in their resistance to this demand, tending, as Levy has argued (2008, p. 956) to 'absorb and deflect threats in ways that protect system fundamentals' (See also Barrientos & Smith 2006, p.16). The deflection has come in the form of a raft of reservations and references to systemic obstacles: fragmented buyer responsibility for compliance, a continuing lack of consensus regarding an appropriate living wage benchmark and what constitutes fair compensation, the problem of price elasticity in apparel retail markets (aka the compound price escalation issue), anti-trust considerations in relation to buyer collaboration, the absence of appropriate costing mechanisms for delivery, poor supplier efficiency and the thorny question of implementation.

**Figure 2: Monthly minimum wages for the top 20 apparel-exporting middle and low income countries in USD as of 1 January 2015**



Source: ILO 2015 Minimum wages in the global garment industry: Update for 2015 ILO compilation based on national sources. Exchange rates: IMF and xe.net

Despite the formidable nature of some of these obstacles we now seem to have arrived at a crucial juncture as a number of initiatives - academic, legal and industrial - have been grappling with these impediments to progress. A multi-agency effort is finalising a credible methodology to determine living wage benchmarks tailored to local settings<sup>3</sup>, an offshoot of

<sup>2</sup> CCC 2014 Can you earn a living wage in fashion in Italy? <http://www.cleanclothes.org/resources/publications/italian-living-wage-report> [accessed 5 August 2015]; CCC 2014 Stitched Up: Poverty Wages for Garment Workers in Eastern Europe and Turkey <http://www.cleanclothes.org/resources/publications/stitched-up-1> [accessed 05 August 2015]; CCC 2014 Tailored Wages <http://www.cleanclothes.org/livingwage/tailoredwages/tailored-wage-report-pdf> [accessed 05 August 2015]; Anna McMullen 2015 Shop Till They Drop, Bristol: Labour Behind the Label and Phnom Penh the Community Legal Education Centre, <http://www.cleanclothes.org/resources/national-cccs/shop-til-they-drop> last accessed 05/08/2015; Center for American Progress op.cit. ; Worker Rights Consortium 2013 Stealing from the Poor: Wage Theft in the Haitian Apparel Industry <http://www.workersrights.org/freports/WRC%20Haiti%20Minimum%20Wage%20Report%2010%2015%2013.pdf>; Asia Floor Wage Campaign <http://asia.floorwage.org/> [accessed 05 August 2015] cf. the Joint Letter re the FLA re. Wage Strategy <http://www.laborrights.org/publications/joint-letter-fla-re-wage-strategy> Consultancy UK 2015 <http://www.consultancy.uk/news/2306/accenture-living-wage-supply-chain-basic-human-right> [accessed 7 August 2015]

<sup>3</sup> A Shared Approach to Estimating Living Wages: Short description of the agreed methodology

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a renewed effort by Fairtrade Labelling International to revisit its Fairtrade Textile Standard in respect of the whole apparel value chain<sup>4</sup>. The Fair Wage approach promoted by the Fair Wage Network has also been developed and is being followed by a number of brands and NGOs (ETI-Norway, Solidaridad)<sup>5</sup>. In the same direction, the Fair Labor Association is currently engaged in an effort to establish amongst other things consensus as to which wage elements might constitute fair compensation and to compile a set of national living wage benchmarks<sup>6</sup>. The impact of increases in the labour cost element in the CMT has been modelled<sup>7</sup> and found to be largely negligible at the retail end, particularly if retailers and brands do not insist on their percentage margin on the FOB increase<sup>8</sup>. One multi stakeholder initiative (the Dutch Fair Wear Foundation) has been examining ways in which the ‘silo’ behaviour of buyers which has long been reinforced by competition/anti-trust law might be changed in respect of labour costing in a shared facility<sup>9</sup>. This is critical, particularly if there is to be change at the level of the firm in global supply chains. Perhaps most significantly there are signs within the industry that effective solutions to the living wage issue can only be found collectively. Three multi-stakeholder initiatives – the UK, Norwegian and Danish Ethical Trading Initiatives have joined forces to rally their member companies to transcend their fragmented responsibility on this issue (Joint ETIs 2015), and groups of buyers, some of which are members of these same MSIs, have jointly declared in letters to both the Government and the National Garment Manufacturers’ Association in Cambodia readiness to cost national wage minimum wage increases into their FOB/CMT negotiations with their suppliers.<sup>10</sup> Emanating from this latter initiative comes an agreed ‘back to the future’ programme of action on the part of a handful of leading brands and the global union IndustriALL 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’<sup>11</sup>. The MOU signed in 2015 establishing the so-called ‘Action, Collaboration, Transformation’ initiative (ACT) recognises the significance of national minimum wage determination in the sector, setting as it does ‘a common baseline for wages, but (which) is typically below the level of a living wage in most major garment producing countries’ and acknowledges that sectorial collective bargaining

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Richard and Martha Anker, November 2013, for the ISEAL Alliance Living Wage Working Group  
<http://www.isealalliance.org/sites/default/files/Descripton%20of%20Living%20Wage%20Methodology%200131124.pdf>

<sup>4</sup> Fairtrade Labelling Organisation 2014 Weaving Further Impact for Textile Workers  
<http://www.fairtrade.net/single-view+M582347df884.html> [accessed 06 August 2015]

<sup>5</sup> Fair Wage Network [www.fair-wage.com](http://www.fair-wage.com) <sup>6</sup> Fair Labor Association 2015

<sup>6</sup> Fair Labor Association 2015

<sup>7</sup> Cf. Pollin et.al 2004

<sup>8</sup> Fairwear Outdoor Group project cf. [http://www.fairwear.org/ul/cms/fck-uploaded/documents/fwfpublishations\\_reports/LivingWageEngineering20141.pdf](http://www.fairwear.org/ul/cms/fck-uploaded/documents/fwfpublishations_reports/LivingWageEngineering20141.pdf) [accessed 30 July 2015]. See also Pollin et.al. 2012

<sup>9</sup> Arnold & Porter 2015 The Application of EU Competition Law to the Adoption of the Living Wage Standard, Memorandum to Fair Wear, <http://www.fairwear.org/ul/cms/fck-uploaded/documents/policydocs/OpiniontoFWF-theApplicationofEUCompetitionLawtoFWFLivingWageStandardfinal1.pdf> [accessed 18 July 2015]

<sup>10</sup> Cf. Joint brands letter to Cambodian govt. and GMAC in advance of the 2014/5 minimum wage declaration. <https://www.cambodiadaily.com/news/global-brands-pledge-to-pay-more-for-garments-68261/>, [accessed 30 July 2015] Also the letters from the FLA and ETI to Ministry of Labour, Myanmar dated July 14<sup>th</sup> 2015 See also ILO call on buyers [http://www.islo.org/asia/info/public/pr/WCMS\\_332064/lang--en/index.htm](http://www.islo.org/asia/info/public/pr/WCMS_332064/lang--en/index.htm) [accessed 1 April 2015].

<sup>11</sup> Action, Collaboration, Transformation (ACT) 2015 *Memorandum of Understanding between ACT corporate signatories and IndustriALL global union on establishing within global supply chains freedom of association, collective bargaining and living wages* March 5th, 2015.

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would normally ‘build on such wage setting mechanisms - establishing wages and conditions that are appropriate for the industry’<sup>12</sup>.

Despite these overtures there is a sense in which the industry is still at the level of intent rather than action and still in search of scale-able and replicable improvements. Moreover, the path is beginning to fork between firm based (buyer and supplier) and sector based approaches. As we move into this critical phase, it is necessary to take analytical stock of those practical initiatives which have taken place or are currently underway at both these levels. The nexus of analysis for this paper is the buying practice – specifically the question of how labour should be costed – which is a relevant question for both individual and collective approaches. In Part 1, we begin with a review of the key elements of current purchasing practices as they relate to the pricing of labour and seek to model the way in which sourcing companies currently accommodate wage hikes in their product costing. In Part 2 our focus is on buyer efforts to redistribute value-added within the supply chain in the direction of workers at the level of the factory and the way in which labour costing has featured in that process. Part 3 considers an example of a supplier driven move towards a living wage while part 4 critically assesses a number of pilots undertaken by brands to unilaterally move towards a living wage at the supplier level and efforts to model how a collective approach to labour costing at the level of the firm might work. In Part 5 we shift our level of focus to the sector and examine some of the methodological issues involved in costing for decent wages at a sectorial level.

We confine our attention to costing labour and efforts to improve wages towards a living wage figure at the mass production manufacturing stage of the apparel value chain. Our data is based on interviews with industry practitioners at both the buying and supplying end who have generously provided real costing and wage data. In some cases, because of the sensitive nature of the data, we have had to apply anonymity. We use data from a number of countries including Cambodia and Bangladesh – the two countries where minimum wages are the lowest and which, unsurprisingly, are the first targets of ACT efforts<sup>13</sup> but also Thailand and Macedonia. A note of qualification is necessary at the outset –whilst the pricing of labour is a critical element in buying practice–non price aspects of buying behaviour continue to have a significant impact on the ability of a manufacturer to meet the code requirements set by both their buyers and other stakeholders particularly in the area of wage compliance (Winum G. and Karlsen K. 2014, Anner 2015; Hearson 2009; Barrientos 2012; Impactt/Traidcraft 2008; Oxfam Hong Kong 2004; Vaughan Whitehead 2010). These are dealt with in another ILO working paper (Starmanns forthcoming).

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<sup>12</sup> ACT Info Sheet 2015

<sup>13</sup> Ethiopia is also a target country.

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## Part 1. Existing buying practices in supply chains

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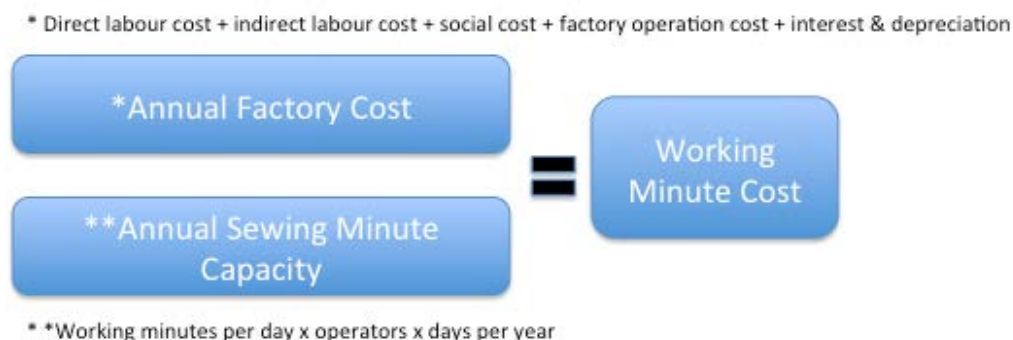
### 1.1 The wage problem in the Garment Assembly sector

With very few exceptions, wages in the global apparel sector are determined via national minimum wage declarations. Given the need to remain internationally competitive, governments have not surprisingly been less than forthcoming to declare a floor wage which meets the basic food and non-food needs of workers in the sector. Where local labour markets and production needs dictate wage elements over and above the national minimum, manufacturers in supplier countries are expected to cost their transactions with buyers at a level sufficient to cover all such wage costs (relating to both direct and indirect workers) at their facilities. There is some evidence to suggest that this is less than methodical (Vaughan Whitehead 2014, pp. 68-102; Lezama et.al 2004; Distler et.al 2014; Miller 2014, pp.103-126; IEH 2015). At a buyer level, the outsourcing of production management (including industrial engineering) and the general separation of the managerial functions of purchasing and code compliance has meant that brands and retailers have struggled to exercise due diligence in the area of wages. Consequently pay has undoubtedly become ‘the residual variable at the micro level’ in the industry (Vaughan Whitehead 2010, p.22 ) and given the buyer-driven nature of the industry, where suppliers may fear a relocation of orders to other lower cost countries, prone to price pressure (ILO 2014, p.1).

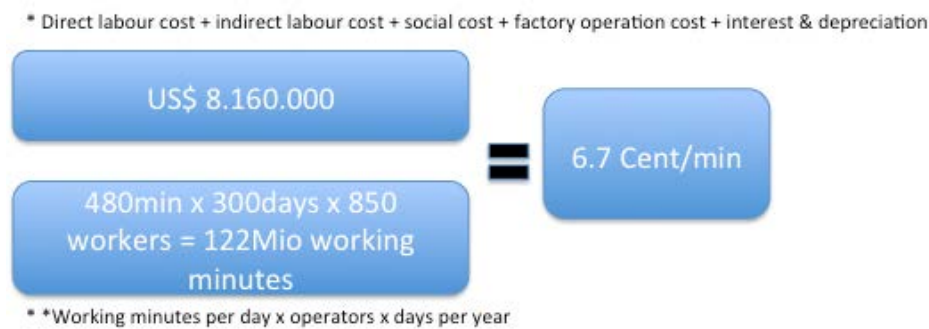
### 1.2. The transaction process between a buyer and suppliers

Transactions in the apparel industry are generally conducted in two ways. The buyer sources the fabric and trim and requires the supplier to assemble the garment – this is the CMT or cut make and trim model. Alternatively the buyer sources the complete finished garment from the supplier. This is full business or FOB (free on board or ex-factory price) model which incorporates an assembly (CMT –cut make and trim) cost. The CMT price quoted by the manufacturer to a buyer as part of the free on board price consists of two main elements – factory overhead and labour cost. To this is added the factory profit margin expressed as a percentage. The CMT cost is often expressed as the *factory working minute price* or *sewing minute* which is arrived at by dividing the factory’s total operating cost (including factory overheads) by the number of workers x the available minutes over a year. (See Figures 3 & 4 below). From a manufacturer’s viewpoint the practice of costing on the basis of a sewing minute is axiomatic since it is the direct workers on the sewing lines who earn the money for the entire factory through their sewing minute availability.

**Figure 3 Formula for calculating the working minute price**



**Figure 4 Example of a working minute price from a Thai sportswear factory**



### 1.3. The move towards open costing

Increasingly buyers have been requesting a more *open costing* from their manufacturers. Under a full open costing approach the buyer (brand) and seller (factory) agree on those costs which are chargeable, and the margin that the supplier can add to these costs. In apparel the level of transparency in open costing can vary from disclosing only the total cost of working minutes, to detailed work plans discussed with the buyer on manufacturing process steps, related efficiency factors and supplier profit levels. Manufacturers have resisted disclosing their labour costs preferring to quote labour and overhead as one figure or an entire CMT price including the profit margin lest too much transparency results in buyers driving the price down. There is a suggestion that this may be a growing trend (Birnbbaum 2015). From the evidence we have seen there is considerable variation in the understanding and use of the term open costing. Some buyers may insist on access to the full operating costs of the factory. Where long term relationships exist between buyers and suppliers based on trust, such open costing may not be an issue. Some may use this for benign reasons to determine whether the working minute price is sustainable – i.e. when all other cost variables are taken into account – is sufficient to cover the existing wage cost. Others may use the data to drive the price down even further. For jobbing manufacturers, such requests may, however, appear symptomatic of the wider existing commercial power imbalance (Lamming et.al. 2005) and there may be a reluctance to share costing data which might result in further pressure on price from the buyer. As we shall see later in the paper, it will be difficult to make progress in developing purchasing practices to result in a re-distribution of value added to labour without transparency regarding the true labour cost (Action Aid 2010). Establishing the factory labour minute value or working minute price provides the buyer with one part of the equation which must be multiplied by the time taken to complete the garment from cutting room to packing/dispatch otherwise known as the SAM – *standard allowed minutes*. This is a relatively easy exercise in the case of basic garments where cumulative industry analysis has generated standard times. In the case of more complex garments in the fashion, work wear, outdoor wear and sportswear segments of the market, some predictive costing is possible where manufacturers (and buyers) have invested in costing software. Such software is based on predetermined motion time systems which establish synthetic times for basic human physical motions applied to the construction of a garment (Miller 2014). For new styles, SAMS will have to be generated by a manufacturer’s sampling department which would then usually be subject to a process of negotiation.

The basic formula for calculating the garment labour cost then looks like this:

Price per Working Minute × Working Minute SAM

Figure 5 shows open costing sheets across 3 suppliers in 3 different sourcing countries for male adult 5 pocket jeans. Here the labour minute value is described as the *SAM cost* and the CMT cost ex profit and overhead is calculated by multiplying the SAM cost by the number of SAMs for the particular garment in question.

**Figure 5<sup>14</sup> Open costing for adult male Jeans across 3 supply countries**

Supplier			
Country	China	Bangladesh	Cambodia
Description	REGULAR TWILL BASIC JEAN	Men's Regular Twill	Regular Twill
Season	SS <sup>15</sup> 16	SS16	SS16
Type	FOB - Far East	FOB - Far East	FOB - Far East
Currency	USD	USD	USD
Materials			
Fabric Type	100% COTTON TWILL, SOLID DYED	100% cotton twill, 10x7	100% cotton twill
Fabric Width/GSM <sup>16</sup>	315 GSM	58"	56"
Main Fabric Cost	USD 2.09	USD 2.10	USD 2.22
Usage	1.36	1.37	1.31
Total Fabric Cost	USD 2.84	USD 2.88	USD 2.91
Trim Cost	USD 0.75	USD 0.55	USD 0.79
P & P Cost	USD 0.20	USD 0.07	
Total	USD 3.79	USD 3.51	USD 3.69
CM <sup>17</sup> cost			
<b>SAMs<sup>18</sup></b>	<b>16</b>	<b>20</b>	<b>18</b>
<b>Cost per SAM</b>	<b>GBP 0.090</b>	<b>GBP 0.055</b>	<b>GBP 0.066</b>
<b>CM cost</b>	<b>USD 1.44</b>	<b>USD 1.10</b>	<b>USD 1.19</b>
Other Costs			
Ancillary	USD 0.17	USD 0.20	USD 0.20
Shipping Pkg	USD 0.02	USD 0.12	USD 0.10
Shipping Costs	USD 0.03		USD 0.11
Export Rebate			
Total	USD 0.22	USD 0.32	USD 0.41
Direct Cost	USD 5.45	USD 4.92	USD 5.29
Overhead	USD 0.20	USD 0.07	USD 0.05
Margin	USD 0.28	USD 0.05	USD 0.25
% age	8.1%	2.4%	5.4%
Contribution	USD 0.48	USD 0.12	USD 0.30
Supplier Cost	USD 5.93	USD 5.04	USD 5.59

<sup>14</sup> Industry figures

<sup>15</sup> SS = summer season

<sup>16</sup> GSM = grams per square metre

<sup>17</sup> CM = cut and make cost

<sup>18</sup> SAM = standard allowed minute



As a rule, fabric is the most costly item in the overall FOB price and the example here bears this out. What is significant here is that at between USD 1.10 and USD 1.44 the labour cost remains a constant irrespective of the retail market segment for the jeans whether value or luxury. In this formula the working minute price includes all factory overheads. Some buyers seek to drill this down further, separating out the direct labour cost (those workers directly involved in production e.g. sewers, cutters, finishers,) from the indirect workers (e.g. managers, office and warehouse staff) from other operating costs such as energy, rents, maintenance etc.)

An important variable which must now be factored into the equation is the factory's efficiency. We discuss this issue more fully in part 5 below. Efficiency is a measurement of the factory's output against the available minutes expressed as a percentage. What is important at this stage is that unless allowance is made for the factory's actual operational efficiency (i.e. its ability to reach a production target expressed as a percentage) in the costing of a garment order based on predictive labour costing, the production will be under-resourced and compromised.

For example, if a factory is running at 50% efficiency i.e. is only able to achieve a production target in twice the SAM and the manufacturing cost does not take this into account (or the buyer is not working with the supplier to address those issues which are causing the inefficiency) then there is a distinct possibility that code non-compliances will occur, for example excessive unpaid overtime, payment below minimum wage level, unauthorised outsourcing to underpaid subcontractors or home workers and aggressive supervision leading to worker harassment. (Miller 2014)

To incorporate this factor our formula now would now look like this:



We do not know the extent to which efficiency is factored into the manufacturing cost of a garment in the industry. This remains an important empirical question which merits survey research in its own right. Anecdotal information suggests that this is practiced in a handful of cases at the buyer end. In the context of a buyer squeeze on FOB prices (Milberg 2007; Seiha 2010; Rahman 2012; Staritz 2014; Anner et.al 2015,) addressing efficiency is beginning to be advanced as a part solution to the low wage problem. We return to this issue in Part 5.

#### 1.4. The Relative Value of labour in Apparel GVCs and the price escalation issue.


One of the major criticisms of apparel brands and retailers is the low value afforded to labour in the overall value chain and that a substantial increase in pay would constitute a negligible increase in the retail price (Pollin et.al.2004; Nova & Kline 2014; Miller & Williams 2009). Open costings, as we show in Figure 6 below, do reveal the extent of margin earned on garments by both the brand and retailer as the product moves downstream in the value chain. However, brands and retailers have countered their critics by arguing that wage increases can have a multiplier effect as each level of the chain insists on a percentage mark-up – the co-called compound price escalation effect (Fair Wear Foundation 2012a). The extent of the percentage margin and therefore escalation may vary based on the different business models pursued by actors in the chain. The tendency in the fashion industry is for brands to establish their own retail outlets to capture more of the gain while retailers have



been developing their own private labels/brands to do the same<sup>19</sup>. Going direct from factory to store not only expands margin but also reduces the impact of compound price escalation. Perversely an increase in labour cost would in fact, depending on the price elasticity of the garments in question, have the effect of increasing the retailer's profit on the transaction, as well as boosting earnings of other participants in the value chain!

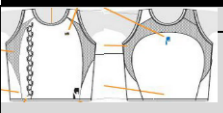
**Figure 6. Full open costing calculated at the development phase of two sportswear garment products along the whole value chain showing labour cost broken down into direct and indirect cost.**

**a) Polo Shirt**

Polo Shirt 1 Sports Brand 1				
		Description	%	\$
	Garment Manufacturing	Fabric cost		6.76
		Accessory		0.67
		Print / Embroidery		3
		Packaging / Hang Tag		0.25
		Material input		10.68
		Direct Labour Cost	33%	0.71
		Indirect Labour Cost (including Management)	38%	0.44
		Factory Running Cost	29%	0.63
		<b>TTL Working Minute Cost</b>	<b>100%</b>	<b>1.78</b>
		Manufacturing Cost		12.46
Factory markup	15%	1.87		
FOB Price		14.33		
Brand		Import Tax / Transport / Insurance	13%	1.86
		Landed Cost		16.19
		Warehouse, Brand markup, etc.	80%	12.95
Retail		Wholesale price (excl. VAT)		29.15
		Distribution, retail mark up (incl. VAT)	130%	37.89
		<b>Retail Price (incl. VAT)</b>		<b>67.03</b>

\*figures taken from open costing in development phase of the product

**b) Functional T-Shirt**

Technical T-Shirt Sports Brand 2				
		Description	%	\$
	Garment Manufacturing	Fabric cost		2.38
		Accessory		0.41
		Print / Embroidery		1.18
		Packaging / Hang Tag		0.23
		Material input		4.2
		Direct Labour Cost	33%	0.89
		Indirect Labour Cost (including Management)	38%	1
		Factory Running Cost	29%	0.78
		<b>TTL Working Minute Cost</b>	<b>100%</b>	<b>2.67</b>
		Manufacturing Cost		6.87
Factory markup	15%	1.03		
FOB Price		7.90		
Brand		Import Tax / Transport / Insurance	13%	1.03
		Landed Cost		8.93
		Warehouse, Brand markup, etc.	90%	8.03
Retail		Wholesale price (excl. VAT)		16.96
		Distribution, retail mark up (incl. VAT)	130%	22.05
		<b>Retail Price (incl. VAT)</b>		<b>39.01</b>

\*figures taken from open costing in development phase of the product

Despite continued pressure from trade unions and campaign groups, buyers continue to resist the value chain argument. Hence it is particularly interesting to consider how they

<sup>19</sup> For manufacturers (as distinct from branded manufacturers which have become a dying breed) value gains are to be secured largely from functional (full package), process (efficiency and productivity initiatives) and product upgrading.

have adjusted their purchasing practices to accommodate major wage shocks following a substantial increase in a national minimum wage. The experience of Bangladesh is instructive here. In 2010 and 2013 the NMW increased significantly –in neither case to a living wage level (Berenschot/CPD 2013) – but by any stretch at 80% and 77% respectively, these were significant increases in labour cost for Bangladeshi manufacturers. The first question we can pose here is: was there a commensurate increase in the FOB to reflect this wage hike? The first observation to be made is that FOB prices did rise in 2011 in some categories, but fell in others as the following BKMEA<sup>20</sup> data on selected garments in Table 1 shows (See also Ahmed and Nathan 2014). The table shows some quite marked differences in the average export price on these basic garments, and that in some cases FOB price changes do not appear to have responded accordingly to meet the new wage increase.

**Table 1: Average Unit Prices in dollars on selected Categories exported from Bangladesh to the USD 2010/11<sup>21</sup>**

HS Code	Apparel Category	2010	2011	% increase
61051000	Men's shirts knitted	2.94	3.11	5.8%
61082100	Women's panties	.53	.55	3.8%
61091000	T shirts	1.29	1.37	6.2%
61102020	Sweaters cotton	2.43	2.58	6.2%
61103030	Sweaters polyester	3.28	3.5	.6%
62034240	Trousers cotton	4.77	4.84	1.5%
62034340	Trousers woollen	5.25	4.66	-11%
62046240	Trousers synthetic	4.47	4.03	-10%
62052020	Men's/boys shirts	3.37	4.38	29%

However, as we have seen, the FOB contains elements other than labour cost. In order to determine whether the wage increase was covered sufficiently in the FOB increase we need to have information about average labour cost per garment in those categories listed in Table 1. Such information is factory specific so we have confined our analysis to one product in the table by way of an illustration. In this case we have used a men's knitted polo shirt (HS code 610510) with an estimated average 8% labour cost ratio<sup>22</sup> (excluding overhead). In this case the average labour cost prior to the national minimum wage increase would have been USD 22 cents. If an 80% increase was applied to the labour cost element of the costing then the FOB in 2011 would have had to rise by USD 17.6 cents if the buyer was to fully absorb the minimum wage increase. Without mutual transparency in open costing it is difficult to determine what might be an appropriate share of the cost of a minimum wage increase between buyer and supplier. As we can see from Figure 7 below (*ceteris paribus*) the labour cost was almost covered on average except for a shortfall of 0.6 cents.

<sup>20</sup> Bangladesh Knitwear Exporters and Manufacturers' Association

<sup>21</sup> Based on US import data – Prices on shipments to the USA are calculated in dozens – Unit price calculation by authors. Source: iART Institute of Apparel Research and Technology based on BKMEA export statistics <http://dktetextilenotes.blogspot.co.uk/2014/01/introduction-to-garments-market-in.html> [accessed 17 June 2015]

<sup>22</sup> Garment manufacturing is labour intensive and labour costs are generally the largest cost factor for a manufacturer. However when it comes to breaking down cost for an individual apparel item fabric remains the largest cost element.

**Figure 7 Managing increases to the national minimum wage, Bangladesh 2010-11, example of a Men's Polo Shirt (2010-2011)**

**2010**

FOB	USD 2.94
Labour cost @ 8%	Labour Cost = USD 0.22

**2011** (post NMW increase @ 80%)

FOB (average actual increase)	USD 3.11 (17 cents)
Required labour cost increase	USD 17.6 cents
Shortfall in FOB	USD .6 cents

If we include the factory overhead (and there is a mounting argument in the wake of Rana Plaza that insufficient provision is being made to cover increasing compliance costs (Moazzem and Bashak 2015), then including factory overheads with an 80% increase, the FOB in 2011 would have had to rise by USD 25.6 cents and not USD 17 cents as was the case.

Example of a Men's Polo Shirt:

**2010**

FOB	USD 2.94
Labour cost (inc. overhead) @ 11%	USD 32 cents

**2011** (post NMW increase @ 80%)

FOB (average actual increase)	USD 3.11 (17 cents)
Required labour cost increase (inc. overhead)	USD 32 + 25.6 cents (32 @ 80%)
Shortfall in FOB	USD 8.6 cents (USD 25.6 – 17 Cents)

In the following example (Figure 8) of costings for a dress shirt assembled in Bangladesh we show how a buyer was aiming to accommodate the impact of the 2013 (77%) wage increase in the RMG sector. Note how in this particular case the costing reflects an expected 5% increase in the factory's efficiency.

**Figure 8 Buyer projection of the impact of the 2013 minimum wage increase in Bangladesh on direct labour cost (Example Dress Shirt)<sup>23</sup>**

**Assumption of increase in Bangladesh Minimum Wage from 3,000 to 5,300 takas = 77% or 2,300 takas increase**

<b>Current calculation of total cost per Standard Minute = \$0.050</b>				
		<b>Labour cost per Standard Minute = \$0.035</b>	<b>(Based on average pay of 5,000 takas per month + social costs @ 45% efficiency)</b>	
		<b>Direct factory cost per Standard Minute = \$0.015</b>	<b>(Including light, heat and power, depreciation and interest)</b>	
<b>Revised calculation of total cost per Standard Minute = \$0.077</b>				
		<b>Revised labour cost per Standard Minute = \$0.062</b>	<b>(Based on average pay increase of 77% + social costs @ 45% efficiency)</b>	
		<b>Direct factory cost per Standard Minute = \$0.015</b>		
	<b>SAM</b>	<b>@</b>	<b>=</b>	
<b>Impact on average shirt @</b>	<b>20</b>	<b>\$0.027</b>	<b>\$0.54</b>	<b>9%</b>
<b>Revised calculation of total cost per Standard Minute = \$0.065</b>				
		<b>Revised labour cost per Standard Minute = \$0.050</b>	<b>(Based on average pay of 7,300 takas per month + social costs @ 50% efficiency)</b>	
		<b>Direct factory cost per Standard Minute = \$0.015</b>		
	<b>SAM</b>	<b>@</b>	<b>=</b>	
<b>Impact on average shirt @</b>	<b>20</b>	<b>\$0.015</b>	<b>\$0.30</b>	<b>5%</b>

<sup>23</sup> Industry Figures. The term efficiency refers to the ability of a factory to attain production targets based on agreed standard allowed minutes expressed as a percentage.

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In the above example the buyer was faced with an increase of the unit labour cost on the specific garment of US 27 cents with the overhead cost remaining unchanged and the factory running at 45% efficiency. However negotiating an expected 5% increase in efficiency reduced the unit labour cost to 15 cents.

From interviews with both buyer and supplier representatives it was reported that minimum wage increases have been offset by a fall in other cost factors such as the price of fibres (Cotton and PET for example)<sup>24</sup> and/or fluctuations in dollar exchange rates. Because of this, CMT costs and not FOB are clearly a better indicator of the ability of a supplier to meet wage compliance standards although such figures will continue to remain commercially sensitive and publically unavailable.

## **Part 2. Buyer-driven costing towards a living wage**

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In 2010 two significant developments occurred in buyer efforts to address the issue of a living wage of relevance to this paper. The establishment of a 'living' wage factory in the Dominican Republic and the first public declaration by a retailer of its intention to cost for a 'living' wage in parts of its supply base.

### **2.1 Alta Gracia – a 'living wage' factory**

In the Dominican Republic a US College licensee, Knights Apparel, was aiming to become a designated supplier under the United Students Against Sweatshops/Worker Rights Consortium programme. Having re-opened the old B J and B factory in Alta Gracia it declared that it would be paying its 150 strong unionised workforce 3.4 times the existing national minimum wage (Kline 2014, pp. 28-32). This was the first time that two key elusive code elements –living wage and freedom of association and collective bargaining– were implemented in one buyer action. Knights Apparel's ownership of the factory along with a 'conscientious consumer' base (university apparel) greatly facilitated compliance with these two central requirements of the USAS Designated Supplier Programme (DSP), but this still required commitment on the part of the owner. Notwithstanding the acquisition of Knights Apparel by Hanesbrands early in 2015,<sup>25</sup> Alta Gracia continues, however, to be an exception to the rule<sup>26</sup>. In part this is because the bulk of the apparel sector continues to be run on the basis of multi-buyer outsourced make to order globalised production. Unless a brand or

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<sup>24</sup> Patricio Ibanez and Eli Townsend 2015, *Sewing up lower costs from falling commodity prices*, McKinsey and Company Insights and Publications, [http://www.mckinsey.com/insights/operations/sewing\\_up\\_lower\\_costs\\_from\\_falling\\_commodity\\_prices](http://www.mckinsey.com/insights/operations/sewing_up_lower_costs_from_falling_commodity_prices) [accessed 10 August 2015]

Jon Devine Alejandro Plastina 2012 *A Passthrough Analysis of the Cotton Supply Chain International Cotton Advisory Committee Intelligence*, [https://www.icac.org/wp-content/uploads/2012/05/plastina\\_2012\\_january\\_beltwide.pdf](https://www.icac.org/wp-content/uploads/2012/05/plastina_2012_january_beltwide.pdf), [accessed 17 June 2015]

<sup>25</sup> The factory remains protected under a covenant within the acquisition agreement <http://www.prnewswire.com/news-releases/knights-apparel-inc-enters-into-definitive-agreement-to-be-acquired-by-hanesbrands-inc-300040697.html> [accessed 11 August 2015]

<sup>26</sup> It would be remiss not to mention here the branded vertically integrated manufacturer American Apparel, which owns its own factories and stores in the USA pays an average sewer almost twice the federal minimum wage ( USD 25,000 per year), plus subsidised transport, lunches and health insurance. However this company which is now struggling has always resisted unionisation and collective bargaining and recent cutbacks forced on it by its parent company has led to serious industrial relations problems.<http://nypost.com/2015/04/02/american-apparel-hit-by-labor-union-pains/> [accessed 13 August 2015].

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retailer owns a factory outright and is therefore the employer, it cannot achieve the payment of a living wage on its own. Where it is not the employer but has a stable and substantial commercial relationship with a particular supplier, some inroads<sup>27</sup> can be made but essentially, apart from philanthropic gestures, a buyer must resort to costing in its transactions with a manufacturer on the basis of a given wage benchmark, and therefore make a proportional contribution to a manufacturer's 'wage costs' bill.

## 2.2 Marks and Spencer -costing for a 'living' wage

Hence, the second significant development in 2010 was the public declaration by Marks and Spencer (M&S), a UK fashion retailer that owns no manufacturing facilities, that it intended to cost for a fair living wage as part of its 5 year *Plan A Sustainability drive*. UK fashion brands had been heavily campaigned by Labour behind the Label, the sister organisation of the CCC, from 2006 onwards to submit annual progress reports on wages in the supply chains (Labour behind the Label 2006-to date). As part of this initiative the company's central sourcing team commissioned a national cost analysis across 8 supply countries which sought to compare a number of indicators.

Taking aggregate values from the company's supply base in key sourcing countries and externally generated data, central sourcing at M&S was able to generate –to take Bangladesh in 2010 as an example– an aggregate labour minute target cost which would enable a factory to meet an average monthly earnings target of USD 98 (BDT 7619) –this latter figure having been calculated on the basis of commissioned desk and field research by a UK consultancy.

To achieve this, suppliers were requested to submit open costings to the retailer's central sourcing team who then decided whether the factory's CMT price estimates were above or below the target cost. Those factories which costed below target were expected to increase their cost price. A number of suppliers in Bangladesh, India and Sri Lanka (as per declaration in the Plan A 2010-2015 objectives) were offered participation in the company's rolling 'model factory' programme, designed to bring about improvements in wages through productivity, improved human resource management, and where necessary higher FOB prices.

M&S partnered with local organisations including GTZ, a German government agency, the Bangladesh Institute of Management and GSD (General Sewing Data) to deliver worker rights training; HR systems and industrial relations management training for middle management; and HR personnel, and productivity training for industrial engineers and production line management. In GVC terminology, M&S were deploying process (economic) upgrading in key Bangladeshi manufacturers to deliver social upgrading. As stated by the company, 'with better planning and production techniques in place, productivity and efficiency increased significantly' leading to an increase in the workers' wages at three participating factories between 8 and 42 per cent'. These 'increases' were achieved either on the basis of an enhanced production bonus or re-gradings – specifically from grade 7 (helper) to grade 6 machinist following retraining.

This approach was eventually up-scaled through a project part funded by a UK government Responsible and Accountable Garment Sector initiative which ran between 2010 and 2014. Entitled *Benefits for Businesses and Workers*, this joint buyer programme, which included M&S, rolled out a training programme in shared facilities which focused on

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<sup>27</sup> We refer here to the recent pilot conducted by Continental Clothing cf. Fairshare Living Wage Project. A project by Continental Clothing Co. in collaboration with BSD Consulting and the Fair Fashion Network available at : <https://starmanns1.wordpress.com> [accessed 21 March 2016]

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productivity and quality to deliver improvements in working conditions in some 63 business operations across Bangladesh and India. In Bangladeshi factories, average take home pay rose by 7.63% and by 5.09% in Indian facilities. These increases were achieved largely as a result of improvements in cut to ship ratio (quality) and productivity (Impactt 2014) –thus enabling buyers to avoid paying more. A key realisation for M&S was that the ability of a buyer to have a significant impact on wages in a factory is heavily compromised by the unwillingness of other buyers to engage on improving wages. Hence the company’s involvement in up-scaling activity with other buyers in shared facilities<sup>28</sup>.

### **2.3 Partnering towards ‘living wage’ factories: H&M**

One company which has taken a step further whilst pursuing its own living wage strategy is the Swedish headquartered fashion retailer H&M. In 2013 they launched their Fair Living Wage strategy which identifies collective bargaining as the best way to establish and achieve living wages. H&M is pursuing a systemic approach which embraces a range of stakeholders, including dialogue with governments to support improved legal and institutional frameworks relating to issues such as minimum wage reviews, freedom of association and collective bargaining. The company has initially focused on their strategic suppliers and set an ambitious target to have democratically elected worker representatives and improved wage management systems supporting fair living wages in place by 2018. H&M is also part of the Action Collaboration Transformation initiative to establish industry wide bargaining. (See Part 5).

As a part of the strategy, H&M has initiated local projects on social dialogue and industrial relations, so far covering Bangladesh, Cambodia and China. For instance, a social dialogue training centre has been established in Bangladesh with the aim is to help establish democratically elected workplace committees and improve the dialogue between management and factory employees which the company views as key first steps towards freedom of association and collective bargaining. The goal is to cover 100% of H&M supplier’s factories in the country by 2018. In parallel, a pilot trialling of the Fair Wage Method was introduced in three factories in Bangladesh (2) and Cambodia (1) during 2014 with a commitment from H&M to utilize 100% of their capacity for 5 years. During 2015 the Fair Wage Method was introduced to an additional 68 factories, (where H&M is one of several buyers). The method will continue to be scaled up to more factories in more countries in the coming years. At the same time, H&M has stated its intention to develop its purchasing practices including an updated method of pricing to more accurately understand the labour cost of each product and enable their suppliers to pay their workers a fair living wage and reduce overtime<sup>29</sup>. At the time of writing, H&M had made the announcement they would cover all their suppliers with this approach by 2018, but were unable to release details of how they would modify their costing method<sup>30</sup>.

## **Part 3. Supplier–driven labour costing – the case of Echowtex Ltd. Bangladesh**

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The general characterisation of global value chains in the apparel industry is that commercial transactions are buyer-driven (Gereffi 1994). This is interpreted as suppliers

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<sup>28</sup> Interview with Head of Ethical Sourcing Clothing, Marks and Spencer.

<sup>29</sup> <http://sustainability.hm.com/en/sustainability/commitments/choose-and-reward-responsible-partners/fair-living-wage.html> [accessed 20 August 2015]

<sup>30</sup> Email correspondence with H & M.

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wielding little influence over the terms of the contract and enduring price pressures which may compromise wage compliance and render it very difficult for a manufacturer to fall into line with a buyer's living wage code aspirations. One Bangladeshi company at least has bucked this trend. Echo Sourcing originally a sourcing/design company based in London, set up Echotex Limited as a UK-Bangladesh joint venture manufacturing company with a business nature of Jersey-composite textile (comprising knitting to finished good). It has established a full package manufacturing arm based in Gazipur with a current workforce of 7000 which produces non-printed and printed jersey wear for UK buyers New Look, Debenhams, Fat Face, Primark and Sainsbury's.

With previous and current experience in BRAC –a Bangladeshi NGO– the managing director decided to 'reverse engineer' the relationship with buyers focusing on decent work as a core business principle. Consequently Echotex has developed an extensive set of wage elements and employee benefits beyond the statutory minima included in the national minimum wage (See Table 2). Firstly, workers receive a discretionary additional amount on their basic wage separate from other bonuses and allowances. This accounts for the difference between gross pay (column 4) and average basic pay (column 6). Although attention would normally be drawn to entry grade 7 (helper grade) and here average earnings (exclusive of overtime and production bonus) at June 2015 were BDT 8,000, it is important to note that this grade accounts for only 20% of the workforce and that the company has a policy of moving helpers to grade 6 following a year's service. Allowing for inflation since 2013, Table 2 shows that the majority of workers at Echotex Ltd. were earning above the national living wage benchmarks generated both by the workers' representatives<sup>31</sup> (BDT 8,114) and by an independent think tank<sup>32</sup> (BDT 8,216) in advance of the 2013 national minimum wage determination.

Echotex Ltd. is not typical of factories within the Bangladesh RMG and at least two important factors account for their wage success: their ability as a full package operator to capture the full value of the manufacturing phase by using backward linkage to retain the value added in its fabric, dyeing and printing operations as well as the CMT price. Secondly, the company has established a close and on-going relationship with key UK and EU buyers and a readiness to engage in projects to improve productivity and welfare.<sup>33</sup> The managing director was keen to stress that employee benefits were driven by the company which then approached its buyers to take on board the additional cost. This proved particularly critical during the rise in food prices 2007-08 in Bangladesh. It was a company policy to provide a free cooked lunch for all employees from day 1, which the company has undertaken as one of their key element of worker welfare. Approaching one of their key UK buyers New Look for assistance, the fashion retailer agreed to share in the cost of the provision of a lunch for the workforce. Valued at BDT 1,000 per month this in-kind benefit, introduced outside of the national minimum wage determination process, has since become a permanent fixture in the company remuneration package.

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<sup>31</sup> Rony op. cit.

<sup>32</sup> Moazzem op.cit

<sup>33</sup> London College of Fashion 2011 Steps towards Sustainability in Fashion: Snapshot Bangladesh: A resource for fashion students and educators, [http://ualresearchonline.arts.ac.uk/5671/1/CSF\\_Vol.6\\_Steps\\_towards\\_Sustainability\\_in\\_Fashion\\_Snapshot\\_Bangladesh.pdf](http://ualresearchonline.arts.ac.uk/5671/1/CSF_Vol.6_Steps_towards_Sustainability_in_Fashion_Snapshot_Bangladesh.pdf) [accessed 17 August 2015]



**Table 2 Echotex Wage Structure**

MONTH	GRADE and Occupation(s)	NMW GRADE BASIC	GROSS SALARY	No. of employees	Average Basic Pay	Average Overtime (for what average OT hours?)	Attendance Bonus why no mean for this one?	Good Conduct Bonus	Mean production Bonus	Mean Eid bonus	Mean cost of lunch	Mean Provident Fund contribution	Mean Holiday pay	Mean net payment excl. O/T	Avg. net payment incl. O/T
01/06/2015 Apparel only	3 Sample Machinist, Senior Machine Operator	4075	6805	312	7942	2606	400	200	343	812	1000	391	262	11351	13957
	4 Sewing Machine Operator, Quality Inspector, Cutter, Packer, Line Leader	3800	6420	2841	6905	2722	400	200	199	683	1000	332	222	9941	12663
	5 Junior Machine Operator, Junior Cutter, Junior Marker	3530	6042	356	6541	2386	400	200	285	566	1000	311	208	9511	11897
	6 Operator of General Sewing/ Button Machine	3270	5678	443	6073	2179	400	200	240	571	1000	284	190	8958	11137
	7 Grade 7: Assistant Sewing Machine Operator, Assistant Dry washing man, Line Iron Man	3000	5300	867	5576	2070	300	200	210	507	1000	256	171	8220	10290

GRADE	MAN POWER
3	72
4	583
5	36
6	128
7	118
Total worked for over 5 years	937

Note: AVG Earn leave encashment (Holiday Pay) in a year amounting to 16.72 days basic pay  
 Gratuity is payable who have worked for 5 years at least and get one month's basic for every year worked.

## Part 4. Assessing Living Wage pilots

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From what we know most of the companies which are engaging on living wage are members of multi-stakeholder initiatives. Until recently, however, (Joint ETIs 2015) it has proved difficult for these organisations to drive any coordinated work on wages in shared facilities. In part this is caused by adverse legal opinion regarding buyer collaboration on cost issues. Because several brands often source from a shared supplier, assuring fair pricing and agreement on purchasing practices at a factory level would require a degree of collaboration between brands which would be seen as collusion on price. There are two main concerns here. Where production costs jointly agreed between buyers and a manufacturer constitute a significant proportion of the variable costs of production, in effect amounting to a joint purchasing agreement, leading to a commonality of cost they would, it is argued, be unable to compete effectively on price in the retail market<sup>34</sup>. Secondly, where a collective effort among competitors to increase wages resulted in an increase in prices leading to increased margins for such competitors due to the application of percentage margins throughout the chain it would be more difficult to demonstrate that the collaboration was solely for humanitarian purposes<sup>35</sup>. This elephant in the room –whose validity has not yet been conclusively tested in the sector– is one of the principal reasons why major buyers have been ploughing their own furrows on living wage. We examine three such initiatives in this section undertaken by European headquartered SMEs which have made their findings public.

### 4.1. Nudie – improving wages through a production bonus

In 2011 as part of the promotion of an Amnesty T shirt collection entitled ‘Empowerment,’ the Swedish apparel retailer Nudie switched its sourcing from Portugal to India to access Fairtrade certified cotton and to lower costs. During the initial visits to the preferred supplier –Armstrong Knitting Mill in Tiripur– it became clear that wages were well below a living wage level –a matter of concern to Nudie managers and Amnesty as a sponsor of the Empowerment initiative. In order to make progress on the issue Nudie elected to become involved in a pilot project run by the Dutch MSI –Fair Wear Foundation and Fairtrade Labelling International (FLO) aimed at, among other things, calculating the cost of paying living wages<sup>36</sup>. Using the Asia Floor Wage benchmark the pilot project estimated that paying living wages at Armstrong would require 140% wage increases and cost Nudie EUR 0.26 per t-shirt. This pilot has been extensively analysed elsewhere as a contribution to the debate on SMEs and global production networks (Egels-Zanden 2015). Here we focus our attention on some of the key features of this case as they relate to the question of living wage implementation.

The buyer handed over the responsibility for managing the living wage increase almost entirely to the supplier –while it dealt with the public relations issues back in Sweden. Although the AFW was originally mooted as a benchmark, the company opted to establish its own living wage basket undertaking their own survey of 100 of their machinists. In calculating the difference between existing earnings and the machinists’ basket of goods survey, management included overtime and therefore reduced the additional amount

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<sup>34</sup> Arnold & Porter 2015 The Application of EU Competition Law to the Adoption of the Living Wage Standard, Memorandum to Fair Wear para. 3.8.

<sup>35</sup> Ibid. para. 3.18

<sup>36</sup> Fair Wear Foundation 2012b Overview of the activities and results of the pilot project ‘third party verification in the textile supply chain of Fairtrade-certified cotton’ End report FLO pilot option 1, [www.fairwear.org](http://www.fairwear.org)

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required to bridge the gap. The change was not systemic, i.e. did not alter the existing grading system introducing instead the increase in the form of a premium payment for the particular consignment, since at this point in time a roll forward was not guaranteed (Egels-Zanden 2015, p.21). Armstrong and Nudie had wanted initially to pay only those workers producing its garments, however Armstrong later became anxious to avoid industrial relations problems arising from such differentiated treatment of its workers since as things stood only the CMT workers and not those employees in the spinning and knitting units received the bonus. Since this was a one off premium which did nothing to increase the basic rate of pay and fell far short of the AFW target originally mooted as a benchmark figure, it illustrates the limits of a single buyer intervention in a factory supplying multiple clients.

#### 4.2. The Switcher<sup>37</sup> ‘solidarity’ fund

Switcher, a Swiss based firm approved (to run from the second financial quarter in 2013) an additional amount of EUR 2.5 cents per piece to be made available to the workers at two of its factories in Bangladesh as per projected orders for that year through its so-called ‘solidarity fund’. Switcher targeted the CMT workers at these factories although it planned to extend the initiative to workers in the knit and dyeing units in 2014. Since this was an entirely new initiative, the company asked the MSI of which it was a member to undertake a feasibility study via a consultation exercise with workers and management at the two facilities, Bangladeshi legal experts and the 4 main union joint bodies for the sector.

Management and employees at both factories welcomed the Switcher initiative to pay more to the workers with a roll forward from Q2 2013 and were asked to consider the most effective way of managing this either through a wage enhancement or through a workplace fund. Both management and employees at both factories opted for the wage enhancement with a consensus in both cases for a single (annual) one off payment as a separate allowance made to *all* employees at each factory, unlike the outcome at Armstrong Knitting Mills. Following the signing of an MOU, it was agreed that the transfer would occur in the final purchase order for the year following the Muslim Eid festival when a specific bonus related to the festival is usually paid out. This would avoid any additional payment by the brand being used to offset the bonus by the factory management. Taking Factory A as an example, some 4,500 workers were in line for a one off payment of BDT 437 (USD 5.5) with a possible roll forward as part of future orders. Significantly, a separate off site trade union consultation on the initiative produced an entirely different proposal. Viewing the amount as a negligible one off payment, the union consensus was that unless the gesture was the vanguard of a wider buyer or even MSI initiative, it might be seen as a charitable gesture designed to boost the profile of the buyer rather than genuinely address the issue of poverty wages and absence of benefits amongst Bangladeshi garment workers. Consequently the majority of the representatives present opted for a collective welfare fund beginning first at factory level. USD 25,000 as a lump sum in a fund would be an amount of money which could be matched by the employer and if workers and the company each made a monthly contribution of BDT 5 this could form the basis of a welfare fund which could accrue to make retirement benefits, housing, health insurance and child benefits a future possibility<sup>38</sup> Transferring money into a fund, notwithstanding administrative hurdles (Miller 2012, p.118) would have circumvented the compound price escalation issue since this would have been separated off from the FOB.<sup>39</sup> However this never came to pass. Since neither of the factories had a trade

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<sup>37</sup> Switcher declared bankruptcy in 2016

<sup>38</sup> Towards a ‘Solidarity Fund’ for Switcher suppliers in Bangladesh Internal Report of a scoping study undertaken for the Fair Wear Foundation Dhaka 14-19 January 2013

<sup>39</sup>Such uncoupling may eventually cause a buyer/manufacture to run into problems with a supplier country’s tax authorities. Significantly following the Rana Plaza disaster a proposal emanated from Bangladesh for

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union presence nor collective bargaining, plans were put in place to proceed with the one off payment instead of the establishment of a welfare fund. However verification audits undertaken at one of the factories revealed a significant code breach and quality issues at the other supplier, and thus severely compromised the relationship of trust between Switcher and its supplier factory. It prompted the brand to abandon its initiative in Bangladesh and to make one off payments to workers at a smaller supplier in Xiamen, Southern China in 2014, where it took up 25% of the factory's capacity as against only 2% in each of the facilities in Bangladesh. Applying its formula of 1% of its total annual buy, the solidarity fund for distribution to the 66 workers at this factory amounted to EUR 11,500. Each worker received CNY 1,130 (EUR 174) almost half of one monthly salary. Switcher was planning to roll this forward in other supply countries<sup>40</sup>.

### 4.3. Mayerline: promoting collective bargaining at a supplier factory

Mayerline is a Belgian fashion brand which sources from South East Asia, China, Portugal, Italy, Lithuania, Tunisia and Turkey. In 2012 it commenced sourcing from Turkey where it fairly quickly ran into problems relating to freedom of association beginning with the dismissal of 37 union members who had objected to the introduction of new working methods. Following a three month worker protest in front of the factory, the Textile, Knitting and Clothing Workers' Union of Turkey (TEKSIF) submitted a formal complaint through the complaints procedure of the Dutch MSI Fair Wear Foundation of which Mayerline was a member<sup>41</sup>. Following active mediation by FWF and Mayerline, the factory started protracted negotiations with the union Teksif and finally signed a three year collective bargaining agreement in December 2013. Following a verification audit in 2014, earnings at this factory were deemed close to or above local living wage estimates for a single person (around TL 1,600 or EUR 680), though living wage estimates for a family of four are still considerably higher<sup>42</sup>. In addition overtime was curtailed and workers awarded a food support and a child allowance. Some of the dismissed workers were reinstated after given the choice between reinstatement or compensation.<sup>43</sup>

Mayerline was not the biggest buyer in the factory with only a 10% stake in the production and the CBA came at a financial cost to the factory since it would appear that not all buyers were prepared to cost on the basis of the new wage and benefits package.<sup>44</sup> As FWF has observed in the wake of this difficult case, 'other brands sourcing at this factory must also adopt pricing policies that support the CBA and reflect the additional costs to the manufacturer.'<sup>45</sup>

The Mayerline case is illustrative of the importance of the collective approach required if there is to be a new payment system and structure supported by buyers and a specific supplier. This brings buyers and suppliers into uncharted territory since a CBA

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foreign buyers to jointly fix a minimum international wage for the sector at twice the then hourly rate and to pay the additional amount directly into a Garment Workers Welfare Trust to address a range of issues inadequately covered - safety, work environment, pensions, healthcare, housing, their children's health, education, childcare, retirement, old age and travel. (M. Yunus 2013)

<sup>40</sup> <http://www.getchanged.net/webautor-data/47/C3-SWITCHER-LW-BSD-03-2015.pdf>

<sup>41</sup> Mayerline Social Report 2012; <http://www.fairwear.org/ul/cms/fck-uploaded/documents/socialreports/2012/Mayerlinesocialreport2012.pdf>, [accessed 17 August 2015].

<sup>42</sup> The lowest estimate recorded in the Fair Wear Foundation Wage Ladder was 3333 TL for 2014.

<sup>43</sup> <https://www2.fairwear.org/living-wage-portal-obstacles/need-for-real-world-examples/#!/content/https://www2.fairwear.org/living-wage-portal/doing-great-things-together/> [accessed 18 August 2015].

<sup>44</sup> *ibid*

<sup>45</sup> Interview with Fairwear Verification Coordinator, Ruth Vermeulen.

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would require some form of collective buyer industrial relations engagement at a shared manufacturing facility. Such a development poses a number of challenges mentioned at the outset of this paper.

#### **4.4. Working through an attempt to establish a labour minute costing approach in shared facilities: the Fair Wear Experience.**

FWF is a multi-stakeholder initiative which has some 82 member firms as at October 2016 plus a further 3 manufacturers. FWF has intentionally restricted its focus to the garment manufacture part of the overall value chain where sewing is the main activity since it views this as one of the most labour-intensive phases of the production process and also the stage of production where many labour problems are found, and where effective remedies can positively impact the lives of millions of workers and their families.

In addition to factory verification audits conducted on behalf of its member firms, FWF has acted as a ‘laboratory’ for testing a number of those perceived obstacles which have prevented movement on the living wage standard: looking at the relationship between factory efficiency and wages with manufacturers in Macedonia; enabling member firms to understand where prevailing wages in their supplier firms sit in relation to national living wage benchmarks (the so-called wage ladder tool –a visualisation tool for representing wages at the audited factories in relation to existing in-country benchmarks); understanding the retail price dynamics of an FOB increase to address the living wage gap (the compound price escalation issue) (Fair Wear 2012a); examining the possibilities for brand collaboration under the terms of EU competition law (Fair Wear Foundation 2015a). As a member based organisation it continues to urge its affiliated companies to deliver in relation to the FWF living wage code.

Following an interim assessment of an on-going project to improve wages via productivity in Macedonia, it became clear that in order to ensure sustainable improvements, other measures including ‘adjustments to margins and FOB prices’ would need to be investigated by FWF’s member companies sourcing there, specifically looking at the potential of labour minute values. Working in parallel, FWF staff have been exploring ways in which member brands might be in a position to achieve this and also collaborate on the living wage issue in shared facilities. Following extensive dialogue with Arnold and Porter, a legal firm specialising in competition law (Fair wear 2015a) FWF consulted with the competition authorities at EU level on the issue of buyer collaboration on labour minute values with a view to determining the means by which buyers in a shared facility might usefully collaborate in raising wages and making transparent their fulfilment of the MSI’s code commitment on living wage. On the back of this legal opinion FWF has arrived at a possible way forward for its members to progress on their work on living wage in shared facilities:

In essence members would agree to pay a small uplift on the FOB price of a given garment achieved through the payment of a per unit production price that is calculated by reference to:

‘..... a labour minute value (i.e., a measure of how much a minute of labour costs at a given factory)... which....would be constant across the factory, and agreed collectively by the factory owner, the members using the factory and local stake-holders, workers and trade unions representatives. The labour minute value could be set at a level which incorporates a living wage (as well as other costs resulting from the maintenance of fair working conditions (for example, investment in health and safety measures)’ (FWF 2015a)

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This call prompted preliminary research (FWF 2015b) into the feasibility of providing guidance to member firms in costing for a living wage. Since this research has thrown up a number of critical issues it merits some scrutiny here.

It is important to note that the Macedonia project has been based on an approach which seeks only to bring those workers who are currently below what is deemed to be a living wage benchmark for the factory/country in question up to a new basic floor wage. It is not seeking to lift all workers on higher grades and necessarily maintain differentials where they may exist although such a move may indeed lead to appropriate wage adjustments as would happen following a single rate national minimum wage increase. The model and formula presented here is not intended to move a factory to an entirely new grading system for all workers. Fair Wear is clear that this is the function of management and trade unions/worker representatives through collective bargaining processes either at the factory/company level, or via national minimum wage determination authorities and/or sectorial collective bargaining between manufacturers associations and trade unions at industry level.

FWF specifically sought a legal opinion regarding the question whether a generic living wage labour cost could be agreed between the management of a facility shared by its member firms and the union/worker representatives. The preliminary research demonstrated that the calculation of such a labour minute value was indeed possible but that it would need to be locked in by way of a collective agreement and reflected in the costing practice of the factory/buyers in question. The unit labour cost i.e. the ('living' wage) labour minute value multiplied by the time taken to assemble a garment would of course continue to be negotiated between an individual buyer and the manufacturer subject to the specific design of the garment ordered thus preserving confidentiality on price negotiation as dictated by competition law.

In the example used by FWF researchers, real data for 2014 was used from a CMT factory in Macedonia. The existing labour minute cost was calculated at 4.3 cents. In the absence of an official living wage benchmark for this country, a number of organizations were consulted resulting in a wage ladder for Macedonia which revealed a variance of between MKD 12.705 / EUR 203 and MKD 48.700 / EUR 791 per month. In the FWF guidance note calculations, two of the 5 LW benchmarks – EUR 521 per month and the target wage estimate of EUR 243 per month were used in line with its principle of establishing a minimal starting point for a living wage figure. FWF costed against these 2 benchmarks for the purpose of achieving a new wage floor. The factory sampled provided data on all of its employees for a quarter (3 months) from which it was able to construct an annual wage bill multiplying the average for the 3 months by 4.

The average earnings amount per worker (salary + in kind benefits including pay roll and social security taxes but excluding overtime and production bonuses) were compared with the benchmark figure to determine the difference to be covered. In this particular factory by adding up the difference for all the workers it was possible to arrive at a total additional labour cost necessary to reach a new living wage minimum.

**Figure 9: Average Wages in Macedonian Factory**

#	Employee	Salary(NET)	Benefit 1 Non-compens. (MEALS)	Benefit 2 Non-compens. (Transportation)	Benefit 3	Benefit 4	Benefit 5	Total Salary	Living Wage Benchmark	Delta Total Salary vs. Living Wage
1	Worker A	Net Salary €	MKD 1,061.00					MKD 1,061.00	MKD 12,705.00	MKD 11,644.00
2	Worker B	MKD 12,604.00	MKD 1,061.00	MKD 1,262.00				MKD 14,927.00	MKD 12,705.00	MKD 0.00
3	Worker C	MKD 10,100.00	MKD 1,061.00	MKD 1,262.00				MKD 12,423.00	MKD 12,705.00	MKD 282.00
4	Worker D	MKD 14,601.00	MKD 1,061.00	MKD 1,262.00				MKD 16,924.00	MKD 12,705.00	MKD 0.00
5	Worker E	MKD 9,507.00	MKD 1,061.00					MKD 10,568.00	MKD 12,705.00	MKD 2,137.00
6	Gocevska Desa	MKD 13,107.00	MKD 1,061.00	MKD 1,262.00				MKD 15,430.00	MKD 12,705.00	MKD 0.00
7	Hristova L.	MKD 11,102.00	MKD 1,061.00					MKD 12,163.00	MKD 12,705.00	MKD 542.00

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Using the Employers' Association (TTA) and the Trade Union Federation (SSM) 'target' wage estimate MKD 14.000-15.000 (eq. EUR 227-243) we can see from this snapshot of the wage data at the factory in question that some workers (A,C & E) are already being paid this target figure while others B & D would require an uplift. By reviewing and adding up the final column for all workers requiring an increase, the total extra money to be found in this particular factory would be EUR 85.250. This is the total amount a single buyer or a collective of buyers would be required to find across a year. Dividing this figure by the available capacity (6.075.000) minutes per year, one arrives at a new living wage labour minute factor of EUR 0.0124. This amount has to be added to the existing 4.3 cents labour cost which gives us a new labour minute value of EUR 0.056 (5.6 cents). Using the higher benchmark would yield a new labour minute value of 11.6 cents and require an additional EUR 505.460 funding. Since these values have to be multiplied by the standard allowed minutes for the particular garment(s) the new unit labour costs would then vary from garment to garment and depending on the benchmark chosen. If we take a dress shirt as an example one would arrive at new unit labour costs of EUR 50 cents and EUR 2.94 respectively.

By locking in the new labour minute value the supplier and buyers would at least be able to claim that they were costing for a living wage. However, it became clear that aiming to establish a new wage floor and NOT a new wage structure would lead to considerable industrial relations problems since workers in higher grades would see their differentials eroded. In unionised facilities it would normally be expected that the outcome of successful wage negotiations would be the establishment of a new –higher-wage structure. However, in unorganised workplaces, unless the buyer agreement on a new labour minute value was supporting the emergence of a of process of social dialogue and/or collective bargaining which included capacity building for the union/worker representatives and to the establishment of a new wage structure, such an initiative could be open to supplier abuse since there would be no checks on the implementation of the wage uplift other than by periodic verification. Moreover, in the absence of a consensus on a credible methodology for determining a living wage benchmark,<sup>46</sup> FWF only provides a visualisation of existing benchmarks by way of its wage ladders. Nevertheless it does hold out the periodically adjusted, supra-nationally generated Asia Floor Wage as a target figure in those FWF sourcing countries which the AFW covers. Such a target figure is considered to be ambitious for buyers and suppliers and may clearly lead to a failure to achieve a consensus on the part of those buyers sharing facilities. Wider stakeholders around an appropriate national living wage benchmark also leaves the labour minute value approach to a living wage a notion yet to be realised in practice.

#### **4.5. The limits of individual buyer approaches**

Figure 10 summarises, in the form of a spectrum, the initiatives hitherto undertaken to address the redistribution of value added in apparel value chains. These are still very much in their infancy both at single and collective buyer level. Even the most progressive can be characterised as 'ad hoc' and collective buyer interventions have hitherto remained at arm's length, delivering efficiency gains through capacity building or amounting to exhortations towards national governments in advance of NMW determinations. We discuss the most recent collective initiative in section 5. For the time being we must conclude that individual efforts by some brands to unilaterally drive wage increases in factories operating in a multi-buyer sourcing environment are fraught with challenges. These are summarised in column 1

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<sup>46</sup> Some consensus is emerging as to the set of principles which might assist parties in determining how robust a benchmark might be cf. ISEAL 2013; FLA 2015.

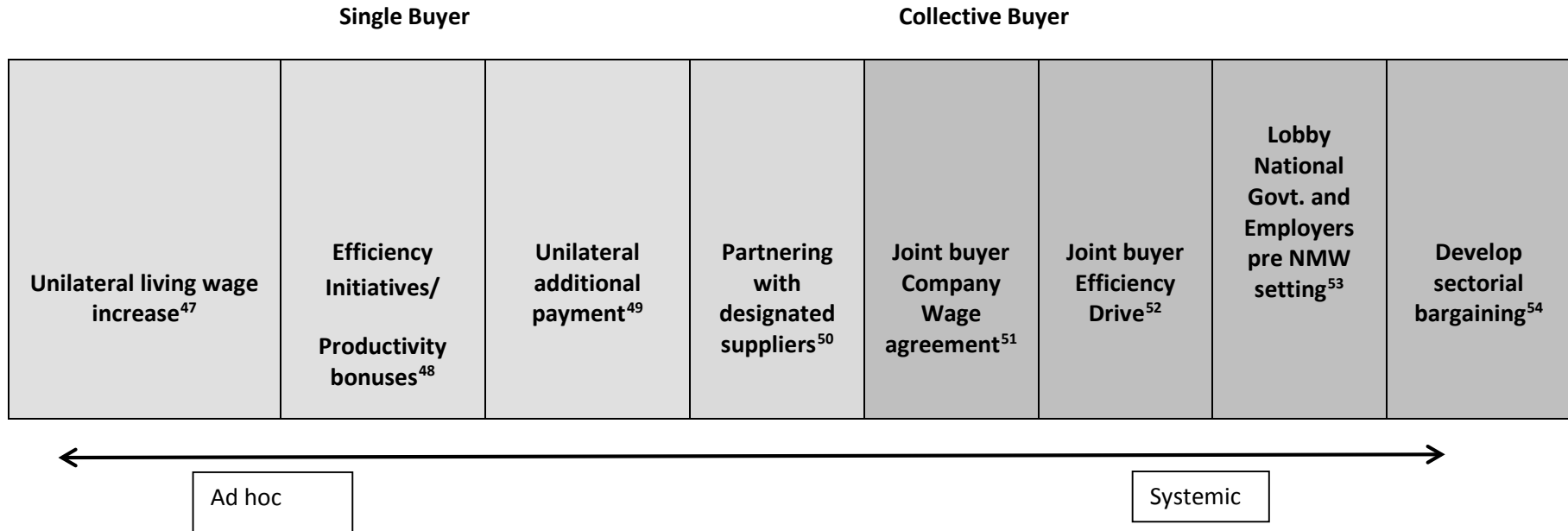


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of Table 4 below. How can a buyer wage intervention be sustainable when there is no longevity guaranteed in a commercial relationship? How will buyer collaboration in a shared facility sit with anti-trust law? What really changes in the wage structure when buyer wage interventions appear to be in the form of a one-off premium, tied to a specific sales campaign and do not affect the basic rate of pay? What are the likely industrial relations impacts specifically in relation to differentials where efforts to raise the wage floor only target those beneath a specific benchmark? What scope is there for worker participation where the prime mover is the buyer or MSI and not the factory and its workers and their representatives, and where the initiative is entirely voluntary? What adjustments are necessary to the costing breakdown when a substantial wage increase is mooted?

Columns 2 and 3 of Table 4 attempt to clarify what is possible under a national minimum wage declaration and an industry wide wage agreement and the ways in which technical and legal problems may be overcome at this level. Theoretically, an industry wide bargained wage between representative trade unions and employers associations where the process of negotiation regulates a cost of living benchmark leaving flexibility for company level supplementary bargaining would appear to hold out the greatest possibility for an up-scaled approach to the redistribution of value added. In the next section we examine the implications of the more systemic industry wide approach for buying practices and specifically labour costing.

**Figure 10: Spectrum of Buyer Approaches to Living Wage \***



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NB: These are examples and do not constitute an exhaustive list. Some ACT buyers have also been involved in efficiency initiatives.

<sup>47</sup> Knights Apparel

<sup>48</sup> M & S, New Look, Asda George

<sup>49</sup> Switcher, Nudie, Continental Clothing.

<sup>50</sup> H & M Bangladesh/Cambodia Fair Wage factories.

<sup>51</sup> Mooted under the Fair Wear Labour Minute model

<sup>52</sup> Achieved via jointly funded training programme in the BBW initiative : M & S, Tesco, New Look, Mothercare, Ralph Lauren, Varner Group, Sainsbury's, Arcadia Group. Did they bring systemic changes?

<sup>53</sup> Cambodian Buyers 2014: Inditex, C & A, Tchibo, Brown Group, Next, H & M, Primark, New Look. Myanmar Buyers 2015

<sup>54</sup> ACT Arcadia, ASOS, C&A, Debenhams, H&M, Inditex, N Brown, New Look, Next, Pentland, Primark, Tchibo and Tesco.

**Table 3: Modes of Living Wage Implementation**

	<b>Firm level living wage intervention</b>	<b>National Minimum Wage increase</b>	<b>Industry wide bargained increase</b>
<b>Permanency</b>	Dependent on length of buyer/supplier relationship	Legally defined and lasts for the duration of the declaration	Defined by duration of the agreement
<b>Competition law restrictions on buyer collaboration</b>	Possible cooperation via the joint negotiation of labour minute value within a facility	n/a	No restrictions
<b>Possible wage interventions</b>	Floor wage New grading structure/regradings Production bonus, one off payment	Rates of Pay Grading structure for all workers Additional allowances	Wage rates Grading structure, Additional allowances and other terms and conditions
<b>Differentials</b>	Not guaranteed where only a new wage floor is established	Integrated in wage structure	Established in pay scales as part of a wage structure
<b>Scope</b>	Restricted to single manufacturers	Whole sector/economy	Members of manufacturers' Association / Non Members if the agreement is extended by government
<b>Prime Mover(s)</b>	MSI + Members Individual sourcing companies, in rare cases supplier	National Government	International buyers, global unions, national unions, manufacturers' associations
<b>Living Wage Benchmark</b>	Multiple sources International + national + worker	Multiple national sources	Generated by trade union members with additional possible input from labour support organisations
<b>Mode of implementation</b>	Unilateral buyer supplier / collective bargaining where unions are established	Government Declaration	Collective Bargaining
<b>Increase via FOB</b>	Negotiable between buyer and supplier	Negotiable between buyer and supplier	Negotiable between buyers', suppliers and associations and trade unions?
<b>Enforceability</b>	Voluntary	Legally enforceable	Voluntary or legally binding

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## Part 5. Sectorial Bargaining towards a Living Wage

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At the last tripartite summit to discuss the state of the sector, a point of consensus within the ILO alluded to the need for international buying companies to be involved in sectorial social dialogue.<sup>55</sup>

### 5.1. The emergence of sectorial social dialogue

With the exception of some European countries, sectorial bargaining is quite rare in apparel particularly in the centres of production in Asia where minimum wage determination holds sway<sup>56</sup>. It has been, however, the collapse of the Rana Plaza factory in Bangladesh in April 2013 which has prompted the creation of two buyer coalitions to address factory safety in a national sector –the Accord and the Alliance for Worker Safety. In the former case a 5 year work programme has been established by dint of a collective agreement between buyers sourcing from Bangladesh, UNI and IndustriALL and its national affiliates. This has given the idea of sectorial social dialogue fresh impetus and opened up the debate for sectorial buyer involvement in other compliance issues including wage determination (Anner et.al 2014). Anner et.al place the Bangladesh Accord in particular in its historical context by reminding us of the high watermark of collective bargaining in the USA in the 1930s in the form of triangular *jobbers' agreements* between clothing contractors, manufacturers and trade unions. Such agreements were the articulation of a fundamental recognition of an important principle –that contracting companies i.e. today's brands and retailers, are jointly responsible with their suppliers for safeguarding working conditions in a buyer driven value chain, a tenet now found in the UN Guiding Principles. Jobbers' agreements had broad coverage because they were negotiated and signed not with individual firms but rather with manufacturers' associations. Secondly, they included the majority, if not the entirety, of jobbers and contractors making a particular type of apparel. Thirdly, the agreement enshrined the principle that jobbers were to pay contractors at least an amount sufficient to enable the contractor to pay the workers the wages and earnings as laid down in the agreement, and in addition a reasonable amount to cover the contractor's overhead and profit (ibid p.22).

An initial small group of companies within the Accord coalition began to address the question of collaboration on the wage issue venturing to issue joint public declarations for minimum wage increases vis à vis the Bangladeshi and Cambodian governments in 2013 and 2014 respectively and latterly in 2015 the government of Myanmar, in response to pressure from IndustriALL and campaign groups. The text of their most recent declaration for Cambodia is worth reproducing here:

‘As responsible businesses our purchasing practices will enable the payment of a fair living wage and increased wages will be reflected in our f.o.b. prices, taking also into account productivity and efficiency gains and the development of the skills of the workers, carried out in cooperation with the unions at the workplace level’<sup>57</sup>

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<sup>55</sup> ILO 2014 Global Dialogue Forum on Wages and Working Hours in the Textiles, Clothing, Leather and Footwear Industries, Points of Consensus, Geneva, 23–25 September 2014  
[http://www.ilo.org/wcmsp5/groups/public/---ed\\_dialogue/---sector/documents/meetingdocument/wcms\\_311155.pdf](http://www.ilo.org/wcmsp5/groups/public/---ed_dialogue/---sector/documents/meetingdocument/wcms_311155.pdf) [accessed 20 August 2015]

<sup>56</sup> The most notable example is South Africa (Grawitzky 2011) and there has been a recent breakthrough in Jordan. cf [http://www.ilo.org/beirut/media-centre/news/WCMS\\_214426/lang--en/index.htm](http://www.ilo.org/beirut/media-centre/news/WCMS_214426/lang--en/index.htm) [accessed 11 September 2015]

<sup>57</sup> Letter to the Permanent Deputy Prime Minister H.E. Keat Chhon dated 18 September 2014.

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The same buyers, since joined by a number of other brands and retailers<sup>58</sup>, have signed an MOU along with IndustriALL to establish the so-called ACT (Action, Collaboration, Transformation) Initiative to enable industry wide collective bargaining in key sourcing countries, beginning with Cambodia, Bangladesh and Ethiopia. For the global union the logic is clear:

‘Industry wide agreements make it very difficult for employers to escape their obligations. They effectively take labour costs out of competition by creating a level playing field that enables conditions to improve for all workers in the industry.’<sup>59</sup>

Whilst local labour market conditions may dictate a degree of wage competition to retain labour, macro economically and globally speaking there remains a need to draw a line beneath the so-called ‘race to the bottom’ whereby sourcing has been dictated as much by labour cost as quality and lead time. We have clarified in Table 3 the limits and possibilities of the individual versus collective buyer approach to resolving the wage issue and suggest a certain logic to an industry wide approach when key obstacles are taken into account. For manufacturers such a development poses, however, a specific challenge since FOB prices have been falling during the last decade (ILO 2016 ) and the respective manufacturers’ associations in Cambodia and Bangladesh, for instance, have been pressing for buying behaviour changes –specifically CMT increases to accommodate new minimum wages and appease an increasingly militant workforce in both countries.

In a recent survey undertaken by the Garment Manufacturers Association of Cambodia of 167 member firms, for example, two-thirds said they could not afford a further increase in the minimum wage so soon after the last hike... while 27% viewed an increase of 1-5 USD as ‘sustainable’, only 7% said they would be able to afford more than 5 USD for their businesses. Some 86% of respondents said they expected their garment export volumes to decline between 10% and 30% in the second half of 2015 and the overwhelming majority (99.4%) of firms surveyed said they were still receiving the same price or less for their garments than they were in 2014, with 30% noting a 10% reduction in the FOB<sup>60</sup>.

From a the Garment Manufacturers’ Association (GMAC) perspective the onus is on buyers to address their day to day transactions with their suppliers to ensure that industry wide bargaining outcomes (should they be established) can be met at the factory level. This sentiment is present in a piece of analysis undertaken by the ILO early in 2015 to assess the additional contribution which buyers would need to make in their FOB in order to accommodate the new minimum wage of 128 USD in Cambodia and how much would have to be achieved through productivity gains<sup>61</sup>. Assuming a +4% productivity growth, factories would be able to afford a wage increase of USD 7, with global garment buyers absorbing the bulk of the rest of the wage increase (USD 27 per month). To accommodate this cost increase, FOB prices would need to increase on average by 2.7%.

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<sup>58</sup> Arcadia, ASOS, C&A, Debenhams, H&M, Inditex, N Brown, New Look, Next, Pentland, Primark, Tschibo and Tesco.

<sup>59</sup> Jenny Holdcroft, Policy Director IndustriALL in Just-Style.com available at <https://www.just-style.com/pap.aspx?ID=126021> [accessed 23 August 2015].

<sup>60</sup> Smith K. 2015 ‘Unions and wages top buyers’ concerns in Cambodia’ in Just-Style.com available at <https://www.just-style.com/pap.aspx?ID=126142> [accessed 13 September 2015]

<sup>61</sup> Malte Luebker 2015 Cambodia’s new USD 128 minimum wage: How much will it cost? Modelling the impact on labour costs and FOB prices, Briefing session for ITUC and IndustriALL Co-organized by ILO-ROAP and Better Work.

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## 5.2. Reconciling productivity and efficiency with higher wages

ACT has pledged to ‘develop mechanisms to link purchasing practices to the outcome of industry bargaining; supporting and enabling manufacturers to provide their workers with a ‘living’ wage and working conditions that meet the retailers and brands’ requirements’ whilst simultaneously working with suppliers ‘to develop and implement best practices on manufacturing standards and systems, including efficient human resource and wage management systems’. From what is known it is likely that there will be a trade-off between increases in the CMT cost and pressures from brands and retailers for factories to improve their efficiency. It is certainly true that at a stable and/or increasing order situation significant financial gains can be made by all companies involved in a global value chain by applying world class manufacturing standards to improve productivity and efficiency. Buyers will inevitably seek to focus on factory productivity and efficiency but inefficiencies exist both upstream and downstream in the value chain. Moreover, there is a tendency to present efficiency as a problem of labour –the term ‘labour efficiency’ is often used, erroneously, to describe a much wider spectrum of factors which can influence the operational effectiveness of a factory. Efficiency gains can be achieved through longer term buyer-supplier relationships, joint range planning, stock keeping units (SKUs) and order optimisation, changes to the factory layout, and improvements in managerial competence (Bheda 2012). This is before any improvements in employee motivation, performance and skill level are factored into the equation. Since labour productivity and efficiency are in a direct relation to each other but are often used interchangeably, it is useful to clarify terms here. One can distinguish between operator efficiency, line efficiency and labour productivity.

*Operator efficiency* equals the total minutes produced by an operator measured against the total minutes attended expressed as a percentage. Line efficiency, again expressed as a percentage, is calculated by multiplying the total number of production pieces by the standard allowed minutes for the particular garment and comparing this figure with the total available minutes as measured by the number of workers on the line.

*Line efficiency* is one of the most commonly used performance measuring tools and is of increasing interest to buyers particularly in countering supplier demands for increased prices. The argument is made that a more efficiently organised production would enable greater throughput and maximised earnings.

*Labour productivity* equals the value of production (the gross value of sales minus the value of purchased inputs such as fabric, trim, and energy) divided by labour input as measured by total work hours. Labour productivity expressed as the ratio between output and input can thus be estimated at the national, aggregate level for the industry.

Organised labour has always argued that labour productivity has a tendency to increase when wages have risen not the reverse. If wages are taken out of competition in a global/macro-economic sense then national garment sectors will have to compete on quality and efficiency. Hence it becomes crucial that manufacturers manage their resources optimally.

In the example below we use real data from a Thai sportswear factory to model the type of gains which could be possible with efficiency improvements at factory level. In this particular case the factory has a total annual operating cost of USD 2.221.257, a starting efficiency level of 46% with 382 sewing operators, working a 48 hour per week and 300 days per year. A 10% increase in efficiency was targeted in this factory, which would amount to an annual saving potential of USD 482.882.

**Table 4 Efficiency savings potential at a Thai Sportswear Factory**

Available Working Minute / Year	Efficiency	Productive Minute Output / Year	TTL operation cost Factory US\$	Working Minute Cost US\$cent	Efficiency Saving Potential / Minute US\$cent	Annual Saving Potential US\$
55008000	46%	25'303'680	2'221'257	8.778		
55008000	47%	25'853'760	2'221'257	8.592	0.187	<b>48'288</b>
55008000	48%	26'403'840	2'221'257	8.413	0.366	<b>96'576</b>
55008000	49%	26'953'920	2'221'257	8.241	0.537	<b>144'865</b>
55008000	50%	27'504'000	2'221'257	8.076	0.702	<b>193'153</b>
55008000	51%	28'054'080	2'221'257	7.918	0.861	<b>241'441</b>
55008000	52%	28'604'160	2'221'257	7.766	1.013	<b>289'729</b>
55008000	53%	29'154'240	2'221'257	7.619	1.159	<b>338'017</b>
55008000	54%	29'704'320	2'221'257	7.478	1.301	<b>386'306</b>
55008000	55%	30'254'400	2'221'257	7.342	1.436	<b>434'594</b>
55008000	56%	30'804'480	2'221'257	7.211	1.568	<b>482'882</b>

The calculation shows, that each per cent of efficiency increase is resulting in an annual saving potential of 48.288 USD for this factory. It can either be seen from the resulting decrease of working minute cost, or the ability of the factory to increase the output with the same amount of available resources. This is predicated on order book stability/growth. Since efficiency initiatives are geared towards a reduction of resources, including personnel, there will clearly be impacts for workers beginning with a rationalisation/shedding of non-direct staff and production workers. Whilst there is a logic to retaining as many sewers in a factory since a company is dependent on their productive capacity for its income (new technology notwithstanding), productivity savings may be generated by a reduced cycle time and therefore an increased line production target. Moreover some lean manufacturing programmes have the capacity of rationalising the number of workers on a line as well as reducing the cycle time, as the Figure 11 shows from a Bangladeshi factory making polo shirts. The introduction of world class manufacturing standards, a term which covers a multitude of initiatives to essentially upgrade production systems otherwise known as *process upgrading* in global value chain terminology, may have detrimental effects on the existing workforce.

**Figure 11 Lean manufacturing impacts on polo shirt production in a Bangladesh factory**

ITEMS	UNITS of MEASURE	VALUES	
		CONVENTIONAL	LEAN
Total Team-Workers		57	
Sewing Operators per team		44	21
Total Wages		344,850	18
Produced Pieces		46,904	127,050
Working hours (one-worker)	Taka/Month	10	24,804
Working days	Pieces/Month	26	10
Total working Team-hours	Hours / day	14,820	26
Average Cycle Time per Piece	per month	18.96	5,460
Cost per produced Piece	Hours/Month	7.35	13.21

Buyers are interested in such efficiency gains because they can absorb rising wage costs following a new NMW declaration and thereby keep the FOB pegged back (See Figure 8 above). For the manufacturer such cost savings can increase their own profits where excess capacity is generated to take on more orders. It is understandable therefore that the participating brands and retailers in the ACT are stressing world class manufacturing standards (efficiency gains) as part of the solution for delivering enhanced wages either through NMW determination or sectorial bargaining. Certainly there is room for improvement in target countries such as Cambodia (Nathan Associates 2007) and Bangladesh (Woodruff 2014). However, the general tenet advocated by campaigners is that higher wages should lead to higher labour productivity and not the other way round.

## Conclusion

This paper highlighted that efforts to redistribute value added in favour of apparel production workers operate in a structurally asymmetrical value chain with the potential for wage increases being compromised by a footloose, buyer driven, outsourced system of production as the global apparel industry is concerned.

Whilst it is difficult to measure the distribution of value added to capital and labour both globally, nationally and at brand level, it is however possible to measure the distribution across individual apparel products. This has been the starting point and the methodological basis for this working paper. We have attempted to deconstruct labour cost within the costing of specific apparel items in an effort to determine the limits and possibilities of buyer efforts to address their code of conduct commitments with respect to a ‘living’ wage and due diligence vis à vis the UN Guiding Principles.

Against a backdrop of falling raw materials costs, buyers have been able to manage wage shocks with minimum impact on their FOB. Due to competition law considerations, buyer living wage initiatives have hitherto remained individual and given the fragmented nature of social responsibility within this tier of the apparel value chain – ‘piecemeal’ and experimental. Such initiatives have encompassed one-off payments, and wage increases realised largely on the back of efficiency drives which have led either to the introduction of a productivity bonus or an increase in the same. Efforts to overcome this ‘silo mentality’ by way of a hypothetical joint buyer/manufacturer determination of a labour minute value in a shared facility may withstand a legal challenge as far as EU competition law is concerned. Such technical fixes are presently aimed at establishing a floor wage –i.e. the lowest wage level which would provide workers with sufficient income to cover basic needs plus an



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amount for discretionary expenditures. Such wage floors have the potential of upsetting existing differentials within an established wage structure and thereby underestimates the overall potential cost. This is an issue which potentially complicates existing unilateral living wage efforts at the level of the firm and will require further research.

The establishment of new grading systems and the increases of rates of pay within the same were historically the outcomes of processes of collective bargaining at different levels of the economy: sectorial, company and establishment. Only in very few cases has national minimum wage setting established a grading structure within outsourced apparel production countries. Whilst there appears to be an inexorable logic at work in the collective sector wide approach currently being pursued by a number of key brands and retailers and the global union IndustriALL under the Action, Collaboration, Transformation initiative, we should be under no illusion as to the ambitious nature of this undertaking given the fragmented and competitive characteristics of the global fashion industry. Industry wide bargaining poses, two key challenges for the industry. First from the manufacturer side a key prerequisite is the payment of an FOB price and within this a labour minute value, sufficient to cover such sector wide increases. Global Value Chain analysis suggests that there is room in the supply chain for a redistribution of margin. Second, from the buyer side, there is however the inevitable call for a concerted effort for factories to improve their efficiency. When fibre/fabric prices and the exchange rate have been taken into account, a trade-off between these two is likely to occur. Their respective magnitudes will of course be the 'stuff' of the intra organisational bargaining between buyers and manufacturer's associations outside of the formal collective bargaining process. Any new NMW/sectorial wage agreement would require an agreement between buyers and manufacturers on purchasing practices – specifically on a new labour minute value, an as yet absent methodology for dealing with the efficiency issue at an aggregate level and a principle which ensures that the overall CMT/FOB is adjusted to accommodate a new wage increase. For workers and their unions, efficiency initiatives will pose contradictory challenges. On the positive side upskilling should generate wage pressure and the need to revisit pay structures where such exist. On the other hand process upgrading is likely to have implications for job security and work intensification. Hence the need for workplace trade union organisation and capacity building to deal with these workplace challenges will be as strong as ever.

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