

CAPTURING THE GAINS

economic and social upgrading

Revised Summit Briefing

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This is a revised version of the Summit Briefing which informed panel discussions and stimulated debate at the Capturing the Gains Summit, 'Capturing the Gains in Value Chains', held in Cape Town, South Africa, 3-5 December 2012 (<http://www.capturingthegains.org/summit/>). It incorporates recommendations arising from debate with key stakeholders at the Summit.

The findings and views presented here do not represent those of Capturing the Gains funders or supporting organisations.

Economic and social upgrading in global apparel production networks

John Pickles and Shane Godfrey¹

Abstract

The apparel industry is one of the most globalized. Export production contributes substantially to national export earnings and employs tens of millions worldwide, particularly women in low-income countries. However, the globalization of production has also led to poor working conditions and regional wage depression. Over time, the national structure of manufacturer-driven value chains has given way to increasingly fragmented production systems, but in recent years the trend towards concentration, supply chain transparency and strategic partnerships between buyers and suppliers has improved conditions for some supplier firms and workers. Trade and preferential market access policies severely constrain economic and social upgrading opportunities.

Keywords

textiles, apparel, trade agreements, exports, wages, working conditions

Authors

John Pickles is the Earl N. Phillips Distinguished Professor of International Studies and Chair of the Department of Geography at the University of North Carolina, Chapel Hill, US.

Email: jpickles@unc.edu

Shane Godfrey is a Senior Researcher within the Labour and Enterprise Policy Research Group at the University of Cape Town, South Africa.

Email: shane.godfrey@uct.ac.za



“ Globalization of apparel export production created poor working conditions and regional wage depression. ”



The apparel global value chain

Global apparel exports currently total around US\$350 billion and contribute substantially to national export earnings. Apparel production for export employs tens of millions of workers worldwide, particularly women in low-income countries. The globalization of apparel export production has also created poor working conditions and regional wage depression.

Over time, the national structure of manufacturer-driven value chains has given way to increasingly fragmented production systems in globalized buyer- and retailer-driven value chains. Today, the apparel global value chain (GVC) is organized around five main segments (Figure 1).

Trade policies and trade rules of one kind or another have shaped this geography. Throughout the 1980s and 1990s, the Multi-Fibre Arrangement (MFA) created a quota regime that encouraged the expansion of production in many low-income countries. With the final removal of quotas in 2004, mainland China was the main beneficiary, as well as South and Southeast Asian countries, such as Bangladesh, Cambodia and Vietnam. With each shift in sourcing, prior patterns of production and employment were disrupted, often resulting in profound regional economic declines and high levels of unemployment.

Apparel is an important export earner for many lower-income countries, contributing 6.6 percent of total manufacturing exports in Asian countries, 7.3 percent in Latin America, and 9.9 percent in Africa.

Apparel manufacture has also been an important generator of employment for women, especially in regions where waged work was formerly not available to them. Some argue that these jobs are ‘good’ compared with the alternatives and that they contribute to poverty reduction.

Others see the internationalization of the industry being driven by the need to manage low-skilled labour pools working for low wages, leaving in its wake regional unemployment where contracts have been withdrawn. Apparel workers have, as a consequence, been at the forefront of struggles for collective rights against long and irregular working hours, poor and sometimes dangerous working conditions, low wages and benefits and physical abuse and violence.

Economic and social upgrading after 2004

Capturing the Gains carried out research in 17 low- and middle-income countries in Africa, Asia and Latin America.² The focus was on the relationships between economic upgrading and social

Notes

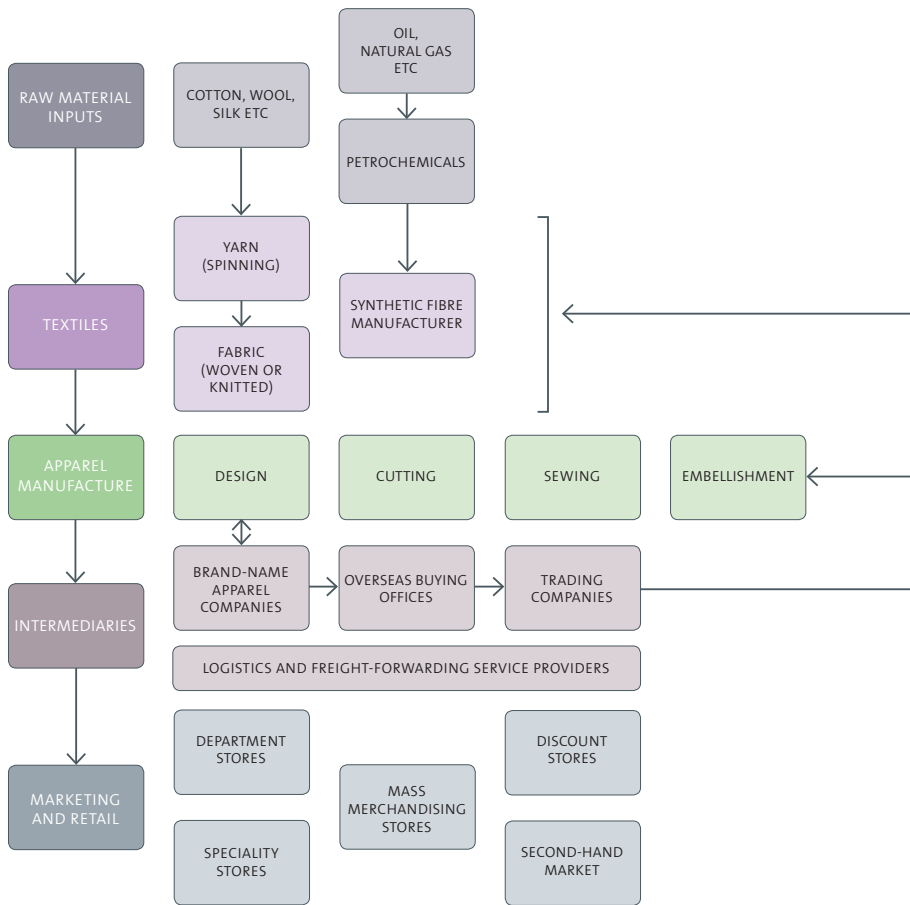
- Contributors: Nazneen Ahmed, Dennis Arnold, Shamel Al-Azmeh, Jennifer Bair, Stephanie Barrientos, Thomas Bernhardt, Gary Gereffi, Annelies Goger, Nguyen Thu Hang, Peter Knorringa, Will Milberg, Doug Miller, Mike Morris, Dev Nathan, Kelly Pike, Arianna Rossi, Cornelia Staritz, Meenu Tewari, Lan Tu and Shengjun Zhu.
- Sub-Saharan Africa (Kenya, Lesotho, Madagascar, Mauritius and South Africa), North Africa and the Middle East (Egypt, Jordan and Morocco), East Asia (Cambodia, China and Vietnam), South Asia (Bangladesh, India and Sri Lanka) and Central America and the Caribbean (the Dominican Republic, Haiti and Nicaragua).





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The shifting of orders from one region to another has seen ... uneven gains for firms and workers.
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Figure 1. The apparel global value chain



upgrading in the apparel industry.³ This section highlights some of the findings relating to economic and social upgrading and downgrading after MFA phase-out and the ending of quotas.⁴ The shifting of orders from one region of the world to another has seen some firms improving their position in terms of value-added and productive

capacity, and some workers are seeing improvement in the terms, conditions and remuneration of employment and respect for rights (Figure 2). But in other regions and other parts of the chain, these gains are uneven; firms and workers have experienced economic downgrading, employment loss, declining wages and poor and uncertain

Notes

- 3. See Bernhardt, T. and Milberg, W. (2012) International Trade and the relation between economic and social upgrading. Capturing the Gains Summit Briefing.
- 4. For a fuller account of these findings see Pickles, J. (2012). *Economic and social upgrading in apparel global value chains: – public governance and trade policy.* Capturing the Gains Working Paper.

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Trade agreements play a crucial role in structuring the apparel global value chain.

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jobs. For example:

- Bangladesh, Cambodia, China, India, Indonesia and Vietnam have experienced economic upgrading in terms of both increased export market share and export unit values.
- The ending of the MFA was partly mitigated in Sub-Saharan Africa by the introduction of the African Growth Opportunities Act (AGOA) in 2000, although Kenya saw declines in both market share and unit values of exports. Lesotho's export market share also declined significantly.
- Because Mauritius has a fully integrated textile and apparel sector and produces higher-value products, it was able to recover quickly from the ending of the MFA by capturing residual contracts from the European Union – so, although its export market share decreased, there was an increase in export unit values.
- Limited government support to the industry, weaknesses in the *maquiladora* export platform model (which locks manufacturers into simple assembly tasks) and a failure to diversify export markets beyond the US have all contributed to Mexico's declining market position in a context of increased competition from low-cost Asian suppliers.

In terms of employment and real wage growth, some countries show clear-cut upgrading (China, India,

Jordan and Nicaragua). China has recorded the highest increase in real wages (+88 percent) and Jordan the largest expansion in employment (+64 percent). Cambodia and Bangladesh have recorded increases in employment but declines in real wages, while the Dominican Republic has experienced increases in real wages but declines in employment. Sub-Saharan African countries have seen declines in both employment and real wages. Sri Lanka has also experienced real wage declines.

Trade agreements play a crucial role in structuring the apparel GVC. They parse out the phases of production under rules that favour value capture in the major markets and the allocation of low-value activities to low-income and low-wage countries. Without strong state interventions to underwrite infrastructural investments and the development of national cotton, yarn, and fabric manufacture, and without workforce and educational investments to underwrite both the knowledge workers needed for design, branding, and marketing, and the consumers to drive demand, low-income countries have few developmental paths open to them.

Effects of the 2008 global recession

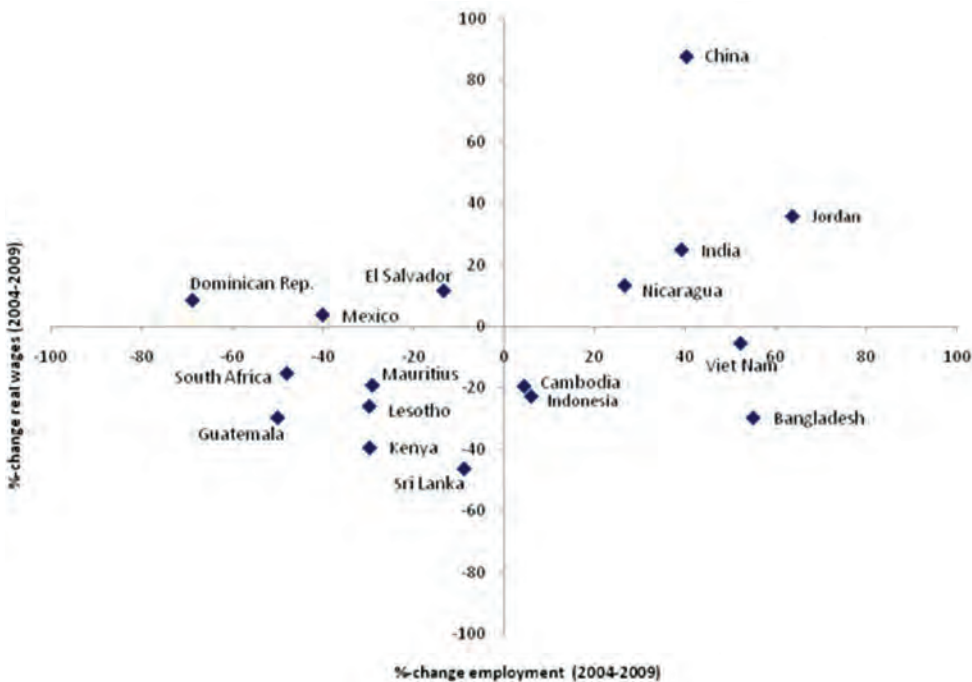
The growing dependence of global apparel trade on value chains has





“... countries that had weathered the ending of quotas better, also weathered the crisis better than quota losers.”

Figure 2: Social upgrading and downgrading in the apparel sector, 2004-2009⁵



Note: Time spans covered are different for Bangladesh (2005-2008), El Salvador (2004-2008), Guatemala (2002-2008) and Vietnam (2005-2008).

important indirect consequences. Our research found that post-MFA gains and losses amplified the ability of specific countries to respond to the 2008 financial crisis. The economic crisis and downturn in demand after 2008 had negative effects across the region, but smaller relative effects in Asian countries that had benefited from quota phase-out and the expansion of domestic markets. In fact, those countries that had weathered the ending of quotas better, also weathered the crisis better than quota losers. By

contrast, the countries most affected negatively by quota phase-out (African and most Central American and Caribbean countries) were also those that were most affected by the economic crisis.

Research findings also suggest that private governance mechanisms (corporate social responsibility, etc.), while positive in their own terms, have been insufficient to counteract the negative effects of post-quota sourcing shifts and the recession. State intervention has been crucial, however;

Notes

- Bernhardt, T. (2012). 'Economic and social upgrading of developing countries in the global apparel sector: insights from using a parsimonious measurement approach'. In Rossi, A., Luinstra, A. and Pickles, J. (eds.) *Toward Better Work: Understanding Labour in Apparel Global Value Chains*. London and Geneva: Palgrave/Macmillan and ILO. In preparation.
- For further exploration of links between economic and social upgrading see Bernhardt, T. and Milberg, W. (2012) *Capturing the Gains Summit Briefing*.



this is seen clearly in the success of the industry in Bangladesh, China, India and Nicaragua.

Trends in apparel GVCs

Quota removal has expanded the range of opportunities for footloose sourcing, which in turn has expanded employment opportunities in some low-income countries. This is often at a cost of poor working conditions, low wages, use of child labour, lack of social protection, the feminization

of work and gender discrimination in compensation and skill acquisition, and environmental damage from effluent discharge and the use of harmful dyes and chemicals.

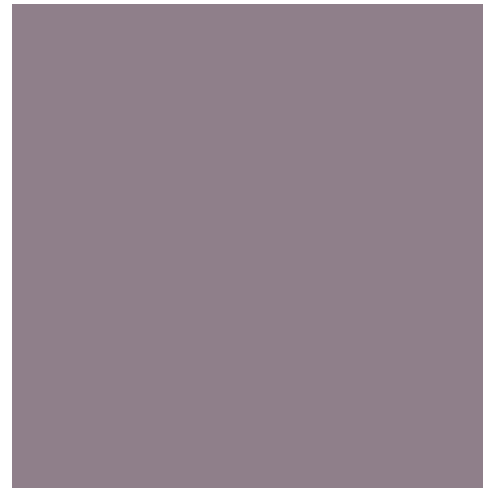
Today, apparel GVCs have squeezed wages to their limit, and buyers have turned their attention to other ways to manage costs (particularly logistics and end-market selection). More now recognize the increasing importance of the business case for investing in wages, working conditions and worker engagement.

Findings and recommendations

Post-MFA global value chain dynamics

- The national structure of manufacturer-driven value chains has gradually given way to increasingly fragmented production systems in increasingly globalized buyer-driven and retailer-driven value chains. The lead firms driving this international division of labour include retailers and brand owners, typically headquartered in the leading markets (Europe, Japan and the US). These firms tend to perform activities in the apparel value chain to which most value accrues – product design, branding and marketing. They mostly outsource the manufacturing process to a global network of suppliers in lower income countries.
- The final removal of MFA quotas in December 2004 expanded ‘footloose’ sourcing and employment opportunities in regions that benefited from the shift (such as China, Cambodia, Vietnam and Bangladesh). These do not necessarily lead to better working conditions or social upgrading. However, a buyer-driven competitive market has led, in recent years, to a reassessment of the importance of social upgrading in apparel global value chains.
- Fragmentation of apparel value chains, and the institutional and cost constraints placed on the equivalent development of yarn, fabric and dyeing industries, have limited opportunities for social and economic upgrading in supplier factories. Yarn and fabric manufacturers in major markets have been able to shape national trade policies and rules to protect their markets in increasingly global assembly chains. They have supported restrictive rules of origin in nearly all preferential market access agreements.
- The resulting apparel GVCs comprise interconnected and diverse production systems and working conditions. Trajectories of economic and social upgrading are correspondingly diverse, depending on variables such as firm size, capacities, product mix, buyer needs, and labour market conditions.





- Exploitation remains a problem, for both workers within many assembly factories and those who have lost their jobs as sourcing has shifted location. Three key points are:
 - Apparel production has been disembedded from integrated textile and clothing complexes, mature industrial labour relations, and strong health and safety state institutions. This has fuelled exploitation and restricted opportunities for developing backward and forward linkages.
 - Increased fragmentation and geographic dispersion of the value chain is compounded by reduced length of contracts, high turnover of suppliers, and higher demands on them, often without an increase in the contract price.
 - Responsibility for decent work has been distributed across a much broader range of actors, many of whom are ill-equipped to afford or facilitate social upgrading.
- The increasing globalization of apparel assembly has led to new sources of employment in low-income countries, particularly for women. While wages and conditions of work for female workers generally remain poor, the wage effects on household budgets and poverty reduction have been important.
- In some regions, markets and product mixes, the race to the bottom (and its search for ever-decreasing wages) may be exhausting itself, with new emphases:
 - In order to manage reputation risk and improve quality, lead firms increasingly elect to shrink their supply chains and source from a smaller range of strategic partners, who can offer a wider range of services;
 - In order to manage market risk, fast fashion and guarantees on delivery times and dates have become more important. The rise of Asian intermediaries and freight-forwarding companies, and the expansion of their services and guarantees, is a great advantage to suppliers in their service area. It is a disadvantage to suppliers and workers in other regions (such as Africa), where exporters with smaller volumes and longer delivery times are less able to benefit from consolidators, trans-loading, and air-sea freight.
- The lack of new facilities built in supplying countries suggests that post-quota shifting is giving way to a period of regional concentration; post-MFA, the export industry is concentrating in fewer leading exporting countries. This globalization is also restructuring traditional north-south trading patterns, and increasing the south-south linkages, especially with the rise of the BICS.

Governance

- Attitudes towards state intervention are changing. Lead firms and suppliers, in particular, are increasingly arguing that responsibilities and costs for social upgrading should be shared. Private governance alone cannot address the complexities of industrial relations in global value chains. In their view, the state should play a larger role in creating a 'supporting environment', including functioning policies on infrastructural and finance support, health and safety regulation, minimum wage controls, business information and technology services, education, testing, and training programmes. Trade and professional associations, NGOs and international standards organizations are also now recognized as having a much more important role than a decade ago.





- State policies have been of particular importance in some countries. In China and Vietnam, the state invested heavily in infrastructure and workforce training. In Bangladesh early on the government created special financing and tax supports for the industry. In Cambodia, the state collaborated with the ILO Better Factories Program and in Sri Lanka, public-private cooperation emerged around ethical sourcing initiatives.
- Countries have benefited the most in terms of social/economic upgrading in the apparel industry when they have enacted proactive governance and regulation policies (e.g., China's labour reforms). However, policy recommendations that argue for state-supported governance and regulation mechanisms must consider the political and economic unevenness in states' capacities to enact policies; it matters that China can enact more forms of governance than Guatemala.

Economic and social upgrading

- Both private and public social upgrading initiatives must take into account the policy environment in which trade policies often operate as constraints on an integrated and sustainable regional production system, locking suppliers into lower value parts of the value chain.
- Social upgrading is constrained by the globalized and fragmented structure of GVC production. This fragmentation, and the embedded limitations on the development of upstream and downstream capacities across the value chain, are significant barriers to social upgrading.
- Integrated apparel factories (i.e., which include yarn, fabric, dyeing and/or embellishment capacities) carry more advantages than disaggregated production networks; yet disaggregation is likely to continue with 'race to the bottom' cost-reduction strategies and nomadic sourcing techniques.
- Supply chain concentration and the development of strategic partnerships between buyers and suppliers are seen, by buyers, as essential to stabilize contracting, reduce uncertainty and upgrade product and work quality.
- Buyers' demand for faster turn-around times has highlighted logistical advantages and disadvantages for suppliers based on geographic location and the enabling environment, leading to the deployment of different technologies and strategies (i.e. air freight as opposed to ocean freight).
- A recurring theme in the country case studies of successful economic and social upgrading is the extent to which each apparel industry in a country was able to mobilize upstream and downstream linkages (often supported by the state) to its benefit. In the absence of such linkages, the only option is often reliance on export and/or domestic markets.

Trade policies and trade rules

- Quota removal led to a race to the bottom: a structure of global apparel production, employment, and trade based on 'nomadic sourcing' in search of low costs. The result of squeezing contract price has benefited lower-wage, higher-capacity suppliers (such as those in China). It has had disastrous consequences for workers in regions unable to compete on price or where price has been met by sweating labour and reducing investments in wages and working conditions.





Capturing the Gains brings together an international research network to examine economic and social upgrading in business communities across the developing world.

The programme explores the connections between business competitiveness and social prosperity with attention to firm innovation, trade expansion, labour standards and decent work.

Its research allows policy-makers and business leaders to better understand the relationship between business growth and poverty reduction in the global South.

- The impacts of trade liberalization and quota removal have been heavily mediated by unilateral and preferential trade agreements, regional trade agreements, rules of origin, bilateral agreements, and differential duties and tariffs. The proliferation of agreements and the complexity of trading regimes and rules led to differentiated growth patterns in low-income countries, with some production booms.
- Trade preferences remain critical for employment, but do not guarantee decent working conditions:
 - Preferential access can lead to growth booms (as in Bangladesh), but in some situations rapid growth is unregulated, leading to poor working conditions or disastrous unregulated factory over-building.
 - Uncertainty around preference renewal and delayed renewal has been disastrous for suppliers whose orders are preference-dependent but must be placed six to eight months in advance.
 - Social clauses (e.g., AGOA), supply chain transparency and early policy renewal are vital.
- Restrictive rules of origin in preferential market access agreements benefit textile exporters, but disadvantage apparel exporters. Locked into assembly-only contracting, options for economic and social upgrading are extremely limited.
- Uncertainty around changes in policy can lead to massive over-capacity in some regions and threats to apparel workers' livelihoods.
- End markets are crucial for suppliers. Suppliers' trade preference dependency on specific end markets can be a double-edged sword for them and their workers. For example, EU and US end market requirements differ significantly. Differences in the size of order, timing of delivery, currency exchange rates, and the relative balance among timing of delivery, volume, quality, penalties for delays, and price, are all important in shaping the practices of value chains.
- Dependency on rich country markets is concentrated geographically: Latin American producers (especially Dominican Republic and Mexico) are heavily dependent on the US; and African producers are heavily dependent on Europe, except for AGOA preferences for the US market and the growing internal African market.
- Trade liberalization has not led to a more simplified global trade regime, because of the many regional free trade and bilateral agreements. With quota removal, a more complex, varied and geographically uneven trade regime has emerged. Although preferential access agreements had ambiguous effects globally and did not always benefit low-income countries (e.g., sub-Saharan Africa), some examples of success have been the result of a rich country granting political favour, either as humanitarian gestures (Haiti's HOPE/HELP) or because of geopolitical interests (Qualifying Industrial Zones in Jordan and Egypt).
- Despite the recent shift of sourcing to Southeast and South Asia, China remains the main beneficiary of post-MFA trade policy.
- The Trans-Pacific Partnership (TPP) negotiations may put an end to two assumptions about global apparel trade:
 - The support of, and protection for, the US textile industry is essential for apparel trade agreements to pass the Congress.
 - Free trade agreements increase trade liberalization, which directly benefits the US.
- TPP Plan A will benefit every member. It will reduce guarantees for US suppliers and create large benefits for other members, such as Vietnamese textile and apparel manufacturers.

capturingthegains@manchester.ac.uk

www.capturingthegains.org

