



FLA STAKEHOLDER FORUM REPORT

Wages Along the Supply Chain: Assessment and Prospects

Washington, D.C.
October 26, 2009

Within global trade, wage practices along the supply chain are characterized by a number of serious problems, which have long gone unaddressed and have been further exacerbated by the current global economic crisis. While there is increasing international concern and a number of corporate social responsibility (CSR) initiatives on wages, work on this topic remains rather fragmented and would benefit from a more comprehensive and coherent approach.

To this end the FLA held a conference on October 26, 2009 aimed at enhancing the mobilization of CSR actors on wage issues and improving their ability to address wage issues along the supply chain. The event brought together academics and practitioners who have focused on wages, working conditions, and corporate social responsibility in their work to provide different theoretical and empirical perspectives on wage issues, as well as to report on current wage practices and the work of various CSR initiatives in this field.

The conference sought to discuss: (1) the main wage issues along the supply chain; (2) the initiatives that have been undertaken to address these issues; (3) recommendations on how wage issues might be progressively included into CSR; and (4) the roles different stakeholders can assume in helping develop and implement solutions to wage issues. The conference also sought to clarify the most relevant dimensions of “fair” wages and to launch future engagement on the topic that could lead to a dynamic framework for improving wages for workers within a broad “fair wage” spectrum.

The one-day conference was structured as three panels with invited guests and a concluding session. The first panel consisted of a general discussion of issues and challenges regarding wages along the supply chain. The second panel brought together practitioners from non-governmental organizations, including a consumer perspective, to discuss efforts to address wages in different supply chains. The third panel presented two concrete industry approaches to improving worker wages/compensation and challenges associated with each approach. The concluding session sought to assess prospects for greater incorporation of wages into CSR and set out next steps.

Conference Introduction

In setting out a conceptual framework for the conference, Aret van Heerden, President and CEO of the FLA, recalled that the issue of wages has been an ongoing concern of the FLA since its inception. The Apparel Industry Partnership, the predecessor of the FLA, requested a report on wages of apparel workers around the world from the Department of Labor that was completed in 2000. The FLA first held a multi-stakeholder conference on living wages in October 2003. The current conference is one more effort on the part of the FLA to focus attention on this very important topic, in a setting that leads to open discussion and exchange of ideas.

The challenge is to find an approach to wage setting that can be: (1) equitably applied; (2) scaled throughout a company's supply chain; (3) measured, audited, and remediated; and (4) sustained. A premise of this conference is that the "national wage setting machinery" based on minimum wages does not address these concerns in a satisfactory manner. Wages are the step child of CSR initiatives. While much attention and progress has been made with respect to other elements of CSR, discussions on wages seem to be stuck on sterile arguments about minimum wages or living wages, with little consideration of what is actually going on in the marketplace. The concept of fair wages, which takes into account the multidimensional character of wages, might be an approach. But the aim of this conference is not to focus on fair wages per se, but rather to start a multi-stakeholder conversation about options regarding wages along the supply chain and hopefully to develop momentum and a set of concrete follow-up steps to continue to focus on these issues.

Session 1. Wages Along the Supply Chain: General Assessment

"Incorporating Wages into CSR"

Daniel Vaughan-Whitehead, Senior Adviser, Wages and Working Conditions Program, International Labor Organization (ILO), and Professor at Sciences Po-Paris

Daniel Vaughan-Whitehead highlighted some of the wage issues causing increasing international concern. His research shows that while there has been some "catch up growth" in wages, the rate of growth in wages has remained very low despite strong global economic growth over the last decade. His research also found that the slower wage growth has been accompanied by a downward trend in the share of national income or gross domestic product (GDP) distributed to labor in over 70% of the countries for which the ILO has usable data. Vaughan-Whitehead argued that the growing wage disparity is one of the causes of the global economic crisis, as also emphasized by a number of eminent economists like Stiglitz. Solutions should thus be found to stop such adverse wage trends. However, during the current economic crisis, wage trends seem to be further deteriorating, since wages in many surveyed companies were found to have fallen in real terms, and to have declined even more than profits.

An examination of data gathered through FLA audit exercise and made available to Vaughan-Whitehead revealed that nearly three-quarters of the factories surveyed did not

know whether their starting wages enabled workers to have a decent living standard and more than half did not know if their wages were close to prevailing wages. Vaughan-Whitehead also found a number of issues surrounding wages, among them fake records, late and non-payment of wages, and difficulty paying overtime and minimum wage. The microdata thus reinforced trends observed globally.

Vaughan-Whitehead identified several dimensions of fair wages, among them payment of wages, minimum wage, living wage, prevailing wage, real wages, wage share, and wage costs and social dialogue on wages. He noted that many fair wage dimensions are already accounted for in one way or another in many CSR initiatives. However, within codes of conduct, there is a tendency to focus narrowly on legal wage dimensions and not the fuller picture. If the wage is not regularly adjusted and does not reflect the other wage dimensions, then other wage problems remain hidden. He argued for a multidimensional approach to wages, and proposed the 'Fair wage approach' based on 12 complementary fair-wage dimensions, that could lead to significant changes in wage practices along the supply chain. More information regarding Vaughan-Whitehead's fair wage dimensions can be found in his presentation "Incorporating Wages into CSR," which is posted on the FLA website.

"Efficiency Wage, Fair Wage and Pay Systems"

Takao Kato, Schupf Professor of Economics and Far Eastern Studies, Colgate University

From an economist's point of view, Takao Kato said, what matters in the discussion of wages are lifetime earnings. A long-term perspective is important to understanding whether various fair wage initiatives (FWIs), which encourage companies to pay above the prevailing wage, are sustainable. One argument against fair wage initiatives suggests that they will lead to cost increases, weakened competitiveness, a loss in market share and ultimately the retrenchment of employees. In other words, if a worker is paid a living wage today, a company may not be able to sustain this wage in the future and may have to lay off workers, causing them to lose income and reduce lifetime earnings.

Major developments in economics show, however, that contrary to the "harsh business reality" above, fair wage initiatives can be sustainable over the long-term. Kato identified some of the conditions under which they can be sustained.

According to efficiency wage theory, when monitoring individual worker effort is costly due to the nature of work, paying wages above the prevailing wage is a viable alternative to monitoring. The higher wage acts as a motivator and gives workers a sense of having a stake in the company. Workers with a social preference respond to the wage increases by working harder. They view pay as an act of kindness, said Kato, and reciprocate by increasing their effort. Lab evidence shows that this works. Several cases, for example, showed that an increase in wages above the prevailing wage reduced the labor turnover rate, absenteeism, and disciplinary firing, as well as increased productivity and profits. The policy implications are that FWIs are more likely to be successful when monitoring is costly (and hence the efficiency wage may pay for itself by saving on monitoring the efforts of each worker). In addition, the gift exchange between the firm and workers is

more likely to occur and hence FWIs are more likely to succeed when the fair wage reference is above the prevailing wage.

How much a worker is paid is thus very important, but Kato stressed that how they are paid also matters. Selecting the right pay system can help increase the sustainability of fair wage initiatives. Piece rates systems are often used when the cost of monitoring individual output of workers is low. While attracting the most productive workers, the system encourages workers to stress quantity over quality. Time rate systems, which are used when monitoring is expensive, may attract lower-skilled workers and provide no incentive for them to work harder. Neither system invites collaboration with other workers.

Kato's previous works on Japanese pay system show that group incentive pay such as profit sharing, gain-sharing, and employee stock ownership plans promotes teamwork and collaboration, resulting in a significant productivity gain of 7 - 9% per year. Such productivity effects are, however, not felt immediately, and it took Japan more than a few years to enjoy the benefits of the introduction of these approaches, pointing to the importance of a long-term perspective.

“The Perspective of NGOs”

Marianne Voss, Manager, Private Sector Department, Oxfam America

Marianne Voss echoed van Heerden's sentiment that the international community could not rely on government action to solve wage issues along the supply chain. Oxfam promotes the living wage as an important means of reducing poverty. Oxfam defines a living wage as at least a minimum wage that, without overtime, would allow a worker to support his/her family and have some discretionary spending. Voss agreed that wages have to be approached in a multi-dimensional way and sees merit in the JO-IN project's wage ladder (see below) as a realistic means of advancing wages, while also stressing the importance of dialogue with local stakeholders on what a living wage should be. Oxfam takes a rights-based, bottom-up approach, believing that workers must be enabled through unions and collective bargaining to have a voice in the wage determination process.

Oxfam engages in campaigns that target companies to urge them to address issues in their supply chains, but it also often works with companies as well, such as the work Oxfam did with Coca Cola on a poverty impact assessment. While it is sometimes complicated, companies and NGOs can work together – with the right incentives for companies and suppliers – to do the right thing for workers.

Discussion: The follow-up discussion explored: (1) the structure of the market at the retail level and how it affects wages and (2) the extent to which quality improvement techniques interact with pay systems. Vaughan-Whitehead stated that, in many instances, suppliers are price takers, having to adjust their production costs to meet the price offered by buyers who want to offer a low-priced good to consumers. With many costs fixed and not subject to negotiation (e.g., energy costs, rent), suppliers often have no alternative

than to use labor cost – and wages – as the adjustment factor, cutting them in order to remain in business. Brands need to be more aware of the impact that their actions have on wages and be mindful of the different dimensions of wages. Kato stated that payment systems and quality improvement efforts are complementary: it is essential for incentives (wage system) to be consistent with organizational changes to improve quality (such as quality circles). The two need to be coherent or quality improvement techniques will not be effective.

Session 2. Practitioners' Initiatives and Tools on Wages

“The Fair Wage Guide for Crafts Artisans”

Ella Silverman, Executive Director, World of Good

Trends toward informal employment globally are on the rise, exacerbated by the recession and accounting for the bulk of new employment in recent years. World of Good develops technological tools to educate workers (primarily women) in the informal/unorganized/home workers sector. In this respect, in 2005, World of Good launched the Fair Wage Guide, an online tool that translates piece rates into time rates, taking into account many variables, including social variables. The instrument, which is made available free of charge, tells the worker how s/he is being paid based on local and global economic indicators, as well as provides important information about wages and employment locally and regionally. The tool supports back-end data and content for 95 countries. Its use has been encouraged by the World Fair Trade Organizations to demonstrate wage compliance.

A review of information on users of the Fair Wage Guide indicates that informal workers, even those working for good actors, on average are still making under \$2/day in wages. Although it was created originally for craft artisans, World of Good is expanding the Fair Wage Guide tool to the wider apparel industry. Additionally, they are developing means to reach workers without access to computers via mobile phone and creating a dash board for retailers to get informal labor information in real-time.

“Incorporating International Wage Standards in Fair Trade: The Asian Floor Wage Initiative”

Ashim Roy, General Secretary, New Trade Union Initiative, India

Roy asserted that the reality of working conditions in the garment industry in Asia is poverty wages. Wages that garment workers receive are almost never enough to guarantee a decent and dignified existence for them and their families. The current economic model gives much power to global buyers and fails to distribute the benefits of global production fairly. Workers in one region or country are pitted against others in a progressive downward ratcheting of labor conditions and wages.

The Asia Floor Wage (AFW) Alliance has proposed a way to lift the wages of all workers at the same time. The Asian Floor Wage may be referred to as a minimum living wage. It

is calculated from the food cost (the cost of food for one earner, two adults and two children, each consuming 3,000 calories per day) and then doubles it as a way to take into account non-food costs of a family. The minimum wage in many Asian nations is calculated using caloric content intake. However, many Asian countries use a caloric intake number much lower than is internationally accepted. For example, in Bangladesh, the minimum wage is calculated using 1700 caloric intake, which is even lower than the poverty rate of 2100 calories. The Asian Floor Wage, in domestic currency, thus differs across countries, but in each instance it embodies the same level of purchasing power for workers.

Why talk about minimum living wage or living-living wage when workers in the apparel industry often do not get even the minimum wage? Roy believes wages are a human rights issue and that if you have right to life, then you have right to living wage. A living wage should be given automatically and should not be dependent on collective bargaining considering the weaknesses of collective bargaining in certain parts of the world. If FOB, for example, is being calculated by minimum wage levels, then it is impossible to negotiate a wage increase. The minimum wage than is the ceiling.

“JO-IN Multi-Stakeholder Approach: Lessons for Wage Issues”

Henrik Lindholm, International Verification Coordinator, Fear Wear Foundation

Four multi-stakeholder initiatives (MSIs) and two campaign groups joined together in 2003 to find some common, workable approaches to the responsibility and accountability of multinational companies in their supply chains. All six approached the issue of wages in different ways. Rather than engage in a philosophical debate of “what” the wage should be, the group focused on developing a tool that would show the actual level of wages and a path to raise wages in the supply chain. They developed a benchmarking system, called a “Wage Ladder,” to chart wage levels in a factory relative to various wage standards in a country or region and began to test it in Turkey.

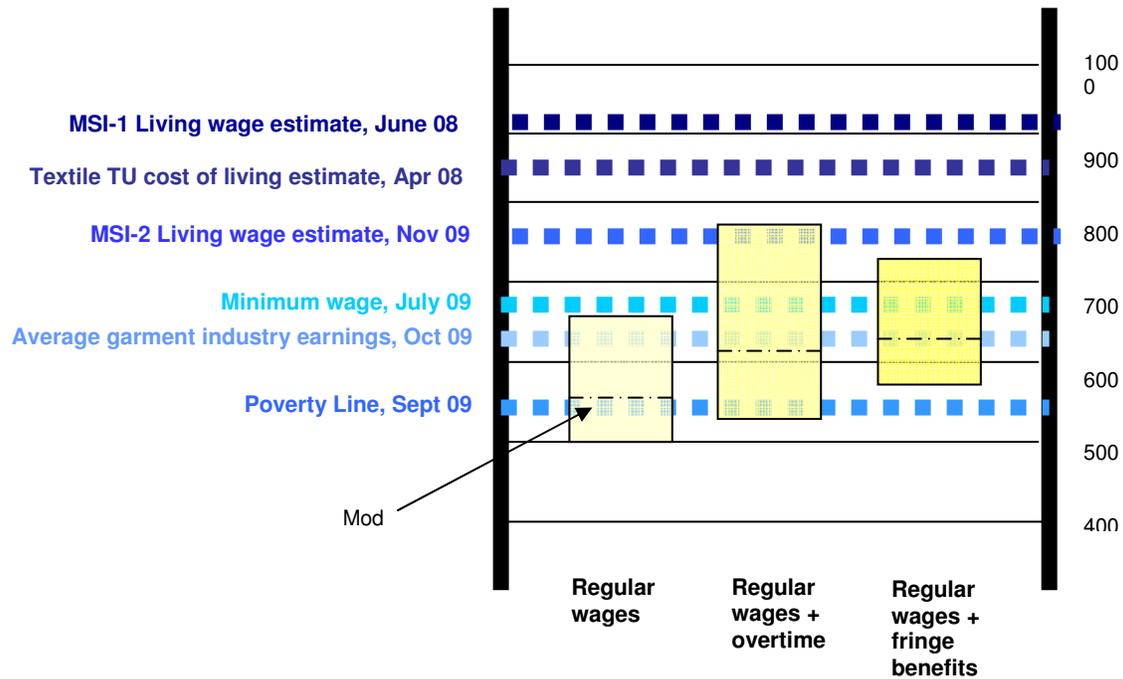
The system serves three main purposes:

1. Illustrates the monetary values assigned to available wage standards and measurements in a country or region.
2. Charts factory wage levels relative to these wage standards, illustrating how workers’ wages measure up to applicable prescribed wage levels.
3. Helps chart factory progress in improving wages over time.

The rungs on the wage ladder – for a country or region – include minimum wage requirements, negotiated wages resulting from collective bargaining agreements (CBAs), living wage measurements provided by partner organizations, cost of living estimates, poverty line, national wage statistics, and wage scales from factories identified as “best practice.” (See illustration on page 7) Also added to the chart is the following factory information: regular wages, regular wages plus overtime, and regular wages plus fringe benefits. The span of the wages, from the lowest to the highest, are indicated as a bar in the wage ladder. The wage earned by the majority of workers is indicated with a line in

the bar. The reason for charting these different variables is so that factories cannot show an increase in regular wages, for example, by reducing the fringe benefits or overtime pay where the net improvement for workers does not change.

Sample Wage Ladder (Factory data in the context of country's wage situation)



The Fair Wear Foundations is already using a simpler form of the wage ladder in all audit reports. It intends to use it as an element for conversation with managers and also share it with workers and stakeholders.

“Fair Trade: Testing Consumer Potential to Raise Wages”

Heather Franzese, Fair Trade

The Fair Trade movement has achieved quite a bit of success worldwide: in 2008, global fair trade sales were approximately \$4 billion, and \$1.2 billion in the United States. The standards under which products are grown or made is important to consumers. A survey of 15,000 consumers worldwide revealed that 89% of respondents indicated that it was very important or important for companies doing business in poor countries to pay farmers/workers fairly. The same survey also revealed that 49% of respondents would be interested in purchasing labeled Fair Trade textiles if they were available. Some consumer research suggests that consumers are willing to pay more for goods that embody their values (up to 14% in one experiment involving “ethically certified” polo shirts).

Fair Trade has raised wages and driven consumer awareness and purchasing behavior in the commodities sector. UK Fair Trade cotton demand, for example, has increased 77% since 2005 and sales have channeled \$1.5 million of additional income back to farm workers. The organization will soon pilot a similar program in the apparel sector. The Fair Trade approach to raising wages for workers requires that buyers pay a premium over the minimum wage into a worker-controlled fund, as well as to make progress toward living wage. As progress is made toward the living wage, premium requirements are reduced. Wage levels for each country are developed with the engagement of local stakeholders.

Discussion: The discussion that followed centered on: (1) the possibility of gaming the system of fair wage certification, particularly the possibility – if audits are infrequent – of shifting workers to other locations, changing work assignments, and so on; (2) Fair Wear Foundation’s practical experience in obtaining the necessary data to implement the wage ladder; and (3) next steps for the Asian Floor Wage Initiative. Franseze indicated that their approach is worker-centric and they seek to have mechanisms that permit real time information from workers between audits, such as by using complaint processes and also working with civil society organizations to stay abreast of developments. Lindholm stated that to date, FWF has implemented the wage ladder in an ad hoc basis on a limited number of audits, but it is working on laying the foundation for wider use in the future; to date, lack of data has not been a major concern. Roy set out a number of next steps for the AMW Alliance: (1) put in place something akin to the wage ladder for Asian countries; (2) explore the possibility of using wage pools and other forms of group compensation at the factory level; and (3) promote legislation to reduce the discretion of employers in wage setting and develop sources of revenue to pay for wages and benefits, such as an export tax to fund social security payments.

Session 3. Company Pilot Initiatives

“Above and Beyond”

Joe Bozich, CEO, Knights Apparel

Knights Apparel, one of the largest apparel licensees to U.S. colleges and universities, is launching Above and Beyond, a new socially responsible apparel brand. Above and Beyond factory operations will start in the Dominican Republic. They will provide all workers with a living wage; according to its calculations, the living wage in the Dominican Republic is 3.6 times the legal minimum wage. The brand, which is targeted initially to the collegiate bookstore market, will ask the consumer to pay slightly more (a price premium) for the product. Conversations with over 200 bookstores suggest there is strong retail support for this product. Other retail meetings suggest there are other opportunities to introduce the brand into non-collegiate environments as well.

The biggest challenge for this initiative, Bozich noted, will be matching factory output with retail demand throughout the year. The collegiate market is cyclical, and there will be production peaks and troughs. For periods when collegiate demand slackens, he said,

Knights Apparel will need to support the factory by supplying orders for other product for markets where the company will not be able to get a price premium until demand can be created with other brands that create demand in the non-peak periods for collegiate product. Knights Apparel has engaged a communications firm that specializes in cause related marketing to tackle another challenge: getting the message to consumers.

Bozich stated that there are challenges in replicating the Above and Beyond methodology in the existing supply chain model common in the apparel industry, where factories produce product for many companies, many of whom are not in the collegiate industry . A factory with multiple buyers could not support the Above and Beyond methodology unless all the buyers agreed to pay higher prices associated with paying a living wage for 100% of the factories production.

“Rewarding Labor Compliance by Growers”

Juan Gonzalez-Valero, Head of Corporate Responsibility, Syngenta

Gonzalez-Valero described Syngenta Seeds’ activities in India aimed at improving the working conditions and income of seed growers. By and large, fees are driven by the market, with companies having limited impact. There is, however, one way in which fees can be increased. Syngenta is incorporating into the quality discussion compliance assessments, which include raising labor standards and offering incentives to farmers for performance in these areas.

Gonzalez-Valero stressed the need to have a continuous dialogue with the community where production occurs, whether about wages or other labor issues such as child labor. The high cost of monitoring thousands of small, family farms led Syngenta to train and leverage the existing network of people that work with farmers to get the seed to market for labor standards monitoring. He acknowledged that the system was an imperfect model, but offered that it was the best way of reaching the thousands of farmers involved. With respect to wages, the assessment has been simplified to focus on three core elements: (1) daily payment (on time and accurately); (2) lack of gender bias; and (3) payment of overtime. As part of the improvement plan with the participating farmer, Syngenta pays a 5% incentive premium for meeting or exceeding health and safety and child labor standards.

Gonzalez-Valero further stated that eventually he would like to see labor compliance programs develop from stern standards to setting improvement targets instead, understanding that business targets operate this way.

Discussion: The discussion that ensued centered on: (1) the potential socio-economic effects of a high-wage factory in a community characterized by enterprises that pay lower wages; and (2) the scalability of pilots that pay higher wages. Bozich stated that as he planned and designed Above and Beyond, concerns were expressed about the possibility of displacement of workers because of the disparities in wages, but that this was not a concern in this case because the community where the factory has been established does not have any other competing factories. Gonzalez-Valero stressed that “high-wage

islands” in a market with different standards were unsustainable. A potential ray of hope is through quality; in India, there is some competition amongst buyers for the better farmers, who produce higher quality seeds and command a higher return. Higher remuneration for quality goes with the market rather than against it.

Concluding Session: Prospects for Greater Incorporation of Wages into CSR

In the wrap-up session, Vaughan-Whitehead indicated that he is convinced that what is going on in the supply chain around wages is not sound economics. “Current companies’ wage behavior is not providing the right incentives to the ‘real economy’ – if we were in a real economy, then brands and suppliers would need to rethink their business model.” Workers have been treated as costs to be contained, rather than assets to be developed, and this slanted view has largely defined the approach to wage issues. A cooperative framework among all CSR actors would be needed to change wage practices.

Van Heerden stated that the CSR community at large has “done a lousy job of bringing the consumer along with us. The link back to the consumer has not been made and consumers don’t even have a place to go to check on where their clothing has been made.” He echoed the need for having retailers and suppliers in the room when these issues are discussed, as well as the voices of consumers. There is urgency to the situation, he argued. Conflict is emerging in places like Bangladesh over wage frustrations and the lack of unions makes it difficult to direct worker frustrations to positive outcomes. There is need for an analytical approach to solving the problem based on continuous improvement that can be monitored through KPIs.

A number of possible next steps for the FLA and its affiliates emerged from the discussion:

1. Start an international network on wage issues – notably through an electronic website and a permanent observatory and analysis of wage trends along the supply chain – that would promote sharing of information on wage developments, wage data, wage setting mechanisms, best practices, and so on.
2. Hold regular meetings of stakeholders to continue the dialogue over wages, with the next meeting to be held in a supplier country with the participation of suppliers.
3. Formalize a commitment to working on wage issues and introduce into FLA audits the concept of a wage ladder.
4. Seek commitment from brands to support anonymous self-assessments by their suppliers on wages, in order to develop a database that would permit analysis of wage information and development of strategies going forward.
5. Explore the possibility of constituting a formal Working Group within the FLA to work on wage issues and make recommendations to the Board.