Document 1

Assessing the impact of purchasing practices on code compliance

A case study of the Bangladesh garment industry

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Executive Summary

This research was commissioned by the MFA Forum Bangladesh Buyers' Group to broaden and deepen existing research by the group into the impact of their purchasing practices on their manufacturers' ability to implement their codes of conduct. It was funded by GTZ. The aim of this research project was to identify the practices among brands that most significantly undermine manufacturers' ability to comply with the brands' codes of conduct. A total of 35 interviews were carried out with representatives from:

- 7 international brands
- 4 local offices of international brands
- 7 buying houses
- 17 suppliers

The research identified six practices that undermine code compliance:

1. Unstable relationships
2. Downward pressure on prices
3. Increased quality demands
4. Shorter time pressures
5. Changes to orders
6. Cancellations of orders

These issues intensify the downward pressure on prices, conditions and terms within the industry. Working on one-off contracts at rock bottom prices increases insecurity in the industry and undermines manufacturers' ability to invest in their business, plan production appropriately and support code compliance. While any of the issues highlighted could be tolerated in isolation, the degree, scale and consistency of these practices is unsustainable. The research shows that not only undermine conditions for manufacturers and workers, but they are also detrimental to brands. These are sensitive issues and it is important to seize the current moment to begin a dialogue between brands and manufacturers, for this purpose a series of recommendations have also been proposed alongside the research findings.

Unstable relationships (for more details, see page 7)

Large brands are developing more long-term strategic relationships with key suppliers as well as very flexible relationships with other suppliers, based on competitive one-off volume contracts.

Research findings

1. Manufacturers gain some stability working with big brands
2. A small minority of suppliers get 'strategic partnership' status gains

3. Volume contracts are one-off rolling contracts that increase insecurity among all manufacturers.
4. Good compliance does not appear to increase business for manufacturers

Recommendations for brands
1. A re-evaluation of one-off rolling contracts.
2. Prioritise awareness training for buyers on the implications of brand's commercial decision making on the implementation of their code/workers conditions in their supplier factories
3. Follow on with training for all staff on the impact of their decisions on manufacturers and code compliance.
4. Reward manufacturers with high compliance levels

Recommendations for manufacturers
1. Consider upgrading services
2. Develop links and partnerships within the industry to increase service provision
3. Training for management

Downward pressure on prices (for more details, see page 9)

Retail garment prices are decreasing. In the UK, this is due to decreases in prices on the high street, where women's wear has decreased by 30% - 40% in the UK in the past decade.

Research findings
1. Prices have decreased by almost 40% for some garments
2. Use of counter quotes and open book costing are common place and further drive down prices
3. There has been a shift from Letters of Credit to Purchasing Orders and contracts
4. There has been an increase of 30 days in the duration between shipping and payment
5. Charges for delays can be unfairly imposed

Recommendations for brands
1. Develop a sustainable cost model in collaboration with manufacturers
2. When looking for cost savings, it is necessary to take a holistic look at price that goes beyond FOB
3. Terms of payment need to be re-evaluated
4. When looking for cost savings, less visible costs are incurred by current purchasing practices. These can be minimised.
5. Lobby government for bonded warehouse

Recommendations for manufacturers
1. Develop a sustainable cost model in collaboration with brands
2. Create greater internal efficiencies through improved planning techniques and industrial engineering
3. Re-examine avoidable losses e.g. fines for poor quality
4. Lobby government for bonded warehouse in collaboration with brands

Increased quality demands (for more details, see page 12)

Improved quality is no longer a negotiable issue. Buyers have fixed prices, fixed delivery deadlines and fixed quality levels that have to be met.

Research findings
1. Quality levels have increased in the past two years
2. Increased quality has not led to increased prices

Recommendations for brands
1. Reconsideration of quality/cost relationship

Recommendation for manufacturers
1. Implement more rigorous quality systems

Shorter time pressures (for more details, see page 13)

In the pursuit of the next 'must-have' garment, production time has been shrunk.

Research findings
1. Lead time has decreased due to improved raw material procurement
2. Delayed information from buyers creates production problems
3. Inexperience of buyers and mid-level merchandisers creates avoidable delays, especially when problems arise.

Recommendations for brands
1. Research internal critical path and develop deadlines for delivering information on time
2. Identify key decision makers and include on-time delivery of information in their performance indicators
3. Trial local sample approvals or alternative methods
4. Identify and approve local labs

Recommendations for manufacturers
1. Improve production planning by incorporating frequent delays

Changes to orders (for more details, see page 16)

Changes are a constant feature of the industry as brands respond to market signals.

Research findings
1. Changes in design are more disruptive than increases or decreases in volume of 20%
2. Inaccurate forecasting drives changes
3. Extensions are not always a solution as they cause delays for other orders after the affected order

Recommendations to brands
1. Develop cut-off deadlines for different categories of change
2. Develop criteria for accepting and rejecting changes to volume and design
3. Become more selective in approving changes

Recommendations to manufacturers
1. Upgrade workers' skill levels to cope with changes in style and shorter product volumes more efficiently

Cancellation of orders (for more details, see page 17)

Cancellations are based on responses to market demands that are made quite late in the process.

Research findings

1. Cancellations are linked to poor forecasting and sub-standard quality in some cases
2. Manufacturers are given inadequate compensation for cancellations

Recommendations for brands

1. Continue to improve forecasting tools
2. Re-evaluate compensation
3. Develop guidelines for cancellations

Recommendations for manufacturers

1. Develop comprehensive cost breakdown for cancellations
2. Monitor quality inspections to ensure consistent quality and avoid cancellations

Definitions

BGMEA	Bangladesh Garment Manufacturers and Exporters Association
BKMEA	Bangladesh Knitwear Manufacturers and Exporters Association
Brand - Manufacturers	suppliers who produce for the brands participating in the study
Brands	Retailers in the Buyers' Group. 'Brand' is the collective term assigned to both retailers and brands, as all 'brands' participating in this study were not all retailers with their own stores.
Buyers	interviewees employed by brands. While some interviews were conducted with buyers, this group also includes technologists and directors of sourcing among others.
Buying house	third party agents who act between brands and suppliers
CSR	Corporate Social Responsibility
FOB	Freight on Board price
GTZ	German Technical Cooperation
KPI	Key Performance Indicators
LC	Letter of Credit
MFAF	Multi-Fibre Arrangement Forum
NGO	Non-governmental organisation
Non-brand Manufacturers	manufacturers who do not supply big-name brands.
Purchasing practices	the decisions made by a buying company related to every aspect of doing business, including all terms and conditions of trade

Acknowledgements

The researchers acknowledge the support of the MFA Forum Buyers' Group and GTZ in funding this project; BGMEA and BKMEA for providing contacts and introductions to both suppliers and buying houses; and the willingness of suppliers, brands and buying houses to nominate interviewees and take part in the research.

Background information

One of the key issues regularly raised by suppliers in Bangladesh is the purchasing practices of their buyers. This led to research to establish an overview of projects undertaken by members of the MFA Forum's Bangladesh Buyers' Group to address the issue of purchasing practices. These projects were not necessarily specific to Bangladesh but would be relevant in that country.

The first part of the research was completed and presented to the Buyers' Group meeting which was held in Toronto, Canada on April 16, 2007. The Bangladesh Buyers group determined that a second phase was needed to deepen the insights from the first phase. The proposal was that three further actors would be interviewed in order to develop a more complete picture of the challenges that the purchasing practices of brands and retailers create in suppliers' ability to comply with their codes. GTZ saw this as a key part in the development of the three year proposal for the garment industry in Bangladesh and agreed to fund the research and co-manage it with the Forum. Therefore, a study was agreed which would develop a more complete and comprehensive understanding of the challenges that the purchasing practices of brands and retailers create on the suppliers' ability to comply with these codes.

Introduction

Compliance is not solely the responsibility of manufacturers. Retailers and brands have contributed to these conditions, however unconsciously and unwittingly. It is clear from the research that insecure finances, production management and code compliance are inextricably interlinked. Insecure work and decreasing prices force manufacturers to overbook which can create code compliance issues on overtime and payment of overtime. Insecure relationships mean that manufacturers have very limited power in negotiating terms, conditions and changes with buyers. The very real fear of loosing a contract creates pressure to accept terms and changes that can put direct pressure on their ability to implement the buyers' code of conduct. This research highlights these downward pressure on the terms and conditions that are eroding suppliers' ability to compete in a sustainable manner that respects code compliance.

Unstable relationships

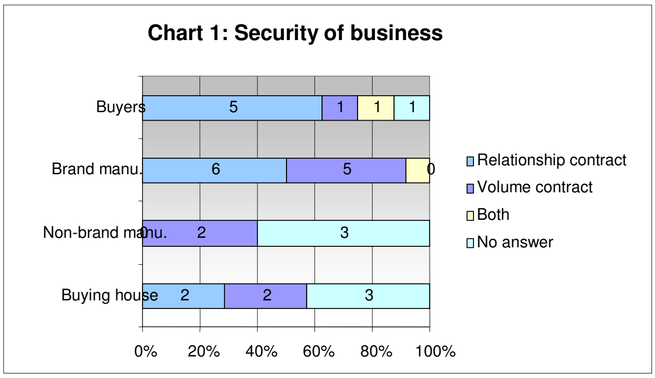

Chart 1: Security of business

In a highly competitive market characterised by oversupply and downward pressure on prices, production relationships are under severe pressure as the research demonstrates.

Industry trend

The trend within the industry is two-fold. Large brands are developing more long-term strategic relationships with key suppliers. They also maintain very flexible relationships with other suppliers, based on competitive one-off volume contracts. These contracts may be repeated over several years but they offer no security to the supplier.

Research findings

1. Some stability working with big brands

The brands interviewed have a ‘pool’ of approved suppliers from whom they source. The first tier of this pool receives 70% - 90% of their spend in monetary terms. There is some turnover in this pool. They change about 15% of suppliers each year. The most common criteria listed by brand interviewees in selecting first tier suppliers are: vertical integration; cost; and code compliance.

Box 1
Conditions for one strategic supplier with a relationship contract

1. Strategic plan in place with brand until 2010
2. Changes in volume are agreed 120 days before shipping before the order is placed
3. No changes to design after the order is agreed
4. Orders are planned and predictable
5. On-line money transfers ensures payment as soon as the goods are shipped

2. Strategic partnership gains

Five out of the eight brand interviewees stated that offer relationship contracts to a small number of approved first tier suppliers (see Chart 1). These contracts offer a far greater degree of security to suppliers as shown in Box 1, as this allows them to plan, invest and develop their business. Although they have relationship contracts in place, they still work with one-off rolling volume contracts as relationship contracts do not include terms covering the volumes purchased or the price paid. The key difference for these strategic suppliers is that they are likely to have more information about the size of orders and the dates they will be placed than manufacturers who only have volume contracts. They also receive more technical support to grow and develop the business.

3. Volume contracts are insecure

The vast majority of suppliers go from one volume contract to another, with little security. With severe pressure on prices, suppliers feel that they have little room to negotiate and are obliged to accept decreasing terms and conditions simply to keep business.

- *As one brand interviewee said, “complaining is not a good idea”, otherwise they will lose the orders. The fundamental insecurity of the relationship means that brands can make increasing demands on suppliers.*

There is limited awareness of the impact of these demands by personnel across the brand. For example, designers can ask for changes to a garment, which the supplier will agree to in order to keep the order, but the impact of these changes could possibly undermine code compliance on overtime if it happens late in the process.

4. **Good compliance does not increase business**

Good compliance is taken as an industry standard. There is a perception among suppliers that brands do not reward suppliers that have higher standards of compliance.

Recommendations for brands

1. **A re-evaluation of one-off rolling contracts.**

There can be a win-win resolution that creates more stable relationships.

- *One buyer wants to "bring back 3 year commitments as you get better cost. Season to season working means suppliers can't plan business due to the inconsistency of orders placed."*

What possibility exists for increasing the pool of strategic partners - preferencing suppliers with a solid track record who consistently aim to improve compliance - and developing more stable relationships with them?

2. **Training for buyers**.

Buyers currently have limited awareness of the impact of their decisions on suppliers and their ability to comply with codes. According to one buyer, "[d]iscipline is a big thing for [our] buyers." He felt that because of the power of the brand, it is very easy to lean on a supplier to get an order accepted, changed or have the price decreased.

3. **Training for all staff**

This training and awareness building is particularly important for personnel whose decisions can have far reaching consequences for manufacturers. Although they may not be in direct contact with manufacturers designers', technologists' merchants' and forecasters' decisions can have multiple impacts on manufacturers and code compliance of which they are unaware. Training could help ensure that only changes that are essential are made and that they are done within appropriate time frames, agreed in negotiations with the supplier.

4. **Reward manufacturers with high compliance levels**

Increase the orders that are placed with manufacturers that have high levels of compliance so that they get priority, where possible.

Recommendations for manufacturers

1. **Consider upgrading services**

In order to gain greater security it may be possible for some suppliers to develop their services to become a key partner

2. **Develop links and partnerships within the industry**

Industry expert David Birnbaum believes that the old model of cost/quality/on time is no longer enough. These are now industry standards. Birnbaum believes that in order to compete manufacturers need to develop full service models (including additional services such as raw material procurement; shipping; independent in-house quality inspections; design etc.) to increase value. If it is not possible to develop these additional services, develop links with others in the industry to offer these services

3. **Training for management**

Brands frequently mentioned the need to support manufacturers in sorting out production problems and providing support on internal management issues that should be the responsibility of management within the supplier. This indicates a need for greater training and education at all levels of management.

Downward pressure on prices

Industry trend

Retail garment prices are decreasing. In the UK, this is due to decreases in prices on the high street, where women's wear has decreased by 30% - 40% in the UK in the past decade.[1] This has been fuelled by the increase in 'value retailers' in the fashion market.[2] They now account for 40% of the UK market by volume and are supporting the trend among certain market segments to buy fashion frequently without increasing spending. Women now buy 40% of all our clothes at value retailers, with just 17% of their clothing budget.[3]

At the manufacturing level this is reflected in decreased unit prices and a shift away from Letters of Credit to Purchase Orders or contracts.

Research findings

Bangladesh competes in the high volume/low cost market. Price is the primary reason for buyers coming to Bangladesh. However, in an industry where prices are decreasing and costs are increasing, prices are being forced below what is sustainable for many suppliers.

1. **Decreasing prices**

   There is agreement among suppliers, brands, non-brand manufacturers and buying houses that prices have decreased in the past two years. Estimates vary from an 8% decrease in the opinion of brand interviewees to a 20% decrease according to brand manufacturers.
   Between 2004 – 2006, there has a 36% decrease in the biggest knit category exported from Bangladesh (sweaters, pullovers, sweatshirts and vests) and a 22% decrease in the biggest woven export (men's and boy's trousers, overalls and shorts).[4] The pressure caused by decreased prices is further intensified by unstable yarn prices.

   - *According to one buying house, yarn prices have increased by 25% in two years.*

2. **Use of counter quotes and open book costing**

   Brands are increasingly demanding open book costing. Manufacturers feel that this strips out their ability to make even legitimate profits. Getting counter quotes from various suppliers in different countries and different regions is standard practice among buyers.

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1 The Guardian (2006): 'Going Cheap', February 28th
2 Mintel (2005): 'Value Clothing Retailing – UK'
3 TNS Worldpanel (2006): Fashion Focus issue 29, online at <http://www.tns-global.com/uk>
4 Source: *Benchmarking the Bangladeshi RMG Sector: A Comparative Analysis of Major Competitors* (GTZ, Dhaka, forthcoming)

- *One buying house stated that they get quotes from Bangladesh in order to negotiate lower quotes in Turkey and China.*
- *A brand manufacturer noted that a buyer approached him with the cheapest quote the buyer had received from other manufacturers. The buyer then asked for a 25% decrease on the cheapest quote. At the end of the negotiation, the buyer settled for a 10% decrease on the cheapest quote.*
- *According to a local office buyer, this form of "cherry picking is feeding the errant and stalling the progress of those who are progressive."*

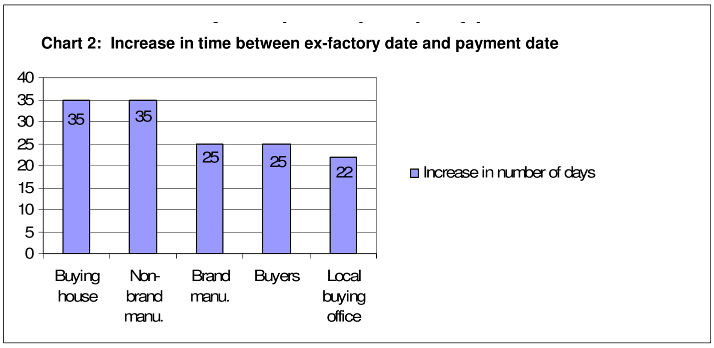
3. Shift from Letters of Credit to Purchasing Orders and contracts

Letters of Credit used to be standard practice in the industry. This is changing rapidly. This has been driven by brands and retailers as it decreases their liabilities. With a letter of credit, the payment money is kept to one side and cannot be spent after the letter of credit is opened. Banks are willing to open letters of credit for manufacturers who have purchase orders, but the buyer does not have to have the money kept to one side. The disadvantage for suppliers is that they may have pay raw material suppliers before they are paid by the buyers. This increases the financial costs for the manufacturers.

4. Increase in time between shipping and payment

There is widespread acknowledgement that payment dates have been pushed back – this ranges from an average of 25 days according brand suppliers and brand interviewees and 35 days according to buying house interviewees and non-brand manufacturers (see Chart 2). In general, there appears to be a shift from 30 day agreements to 60 day agreements.

- *One manufacturer said that one of his buyers give a 30 day ex-factory letter of credit, but he has to accept a decrease of 5% in the amount he is paid in exchange for a shorter payment period.*
- *According to a brand representative working in a local office, manufacturers in other regions are now offering 60 – 90 day payment periods as part of their enhanced service offerings. Payment periods are becoming a marketing tool.*



5. Charges for delays can be an issue

While on-time delivery is expected as an industry standard, it is not always possible. There are now clauses in contracts that automatically fine the manufacturer for delays, even if they are agreed upon with the buyer.

- *Some manufacturers said that the buyers waive these fines.*
- *One manufacturer recounted that he was given a one day extension from the buyer but he then had to pay 300 Euros to get an amendment which is an official letter stating that the buyer had agreed the delay and the fine would be waived.*

Recommendations for brands

1. Develop a sustainable cost model

A comprehensive cost model is needed: this must takes all macro and micro into account and needs to be developed and agreed upon in collaboration with manufacturers to ensure that it is genuinely sustainable. Although the majority of buyers stated that they had a sustainable cost model in many cases they were referring to open book costings. This is not necessarily sustainable. There is a significant possibility that buyers are getting quotes from manufacturers with lower rates of compliance and pressurising compliant companies to negotiate down to these costs. This is not comparing like with like and erodes the investment that more compliant manufacturers have made in their units.

2. Taking a more holistic look at price that goes beyond FOB

There is an over-emphasis on the Freight on Board cost (FOB). Within production 60% - 70% of costs are raw materials. Cut, make and trim account for approximately 10% of the FOB (see Table 1)[5]. This represents a tiny portion of the overall cost of the garment and an even smaller percentage of the retail price of the garment. When
decreases prices it may be wise to look at other areas, for example logistics, mark-downs etc.

Table 1 Freight on Board Price (men's jeans)	
Unit labour cost	$0.75
Profit & overhead	$1.50
Trim	$0.75
Fabric	$4.00
Total	**$7.50**

- *According to one brand interviewee, "[m]aterials are 60% of FOB…the profit the factory controls is very small. There are [equal] carry on costs and mark ups; this is the cost where [we] have the greatest control and leverage, instead of messing with FOB which is so small." For this interviewee, the big savings can be found by decreasing supply chain costs (e.g. supply chain integration), in-store discounting and speed to market.*

3. Re-evaluation of terms of payment

There is an increased transfer of risk from brands and retailers to manufacturers. Increasing the payment period and forms of contract shifts responsibilities and costs from the brands to the manufacturers. These terms increase insecurity for manufacturers which undermines planning, investment and compliance. Payment schedules and contracts need to be re-examined.

4. Examination of less visible costs that purchasing practices create in terms of production and code compliance

When looking at reducing costs, it is important to move beyond the FOB cost focus. Other areas where savings could be made come directly from improved purchasing practices. These include faster turnaround of samples, more efficient lab dip tests and the development of rigorous internal deadlines for key deliverables specification sheets for samples.

5. Lobby government for bonded warehouse

A bonded warehouse would allow manufacturers to purchase and store yarn and materials when prices are lower and / or before the peak season when demand will be higher. This could help contain raw material costs and further shorten leadtime.

Recommendations for manufacturers

1. Develop a sustainable cost model

A comprehensive cost model is needed: this must takes all macro and micro into account and needs to be developed and agreed upon in collaboration with brands to ensure that it is genuinely sustainable.

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[5] D. Birnbaum, 2006, *How factories can ease the cost squeeze*, www.Just-Style.com, October 3

2. **Create greater internal efficiencies**
Improved production planning and industrial engineering could help cut down bottom line costs for manufacturers which can help them survive in an increasingly competitive environment. Courses and consultancy work in these areas is available – either for free or reduced prices – from both brands and industry organisations.

3. **Re-examine avoidable losses**
Savings can be made by reducing the costs that do not have to be paid. For example, fines for poor quality could be reduced through better production techniques; fines for delays could be reduced through improved line planning techniques.

4. **Lobby government for bonded warehouse**
A bonded warehouse would allow manufacturers to purchase and store yarn and materials when prices are lower and / or before the peak season when demand will be higher. This could help contain raw material costs and further shorten leadtime.

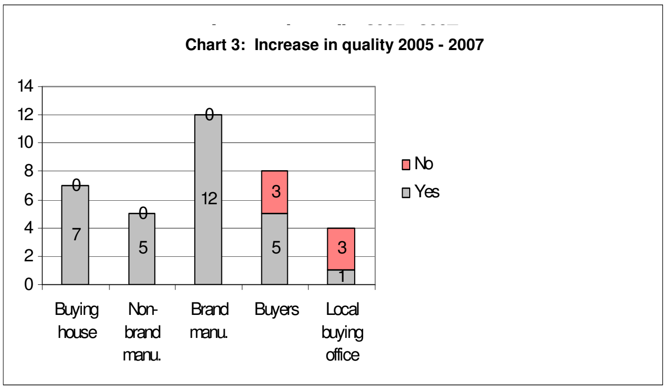
Increased quality demands

Industry trend

Improved quality is no longer a negotiable issue. It is not variable. Buyers have fixed prices, fixed delivery deadlines and fixed quality levels that have to be met.

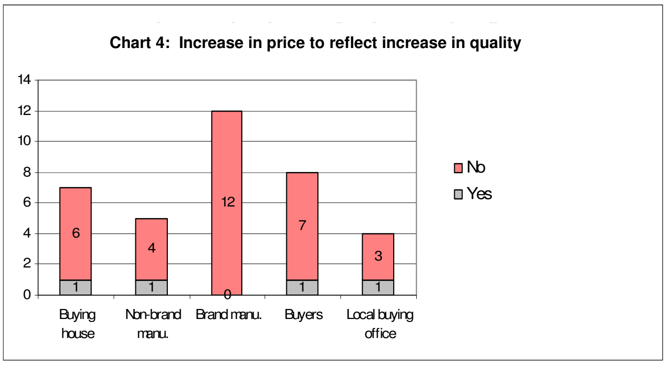
Research findings

1. **Quality levels have increased**
There is widespread agreement among the interviewees that quality demands have increased over the past two years (Chart 3). This has led to increased costs including materials, production systems and quality inspections. While some of these improvements may offer advantages for the manufacturers, the fact that they have not been accompanied by increased prices – but by decreases in prices over the past two years – is an issue for manufacturers.



2. **Increased quality has not led to increased prices**
Prices have not increased to reflect the increased quality (Chart 4). On the contrary, prices have decreased in the past two years. Decreased prices combined with increased quality demands means that the net price decrease is actually greater. This does beg the question: if upgrading the product is not increasing prices, does 'added value' only add value for buyers?

- *One buyer said that there had been 'no real increase in price to reflect increase quality'. He then added that there are occasional increases. His example was that a buyer cannot get cashmere jumper for the price of acrylic jumper. However, if "you're negotiating on $5 extra, you will try to get it for acrylic price and maybe settle with paying $2 extra."*



Recommendations for brands

1. Reconsideration of quality/cost relationship

Increased quality demands inevitably increase costs for manufacturers. These costs need to be met somewhere and when they are not included in the price paid by buyers, they may be recouped elsewhere, for example through hiring contract workers, unauthorised subcontracting and decreased code provision. The link between financial insecurity, production planning and code compliance cannot be overstated.

Recommendation for manufacturers

1. Implement more rigorous quality systems

Ten years ago, Bangladesh used to operate in a high volume, low quality segment. Industry requirements have changed. Quality is no longer optional for buyers. However, according to several manufacturers, some manufacturers are still a little "lazy" about quality. In order to stay in business, manufacturers need to prioritise, and standardise quality within their units.

Shorter time pressures

Industry trend

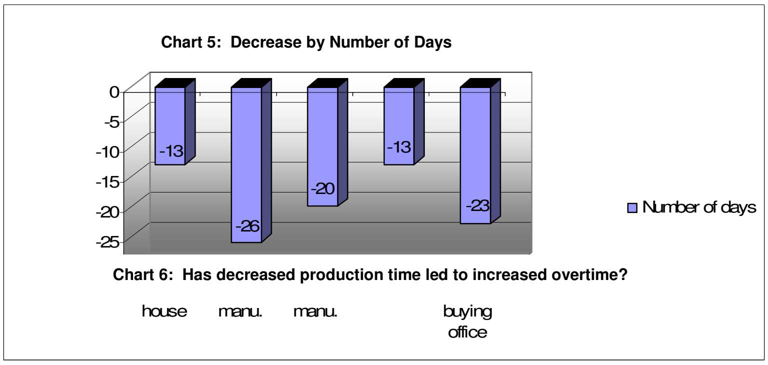
In the pursuit of the next 'must-have' garment, production time has been shrunk. The shorter the production time, the more designers can create high fashion designs that are selling right now. The pioneers of fast retailing have production lead times of 30 days or less. Some brands in Japan place their order in China on Monday and it's shipped on Friday, in the depot on Tuesday and on the floor by Thursday. This has increased pressure on buyers' critical paths, shrinking them from 11 months to 9 months in the USA and down to 4 or 5 months for some European brands.

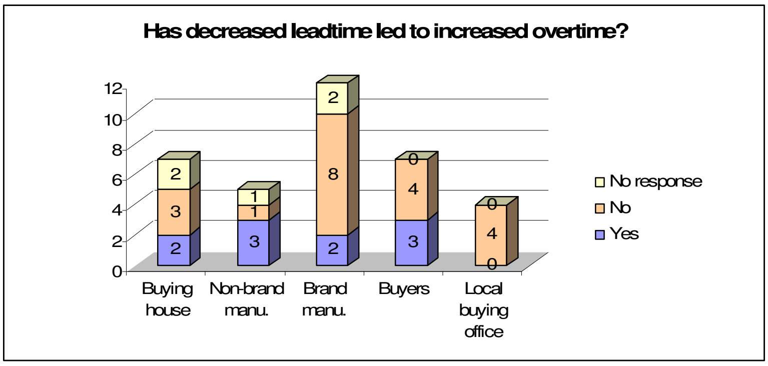
Research findings

1. Lead time has decreased

The research shows a clear decrease in the lead time over the past two years ranging from 13 to 25 days (Chart 5). The general trend was a decrease from 120 days production lead time to 90-100 days production lead time.

- *According to one knit supplier, the time has decreased to 75 days, due to backwards linkages with knitting mills. A buying house interviewee stated that he is under pressure from his head office to reduce production lead time for 90 days to 50 days.*





Buyers and many suppliers interviewed stated that this had not led to increased overtime for workers (Chart 6). All interviewees said that this decrease is due to efficiencies in backward linkages and raw material procurement. While port efficiency could be improved, many interviewees stated that since the Emergency Government had come into power transit through Chittagong port had decreased from 21 days to 3-5 days. The lead time decreases they highlighted take place outside the factories and are not related to decreases in production time. However, production time is being squeezed.

2. Delayed information from buyers creates production problems

While production time is being squeezed, many buyers are not taking equal responsibility for shortening their turnaround times. Manufacturers repeatedly highlighted:

- *Late opening of Letters of Credit (LC)* – this is particularly serious for smaller manufacturers who do not have an adequate credit rating to purchase raw materials without the LC. This delays production.
- *Late and inaccurate specifications sheets* – chasing the correct information can take several days, or several weeks in worst cases
- *Slow sample approval* – manufacturers consistently reported problems with sample approvals, stating that the buyers lack deadlines for sample approvals so they can take several weeks.
- *Slow lab dips tests* – again lab dip tests for colour are another very common delay in the production pipeline.
- Some of the buyers acknowledged that internal issues played a significant role in creating delays for the suppliers.
- *According to one buyer, "65% of delays are caused by us, for example lack of timely information on colour, size, volume breakdown." According to him this brand needs "a clear contract with suppliers where suppliers make explicit that any deviation from those deadlines will affect [on-time] delivery."*

- *Some brand interviewees said that they pay to air production if they are responsible for the delays. However, manufacturers and one brand interviewee stated that the cost of airing is negotiated because some brands try to get manufacturers to contribute to cost.*
- *One supplier noted that if one order had four delivery 'flows' on different dates and on flow had* to be aired, that wiped out his profit on the entire order.

3. Inexperience of buyers and mid-level merchandisers

This was recognised as an issue by both manufacturers and some brand interviewees. The lack of experience and technical knowledge among mid-level buyers and merchandisers, according to the interviewees, creates problems with specification sheets. It also slows down production when there are issues that need to be solved as they are unable to make decisions.

- *According to one brand interviewee, "specific dates [are needed] for each of the information deliverables… this would be a roadmap for the buyers who are 12 years old and have zero experience".*

The high turnover among buyers across the industry prohibits the development of long term relationships with suppliers. It may also contribute to the fact that they have little independent authority to make decisions so even small issues are escalated, wasting time and resources.

Recommendations for brands

1. Research internal critical path

Identify the key decision points in the internal production pipeline and develop rigorous deadlines for the information required at each of these decision points

2. Identify key decision makers

Identify the decision makers at each of the key decision points. Include on-time decisions and accurate communication of information in their Key Performance Indicators (KPIs) and monitor performance on this issue. This will not only decrease delays which can put enormous pressure on production planning – and consequently on code compliance – but it can also support moves to decrease the internal production pipeline and improve internal efficiency.

3. Trial local sample approvals or alternative methods

This is more achievable for brands with local offices. Local trials could create significant time savings for both manufacturers and brands. Alternative methods may include developing design specialists within the producing country; increased use of electronic communications are being trialled by some brands.

4. Develop local labs

Identify and accredit more local labs to run lab dip tests to speed up turnaround

Recommendations for manufacturers

1. Improved planning

As has been already stated in this report, production planning has been identified as an on-going issue over the past ten years in Bangladesh. While important strides have been made, improvement is still possible. Factoring in on-going challenges such as:

- delayed samples
- worker turnover

- how accurately the daily quota target has been achieved over the past 3 months
- national holidays
- complexity of the garment
- and a buffer to account for delays.

More accurate production planning is an important tool in supporting greater efficiency and code compliance.

Changes to orders

Industry trend

Changes are endemic to the industry. Planners change volume forecasts depending on what is selling or not and designers change the designs to create that 'must-have' garment. Some buyers see the acceptance of changes as a favour from manufacturers, others see it as part of a flexible service.

Research findings

1. Changes in design are most disruptive

The most disruptive change identified by brand and non-brand manufacturers was changes to design. As Table 2 shows, these can affect up to 20% of orders, with 1-2 changes per order. One interviewee from a high fashion brand noted that up to 50% of their garments have changes, with 4-5 changes made on these orders. The most significant impact is the delays that changes can create as they undermine production planning, output and code compliance across the factory. They can also necessitate resampling and doing additional lab dips.

Scale of change experienced by brand suppliers	Scale of change experienced by non-brand suppliers
• Changes affect 20% of orders • Normally 1-2 changes on these orders • 25% of affected orders are delayed by 2 weeks +	• Changes affect 20% of orders • Normally 1-2 changes on these orders • less than 20% of affected orders are delayed by 2 weeks +

Table 2: Comparison of the scale of changes between brand manufacturers and non-brand manufacturers

- *According to one manufacturer, he has changes on 5% of orders: "although 5% is a small percentage of orders to be affected by changes to design this can be very harmful for the factory. It can be the whole profit margin of a factory wiped out. If you have turnover of $5 million, you could lose 2.5% of total turnover through this."* If this is the case, it does beg the question, 'how can manufacturers meet code requirements, especially with regard to paying a living wage and overtime payment?'

2. Inaccurate forecasting creates changes

There is awareness among buyers that changes to forecasts create problems for suppliers, though opinions on this subject are divided.

- *One buyer stated that it is impossible to have accurate forecasts while another said that all large brands now have enough skills and knowledge to forecast "pretty accurately".*
- *According to a third buyer, "changes are because of constant changes in the demand signal from the market, so forecasting is the issue. But our scale is so large that this has huge impact if we change from 24 million t-shirts to 18 million t-shirts. These are large fluctuations with a large impact [globally]."*

3. Extensions are not always a solution
When compensating for a brand's delays, extensions are of limited value. Several manufacturers stated that extensions delay the production that is scheduled after the delayed order. As delays are a consistent theme within the industry, this seems to imply that there are on-going issues around planning and the manufacturers' inability to plan due to insecure orders, late information and changes.

Recommendations to brands

1. Develop cut-off deadlines for different categories of change
Tight cut off deadlines need to be developed for changes to design and increases and decreases to volumes. Changes to design and volume that occur before the orders are placed are not considered a serious problem by the manufacturers interviewed. However, changes to design after sampling and lab dips are a much greater challenge in terms of production planning.

2. Develop criteria for accepting and rejecting changes to volume and design
These criteria need to reflect the scale of impact the change will have. There is a difference between a 5% increase and a 40% decrease in volume. There is also a difference between changing the trim on a t-shirt and changing the colour of the t-shirt.

3. Become more selective in approving changes
Not all changes add value to the brand. This is particularly the case with design changes that can be very subjective. These can increase the workload across departments for both brands and manufacturers: this increases delays and creates additional costs for all parties.

Recommendations to manufacturers

1. Upgrade workers' skill levels
Globally there is a greater emphasis on lean manufacturing to cope with shorter production times and high fashion orders with shorter runs. Efficiency on high volume output for a single style is becoming less important. Adaptability to changes and the ability to learn new styles quickly is increasingly important. This requires different skill sets and more training in order for production to come in line with the dominant trend within the garment industry.

Cancellation of orders

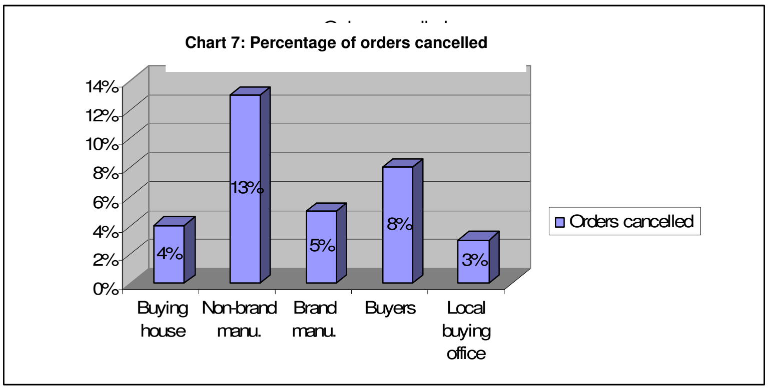
Industry trend

Cancellations are a part of the industry. They are based on responses to market demands that are made quite late in the process. Clearly, the cancellation of an order is the most drastic form of change a buyer can make. In some cases, cancellations are made as a result of poor quality products.

Research findings

1. Cancellations are linked to poor forecasting
Brand manufacturers had a lower rate of cancellations (5%) than non-brand manufacturers (13%) the orders cancelled (Chart 7). One third of brand interviewees stated that they cancel orders after the cut date.

- *According to one buyer, the brand does a "very poor job" on forecasting. He said that it needs to become much more exacting because at present they "commit and cancel orders more than half way through."*



2. Inadequate compensation for cancellations
The financial cost of these cancellations is not taken on by the brands. Half the buyers interviewed stated that they either pay the cost of raw materials or reuse the materials in a later order.

- *Only one buyer said that they are willing to negotiate the costs incurred by lost production time, loss of opportunity and impact on production planning on cancellations that are their responsibility.*

Recommendations for brands

1. Continue to improve forecasting tools
Forecasting drives much of the garment industry therefore it directly benefits both brands and manufacturers if forecasting tools become more accurate.

2. Re-evaluate compensation
At the very minimum manufacturers should have raw material costs reimbursed by all brands and retailers. The additional costs that are incurred from overhead costs and workers' wages when they are idle and/or sent home early to missed opportunities need to be considered more seriously by brands.

3. Develop guidelines for cancellations
These should include guidelines on deciding which manufacturers will have their orders cancelled and what sort of compensation is provided to them. If they are promised additional or replacement orders this should be tracked to ensure that they receive this compensation.

Recommendations for manufacturers

4. Develop comprehensive cost breakdown for cancellations
At present brands and retailers are not paying the full costs for cancellations. Raw material costs are only element. There are other costs that need to be factored in and presented to brands. These include overhead costs, lost opportunity, payment for workers for completed work, as well as payment for the time they are idle and/or sent home due to lack of work.

5. Monitor quality inspections to ensure consistent quality
The cancellation of orders because the quality is sub-standard is a loss that manufacturers can avoid through the development and implementation of more rigorous quality inspections.

Conclusion

This research clearly shows that a more mature model of trading relationships would benefit brands and retailers, manufacturers and workers. The current system is fundamentally insecure. This drives pressure on terms, conditions and costs, undermining manufacturers' ability to provide well managed factories and support code compliance.

The levels of cooperation and trust between brands and manufacturers where relationship contracts are in place show the benefits available to all parties. Increased dialogue on issues ranging from forecasting and planning to costs and compliance delivers gains for product, quality and service for brands; it delivers gains on planning, costs and compliance for manufacturers, and improved working conditions for workers.

At present, there is a clear split within many brands and retailers between 'the business' and CSR. Their employees are focused on product and price; there is little or no awareness of the impact of their decisions on manufacturers or workers. In many cases they are, however unintentionally, exploiting the current downward pressure on prices and conditions to achieve lower prices and greater flexibility. But are these gains sustainable? Do they support or undermine the development of the kind of manufacturers with whom they wish to do more business?

The current focus on purchasing practices is a pivotal moment in the CSR debate and within the development of a more mature model of industrial relations. Over the past decade there has been an external focus on the rights of brands and retailers and the obligations of manufacturers. Code compliance was seen as the responsibility of manufacturers and brands and retailers developed and policed codes to reassure consumers.

The willingness of brands and retailers to look internally and begin to examine their own practices – and the impact of these practices on manufacturers and code compliance – marks a fundamental shift in attitude. It is the beginning of an acknowledgement that brands, retailers and manufacturers share rights and responsibilities. Through increased understanding of the issues that undermine good business, we are creating an opportunity to begin dialogue on some difficult and sensitive areas. This slowly builds trust within the relationships and opens the door to the development of mutually agreed terms and conditions of trade, and to mutually agreed definitions of the costs involved in doing business in a sustainable and compliant manner.

Appendix 1

Research Methodology

This research builds on the previous report to include the opinions of suppliers, buying houses and local offices of international brands. A total of 35 interviews were carried out with representatives from:

- 7 international brands
- 4 local offices of international brands
- 7 buying houses
- 17 suppliers

Seven brands within the MFA Forum's Buyers' Group took part in the research. In the case of one brand, two buyers were interviewed. The findings therefore reflect the answers of 8 buyers rather than 7 brands. Three of the four local offices were subsidiaries of the brands interviewed. One local office is a subsidiary of another international brand that sources for a member of the Buyers' Group. Unless otherwise stated, the views of the local offices reflect those of the international offices.

Of the seventeen suppliers interviewed, twelve supply members of the Buyers' Group. Five suppliers work for national or regional brands.

A seven page questionnaire, covering eight topics, was designed for each group and pre-circulated. Interviews with buyers were done by phone from the UK. All other interviews were carried out in Bangladesh and were face-to-face, with three exceptions: one telephone interview; one video conference interview; and one questionnaire was filled in by a supplier and faxed to the researchers.

A validation workshop was held in Bangladesh to verify the findings and get additional feedback. This was attended by approximately twenty people representing industry associations, brands, buying houses, suppliers, an NGO and the GTZ. All information has been collated and anonymised to ensure confidentiality.

Limitations of the research

The small size of the respondents' group limits the research findings. This is an indicative case study that highlights issues that are acknowledged challenges within the industry at present. It provides a baseline of the key issues that emerge from current purchasing practices. Detailed information on each of these issues would require additional research.

The sample of brands and suppliers is not representative. This is for several reasons. First, many brands and suppliers found the issue too sensitive and declined to take part. Those that took part were self-selecting and therefore not necessarily representative or randomly chosen. Second, the interviewees in each brand and supplier varied. This is because job titles vary between companies and the sensitive nature of the subject meant that personnel in different departments and at various levels of seniority were willing to participate.

Third, many of the suppliers were recruited through industry associations in Bangladesh and, consequently, are not necessarily representative of the entire industry. It was very difficult to get non-brand suppliers to participate; therefore the sample size is unbalanced with 12 brand suppliers and 5 non-brand suppliers.

Appendix 2

MFA Forum Purchasing Practices Project

Questionnaire for Brands and Retailers

This questionnaire is part of the second phase of the MFA Forum's research into purchasing practices. The first phase identified brand and retailers' projects on purchasing practices. Not all projects were based in Bangladesh, but they could benefit current practices within Bangladesh. The second phase of the research is examining the key issues that undermine current purchasing practices in Bangladesh. The research focus has widened to include buyers within the brands and retailers, buying houses / agents and suppliers.

You do not need to fill out the questionnaire. It is being pre-circulated for your information. All information will be collated and anonymised.

Relationship with suppliers

1. **What are the top three criteria you use to select first tier suppliers?** *(Please tick three boxes)*

☐ Size of manufacturing capacity
☐ Availability of additional services e.g. design, logistics etc.
☐ Vertical integration
☐ Cost
☐ Turn around times
☐ Personal contact
☐ Code of conduct in place
☐ Other (please specify) ____________________

2. **What percentage of first-tier supplier locations do you know?**
☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

3. **Do you have a contract with your first tier suppliers?** Yes ☐ No ☐

4. **If yes, is it a relationship contract or a volume contract?** *(Please tick one box)*
☐ Relationship contract
☐ Volume Contract

5. How many of your first tier suppliers have an on-going relationship with you?
☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

6. What percentage of products do you buy from suppliers in on-going relationships?
☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

7. **How much does your annual spend with suppliers in on-going relationships vary each year?**
☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

8. **What percentage of your first tier suppliers change each year?**
☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

9. **What are the top three reasons for changing first tier suppliers?** *(Please tick three boxes)*

☐ Costs are too high
☐ Repeated quality failures
☐ Repeated missed delivery deadlines
☐ Code violations
☐ Other (please specify)____________________

10. **Do you have a responsible closure policy for factory exits?** Yes ☐ No ☐

11. **Do you have a responsible closure policy for country exits?** Yes ☐ No ☐

12. **Do you work with buying houses / agents in Bangladesh?** (*If no, go to Q18*) Yes ☐ No ☐

13. **If yes, do you have a contract with the buying houses / agents?** Yes ☐ No ☐

14. **If yes, is it a relationship contract or a volume contract?**

☐ Relationship contract
☐ Volume Contract

15. **If yes, what is the average commission charged by a buying house / agent?**

☐1-5% ☐ 6 - 10% ☐ 11 - 15% ☐ 16 - 20% ☐ 21 - 25%

16. **If yes, what are your top three reasons for using a buying house / agent?** *(Please tick three boxes)*

☐ Order management
☐ Expertise in procurement
☐ Outsourcing design, production and other functions
☐ Cost savings
☐ Responsiveness to requests
☐ Other (please specify)____________________

17. **If yes, what is the main drawback of using buying house / agents?** *(Please tick one box)*

☐ Lack of control over production
☐ Potential for negative publicity if non-compliant conditions are found
☐ Cost
☐ Quality failures
☐ Delays
☐ Other (please specify)____________________

Delays

18. **Has lead time decreased in the past two years?** Yes ☐ No ☐

19. **If yes, how many days has the lead time decreased by?**

☐ 5 days ☐ 10 days ☐ 15 days ☐ 20 days ☐ 25 days ☐ 30 days ☐ 35 days

20. **Has this led to increased overtime for workers?** (*If no, go to Q22*) Yes ☐ No ☐

21. **If yes, do you pay a premium to cover these increased labour costs?** Yes ☐ No ☐

22 **Do you penalise suppliers for occasional late deliveries?** Yes ☐ No ☐

23. **If yes, how?** *(Please tick all appropriate boxes)*

☐ Delay payment
☐ Financial fine
☐ Decrease orders
☐ Cancel future orders
☐ Other (please specify) ______________________________

24. **Do you examine the root cause of serious delays?** Yes ☐ No ☐

25. **If you create a delay, do you give an extension on the ex-factory date?** Yes ☐ No ☐

(*If no, go to Q29)*

26. **If yes, what percentage of delayed orders get an extension?**

☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

27. **If yes, what percentage of delayed orders get an extension equal to the delay?**

☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

28. **If yes, do you pay an additional fee to cover the increased costs of shorter production time due to delays your company caused?** Yes ☐ No ☐

29. **Name one change that would significantly reduce delays**

____

____

Changes

30. **What is the most common form of change you make to an order?** *(Please tick one box)*

☐ Increase in volume
☐ Decrease in volume
☐ Change to design

31. **What percentage of orders do you change after the order is placed?**

☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

32. **If an order is changed, what is the average number of changes made to one of these orders?**

☐ 1 change ☐ 2 changes ☐ 3 changes ☐ 4 changes ☐ + 5 changes

33. **How many orders are delayed by more than one week due to changes you make?**

☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

34**. In general, are changes made after the order is placed or after the cut date?**

☐ Before the order is placed
☐ After the order is placed
☐ After the cut date

35. **On average, how many days are between the last change and the delivery date?**

☐ 5 days ☐ 10 days ☐ 15 days ☐ 20 days ☐ +25 days

36. **Name one difference that would significantly reduce the number of changes made**

____

____

Forecasting and Cancellations

37. **Do you give suppliers advance warning about increases or decreases in your forecasts?** Yes ☐ No ☐

38. **In general, at what point do you provide that information?** *(Please tick one box)*

☐ At forecasting
☐ After initial price negotiations
☐ After the order is placed
☐ After the cut date
☐ Other (please specify) ______________________________

39. **What percentage of orders is cancelled?**
☐ 5% ☐ 10% ☐ 15% ☐ 20% ☐ 25% ☐ 30%

40. **At what point is an order most commonly cancelled?** *(Please tick one box)*

☐ After the order is placed
☐ After the cut date
☐ After production begins

41. **Do you provide compensation to cover lost production etc.?** Yes ☐ No ☐

42. **If yes, what compensation do you provide after a cancellation?**

____

____

Sustainable Pricing

43. **Do you have a supplier scorecard?** *(If no, got to Q.45)* Yes ☐ No ☐

44. **If yes, do you reward suppliers that achieve a high scorecard ranking?** Yes ☐ No ☐

45. **Do you have a sustainable cost model on which you base unit price negotiations?** Yes ☐ No ☐

46. **Do you have a mechanism for suppliers and sub-contractors to approach, if they feel prices are not sustainable?** *(If no, got to Q.48)* Yes ☐ No ☐

47. **If yes, how does this work?**

____

____

48. **Has the unit price decreased over the past two years?** *(If no, got to Q.50)* Yes ☐ No ☐

49. **If yes, by how much?**
☐ 5% ☐ 10% ☐ 15% ☐ 20% ☐ 25% ☐ 30%

50. **Do you negotiate the price before delivery?** *(If no, got to Q.53)* Yes ☐ No ☐

51. **If yes, does this price change after the order is placed?** Yes ☐ No ☐

52. **What is the most common reason for changing the price?**

____

____

53. **If no, why is the price negotiated after delivery?**

____

____

54. **What percentage of orders is subject to price changes?**
☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

55. **On average, how many times does the price change on one order?**
☐ Once ☐ Twice ☐ 3 times ☐ 4 times ☐ + 5 times

56. **Do you pay an additional fee if you request an extra quick delivery?** Yes ☐ No ☐

57. **Do you negotiate extra production for free?** Yes ☐ No ☐

58. **If yes, what percentage of the order negotiated for free?**
☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

59. **Do you negotiate a sale or return clause?** Yes ☐ No ☐

60. **Do you get counter quotes from other suppliers?** Yes ☐ No ☐

61. **Has your quality specification increased over the past two years?** Yes ☐ No ☐

62. **If yes, has the price increased to reflect this?** Yes ☐ No ☐

63. **Do you fine suppliers for quality defects?** Yes ☐ No ☐

64. **Which department has responsibility for deciding price in your company?** *(Please tick one box)*

☐ Planning
☐ Merchandising
☐ Production
☐ Finance
☐ Other (Please Specify)____

65. **Which role has responsibility for deciding price in your company?** *(Please tick one box)*

☐ Vice President
☐ Executive Director
☐ Director
☐ Manager
☐ Other (Please Specify)____

Terms of Payment

66. **Is the timing of payments set out in a legal contract?** Yes ☐ No ☐

67. **What percentage of payments are made on time or before the time agreed?**
☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

68. **Do you charge suppliers a commission in exchange for payment at a specific time e.g. after 30 days?** Yes ☐ No ☐

69. **If yes, what percentage is this commission?**
☐ >2.5% ☐ >5% ☐ >7.5% ☐ >10% ☐ >12.5%

70. **What is the average length of time between the ex-factory date and the payment date?**

☐ >15 days ☐ >30 days ☐ >45 days ☐ >60 days ☐ >75 days ☐ >90 days ☐ 120+ days

71. **Has this time increased over the past two years?** Yes ☐ No ☐

72. **If yes, by how long has the time increased?**

☐ 5 days ☐10 days ☐ 20 days ☐ 30 days ☐ 40 days ☐ 50 days ☐ +60 days

73. **What percentage of payments is late?**

☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90%

74. **What is the average delay between the agreed payment date and the actual payment date?**

☐ 10 days ☐ 20 days ☐ 30 days ☐ 40 days ☐ 50 days ☐ 60 days ☐ 90 days

Transparency

75. **Do you provide suppliers with terms of trade explaining your policy on ordering, poor quality products, promotions, and complaints?** Yes ☐ No ☐

76. **Is there a complaints mechanism for suppliers?** Yes ☐ No ☐

77. **If yes, how are suppliers informed of the mechanism?** *(Please tick one box)*

☐ Formally – through terms of trade documentation or a contract
☐ Informally – through discussions with you or others in your company

78. **Does your company have a formal conversation with each first tier supplier about social and environmental improvement?** Yes ☐ No ☐

79. **If yes, how many times per year does this conversation happen?**

☐ Once ☐ Twice ☐ 3 times ☐ 4 times ☐ 5 times

80. **If yes, which department is responsible for this conversation?** *(Please tick one box)*

☐ Buyers
☐ Production
☐ CSR
☐ QA
☐ Other (please specify) ______________________________

Respect for human rights in the supply chain

81. **How many of your suppliers in Bangladesh knew about expected minimum labour standards before you audited them for the first time?**

☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐

82. **Are there systems in place to help suppliers to meet your code of conduct?** Yes ☐ No ☐

83. **If yes, please describe them?**

____

____

84. **What percentage of your supply base has a collective bargaining agreement in place that includes wages?**

☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐

85. **How many of your company buyers are trained to understand your code of conduct?**

☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

86. **How many buyers are trained to understand the impact of their decisions on suppliers' ability to meet your code of conduct?**

☐ 5% ☐ 10% ☐ 20% ☐ 30% ☐ 40% ☐ 50% ☐ 60% ☐ 70% ☐ 80% ☐ 90% ☐ 100%

87. **Does your job description include prioritising the use of suppliers with high levels of code compliance?** Yes ☐ No ☐

88. **Is prioritising the use of suppliers with high levels of code compliance included in your incentives?** Yes ☐ No ☐

Is there anything you would like to add that you feel is important for brands to consider when discussing purchasing practices?

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____

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Thank you for your participation