The crisis and garment production in Central America

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- Does the industry have a future?
- How are workers being affected?
- Does the decent work agenda fit into future plans?

LAST YEAR MSN CARRIED OUT interviews with 10 major North American apparel brands concerning changes in their sourcing practices since the end of the import quota system in January 2005.[2] We also asked them to look ahead at possible changes in their sourcing practices in the next five years and to explain what factors – changes in production practices and/or government policy – would encourage them to maintain or increase sourcing in Central America and/or Mexico.

At the time of the interviews no one anticipated the financial – and now global economic – crisis that was about to hit us all, or how deep the crisis would be.

Although the information we received from the buyers we interviewed indicated that changes in their sourcing patterns and practices since the end of quotas were having significant adverse effects on a number of garment-producing countries, the reports were not as negative as we had anticipated.

Many industry experts had predicted that with the end of import quotas there would be major geographic shifts between countries where apparel production was taking place. Most experts agreed that orders and investment would shift to a few large Asian countries like China and India that have lower production cost and ready access to materials, while other countries with higher production costs would face significant declines in orders and investment, and some of those countries would see their garment industries decimated.

Of the companies we interviewed, almost all had ceased placing orders with at least one country since the end of quotas, however, there was less consistency than we had expected on the countries they had left. For instance, Honduras and El Salvador experienced increases in orders from some companies and decreases in orders or country exits from others. And while there was considerable evidence of companies reducing orders to some countries while increasing orders to others, there was little evidence of a significant decrease in the total number of countries used by these major brand buyers.

While two of the ten companies we interviewed said there were reductions in orders to Central America or Latin America as a whole, some Asian countries were also identified as places experiencing reductions in orders. Countries where more than one of the buyers we interviewed had ceased placing orders included Guatemala, Canada and the Philippines. Countries that more than one buyer identified as new sourcing locations included Haiti (5), Vietnam (4), Nicaragua (2), Cambodia (2), and Egypt (2).[3] Countries where more than one buyer had significantly decreased orders included Mexico (5), El Salvador (2) and Sri Lanka (2). Countries where there was a significant increase in orders included Vietnam (5), India (3) and China (3).[4]

Many industry experts had predicted that China would be the biggest winner as a result of the end of quotas. However, while some of the buyers reported an increase or significant increase in orders to China, others said there was only a small increase or no increase at all in orders to China and an increase in orders to neighbouring countries, such as Vietnam, Cambodia, Bangladesh and India.[5]

So, while there have been major shifts in orders and investment since the end of quotas and these changes have had a dramatically negative impact on many garment workers and garment producing communities and countries, the results have not been as devastating as many experts had predicted. Not all production has shifted to China, and some production has remained in the Americas.

When we asked the companies we interviewed what factors would encourage them to maintain or increase orders to Central America and/or Mexico, all of them pointed to the price of production as the most important factor. However, they also identified a number of other important factors, including proximity to market, delivery time, availability of fabric and other materials, ability to provide multiple services (full package), flexibility to do a variety of styles, capability to do premium products, reliability (ability to meet deadlines), and transparency about their suppliers' own supply chains.

Although labour standards and environmental compliance were not the most important factors listed, these were seen as part of a package buyers look for when making sourcing decisions, particularly when entering new countries or business relationships with new suppliers. Environmental issues, and particularly carbon footprint issues, were identified as at least as important, if not more important, than labour standards issues.

So, while Central America had little chance of competing with many Asian countries on price, it looked like it had a definite advantage in terms of proximity to market and, potentially, speed to market. As well, in a period of high oil prices, it looked like Central America and Mexico would have a big advantage on the cost of transportation and the related carbon footprint issue.[6]

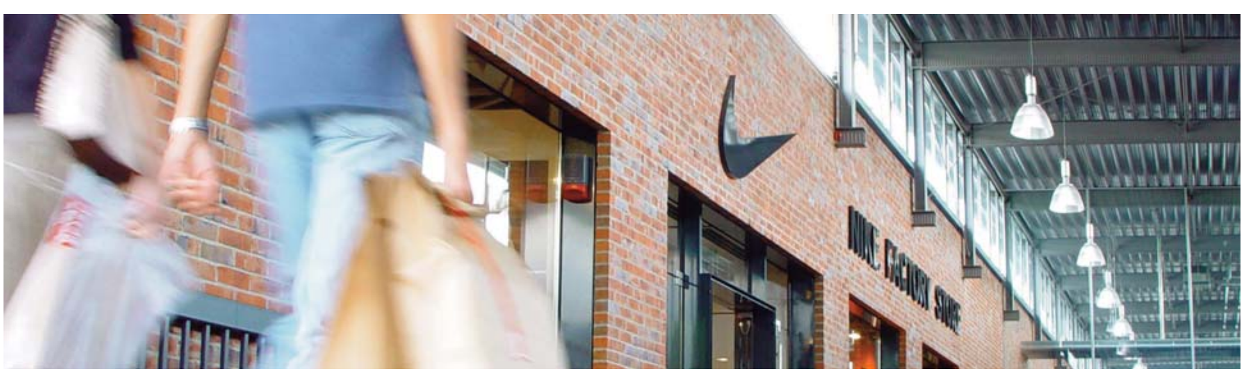
At least this was the situation before the economic crisis hit.

The crisis and its implications for Central America

UNLIKE THE END OF QUOTAS, WHERE WE WERE SEEING shifts in production and the level of production between countries and geographic regions, the economic crisis will likely reduce the total amount of apparel production worldwide, or at least the amount of production of certain kinds of apparel products.

One indication of the impact of the crisis on the garment industry is the reduction in apparel sales in North America, and the fact that this reduction in sales is hurting certain kinds of companies more than others.

For example, the US specialty retailer Gap suffered



a 12% decrease in December 2008 sales and a 19% decrease in January 2009 sales. Abercrombie and Fitch suffered a 24% decrease in December sales. American Eagle Outfitters suffered a 17% decrease in December sales and a 15% decrease in January sales. [7]

In contrast, Wal-Mart experienced a 1.7% increase in December sales and a 6.1% increase in January sales. While these were lower increases than the company had anticipated, Wal-Mart and other discount chains are doing much better than the higher end specialty retailers. And while other discount chains aren't doing as well as Wal-Mart, they are doing better than the specialty retailers.[8] In December, Target suffered a 4.1% decline in sales, and Sears suffered a 7.3% decline.[9]

This would seem to indicate that the crisis is encouraging North American consumers to change their shopping habits, buying on the basis of price rather than on the basis of brand image. The data also suggests that discount retailers like Wal-Mart will likely survive the economic crisis better than the companies that sell products based on their brand images, such as Gap and Abercrombie and Fitch.

A second indicator of the impact of the crisis on the garment industry is the decrease in apparel imports to the US. In December 2008, apparel imports by volume had decreased by 2.73% as compared to December 2007. More telling was the 5.7% decrease in apparel imports in November 2008 as compared to November 2007.[10]

And while China was still the top apparel producer for the US market in 2008, the volume of apparel imports from China had actually dropped by 3.05% compared to 2007.[11] More recently, reports have appeared in *Business Week* about massive layoffs in China – as many as 20 million – and growing fears of social unrest as the unemployed workers return to their rural villages with no prospects of alternative employment.[12]

As far as Central America and the Caribbean are concerned, according to the US International Trade Commission[13], most countries, with the exception of Haiti, have had a drop in the dollar value of clothing exports to the United States, with Guatemala being the most affected. Nicaragua, for example, has seen its exports in dollar value decrease by 15.2% in March 2009 compared to the previous year. In El Salvador, there has been a 12.9% decline for the same period. Although many of the major garment exporters in Asia have also seen declines, for example the Philippines, which saw a 23.5% drop, the losses have not been as significant as those which have occurred in Central America. The average drop for the region, including the Dominican Republic and Haiti, for March 2009 compared to the previous year, is of 17.2%

Unfortunately, the worst is likely yet to come. In a February 2009 management briefing paper, the UK based apparel industry publication *Just-style* noted, "Retailers are overstocked; they have too much inventory, and are cancelling orders."[14]

What does the future hold?

IN THE SAME REPORT, *JUST-STYLE* GOES ON TO PREDICT, "In the future, buyers will want smaller quantities, on short lead times – which mostly means trying to find value-for-money sources closer to home."[15] If *Just-style* is correct, there is some hope for Central America.

In this insecure environment, buyers are going to want to shift more of their risk down the supply chain to the manufacturers. For instance, they will likely favour full-package suppliers that take more responsibility for the total production process, including some design work, and are able to meet their demands for flexibility and speed to market.

Given the lack of access to credit in the current economic environment, only the largest and most financially solvent suppliers will be able meet these demands. As a result, we can expect to see a further consolidation of the industry as some retailers and manufacturers are forced to declare bankruptcy when they are unable to secure loans or to pay back loans taken out before the crisis.

However, it is unlikely that all small garment manufacturers will go out of business. In order to reduce costs, larger manufacturers will be tempted to subcontract more production to small sewing workshops where wages and working conditions are generally worse than in larger factories.[16] Because suppliers will need to hide this practice from buyers, abuses will be much harder to uncover.

The demand for more flexible labour to produce smaller orders of different styles of clothing whenever needed will also have a major impact on workers. We will likely see more employment of workers on consecutive, short-term contracts and/or through third-party employment agencies. Such schemes are often used by employers to avoid making payments to social security or other government programs that are so important to women and their families. Consecutive short-term contracts are also often used to keep out unions since union organizers or sympathizers can find their contracts are simply not renewed at the end of their term.[17]

Flexible labour also means job insecurity for women workers who need a steady income to support themselves and their children. With shorter lead times and smaller orders, employers will likely demand excessively long hours of work in some periods of the year and provide no work in others. And women will be expected to adjust their family life and responsibilities to meet the needs of their employers and the brands.

Job insecurity and the need to work long hours of intensive labour whenever there are orders, and the stress that goes with flexibilized labour, will have a huge impact on workers' health. Women's groups in Central America have already been documenting the workplace injuries suffered by women who work intensively for 11 or 12 hours a day, four days a week. Both of these issues – precarious employment and chronic health problems – require more effective and coordinated efforts.

● One possible survival strategy for Central America would be to position itself as a region that not only enjoys proximity to market, but is also socially and environmentally responsible.

A competitive advantage for Central America?

IN THIS DIFFICULT ECONOMIC ENVIRONMENT, WHAT hope is there for a garment industry that respects the rights of workers?

Despite increased pressure from buyers to cut costs, Central America cannot compete with Asian countries like China, India, Vietnam or Bangladesh on the basis of price and reduced labour costs. *If* there is a competitive advantage for Central America, it will likely be proximity and, potentially, speed to market and the ability to produce small orders of a variety of styles.

And despite the fact that oil prices are not currently a major factor in decisions concerning which countries to source from, though oil prices are certain to rise again, the carbon footprint issue is still a growing concern of Northern consumers and therefore of brand buyers, as well as some discount chains like Wal-Mart. *Just-style*, for example, predicts that there will be a "race to the top" among suppliers on environmental issues, "with the surviving suppliers being those companies that chose to compete on their environmentalist credentials, in addition to cost, quality and other traditional factors."[18]

One possible survival strategy for Central America would be to position itself as a region that not only enjoys proximity to market, but is also socially and environmentally responsible. Doing so at a regional level would discourage negative competition between countries and encourage harmonization upward on labour and environmental standards and practices.

While adopting this high-road strategy might not protect many existing jobs in the short-term, it could position Central America to be globally competitive once we emerge from the recession and enter a period of economic recovery. Given the depth and seriousness of the current recession, Central America will certainly have time to retool to be able to supply this emerging market.

Of course, filling this niche would require upgrading of the industry, and external financial support would be needed for that to happen. It would also require a major change in attitude by Central American governments about labour and environmental standards.

Rather than viewing labour and environmental standards enforcement as a liability that discourages foreign investment, governments would have to realize that for brand buyers and some larger manufacturers, impartial and consistent enforcement of labour and environmental laws is a necessary component of a responsible competitiveness strategy.

It's worth noting that five of the ten brands we interviewed in 2008 commented on the need for improvements in labour practices and labour standards enforcement in Central America and Mexico.[19]

Central American governments would also have to change their attitude toward demands made by the US administration concerning the link between labour and environmental standards and free trade agreements. Rather that viewing such provisions as protectionist threats to local industry, Central American governments would be wise to see the potential advantages of upgrading labour and environmental practices as part of a responsible competitiveness package that also includes investment in industry upgrading to meet the needs of the North American market.

If the new US administration is serious about its stated commitment to linking improved labour and environmental standards to free trade agreements, it should be prepared to invest in industry upgrading in Central America that includes improved enforcement of and compliance with labour and environmental standards.

Living wage and freedom of association must be part of the picture

HOWEVER, FOR RESPONSIBLE COMPETITIVENESS strategies to be viable we in the labour rights and environmental movements need to also make clear demands for improved labour rights and environmental practices on the brand buyers, retailers and discount chains that are most likely to survive the current economic crisis.

If giant retailers and brands want to make a real contribution to economic recovery and economic stability in the post-recession period, they should make a commitment now to give preference in all new orders to countries and factories that provide decent work, including providing wages that meet workers' basic needs by local standards. There has been a lot of debate internationally about how to define and calculate a living wage. But how we define a living wage isn't the real issue; how to get there is.

Paying workers decent wages would be the best stimulus for an economic recovery, since workers spend their incomes locally and don't hide their money in off-shore bank accounts or gamble it on the stock market. Improved wages for women maquila workers would also contribute to social stability, since women use their incomes to support their families and to invest in their children's future.

We need to set a floor on wages regionally and globally that allows workers and their families to meet their basic needs by local standards. If that means prices for consumer goods will be slightly higher in North America and Europe, so be it.

But for a living wage to become a real possibility rather than a distant dream, the giant retailers and brands that survive the current economic crisis need to make a commitment now to a new way of doing business in the post-recession period, one in which they pay sufficient prices to allow manufacturers to pay workers a living wage.

And in order to achieve decent work, companies and governments must begin to see unions as legitimate social actors rather than a threat. If unions were allowed to play their proper role of negotiating on behalf of workers for improvements in wages and working conditions, this would allow workers to have a say in determining what constitutes a living wage that meets their basic needs.

So while the effects of the quota phase-out were not as devastating as initially predicted, the impending economic crisis now appears ready to do much more damage. In order to weather the storm, Central America should avoid the foreseeable trends of greater flexibilization of employment and declining respect for FOA, and instead take the high road of responsible competitiveness and decent work. ■

Endnotes

[1] Based on presentations at two events in Central America: *After the Maquilas Are Gone, What Is Left?* a public forum organized by the Independent Monitoring Group of El Salvador (GMIES) on March 3, 2009; *and The Global Financial Crisis: Its Impact on the Garment Sector and Garment Workers*, for the 11th annual colloquium of the Movement of Working and Unemployed Women, *Maria Elena Cuadra*, in Nicaragua on March 8, 2009.

[2] *Is There a Future for Brand Sourcing in the Americas? Interviews with Apparel*

Brands about Trends in Global Sourcing, Maquila Solidarity Network, September 2008 available at:

http://en.maquilasolidarity.org/sites/maquilasolidarity.org/files/MSN-Brand_Interviews-EN-2008-11.pdf

[3] *Is There a Future for Brand Sourcing in the Americas? Interviews with Apparel Brands about Trends in Global Sourcing*, Maquila Solidarity Network, p.2.

[4] Ibid.

[5] Ibid, p. 2-3.

[6] Ibid, p.7.

[7] *How will the global financial crisis affect the garment industry and garment workers?,* Maquila Solidarity Network, February 2009, p.1, available at http://en.maquilasolidarity.org/sites/maquilasolidarity.org/files/2009-02-25%20MSN-FinancialCrisis-Feb09-ENG.pdf

[8] Ibid.

[9] Ibid, p.2.

[10] Ibid.

[11] Ibid.

[12] "A Tough New Year for China's Migrant Workers." *Business Week*, February 4, 2009, available at http://www.businessweek.com/globalbiz/content/feb2009/gb2009024_357998.htm.

[13] See, www.usitc.gov.

[14] *Just-Style*, "Apparel Industry Outlook for 2009: Management Briefing," January/February 2009, p.2.

[15] Ibid.

[16] For more information on the move to full-package production by larger manufacturers and the "sub-contracting pyramid" see Jennifer Bair and Gary Gereffi, "Local Clusters of Global Chains: The Causes and Consequences of Export Dynamism in Torreon's Blue Jeans Industry" in *World Development,* Vol. 29 Issue 11, November 2001, pp. 1885-1903.

[17] For more on the abuse of short-term contracts and of employment agencies in Mexico see the Centre for Reflection and Action on Labour Issues (CEREAL) October 2007 report entitled *Electronics multinationals and labour rights in Mexico*, available at http://goodelectronics.org/publications-en/cereal-report-multinationals-and-labour-rights.

[18] *Just-Style*, "Apparel Industry Outlook for 2009: Management Briefing," January/February 2009, p.3.

[19] *Is There a Future for Brand Sourcing in the Americas? Interviews with Apparel Brands about Trends in Global Sourcing*, Maquila Solidarity Network, p.8.

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