

RESPONSIBLE INVESTMENT

Pulling the thread: Labour Standards in the apparel industry



Across Quilter we have identified three thematic engagement priorities. This is part of our human rights theme.

The idea of human rights is as simple as it is powerful: that people have a universal right to be treated with dignity. Every individual is entitled to enjoy human rights without discrimination – whatever their nationality, place of residence, sex, national or ethnic origin, colour, religion, language or any other status. Human rights are interrelated, interdependent and indivisible¹.

SDG Alignment



“ *Fast fashion is not free. Someone, somewhere is paying the price.*”

Lucy Siegle, journalist and author

Employing over 300 million people across its value chain, the scale and reach of the apparel industry presents a number of human rights risks². These risks include low wages, precarious working conditions, harassment, health & safety breaches, the inability to form unions and the absence of adequate grievance mechanisms. The potential of adverse events is often more acute in the supply chains of companies that utilise a ‘fast fashion’ sales model. This model relies on companies catering to ever-changing consumer tastes as quickly as possible. In addition to labour concerns, the fast-fashion business model often follows the ‘take-make-dispose’ linear trajectory which can result in a cycle of unsustainable resource exploitation and extensive waste production. The lack of transparency throughout the complex supply chains for both materials and labour coupled with the price-driven culture can result in an increased risk of modern-day slavery. Another challenge faced by the apparel industry is the reliance on self-regulation and self-auditing which compounds the above risks further.

¹ United Nations backed Principles for Responsible Investment
² Ellen MacArthur Foundation - <https://www.ellenmacarthurfoundation.org/fashion-and-the-circular-economy-deep-dive>

Engagement

The engagement programme targeted our most material holdings with apparel manufacturing and retailing activities. We included companies using commonly categorised ‘fast fashion’ models and those with longer production cycles. All the companies have complex, global supply chain arrangements with third party manufacturing facilities typically clustered in China, Turkey, India, Bangladesh, Pakistan and Morocco. Our discussions covered five main areas of labour standards within the supply chain:

- governance of labour standards
- auditing process
- challenges in addressing issues beyond the primary supplier
- grievance mechanisms & remedial actions
- wage setting

This engagement programme was aimed at collating information, with the primary intended outcome to improve our understanding of how investee companies are managing and mitigating these risks. We also wanted to use the information gathered from these conversations to form an assessment of what best practice looks like.

NEXT

M&S
EST. 1884



boohoo.com

PRIMARK³



Key findings from our engagements:

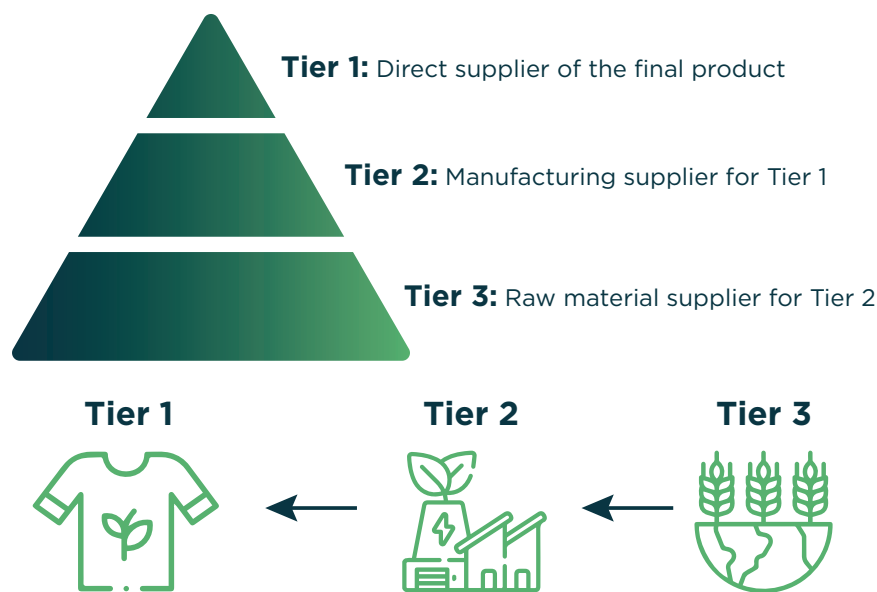
- **Transparency is best practice:** the best performing companies are often the most transparent and we are pleased to say that six out of the seven companies within the engagement reported full lists of suppliers including geographic locations, addresses and (in most cases) employee information on topics such as the workforce gender balance. This is the first step to initiating a culture of supply chain transparency. Based on our analysis, JD Sports was the only company not to publicly disclose this information; we have followed up with the company noting the practices of its peers.
- **Implementing a global living wage is still a challenge:** even companies with a strong history of action on labour standards admitted that implementing living wages across supply chains was a challenge. All companies adhere to national minimum wage provision, with most admitting that this does not always align with a de facto living wage. Some companies such as Adidas, Primark and M&S have been working with the Global Living Wage coalition to help benchmark national living wages. Some of these companies admitted to failed efforts to implement living wages at suppliers, highlighting that any meaningful impact on the provision of living wages, will need an industry wide solution. Benchmarking efforts are the first step.
- **Traditional ‘fast fashion’ firms are improving their performance:** whether a ‘two-pound t-shirt’ can ever be truly sustainable is perhaps a question for a different day but the more classic ‘fast fashion’ retailers are making significant efforts to improve transparency and standards across supply chains. For companies like Boohoo, this is in reaction to previous labour standard scandals. Primark has had a focus on labour standards for some time. Initiatives like the ‘Sustainable Cotton Programme’, a regenerative farming project working with female cotton farmers in India, is an example of best practice and provides over 50% of the cotton currently used in Primark products.
- **When it comes to auditing, a local presence is key:** auditing is the lifeblood of any supply chain monitoring system. It is central to upholding high labour standards across a large and globally dispersed supply chain. The highest performing companies we engaged with had salaried employees in many of the countries in which they had suppliers. Typically, primary suppliers are audited once a year and more often if issues are identified. Based on our analysis of best practice, most audits should be unannounced, and the company should play a key role in designing the specifications of audits in order to ensure that its standards are upheld whether in-house or third-party auditors

³ Primark is wholly owned by Associated British Foods.

⁴ Nike did not respond to our request to engage.

are employed. While admittedly rare amongst our engagement targets, some companies will ask suppliers to pay for audits. This is not best practice and inevitably creates mis-aligned incentives.

- **Internal or external auditors? We prefer the former:** within the group we engaged with we saw examples of both. Around half of the cohort used a mixture of third-party auditors and their own internal audit function, particularly using the former in the absence of a local presence. There does not appear to be consensus in the industry on whether external or internal auditors are more effective. Some companies believe the use of third-party auditors allows them to maintain a better relationship with suppliers and work as a partner to help improve on the audit's findings. Others, including Primark, primarily use their local employees to conduct site visits at suppliers. Alongside Harvard University, Associated British Foods (Primark's parent company) conducted research into this debate, analysing all the audits ever conducted at the company and the results found that in-house teams discover more issues, perhaps as a result of clearer auditing frameworks being applied versus third party auditors who are conducting audits for multiple entities with different expectations. The company has not found using in-house auditors detrimental to building strong supplier relationships. Whilst recognising the above research does not necessarily end the debate, we see the merits of using an internal audit function.
- **Transparency fades further down the chain:** understandably we saw most companies focus auditing efforts on primary suppliers (i.e. Tier 1, direct manufacturers). Some companies like Adidas require Tier 1 suppliers to assess their suppliers (Tier 2) according to specific Adidas standards. The consistency of standards this allows is helpful in mitigating labour standards risk across complex supply chains. That said, this extension of standards beyond primary suppliers was not universal. Monitoring the origins of raw materials is notoriously difficult and often relies on written commitment from suppliers. Some companies, including M&S and Primark are investing in auditing technologies such as material DNA testing. This allows them to trace the geographic region in which input materials were produced.



Based on a diagram produced by Certainty Software.

- **Most have struggled to integrate a truly global grievance mechanism:** many of the companies engaged had country specific grievance mechanisms (usually in the form of a hotline or app). The more sophisticated processes directed grievances to local staff or partner NGOs. Adidas utilises an anonymised app available to all workers across all tiers of the supply chain to register and detail grievances. Most grievances are anonymised, and Adidas reported a 99% close rate for all grievances in 2022. Centralised systems like this are rare, even those with processes in place tend to be fragmented and not available in all supplier markets - just the most material (typically where the largest suppliers are located). All companies face challenges in implementing a global system, with only one company suggesting it had a truly global mechanism. Supplier partners usually manufacture garments for multiple companies and therefore there are different expectations and multiple grievance mechanisms in place. Operating different systems and grievance mechanisms for different companies within the same workplace may well lead to the underutilisation. Different cultural norms and local languages have also added to the complexity in creating global systems across suppliers.

- **Long term partnerships with suppliers can support better standards:** we were encouraged to see many companies had established long-term partnerships with primary suppliers. Many of the engaged entities had been working with most of their primary suppliers for over ten years. Where they have this commitment, they can assist investment in standards and innovations. Long term partnerships are less common at traditional ‘fast-fashion’ retailers who are often placing smaller orders at a greater number of suppliers – further highlighting the challenges the model faces regarding supply chain transparency and implementing long-term standards.

Summary

Monitoring and auditing of labour standards across apparel supply chains is a relatively long-standing practice and for the majority of our investee companies, this is an established process with dedicated resources. For all companies engaged the governance of these issues sits either with the audit and risk committee or at the main board level. In recognition of the significant reputational damage caused by failures in this area, most dedicated supply chain monitoring teams reported directly into the CEO. Good practice was defined by a local presence in the country of manufacture and often partnerships with local NGOs. We recognise the merits of in-house auditing approaches (in terms of standards and flexibility), but whether internal or third-party auditors are used these should be regular, commissioned by the companies, mostly unannounced and should not be boilerplate. Investee companies have opportunities to reflect high standards and values within these assessments.

‘Fast fashion’ production models face inherent challenges from the smaller, higher paced order flow, which can often lead to shorter supplier relationships (and exposure to a more fragmented supplier workforce). That said, companies like Boohoo and Primark have put effort and resources into the monitoring and management of labour standards, particularly in the wake of recent scandals in the case of Boohoo. Companies like Primark compare relatively well to more conventional apparel manufacturers, in terms of local presence and innovative labour related initiatives. Overall, most companies met expectations on labour standard governance and auditing processes. We would welcome innovation in more comprehensive grievance mechanisms and greater industry collaboration on better benchmarking of living wages. It is disappointing that some entities do not meet basic transparency measures by publishing lists of manufacturing facilities publicly. Any perceived gaps in approach were communicated to the company.

Our main aim from these conversations was to benchmark these companies and establish what labour standards risk management looks like. This is an important platform for future discussions on supply chain stewardship and we will continue monitor company progress against best practice expectations.



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