

# Weaving accountability into clothing supply chains

The tragic loss of life in a string of accidents in Bangladesh's clothing factories has focused the world's attention on supply chain issues in the textile industry. Analyst Elsa Ben Hamou Dassonville sheds light on how RobecoSAM evaluates clothing companies' approach to managing their increasingly complex supply chains.

Faced with ever increasing scrutiny from multiple stakeholders – ranging from customers, NGOs and the media, to investors and legislators – the global clothing industry is under growing pressure to improve employee safety and building standards, both of which are important components of a sustainable supply chain management

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strategy. This is particularly true in Bangladesh, where local health & safety regulations have been relatively lax compared to other regions. April's Rana Plaza tragedy sparked a public outcry against multinational garment manufacturers operating in the country and has served as a wake up call for companies, underscoring the importance of managing their supply chains to mitigate reputational risks.

But supply chain management risks are not limited only to reputational risks, nor are they relevant only to the textile sector. As companies across a range of different industries continue to outsource some of their key capabilities to suppliers around the globe, their suppliers' risks become embedded into their own operations. Mismanagement of the supply chain can lead to business disruptions, resulting in a backlog of inventories, reducing efficiencies and ultimately hurting financial performance. For instance, product recalls related to poor production quality can cause companies to incur significant direct costs.

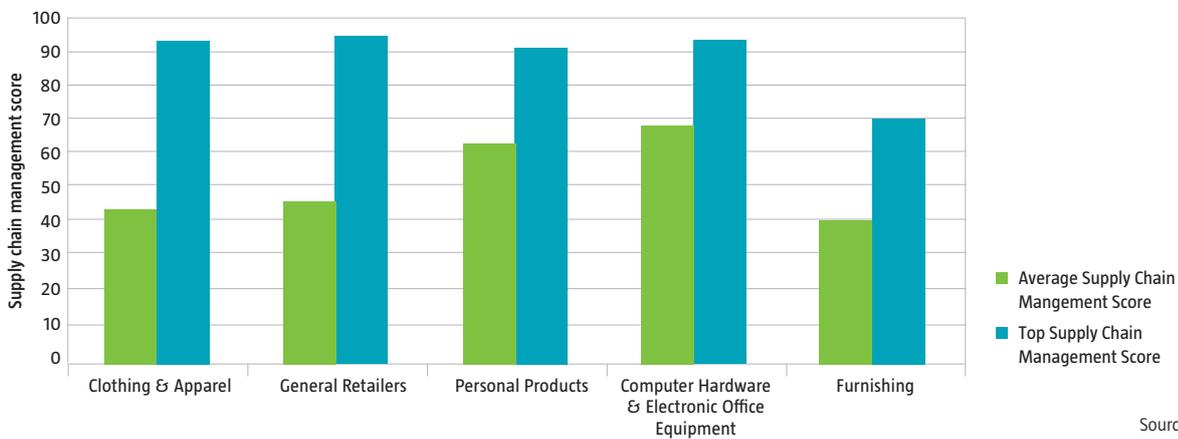
Further, companies that are heavily dependent on manufacturing operations located in other countries must recognize that they have a significant impact on local communities in which their production sites or suppliers are located. This is particularly true given the rise of social media and the constant, real-time flow of information. Any reports of incidents at production sites can be instantly disseminated around the world, further exposing companies to reputational risks and disrupting local operations. Companies that lack an effective stakeholder engagement process that actively involves local communities, local regulators and the media run the risk of jeopardizing their social license to operate in those countries.

Similarly, investors who hold shares in these companies are also exposed to the potential financial and reputational risks arising from the companies' poor management of their supply chains. Therefore, investors also have an important stake in encouraging companies to improve the transparency of their supply chains.

## **A comprehensive framework for evaluating companies' supply chains**

As part of our annual Corporate Sustainability Assessment (CSA), we aim to gain a better understanding of companies' supply chain management risks, and what companies across different industries are doing to manage them. Our framework looks at seven key factors focusing on how companies identify and manage supply chain risks, how they integrate sustainability into their overall supply chain strategies, and how their supply chain management strategies are linked to financial materiality and ultimately, their business performance.

### Supply Chain Management performance by industry



Source: RobecoSAM

We begin by asking companies if they have conducted a comprehensive analysis of their supply chain spend and whether they systematically identify critical suppliers. Once the companies have identified critical and high risk suppliers, we seek to determine whether they have completed an assessment of the sustainability risks embedded in their supply chain and if those risks can be identified as either economic, environmental or social risks. Next, we examine how companies manage the supply chain risks they have identified. We look beyond a traditional approach to supply chain management – which focuses on establishing standards for suppliers and audits to ensure compliance with those standards – and further determine whether companies are implementing more proactive approaches to managing supply chain risks, either by participating in collaborative industry initiatives, or providing training (capacity building) and incentives for suppliers.

A cross-industry analysis of companies' responses to the CSA suggests that the global clothing sector already has a basic understanding of its supply chain risk exposures, and is even ahead of some industries, such as Furnishing. Yet, it still has a long way to go towards developing a better supply chain management framework. Out of a possible maximum score of 100, companies in the Clothing & Apparel sector received an average supply chain management score of 44, with the top company scoring 92. This is comparable to the General Retailers sector, which had an average score of 45 and a top score of 94. Moving on to other sectors, the Personal Product and the Computer Hardware & Electronic Office Equipment industries earned higher average scores of 63 and 67, respectively.

These slightly higher scores can be partly attributed to recent investor and media scrutiny that pushed companies in the Computer Hardware & Electronic sector to launch a series of sector-wide initiatives led by NGOs, investors and legislators.

An important component of our assessment process is the Media & Stakeholder Analysis (MSA), which serves as an additional check on companies' supply chain management policies. We continuously monitor media and other publicly available information from consumer organizations, NGOs or international organizations to determine whether companies have been involved in environmental, economic or social crisis situations that may have a damaging effect

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on their reputation and core business. Incidents that are often related to supply chain management include human rights abuses, labor disputes, catastrophic accidents and workplace safety. If a company or its suppliers have been involved in such an incident, we evaluate the quality of the company's response to minimize the negative impact of the crisis. We look for evidence that the company has taken steps towards improving its management framework by strengthening its codes of conduct or audit processes in order to prevent the recurrence of similar events.

### Collective action: a step in the right direction

Collaborative multi-stakeholder initiatives can be an effective means of accelerating change. Governments, investors, labor unions and NGOs can work together to align objectives and define minimum requirements in line with internationally recognized standards, while companies within the same industry can join forces to exert leverage over their mutual suppliers.

In response to the Rana Plaza disaster, companies have begun to sign the Bangladesh Fire and Building Safety Agreement, an initiative founded by international labor unions IndustriALL, UNI Global Union and various NGOs, which builds on Bangladesh's existing National Action Plan on Fire Safety and mandates the independent inspection and renovation of all factories deemed unsafe.

Such an initiative is a welcome step towards improving poor working conditions, but clearly more needs to be done to ensure similar tragedies are not repeated in Bangladesh or elsewhere. Investors and other stakeholders should continue to insist that beyond signing agreements, companies must set clear targets for their suppliers and subcontractors and commit to robust audit oversight throughout their supply chains. In order to enforce compliance with minimum standards and hold companies accountable, investors must also continue to demand transparency, including public disclosure on all of their suppliers and their progress on meeting targets. RobecoSAM remains committed to continuing to encourage companies to improve their awareness, management and disclosures on their supply chain risks by continuously refining its framework for assessing companies' supply chain management policies.



**Elsa Ben Hamou Dassonville**

Analyst  
SI Research