

Outsourcing trap. Big brands want all the benefits of having highly efficient manufacturing partners in Asia, but at the first sign of poor publicity, they are ready to walk away, whether the headlines are fair or not.

CREDITS: NIKE



Brands want cheap shoes but without social strife

Occasionally, you still hear commentators claim that there is no such thing as bad publicity, but consumer brands know it's not true, or at least not if the bad publicity is connected to social responsibility. News of any failure, or perceived failure, to look after the environment or workers properly is likely to spread quickly. Athletic footwear brands, many of whom make no product themselves, have found out the hard way that this also applies to suppliers.

When negative reaction began to build up in April to the response of outsource footwear manufacturer Yue Yuen to industrial action by the workforce at one of its factories in China, it would probably have been easier to count the major athletic footwear brands that were unaffected than those who must have known from the outset that their names would soon be mentioned in despatches. And it took no time at all for some of the biggest to begin talk of moving business to other partners.

The background here is that workers at Yue Yuen's factory in Gaobu, near Dongguan in southern China, began industrial action on April 14. The facility employs 45,000 people and

A strike by workers at one of Yue Yuen's factories in China in April 2014 brought widespread condemnation for the outsource footwear manufacturer, including threats from big brands that they would take their business elsewhere. Yue Yuen felt it had done nothing wrong except manage its business as efficiently as possible while sticking to all the rules, which is the reason the brands source from it in the first place.

makes shoes for Nike, adidas, Reebok, New Balance, Puma, Under Armour, Converse, Merrell, Asics and around 60 other brands. This factory alone produced more than 30 million pairs of shoes in 2013.

Above the minimum

As is the case with other large manufacturing plants in this part of China, many of the workers come from other provinces and live in factory dormitories, returning home only for major holidays such as Lunar New Year. Many of them send money back to their families, or spend a few years working in Guangdong to save up enough capital to start small businesses such as shops back in their home villages.

In Guangdong, which is the Chinese province with the highest overall gross domestic product, the authorities are strict about minimum wage levels. In May 2013, for example, official minimum wages went up by almost 20% compared to the previous year, with levels in and around the provincial capital, Guangzhou, rising to around \$250 per month. Many businesses have complained that it's impossible to hire people in parts of the province at the minimum wage. Therefore, the monthly wages companies often find themselves paying have to be higher than the minimum. For this reason, in addition to agreed wage rates, Yue Yuen pays workers at Gaobu a series of benefit payments and it was a demand for an increase in these benefit payment that led to strike action in mid-April.

On April 17 and April 24, Yue Yuen issued statements to the Hong Kong stock exchange saying it had agreed to increase the benefit payments for "certain employees" (based on seniority) from May 1 and that, by the time of the second statement, more than 80% of Gaobu employees had returned to work. It also said that, in addition to the higher benefit payments, it had agreed to pay workers there an additional living allowance of around \$35 each per month. It said the incident had cost it approximately \$27 million because of interruptions to production and air freight costs to meet delivery deadlines. As this issue of *World Footwear* goes to press, Yue Yuen has made no further official comment on Gaobu.

'Minimise the impact'

However, there has been plenty of comment elsewhere. On April 24, adidas gave a statement to business media outlet Bloomberg, saying: "We are currently reallocating some of the future orders, originally allocated to Yue Yuen Dongguan, to other suppliers." It explained that it wanted to "minimise the impact on our operations" of the strike. This is ironic because when, in 2012, German television company ARD asked adidas for access to two typical supplier factories in Southern China, the brand nominated a Yue Yuen facility near Dongguan (there are two: one in Gaobu and the other in Huangjiang). As part of this exercise, adidas took ARD to a hospital that Yue Yuen has built in the area to look after the medical needs of its workforce there. After filming was over, the sports brand said it knew none of its suppliers were perfect, but it believed it has a number of "very committed suppliers". We can assume it includes Yue Yuen among these, or it probably would have invited ARD to film somewhere else. In the end Yue Yuen hardly featured in the finished programme.

It took until May 1 for Nike chief executive, Mark Parker, to give his views on the Yue Yuen strike. Speaking in Boston that evening, he said: "We didn't move product out in this case, but we're staying close to it. We're always considering it."

Yue Yuen is part of the Pou Chen Group, which is Taiwanese-owned and was founded in the 1960s. It set up Yue Yuen to concentrate on outsource manufacturing of



The adidas Supernova running shoe, one of the products that Yue Yuen makes for the brand in southern China.

CREDITS: ADIDAS

athletic and casual footwear in 1988 and in the same year set up the first of its factories in China. It has been at the heart of the shift in the global footwear industry: sourcing shoes rather than producing them has become the key for big brands. Last year, Yue Yuen made 313.4 million pairs of shoes across its whole production network, which comprises five factories in China, one in Vietnam and one in Indonesia. At the end of 2012, it had 423,000 employees.

Brands helped build the model

Pou Chen's business built up in the second half of the twentieth century because big brands in North America in Europe moved away from manufacturing to concentrate on marketing, branding and design. In the last five years, adidas has grown its revenues from €10.4 billion in 2009 to €14.5 billion in 2013, an increase of 40%. Over the same timeframe, Nike's sales revenues have increased from \$19.1 billion in 2009 to \$25.3 billion in 2013, growth of more than 32%. They are proud of their management of supply networks and of the contribution this makes to growth, but it would be impossible for them to manage the supply chain as effectively as they do without long-term partners such as Yue Yuen. Yue Yuen has no monopoly, but it is one of only a limited number of manufacturers with the ability to produce the shoes the big brands need, delivering them on time, to specification and on budget. Yue Yuen and companies like it have that ability because they have spent years building up their own economies of scale and establishing strong relationships with the authorities in the countries in which they carry out their manufacturing operations.

Big brands know what is on offer from Yue Yuen and other producers of its size. It suits them to continue to run their supply chains the way they do. It is unfair of them to set up a dynamic that works extremely well for them and then walk away from it, or threaten to do so, at the first sign of a negative headline. 