Fair Trade Tool Kit

Are International Supply Chains increasing poverty?

April 2005 This paper looks at the impact of changes in the way international supply chains operate on workers and producers in developing countries. Relationships within supply chains can be organised be so that each part of the chain benefits in proportion to its contribution. In this way trade would be reducing poverty. This briefing paper charts the sometimes negative impacts of business practices within our increasingly global trading system and recommends some solutions.

How do supply chains affect people in poor countries?
A supply chain is the different stages that a product goes through, from its start as raw materials to its end as a finished product in the hands of the consumer. Producers and workers in developing countries are involved in the earlier stages of international supply chains, often producing the raw material or doing basic assembly work of products that are then further processed or packaged for consumption in the developed world. Trade between countries has existed for centuries, however recent advances in technology and communications now mean that decisions made in one country are almost instantly felt in another. Fair trade demonstrates that being part of a fair international supply chain can be a very positive experience for millions of producers and workers in developing countries. But the way many mainstream supply chains operate can mean that the producer receives very few of the benefits from increased international trade - in fact some of the trading and buying practices in international supply chains actually put workers at risk.

Shifting power
International trade has the potential to alleviate poverty when each link in the supply chain benefits appropriately. However the last few years have seen a fundamental shift in who gains from international trade. In the current trend of globalisation companies pursue flexibility, lowest raw material prices and cheap labour. Increasingly benefits to companies at the top of global supply chains are reaped at the expense of those at the bottom.

Just in time delivery

Every time you buy a product in a supermarket the scanner and computerised till records your purchase. This enables the supermarket to send their supplier last minute and very precise orders, for example they will send an E-mail to Kenya at midday with the order for exactly what produce they need on that evening's flight to be on the shelves the next day. This reduces waste and increases profits for the company. But because orders can go up and down dramatically this means that sometimes suppliers have to meet large orders at very short notice. In order to cope with this lack of predictability and reach these targets, suppliers may have to demand that workers put in significant overtime or may put them on flexible contracts. This leads to insecure employment and vulnerable workers.[1]

The shift has been possible due to the weakening position of workers and small producers at the bottom of the chain in relation to increasingly powerful companies at the top. Protection for workers and small producers has reduced whilst the rights of companies have increased, resulting in a large and growing number of disparate suppliers competing to sell to fewer, ever more powerful buyers. Increasingly, a few big brands control access to consumers, so suppliers are limited to trading with a small number of buyers if they are going to sell their products at all. This significant polarisation of power in supply chains is due to trade liberalisation, the reduction of developing country governments' policy space and the significant number of mergers and acquisitions. Trade liberalisation has led to many developing countries reducing protection for workers in an effort to attract foreign business. Due to conditions attached to aid payments, developing countries have drastically reduced marketing support and agricultural advice for small producers.

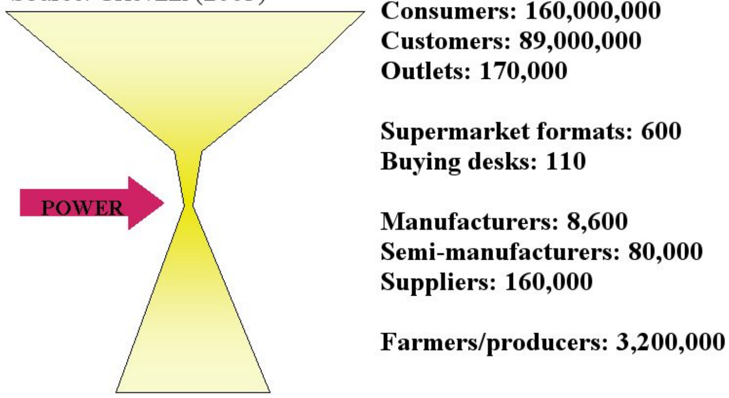
[1] Felicity Lawrence, The Guardian 17/5/03

Traidcraft
Fighting poverty through trade

The rise of corporate power
Recent mergers and acquisitions have created enormously powerful companies, some are economically larger than many countries and as result wield significant influence.

75 % of all food bought in UK is sold through just four companies (Tesco, ASDA, Sainsbury & Morrison)[2]. This concentration of power is replicated in many countries around the world, particularly as existing global retail giants expand their empires, reducing choice for consumers and suppliers.

The Supply Chain 'Bottleneck' in Europe
Source: Grievink (2003)



Unfair demands
The enormous power of the retailers enables them to use a number of techniques to pass the risks of doing business on to their suppliers (see box below). The suppliers will then use their relative power to pass these risks down to their own workers or smaller suppliers. The net result of this buck-passing is that the people at the very end of the chain - usually poor workers and producers in developing countries – bear the brunt of the risk. The supermarkets' overarching power results in 'bully boy' tactics. These were recognised by the UK's Competition Commission when they found that there was a climate of 'apprehension' among suppliers towards supermarkets. The Competition Commission found a clear link between retailers' market concentration and the prices they paid. The biggest supermarket, Tesco, consistently pays suppliers below industry averages, a clear concern when payments to suppliers do not even cover the costs of production.

How supermarkets shift risk

The following is a list of techniques that buyers use, which result in the supplier bearing the risk of business transactions. Some may appear extreme, but they are all commonly used by British retailers.

- Lowering price at the last moment
- Only agreeing a price once the product has been delivered
- Delaying payment
- Shortening lead times (the time between placing the order and when product must be delivered)
- Refusing to sign contracts
- Changing the volumes required at short notice
- Product promotions such as 2 for 1 offers, are usually funded by suppliers. (Often promotions are initiated by supermarkets to achieve their own sales targets. Suppliers keen to please their buyers reluctantly agree to fund such promotions even though they may make a loss.)

Concentration of power
As companies become richer and more powerful, so it becomes easier for them to maintain this position through the way they organise themselves and through their growing political influence. Changes in trade rules have made it easier for foreign companies to buy local companies in developing countries. This means that the price of a product is not governed by the market but instead by internal company decisions. This means they can keep the prices of their inputs low. Furthermore where two or three companies control a market the opportunities for cartel price fixing are high. This is a particular concern in relation to pricing of agricultural inputs. Rich companies spend significant resources on lobbying and can often have considerable influence over government decisions and negotiating positions. The three main objectives of American agribusiness' public sector lobbying to protect their own position include:

a) Competition policy which does not threaten levels of corporate concentration
b) Protection of private property, investment and equal treatment of domestic and foreign firms
c) Policies which encourage oversupply of raw materials. Lobbying has stopped governments developing supply management strategies which would help suppliers realise higher prices.[3] (see Traidcraft's commodity crisis briefing paper)

[2] 'Till Roll Share of Trade' as calculated by independent retail analysts Taylor Nelson Sofres Superpanel
[3] BBC World Service 'Inside the global giants' http://www.bbc.co.uk/worldservice/specials/151_globalgiants/page3.shtml
[4 & 5] OXFAM, January 2004, 'Trading away our rights – Women working in global supply chains' p 74
[6] Ventkateswarlu, D (2004a) 'Child labour in Hybrid cotton seed production in Andhra Pradesh: recent developments', Utrecht: India Committee of the Netherlands

A high price to pay
The result of increased corporate power is that risk and cost are passed down the supply chain to those most vulnerable, such as developing country farmers, and women or migrant or temporary workers. In reality this means:

- Employment becomes more precarious, with fewer workers on permanent contracts as suppliers have no long term contracts to supply.
- Instead of being entitled to benefits, increasingly workers are being fired for being sick or pregnant
- Women workers desperate to keep their jobs are vulnerable to being intimidated by managers and owners, this sometimes manifests itself as sexual exploitation.
- Dangerous working conditions as corners are cut to reduce costs and save time to meet low value orders placed with short lead times
- Family consequences as women work longer hours, frequently in hazardous health conditions, to provide for their families.

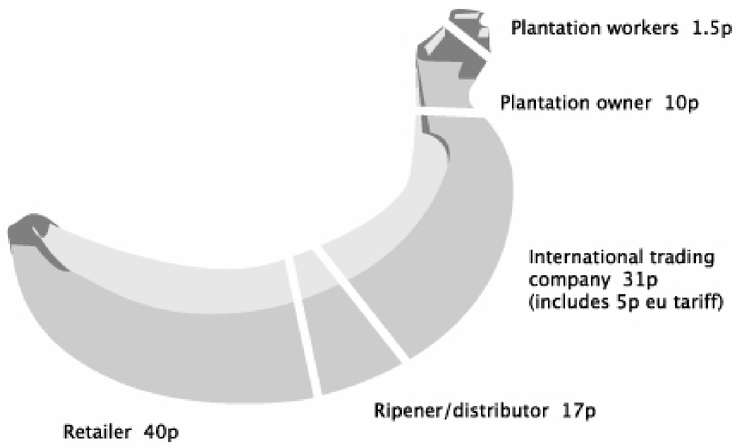
> ' '*We work in the rain … and people get sick. We work in the winter in the frost – but we must because the day's totals must be made*."[3]
>
> 'W*e have asked for protective clothing, but... they say it is too expensive for the farm and we should pay for the clothes*'[5]
>
> "*With the prices we get from companies we cannot afford to employ adult labour*." [6]

This situation is further exacerbated when employers select vulnerable workers desperate for an income because they are less likely to join trade unions, which would help them resist poor working conditions.

Squeezing prices

Buyers can also use their market power to pay low prices - playing one farm or factory off against the other. This can result in poverty wages for factory workers and prices below the cost of production for farmers. The issue of low prices is particularly pronounced in key agricultural commodities such as coffee, tea, cocoa, cotton, and bananas.

The 'Banana Split' – how much of £1.00 retail value of loose Ecuadorian bananas stays with each chain actor to cover costs and margin



The difference between the price of products leaving the farm and consumer prices is widening steadily. So whilst the world price for coffee has fallen by 70% in the last 20 years, the retail price of coffee has not fallen. A coffee farmer gets just 4% of the price of 1kg of processed beans and only 10% of the retail value of coffee is retained by the producing country.[7] 2.5 billion people worldwide are dependent on agriculture for their livelihoods. But despite food being a profitable sector, producers are finding it increasingly difficult to make ends meet.

Poverty wages for global corporations

US$0.07 is the sewing cost per item of Disney's childrens' clothes in a Dominican Republic factory. Yet if Disney's CEO, earning US$63,000 per hour, made the clothes the sewing cost per item would jump to $6,103!

[7] This situation is exacerbated by rich countries' trade taxes which discriminate against products where value has been added to products in the developing countries.

[Fig 2] Source – Banana Link

How far is Fair trade a solution?
Fair trade producers and suppliers subscribe to a robust set of fair trade rules and standards, regarding the economic, environmental and social aspects of trading. The Fair Trade movement has many years experience of putting these rules into practice, with proven experience of how supply chains can be made to work for poor producers. Fair trade aims to re-balance power between the producer and buyer, with rights and responsibilities on both sides. Fair trade buyers commit to paying a fair price and to maintaining long-term trading relationship with the suppliers. On their part, suppliers commit to paying a living wage and providing decent working conditions.

However, Fair Trade is an opt-in system. In addition to supporting proven opt-in initiatives, governments need to provide greater *regulation* to safeguard the weakest participants and level out the power imbalances in the supply chain. Fair trade provides a model for more equitable trade between businesses, and provides insights when designing regulation between supply chain actors.

The way forward: rebalancing the power in international supply chains

Traidcraft is promoting the following solutions to governments and companies:

By Government
1. Workers' rights need to be protected and enforced in every country in order to promote decent employment, gender equality and reduce poverty.
2. UK Competition rules need to be changed to consider the social and environmental impacts of market dominance by a handful of companies and these competition rules need to be enforced.
3. UK company law needs to include new directors duties of care to not violate human rights. This obligation could be demonstrated through company reports on their social, economic and environmental impacts.
4. UK government should allow people and communities to seek redress for harm caused by UK companies in UK courts if they are unable to access justice in the country of violation.

By Companies
1. Companies need to address the social impacts of their own purchasing practices. In particular, they need to develop longer term transparent trading relationships with their suppliers, pay sufficient to cover the costs of production and enable (rather than disable) the realisation of international human rights standards within their supply chains.
2. Companies and their suppliers worldwide need to provide decent jobs for both their male and female employees, including respect for workers' rights to join trade unions and bargain collectively.
3. Companies need to be transparent about public policy lobbying positions and lobbying activities undertaken.

To find out more about these issues please visit our website www.traidcraft.org/policy

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