



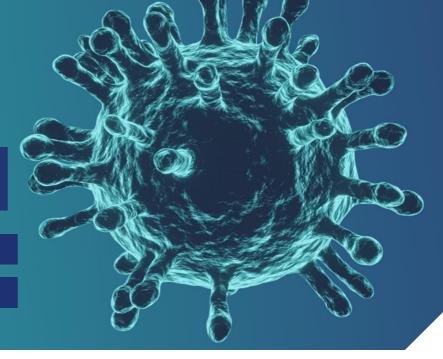
Building resilience during and after the COVID-19 pandemic



COVID-19 guide & action checklist



For garment factories & managers



# Reducing costs

For garment manufacturers navigating the COVID-19 pandemic, this guide helps factory managers reduce costs to ease financial liquidity and cashflow pressures on their factory operations.

### **Getting started**



Includes: Spreadsheet template for costs, action checklist

#### In this guide:

- Why managing costs is essential during the pandemic
- Types of costs in the garment sector
- 8 ways factories can reduce costs in a socially responsible manner



## 1. Why managing costs is essential during the pandemic

The COVID-19 outbreak has most likely put your factory in a challenging financial position, with orders being cancelled and fewer payments coming in. The financial pressures in your factory are going to be multifaceted. Settling invoices for your ordered materials such as fabric, trim or packaging by your supplier could prove challenging if not impossible. Factories, such as FOB factories, which are procuring the fabric themselves, are particularly exposed to this financial pressure.

Building resilience during and after the COVID-19 outbreak.



Paying your workers' salaries will also be difficult in times of low liquidity. A further challenge could be to pay your utility bills for water, electricity or gas. While you therefore may need to reduce costs to safeguard your business in the near future, the COVID-19 pandemic also provides an opportunity to make your operations more cost-efficient in the longer term.

The recommendations in this guide will help you to reduce costs in a socially responsible manner. In doing so, garment operators can ultimately:

- Focus on maintaining operations and minimize strain on the factory in the long-run
- ▶ Build resilience during and after the COVID-19 outbreak, and
- Increase their competitiveness over time.



#### 2. Breaking down costs in the garment sector

Before taking action, it's important to know what your costs are and how they can potentially impact your business and factory operation in a pandemic situation. Garment manufacturers face a wide range of costs that typically can be separated into three main categories:



**Materials cost:** Depending on the sourcing model, e.g. fee on board/full package (FOB) or cut-make-trim (CMT), factories may cover the costs for materials used in production.



**Labour costs:** Wages of workers involved in the production process, such as operators.



**Overhead costs:** These are costs needed to keep the factory running, but that are not directly linked to your factory's production, such as rent and utilities.



What
makes up
the bulk of
costs in
your
factory?

Factory costs can also be divided into fixed and variable costs:



**Fixed costs** do not change with fluctuations in your production volume. No matter how much your factory produces every month, your fixed costs will remain the same. Fixed costs include e.g. the rent of the factory building, property taxes, insurance, security, machinery and equipment costs, compliance costs, etc.



**Variable costs** are to the contrary directly linked to the decrease / increase in your factory's production. Variable costs include e.g., the wages of your workers, utilities, chemicals etc.

Costs also depend on the location of the factory, the factory itself and the sourcing model that it is operating under. For factories that purchase their own fabric, material costs typically make-up approximately two-thirds of total costs while labour and overhead costs account for one-sixth each, as shown below.

For garment manufacturers that operate under a CMT model and use materials provided by their customers, labour costs account for approximately 50 to 60 percent of the cost while overhead costs make up between 30 and 40 percent (as shown below). Accessories, such as thread, needles and zippers account for the remaining 10 percent.

# Cost breakdown of a typical FOB model factory





## 3. Getting ready for action

Now that you've reviewed the types of costs involved in your garment operation, the next section will provide some concrete steps on managing costs and doing so in a socially responsible manner.







# 8 ways factories can reduce costs in a socially responsible manner

01	Review your costs
UI	Develop a clear, detailed picture of spending

- Focus on the low-hanging fruits
  Identify costs you can easily and immediately reduce
- Cut back on the non-essentials
- Reduce material costs

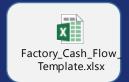
  Look for savings on materials and fabric
- Rationalize and reinvent your inventory
  Keep it at a minimum and look for alternatives to storage
- Seek ways to cut overhead costs
  Reduce monthly expenses and negotiate fixed costs such as rent
- Mitigate impact on workers
  Consider all alternatives to lay-offs and keep employees informed
- O8 Support each other
  Work together with other factories, associations and industry



## Putting the measures in action: Factory checklist

#### 1. Review your costs

Start by taking some time to go through your financial records. You cannot reduce costs if you don't know what they are. **Useful tip:** Use the attached cost worksheet template (at right) to help you lay out your costs.



Action	Ease of implementation	Timeline	Check
<ul> <li>For reviewing your fixed costs, go through your financial records with the following questions in mind:</li> <li>On what do we regularly spend every month that is independent of our production?</li> <li>How much do we spend on each of these items monthly?</li> </ul>	<b>&gt;</b> >>	Short-term	
<ul> <li>For reviewing your variable costs, go through your financial records with the following questions in mind:</li> <li>Which costs vary with our output? As stated above, this could be wages of your workers, utilities or chemicals, etc.</li> <li>Next, you need to know how much you spend for each product.</li> </ul>	<b>~~~</b>	>>>> Short-term	

#### 2. Focus on the low-hanging fruits

As a second step, we will focus on the quick-wins your factory can achieve. For this, try to identify those cost items that you can easily cut or reduce immediately.

	Action	Ease of implementation	Timeline	Check
n CI	n your financial statement or completed template, identify costs which are not essential for your factory to maintain operations but linked to non-ritical activities. These costs may include costs for equipment, office upplies etc.	<b>&gt;&gt;</b>	>>> Short-term	
Fi	ind a way to reduce or cut the costs as soon as possible.	<b>&gt;</b>	>>>> Short-term	

#### 3. Eliminate what does not add value

If necessary, you should also look at eliminating activities, which have in the past not been profitable.

Action	Ease of implementation	Timeline	Check
Review your product lines and activities in the factory for their profitability.	<b>///</b>	>>>> Short-term	
Take a look at your product lines (tops, bottoms, jackets, t-shirt, etc.) and calculate the financial returns per item for each order.  Eliminate the product lines and activities, which have not been as profitable as the others in the last six months and do not hesitate to do so, as it will become harder and harder to recover from this crisis the longer you wait to respond.	<b>~~</b>	>>> >>> Mid-term	

#### 4. Reduce material costs

If your factory purchases its own fabric, it's likely this comprises a substantial part of your total monthly costs. Reducing material costs should therefore be a priority for you as you continue or resume factory operations.

Action	Ease of implementation	Timeline	Check
Never be afraid to ask for a discount. Always negotiate to get the best deal possible.	<b>~</b> ~~	>>> Short-term	
Ask several suppliers (for example up to five) to send you quotations when sourcing materials.	<b>~~</b>	>>> Short-term	
Look at techniques to reduce material waste in your production (e.g. look at your cutting room operations - systematic laying, increased marker efficiency %, increased fabric utilization %, etc.).	<b>~</b>	>>> Short-term	
Consider if you can use alternative (cheaper) fabric without comprising product quality.	<b>~</b> ~	>>> >>> Mid-term	
Build long-term relationships with your material and trim suppliers, which are built on understanding. A good relationship will create a winwin situation for you and the suppliers, in which you will be able to source materials for a lower price and the suppliers have a long term customer.	<b>~</b>	>>> >>>> >>>> Long-term	

#### 5. Rationalize and reinvent your inventory

In the time of COVID-19, many garment factories have been left with cancelled or suspended orders. This has led to a lot of materials which cannot be used. While purchasing materials is costly in itself, additional costs for e.g. staff, insurance, stocktaking, electricity and maintenance will result in costs growing over time.

Action	Ease of implementation	Timeline	Check
Keep your storage organized. This will make your operations more efficient and will help reduce unnecessary costs by avoiding damage to expensive materials.	<b>///</b>	>>> Short-term	
If you have leftover material from cancelled orders, discuss with your buyers how you could use these materials and not let it go to waste.  Contractual arrangements can vary in this regard, but you should push your buyers to allow you to maximize benefits (ship more than the allowed 3% or 5%) in order to stay viable in these exceptional times.	<b>~~</b>	>>> Short-term	
If you cannot re-use the leftover material, consider recycling it. There are opportunities today to recycle materials through various platforms. Talk to your garment association about existing opportunities in your country (produce items for the local market but first check on regulations).	<b>~</b> ~	>>> >>> Mid-term	
If you cannot re-use or recycle your fabric, try to dispose it in an environmentally friendly manner, as it will take up space in your storage and cost you a lot of money over time.	<b>~</b> ~	>>> >>> Mid-term	
Start applying models that will help you carry an optimal level of inventory, such as JIT (Just-In-Time) and/or EOQ (Economic Order Quantity).	<b>~</b>	>>> >>> >>> >>> >>> >>> >>> >>> \tag{Pink}	

#### 6. Seek ways to cut overheads

Regardless of whether your operations are constrained or even suspended, you will still have to pay your fixed costs. Take your time to re-negotiate your fixed costs. Look for both short-term solutions, such as temporarily lowering or deferring your rent, as well as more long-term solutions.

Action	Ease of implementation	Timeline	Check
Cut your utility costs by using less electricity, water and gas (e.g. use the machines with direct drive motors, use push or foot water taps as appropriate, turn off the lights in empty rooms, install translucent roofing sheets for natural lighting, etc.).	<b>&gt;&gt;</b>	>>> Short-term	
Contact your landlord to ask to renegotiate or temporarily freeze the rent.	<b>&gt;</b>	>>>> Short-term	
Call your insurance provider to check if they have a better offer for you.	<b>&gt;</b>	>>> Short-term	
Ask your garment association for guidance related to government taxes and other government programmes / subsidies, which were introduced during the outbreak.	<b>&gt;&gt;</b>	>>>> Short-term to mid-term	
Talk to your bank to see if they can offer lower rates for their financial services such as letters of credit or loans.	<b>&gt;</b>	>>> >>> Mid-term	

#### 7. Mitigate impact on workers

The COVID-19 outbreak might result in you having to reduce your workforce. If this is the case, make sure that you do so in a socially responsible manner. Layoffs will have potentially devastating consequences for your workers, and you should consider how you can mitigate such to the extent possible. For more guidance on how to deal responsibly with retrenchments during the COVID-19 outbreak, click have.

Action	Ease of implementation	Timeline	Check
Seek advice from your garment association on what possibilities you have, before proceeding with any layoffs or scaling down operations.	<b>///</b>	>>> Short-term	
In all cases, businesses must adhere to national legislation and regulations as well as international labour standards.	<b>///</b>	>>> Short-term	
Consult with workers before taking any measures related to layoffs.	<b>///</b>	>>> Short-term	
Provide relevant information to workers' representatives and engage in a dialogue regarding measures to avoid termination of contracts as well as mitigation of effects.	<b>///</b>	>>> Short-term	
Ensure your factory has information about government measures, social protection and support for workers and communicate this information to workers.	<b>///</b>	>>> Short-term	

#### 8. Support each other

Working together with other factories and your associations can help you to lower your costs and to project a common industry position to brands, the government and other stakeholders of the industry.

The COVID-19 pandemic will take a hard toll on your factory as well as that of your peer factories. This is a time to act in solidarity, and for the sector to overcome this crisis by working together with other factories.

Action	Ease of implementation	Timeline	Check
Communicate with your peer factories to understand their situation and to explore how you can work together	<b>///</b>	>>> Short-term	
Source materials jointly to be able to purchase at a lower price.	<b>~</b> ~	>>>> Short-term	
Purchase materials and other inputs from each other if possible, to mitigate the impact of cancelled orders leaving factories with leftover fabric.	<b>~</b> ~	>>>> Short-term	
Explore opportunities to barter with each other to acquire needed equipment.	<b>~</b> ~	>>> >>> Mid-term	
Engage together in the work of your garment association to strengthen the competitiveness and resiliency of your country's garment sector.	<b>///</b>	>>> >>> Mid-term	



This guide was developed by the ILO Enterprises department for the **Decent Work in the Garment Sector Supply Chains in Asia** project, funded by the Government of Sweden.





For more guides and resources to help you navigate the global COVID-19 pandemic, visit:

▶ <u>ilo.org/covid19</u>

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