Research Briefing:

Apparel regional value chains and COVID-19: insights from Eswatini

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The outbreak of the COVID-19 pandemic is having major implications for apparel global value chains (GVCs). State-driven measures to enforce social distancing have led to the downsizing and even closure of supplying firms, especially in developing countries where government support for manufacturers is limited (Teodoro and Rodriguez, 2020). This dynamic has been worsened by the actions of international brands and retailers which, in a number of cases, have delayed or cancelled orders, and have refused to pay for ongoing production and shipments (Anner, 2020).

Whilst increasing attention is paid to the implications of COVID-19 for firms in the global South supplying retailers in Europe and the US (Devnath, 2020; Kelly, 2020; Mirdha, 2020), we know less about the impact of COVID-19 on regional production networks connecting buyers and suppliers in developing countries. This lacuna is particularly relevant against a backdrop where South-South trade overtook North-South trade in the last decade, with intra-regional commerce accounting for a large share of the global South's improved trade performance (Horner and Nadvi, 2018; McKinsey & Co., 2019; Mohanty et al., 2019). As regional value chains (RVCs) increasingly become an important feature of 21st century globalisation (The Economist, 2020; Pasquali et al. 2020), this study aims at advancing our understanding of RVCs and their governance in the global South. We do so by focusing on the country that, since 2014, has grown to become the largest African manufacturer and exporter of apparel to the region: Eswatini (Figure 1).

This research briefing is part of the research project: 'Shifting South: decent work in regional value chains and South-South trade', a collaboration between the University of Manchester, the University of Cape Town, the University of Nairobi, and the Ethical Trading Initiative (ETI). In cooperation with the Eswatini Revenue Authority (SRA). A full working paper is forthcoming.

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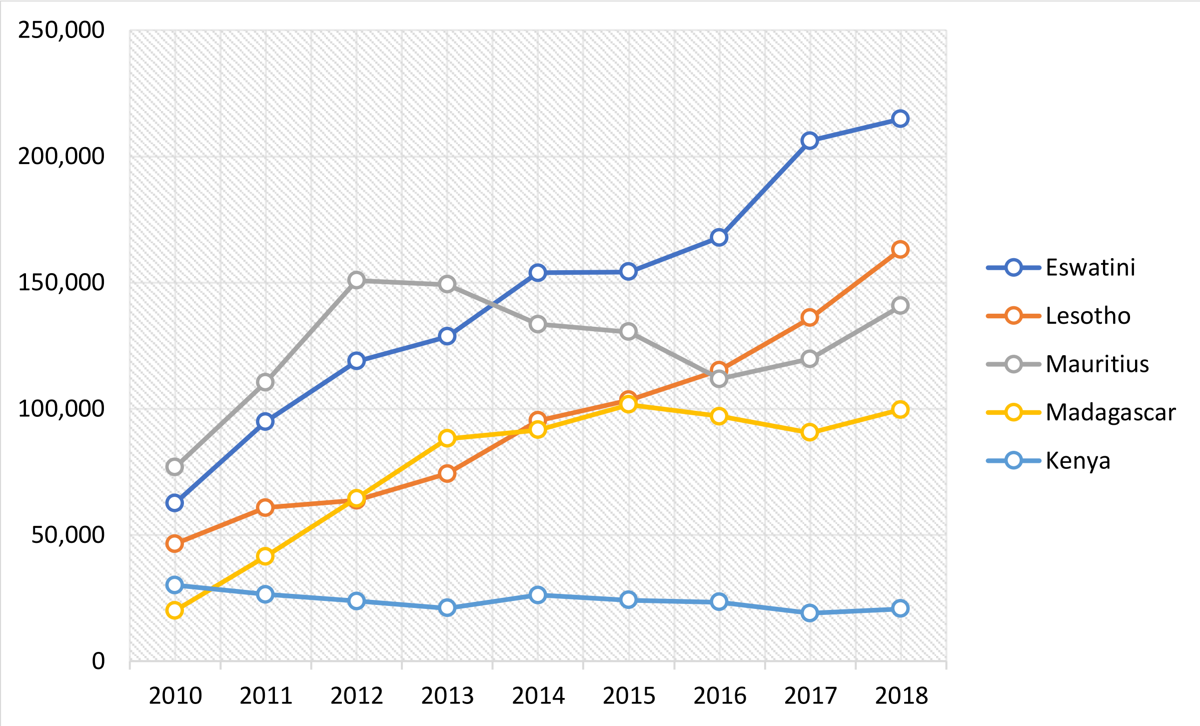
Figure 1: Intra-Africa regional exports by the main exporting countries (trend) – thousand USD.



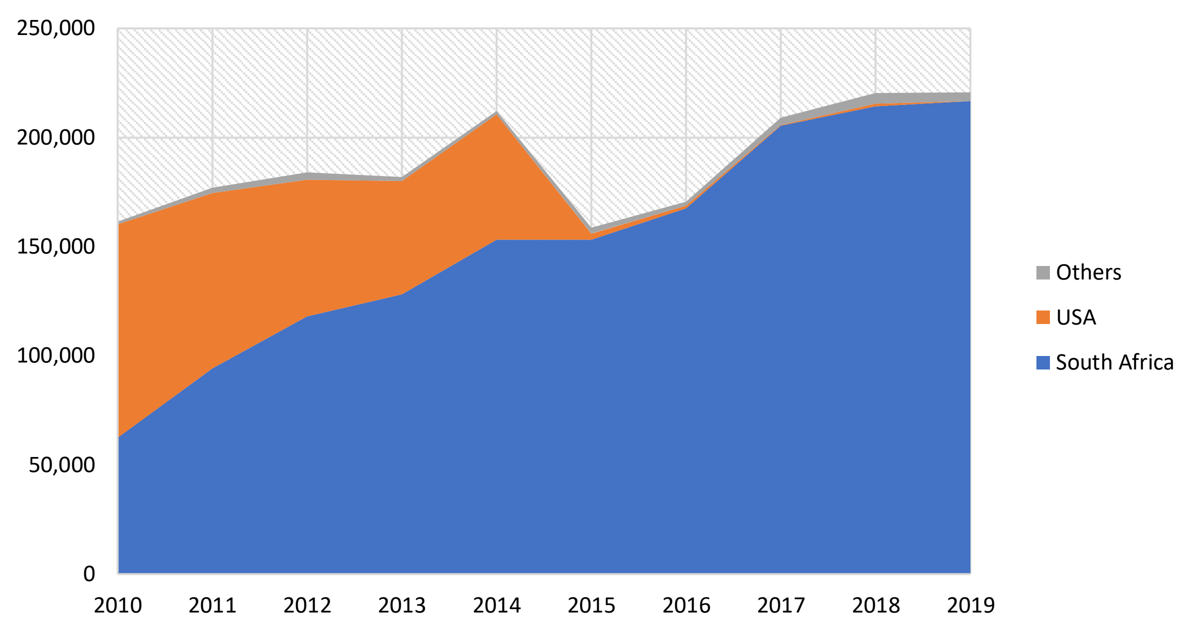
Source: authors' elaboration based on UN-COMTRADE.

Eswatini's apparel industry

The apparel industry emerged in Eswatini during the 90's and early 2000s as a result of quota-hopping foreign direct investment arising from the Multi-Fibre Arrangement (MFA), and subsequently benefitting from duty-free access to the United States (US) under the African Growth and Opportunity Act (AGOA) (Staritz 2011). However, starting from 2005 and increasingly over the last decade, Eswatini's apparel industry strengthened its linkages to RVCs via South African investments attracted by lower labour costs and SACU preferential trade regulations (Morris et al., 2011; 2016). Between 2011 and 2015 (which period included the suspension of Eswatini from AGOA in 2015), all overseas exporters successfully shifted to supply large South African retailers, including major brands such as Mr Price, the Foschini Group, Pepkor, Edcon, Woolworths, and Truworths.[1] Despite Eswatini regaining its AGOA status in 2018, exports to the US have not resumed and South Africa remains the main market for 95% of the country's output (Figure 2). Apparel production represents a crucial source of income for Eswatini's economy, currently employing over 22,000 people and accounting for 10.5% of the country's 2019 exports.

1 Together, these six retailers account for over 90% of the South Africa internal market (Barnes and Hartogh, 2019), and have recently begun expanding across Africa and globally (Pasquali et al. 2020).

Figure 2: Eswatini's apparel export share – thousand USD.

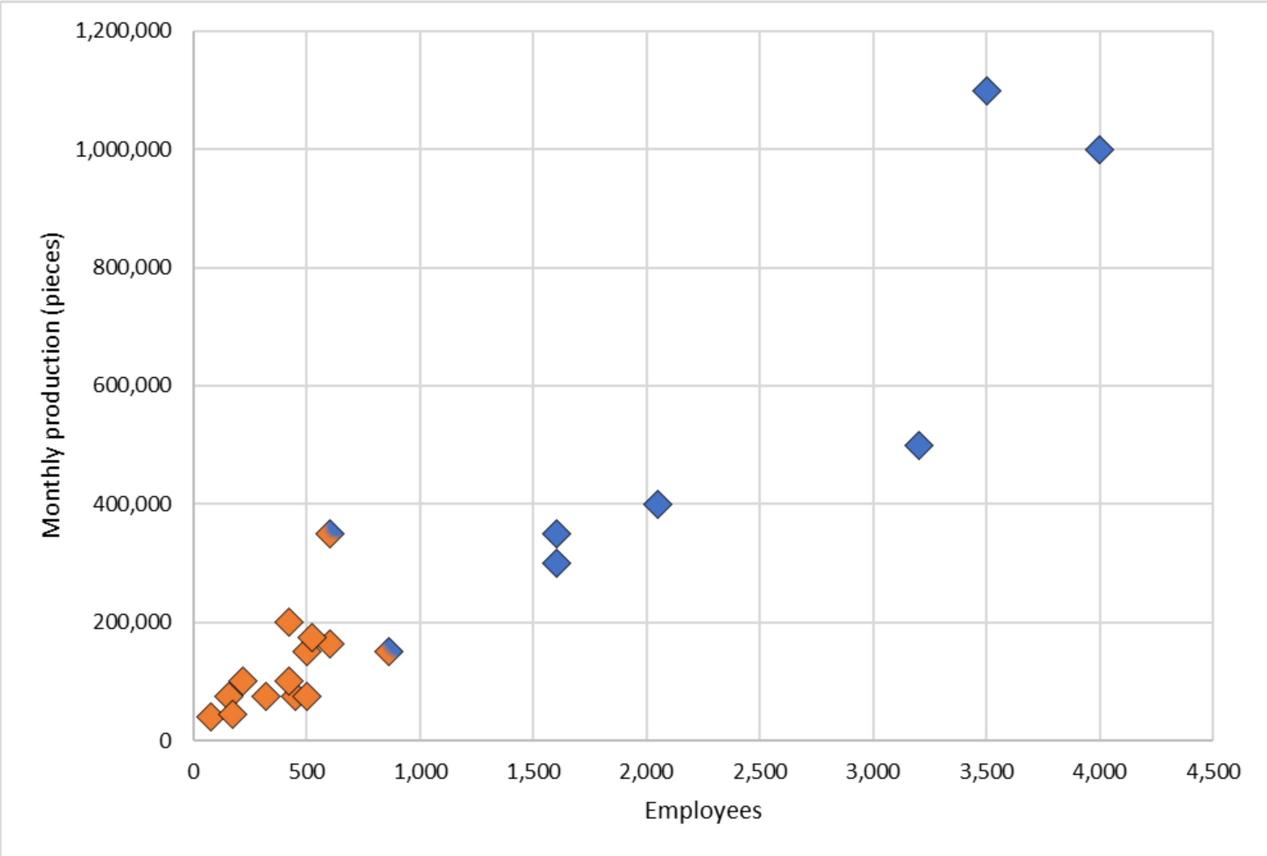


Source: Authors' elaboration based on UN-COMTRADE.

Despite depending largely on South African retailers, the organisation of the apparel value chain in Eswatini is not homogeneous. A survey and interviews conducted in 2019 highlights the presence of two parallel *groups of firms*: those bound to South African retailers via direct contracts (i.e. *direct suppliers*) – 8 suppliers, and those who operate via intermediaries known as *design houses*, which manage the interaction between retailers and suppliers (i.e. *indirect suppliers*) – 12 suppliers. This division is shown to have important commercial and social implications for suppliers and labour:

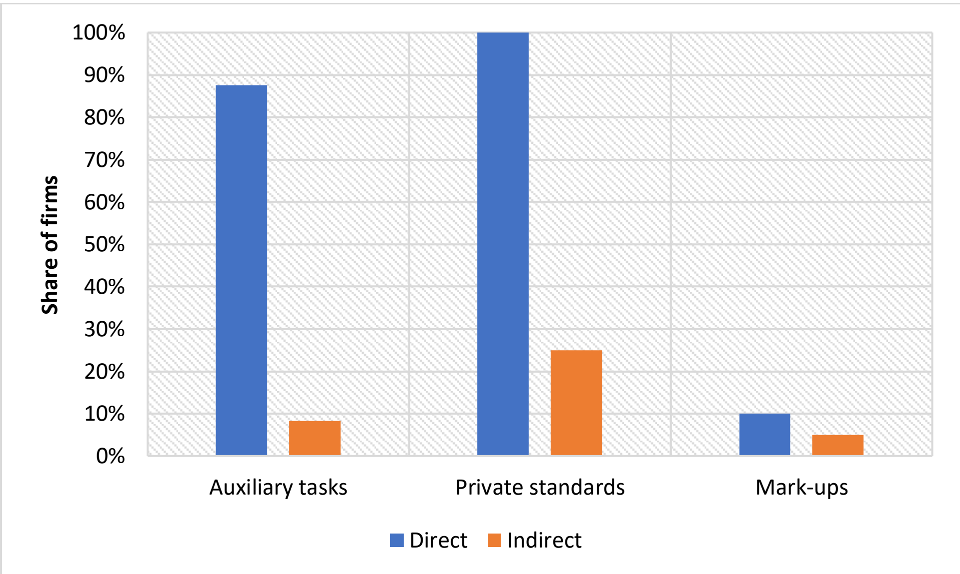
- Commercial implications: direct suppliers are significantly larger both in terms of their production capacity and employment (Figure 3). They produce more complex items with comparatively higher mark-ups, and they are more likely to integrate a larger number of production tasks beyond cut, make and trim services (including laundering, printing, and embroidering). They are also more likely to be regularly audited by buyers (either internally or through third-party certification systems) (Figure 4).

Figure 3: Eswatini apparel suppliers by number of employees and monthly capacity (2019).



Note: Half-coloured dots indicate the two suppliers operating both through direct and indirect linkages.
Source: Authors' survey.

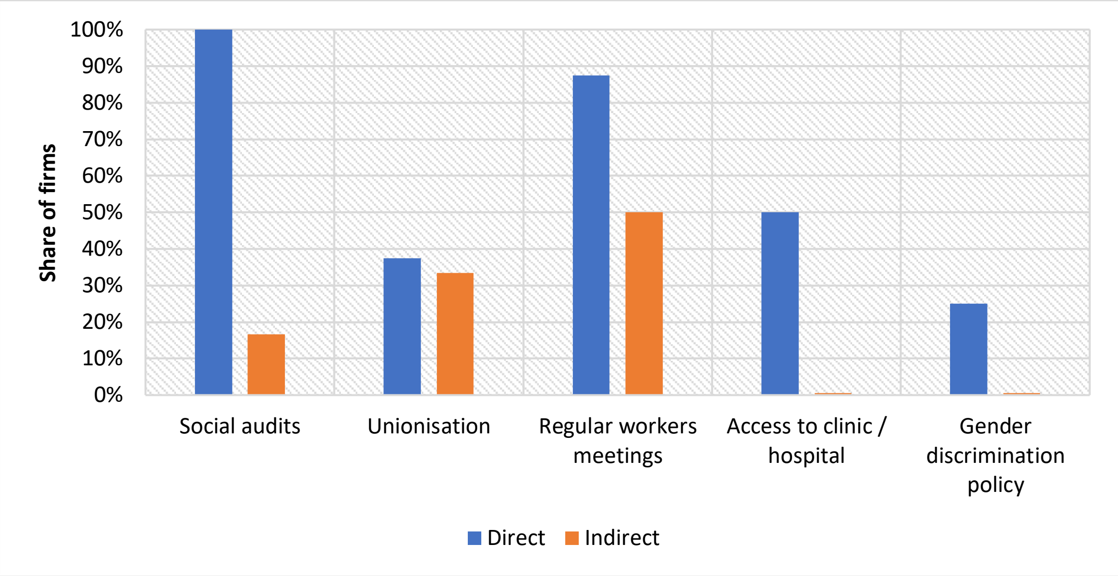
Figure 4: Organisation, governance and mark-ups among Eswatini direct and indirect suppliers (2019).



Source: Authors' survey.

- Implications for labour: whilst almost all firms pay the legal minimum wage (which averages around 115 USD per month for a trained machinist), direct suppliers are more likely to receive regular social audits, hold regular workers' meetings (despite similar low rates of unionisation), provide workers with basic healthcare facilities, and have gender discrimination policies in place (Figure 5).

Figure 5: Labour conditions among Eswatini direct and indirect suppliers (2019).



Source: Authors' survey.

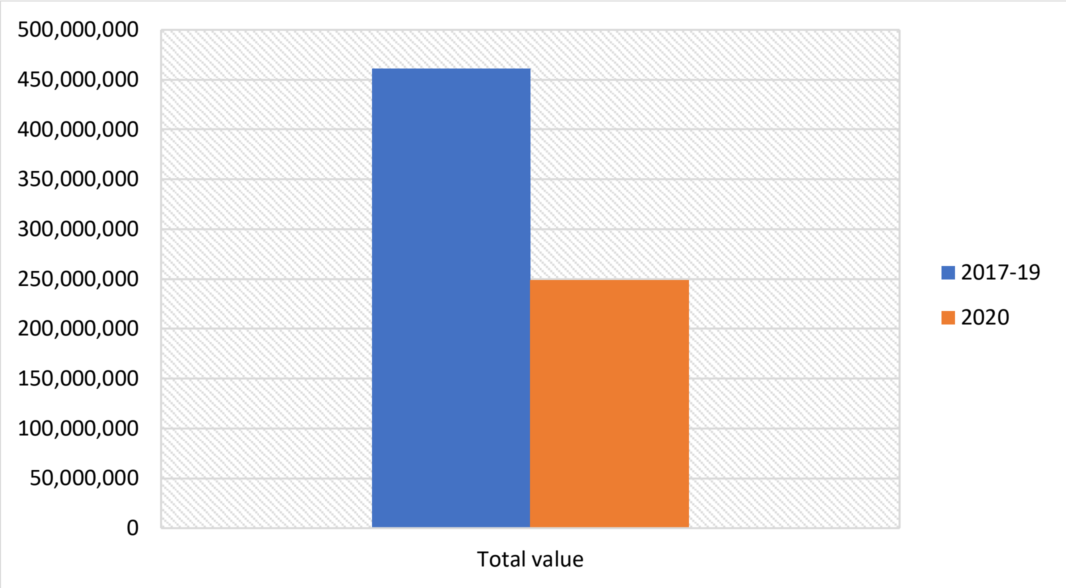
Impact of the COVID-19 lockdown on Eswatini's apparel

The first COVID-19 case was registered in Eswatini on 14 March 2020, with the number of positive patients growing daily over the next two months. Following WHO recommendations, the government enacted a partial *lockdown* on March 26-27th, which lasted for six weeks, including the temporary closure of non-essential business and productive activities, the closure of the country's borders to foreigners, and heightened screening measures for freight, the banning of non-essential internal travel, and the suspension of all commercial flights (Gardaworld, 2020).

As we argue here, the difference between *direct* and *indirect suppliers* is critical to understand the impact of the COVID-19 lockdown on Eswatini's apparel. Drawing on customs export data from the Eswatini Revenue Authority and telephonic interviews with a number of stakeholders, we point to a number of critical implications.

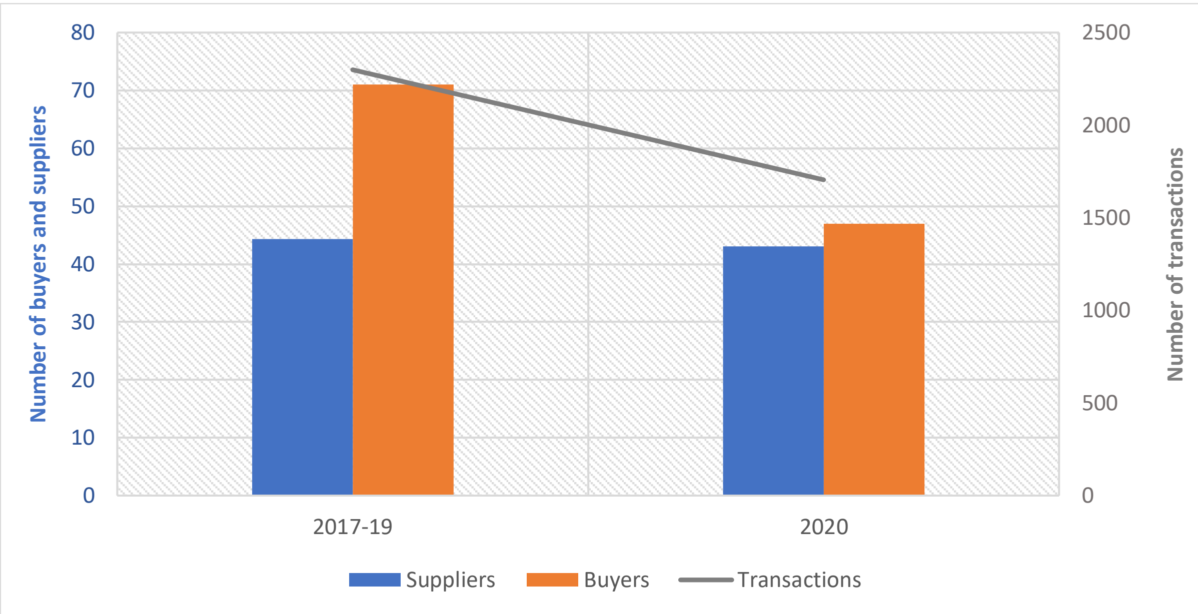
- Comparing the sector total exports over the March-April period in 2020 to the average for the same period across 2017, 2018, and 2019, Eswatini has lost 45% of its seasonal incomes, from around ZAR 455 million to ZAR 250 million (Figure 6). Whilst the total number of exporters in 2020 does not appear to have changed compared to previous years, the number of businesses sourcing apparel from Eswatini dropped by about 34%, while the number of total transactions has also dropped by 26% (Figure 7).

Figure 6: Eswatini apparel total exported value, ZAR (March-April).



Source: Authors' elaboration based on SRA data.

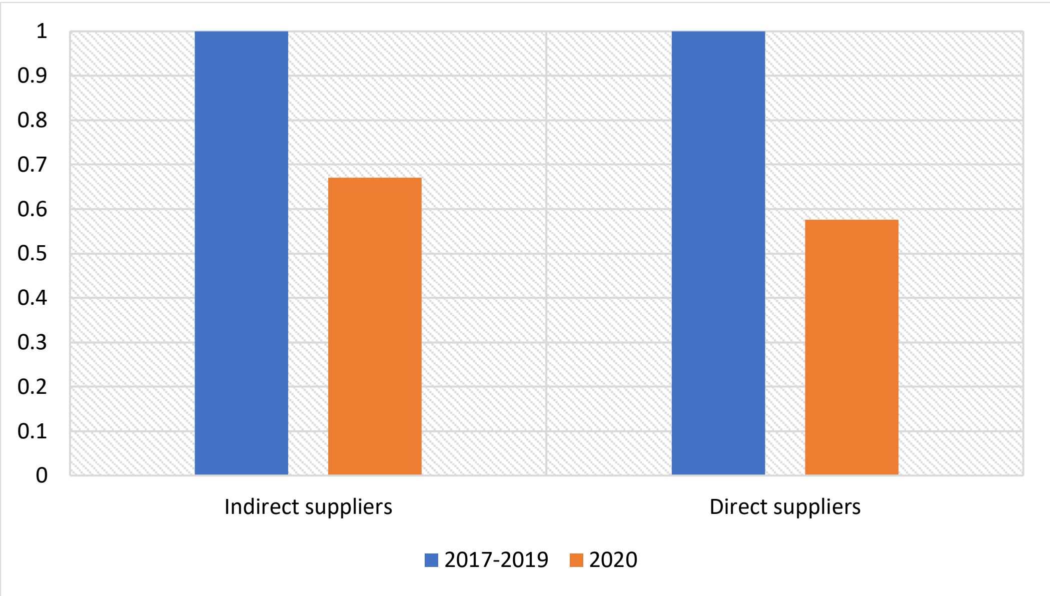
Figure 7: Eswatini number of apparel buyers and suppliers, and total transactions (March-April).



Source: Authors' elaboration based on SRA data.

- *Indirect suppliers* experienced a relatively less pronounced drop in total exports but a significantly more severe decrease in unit prices (Figure 7 and 8).[2] Notably, whilst *direct suppliers* have reduced their total exports without dropping unit costs, *indirect suppliers* have squeezed suppliers, dropping prices by 14% (Figure 8). This is confirmed by all three indirect suppliers that replied to our online questionnaire as well as by the Chairperson of the Eswatini Textile and Apparel Traders Association (ETATA): 'I observed that other companies that do business with those on the other side in Durban [i.e. *design houses*], they are being squeezed and agents try to get them to sell the same products at lower prices. Other firms in ETATA complained about this…' (04/06/2020)

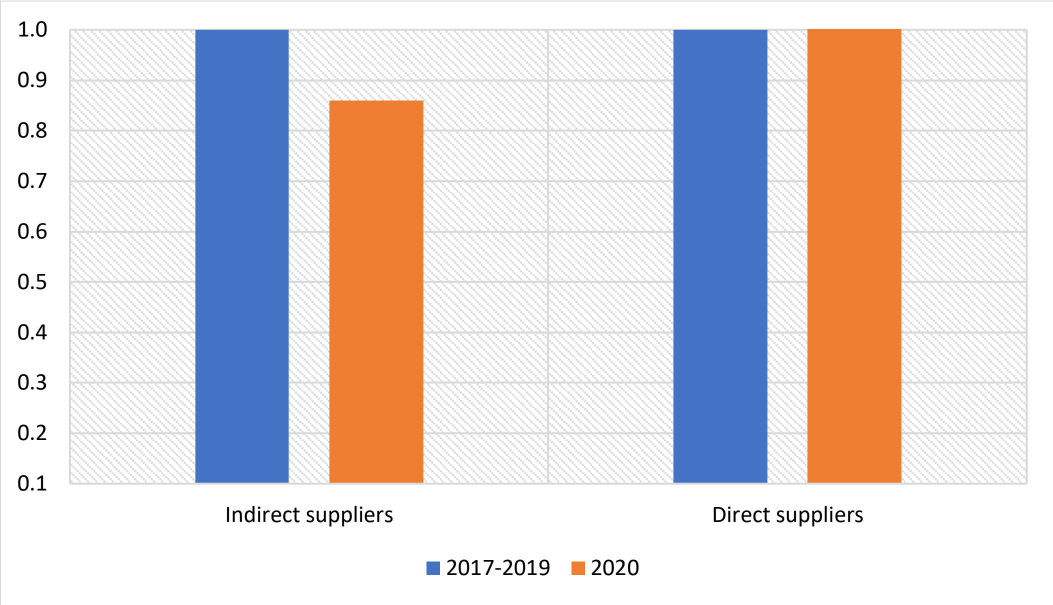
Figure 7: Eswatini apparel firms' average yearly exports - normalised to 1 in 2017-19, (March-April).



Notes: values normalised to 1 in the base period 2017-2019.
Source: Authors' elaboration based on SRA data.

[2] Methodological note: figures are based on transaction-level customs data for apparel exports collected by the Eswatini Revenue Authority over the 2017-2020 period. Every observation in the dataset corresponds to an export transaction with information on quantity (Kg), real value in ZAR, date of transaction, IDs for exporting and importing firms, country of destination, and the World Customs Organization's Harmonized System (HS) 8-digits code identifying the traded product. For the purpose of this paper, we consider only transactions that took place is the months of March and April 2017, 2018, 2019, and 2020. We calculate moving averages for the period 2017-2019 and compare it to their respective indicators for 2020. From the dataset, we isolated suppliers that exported pre- and during the COVID-19 lockdown (i.e. suppliers that exported at least once over the 2017-2019 period and the 2020 period). To further exclude small and occasional traders, we retained only observations for firms that exported at least 1 million ZAR over the 2017-19 period. This resulted in a sample of 18 suppliers. We then computed their average annual exported value, average log unit values, and number of exported products for the period before COVID-19 (i.e. 2017-19 moving average) and the lockdown (March-April 2020) period. In doing so, we separated the upper six firms and the bottom 12, based on their market share in 2017-19. To the extent that data is anonymised, and we cannot directly match firms. However, based on evidence from Figure 3, it is fair to assume that the upper six firms are all large exporters directly contracted with South African retailers, whereas the remaining nine exporters operate through *design houses*.

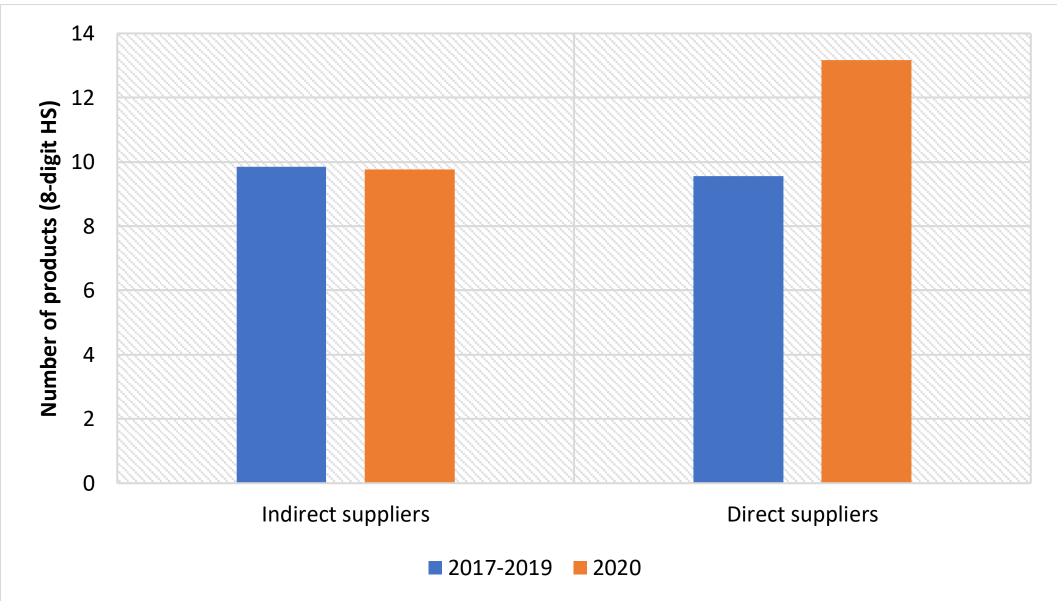
Figure 8: Eswatini apparel firms' average unit values - normalised to 1 in 2017-19, (March-April).



Notes: values normalised to 1 in the base period 2017-19.
Source: Authors' elaboration based on SRA data.

- *Direct suppliers* have differentiated their product basket significantly more than *indirect suppliers* (Figure 9). This is likely due to the fact that at least four suppliers converted some of their lines to the production of PPE for the domestic and export markets. As reported by one manager: 'We got an opportunity to get into producing PPE and face masks and that allowed us to keep working first for the local market and recently also for export to South Africa, as our main buyer won a tender with the government there. This allowed us to keep paying our workers…' (Firm, 06/06/2020).

Figure 9: Eswatini apparel firms' average number of exported products (March-April).

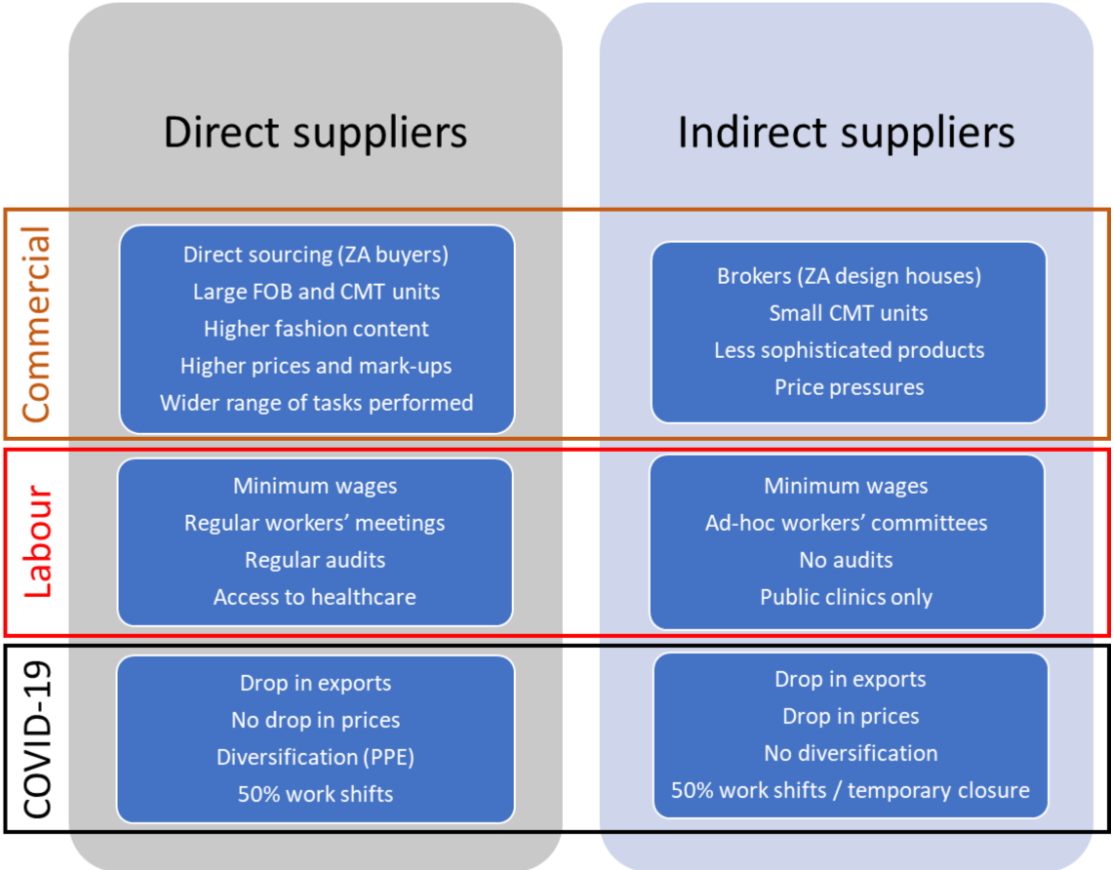


Source: Authors' elaboration based on SRA data.

- The COVID-19 lockdown has also severely impacted Eswatini's apparel workforce. As of June 2020, three relatively small *indirect suppliers* (which employed about 1000 employees in total) have not resumed operations since the beginning of the lockdown in March, and it is possible that these firms will close permanently, with the workers being retrenched. Most of the other plants appear to be operating at about 50% capacity due to social distancing regulations, with the labour force split in half and working on rolling shifts (daily, weekly, and fortnightly). Workers are paid only for the time they work, so their income is currently about half of what they were earning at the start of 2020: machinists are earning ZAR 900-1000 monthly (about 52-59 USD), significantly below the sector's minimum wage and the country's living wage. It should be noted that Eswatini's wages in the apparel sector were already among the lowest in the region, over 60% below wages in South Africa and 10% below Lesotho (Pasquali et al. 2020), and 33% below the country's living wage before the COVID-19 pandemic impacted (SEPARC 2016). Depending on the evolution of the situation in the next weeks and months, the Eswatini Textile and Apparel Traders Association (ETATA) estimates that up to 35% of the sector's labour force could be at risk of unemployment. This risk has recently increased following the potential collapse of the South African retailer Edcon – the only retailer reported to have not respected its contractual obligations with suppliers.
- With the exception of Edcon, no other retailer has refused to pay for orders placed, in process, or shipped. Furthermore, contrary to *design houses*, no retailer has tried to renegotiate prices downwards. Furthermore, three *direct suppliers* noted that retailers have provided them with some forms of financial assistance: 'They assisted me with 80% payment for the staff while I was shut down. They asked me for a list of the staff and they accepted to pay 80% while I was shut. They are also supporting me now by commissioning masks for South Africa' (Firm, 04/06/2019). Similarly, the manager of a large *direct supplier* stressed: 'Fabric supplies are two weeks longer than before and customers' selling performance is not stable yet. Our main buyer gave us a loan of 5 million ZAR to buy fabrics.' (Firm, 12/06/2019)
- Despite ongoing negotiations, government and employers have as yet failed to agree on any form of support to apparel manufacturers and the workforce. Consideration has been given to accessing funds from the state provident fund, to which workers and employers each contribute 5% of the weekly wage, but nothing has resulted as yet. Furthermore, under Eswatini's Employment Act, when starting a business each employer must pay to government the equivalent of one month's wage for each of its employees, which is held in a trust to pay employees if the firm endures financial hardships. However, it appears, according to a key informant, that many of the apparel firms were given exemptions, which has meant that this potential source of funds for supporting workers is effectively missing. Another problem is that few workers have been retrenched, which left them both unpaid during the lockdown and not able to access their severance benefits. The exclusion of the major trade union in the sector (the Amalgamated Trade Union of Swaziland (ATUSWA)) from the negotiations has reduced the degree of workers' representation to their detriment.

Figure 10 summarises our findings on the governance of Eswatini's apparel sector and the initial impact that COVID-19 is having on firms and workers.

Figure 10: Eswatini apparel value chains and COVID-19.



Final remarks

The impact of the COVID-19 lockdown on the Eswatini apparel industry has been severe both on firms' income and on workers. Critically, the gap between *direct* and *indirect suppliers* has conditioned the differential impact of COVID-19 on the industry. Whilst the whole sector is suffering, relatively small *indirect suppliers* are more exposed as they undergo significant price pressures from *design houses*. Conversely, despite reducing the size of their orders, South African retailers (with the exception of Edcon) have honoured their contracts with *direct suppliers*. This evidence sets the Eswatini case apart from Bangladesh, where European and US lead retailers cancelled over 70% of their orders and refused to honour their contractual obligations, leading to the shutdown of factories within weeks of the beginning of the crisis (Anner 2020). We therefore provide concrete evidence that cautions against any immediate association between South-South value chains and relatively lower labour standards (Kaplinsky et al., 2011), further highlighting 'the falsity of the assumption that the global North has all the solutions to tackle global challenges' (Oldekop et al., 2020).

Despite this evidence, however, the situation in the Eswatini apparel sector remains critical. Private initiatives, without the direct involvement of the government and workers' representatives, including the sector's main trade union ATUSWA, are unlikely to ensure the resilience of the apparel industry and livelihoods of workers in Eswatini. We therefore call for concerted forms of public, private, and social governance through the simultaneous involvement of firms (including both buyers and suppliers), state, and the sector's main trade union to produce an effective response to the crisis caused by the COVID-19 pandemic.

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