

**Honesty.**

**Commitment.**



adidas-Salomon

**Inspiration.**

**Authenticity.**

***Background Paper:  
Fair Wages Study, Indonesia***

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# 1 Introduction

## 1.1 Background

International brands have been the subject of criticism from non-governmental organizations, labor organizations and other lobby groups regarding the pay and conditions of workers in developing countries. One of the most hotly debated topics has been whether workers in the apparel and footwear sectors receive fair compensation in the form of a “living, or fair wage”. The arguments presented by the NGOs and others<sup>1</sup> include:

- Living wages are premised on the assumption that the wages paid must support an adequate standard of living including food, housing, health care, transportation, and other needs. That is not guaranteed with minimum wages. In many developing countries existing legal minimum wages do not come close to providing that living standard.
- As a consequence, rock-bottom wages force workers to add exhausting hours of overtime in order to make ends meet.
- The creation of “entry level” employment opportunities, where young people work for a short time and then move on to something better, does not in itself justify the payment of lower wages. In developing countries these entry level workers, many of whom are young women, have family obligations - parents to take care of, sisters and brothers, and sometimes children of their own.
- In less developed countries workers are not sufficiently empowered or well organized to secure for themselves improved pay and conditions. Responsibility therefore lies with the brands to ensure that appropriate wages and benefits are paid.

In recent years several studies have been undertaken which seek to address these issues, the most recent of which was published by the U.S. Department of Labor, Bureau of International Labor Affairs ‘Wages and Benefits, Poverty Line, and Meeting Workers’ Needs in the Apparel and Footwear Industries of Selected Countries’.

The Bureau of International Labor Affairs study examined 35 major apparel and/or footwear exporting countries, together with the United States, and evaluated:

- the minimum wage,
- the prevailing or average wage,
- non-wage benefits, measures of workers’ basic needs (the poverty line), and
- the extent to which wages meet such needs.

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<sup>1</sup> Based on a review of publications: ‘Time for a living wage around the world’, Medea Benjamin, Global Exchange, Fall 1998.

Among the study's general findings it is stated that:

- For the countries considered, there appears to be little conclusive evidence on the extent to which wages and non-wage benefits in the footwear and apparel meet workers' basic needs.
- Many countries take into consideration the poverty threshold (if one has been established), among other things, in setting and adjusting the minimum wage. While in many cases the minimum wage is supposed in theory to meet a worker's basic needs, the level at which it is actually set usually represents a political compromise or a balance between meeting those needs and economic conditions and the employer's ability to pay.
- In assessing the adequacy of wages, decisions must be made on whether one wage earner should be able to support (meet the basic needs of) his/her family (support for how many dependents?); how much is enough (poverty measures usually tell us how much is too little); whether income from other sources (investments, savings, or in-kind or non-cash payments) should be included in determining disposable income; and whether one's position in the life-cycle should be considered. As with the construction of poverty measures, opinions vary widely on these questions, especially with regard to the treatment and valuation of health care and insurance, housing, and child care expenses.
- For several countries where data are available, the minimum wage (and in a few more countries, the prevailing wage in the footwear or apparel industries) may yield an income above the national poverty threshold for an individual (and perhaps one dependent, but not for a family of 4 or 5 with one wage-earner). However, whether this wage is a "living wage" is likely to lie in the eye of the beholder.
- For countries where prevailing or average wage data were available, average earnings in both the footwear and apparel industries, for the most part, tended to be lower than in all manufacturing but higher than the minimum wage level (except for Cambodia, Peru, and the Philippines where the minimum wage appears to be close to the prevailing wage in the apparel industry); average earnings tended to be slightly higher in footwear than in apparel.

## **1.2 Standards of Engagement**

adidas-Salomon has developed a code of conduct to establish minimum standards for its manufacturing partners. These "Standards of Engagement" assist us in selecting and retaining business partners that follow work place standards and business practices consistent with the adidas-Salomon's policies and values. The Standards of Engagement are based on the International Labor Organization's Conventions and the model code of conduct of the World Federation of Sporting Goods Industries (WFSGI).

With respect to wages and benefits our Standards explicitly state that:

*"We will only do business with partners who treat their employees fairly and legally with regard to wages, benefits, and working conditions".*

In February 2001 adidas - Salomon revised and updated its Standards of Engagement. As part of those revisions the employment standard on Wages and Benefits was amended to read as follows:

*"Wages are essential for meeting the basic needs of employees and reasonable savings and discretionary expenditure. In all cases, wages must equal or exceed the minimum wage required by law or the prevailing industry wage, whichever is higher, and legally mandated benefits must*

*be provided..”*

In essence, adidas-Salomon is seeking a commitment from its suppliers to ensure that wage payments match worker's needs, plus some discretionary spending. But commitment alone will not bring about the change desired. In many cases workers' needs are poorly understood by the factory owners, or are ill defined. Wages and benefits also vary widely, based on general economic factors, industry norms, factory-specific labour practices and the local regulatory environment.

### **1.3 Pilot Study in Indonesia**

To establish a sound business case for the payment of “fair wages” adidas-Salomon believes that its Manufacturing Partners require:

1. accurate information on workers needs and income requirements; and
2. management support and advice on appropriate wage-fixing mechanisms.

To assist in this process, adidas-Salomon has commissioned an independent non-governmental organization to undertake an initial pilot study, or Fair Wage Study (FWS), to analyze workers needs and wages in Indonesia.

The appointed NGO - *Lembaga Penelitian, Pendidikan dan Peningkatan Ekonomi dan Sosial* (Institute for Social & Economic Research, Education & Information, or LP3ES) – is an autonomous, not-for profit organization, which was established in 1971 by a group of intellectuals and student activists. LP3ES past track record includes surveys and studies for such organizations as USAID, the American Center for International Labor Solidarity (ACILS) and Business for Social Responsibility (BSR). LP3ES is located in Jakarta, Indonesia.

The Fair Wage Study calls for the direct participation of our suppliers in the development and testing of methodologies and approaches for the setting of fair wages. If successful, the tools developed in this study will be applied to in other countries where adidas-Salomon sources product.

## 2 Fair Wage Study

### 2.1 Broad Strategy

The Fair Wage Study fits within a broad framework, or strategy, which has been developed in a step-wise fashion by adidas-Salomon, as follows:

**Stage 1** - establish a working definition of “fair wage”, one that is reasonable, defensible and universally applicable.

**Stage 2** - develop a standard methodology, based on an initial pilot study in Indonesia, to determine whether earnings and benefits paid by employers match needs, savings and expenditure patterns.

**Stage 3** - apply the methodology in those countries where the national minimum wage, or industry wage, is deemed to be below the general cost of living of the workforce.

**Stage 4** - Where the general cost of living is not met by local wages, adidas-Salomon will work with our Business Partners and production staff to develop appropriate wage-fixing strategies to close the gap.

### 2.2 Scope of Study

#### 2.2.1 Key Tasks

The Fair Wage Study commissioned by adidas-Salomon is itself comprised of four principal tasks, requiring the appointed NGO to:

1. Collect and analyze social and economic data from a sample of the target worker population in Indonesia;
2. Using this data, test the appropriateness/completeness of adidas-Salomon’s definition of a ‘fair wage’;
3. Based on the analysis recommend a model approach, or standard methodology, which can be used to evaluate and equate cost of living with the pay and conditions in the apparel and footwear industry; and
4. For selected factories in Indonesia, examine the existing wage structures and identify ways in which the wage-fixing mechanisms can be amended to take account of local cost of living issues.

## 2.2.2 Definition of a 'Fair Wage'

For the purposes of the study, adidas-Salomon has defined a "fair wage" to be:

*The take-home pay and benefits received by a worker during a legal work week which allow the worker and their immediate family and/or dependents to meet basic needs and save a certain portion for long-term planning and emergencies. Basic needs include food, housing, education, childcare, health care, clothing, energy, water, and transportation<sup>2</sup>.*

## 2.2.3 Participating Suppliers:

Four Indonesian based suppliers have volunteered to participate in the Fair Wage Study, providing access to their factories and their workers. Together, these suppliers employ almost a quarter of the total workforce involved in the manufacture of adidas-Salomon's products in Indonesia.

The location and characteristics of the factories participating in the study are given in Table 1.

**Table 1: Location and Characteristics of Suppliers**

Supplier No.	Factory Locations In Indonesia	Workforce	Product Line	Characteristics
1.	Tangerang	5,802	Footwear	International sourcing, large scale
2.	Tangerang	2,107	Apparel	International sourcing, large scale
3.	Tanjung Priok, Cakung, Tangerang, Cikupa	6,400	Apparel	International sourcing, large scale
4.	Bogor	135	Apparel	Domestic sourcing, small scale

A total of **1,140 respondents** have been selected for one-on-one interviews, proportional to the worker population in these factories.

The sample size has been determined based on a 5% margin of error, with a 95% confidence level.

## 2.2.4 Worker profile and survey data:

A key task in the study is to examine the demographics/employee profile of adidas' suppliers in Indonesia and to determine, through survey and sample interviews, the two sides to the fair wages equation, namely:

- *Needs and expenditure versus income and benefits.*

A profile of the workforce for each participating factory has been developed and captured in the

<sup>2</sup> Under The UN Declaration of Human Rights, Article 23 (3) "Everyone who works has the right to just and favorable remuneration ensuring for himself and his family an existence worthy of human dignity, and supplemented, if necessary, by other means of social protection. Moreover, under Article 25, "Everyone has the right to a standard of living adequate for the health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services, and the right to security in the event of unemployment, sickness, disability, widowhood, old age or other lack of livelihood in circumstances beyond his control."<sup>2</sup>

sampling program. The data collection includes:

- employment status (full or part-time),
- age,
- gender,
- marital status,
- the number and age of their children, if any;
- local or migrant status, and
- whether they form part of a single or dual income household.

For each individual surveyed information on basic needs and general welfare, as well as expenditure patterns and income, has also been collected.

The full scope of the survey data is summarized in the Table 2, below.

**Table 2: Scope of Survey Data**

<b>Needs and expenditure</b>	<b>Income (including benefits)</b>
<ul style="list-style-type: none"> <li>• <i>Basic needs</i> - food, housing, education, childcare, health care, clothing, energy, water, and transportation. Each of these should be defined (calorific value, food basket, educational norms, etc) and assessed.</li> <li>• <i>Welfare needs</i> – pension, social security, and insurance against old age, unemployment or disability. Each of these should be defined and assessed.</li> <li>• <i>Spending patterns e.g. the “basket”</i> of goods and services that the worker needs to buy out of cash income, the price of that basket, the price of that basket over time (to match the wage time series), whether there a residual for savings/discretionary expenditure and how much?</li> <li>• <i>The marital status and number of dependents.</i> In defining " immediate family and/or dependents" an examination must be made of familial obligations (including cultural norms in terms of repatriating money home to support parents or other family members), as well as spouse, and number of children. A profile of the needs for each category of worker should be developed and captured in the sampling program.</li> <li>• <i>Levels of savings.</i> For the purposes of the study it is assumed that 10% of earnings per annum should be saved to meet unexpected costs or pay for additional expenses such as higher education. This assumption should be tested based on actual saving patterns revealed through the worker interviews and household surveys.</li> </ul>	<ul style="list-style-type: none"> <li>• The wage paid (including basic, premium and incentive wages – see example below);</li> <li>• Length of the working week for which the wages are paid;</li> <li>• Equivalent income received over a standard work week (40 hours normal time);</li> <li>• Income paid in kind, if applicable, (accommodation, food, transport) and other benefits or allowances (in Indonesia this may include menstrual allowance);</li> <li>• Government mandated benefits or schemes (e.g. medical care, insurance, social security, pensions) available to the worker;</li> <li>• Wage rates over the last three years;</li> <li>• Dates on which the measurements were recorded (to match price data with wage data).</li> </ul>

### **2.2.5 Other data requirements**

Other broad economic data, which is currently being collected and analyzed by LP3ES, includes:

- An absolute measure of the wage – i.e. what it buys in real terms (including income in kind) and whether this is enough to meet basic needs and leave some discretionary income, given the characteristics of the workforce in question.
- How this wage compares to the poverty line (as locally defined) and to the Government mandated minimum wages at the factory location over the past three years.
- The industry norm for wages and whether the surveyed factories match or exceed that norm.
- A relative measure of the wage – for example the wage expressed as a percentage of per capita GNP.
- Time series data – how the wage has been changing in real terms over the past three years.
- Effects on wages and cost of living from inflation and exchange rate pressures over the past three years. This may include information from consumer price indices where these are available.
- General data on the trends in the poverty line and national minimum wage levels set by the Indonesian Government over the past 10 years.

### **2.2.6 Analysis and recommendations**

Based on an analysis of the survey data and other information collected, recommendations are to be formulated by LP3ES on:

- Needs and fair wage requirements for the survey population in question.
- Appropriateness of the adidas-Salomon definition of a 'fair wage' and whether there should be changes to its scope and content.
- A model approach or standard methodology to be followed in assessing worker needs, irrespective of factory location, or country.
- The accuracy, reliability and usefulness of the published national and regional cost of living data and consumer price indices in Indonesia and their relationship to the minimum wage and industry norms.
- Practical and workable wage-fixing solutions that would enable factory managers in Indonesia to revise cost/pay structures, resulting in a closer match between the workers' wages and benefits and the local cost of living.

### **2.2.7 Peer Review**

To ensure scientific rigor, a Peer Reviewer has been appointed to conduct an independent review of the approach and findings of the study.

## **2.3 Current Progress**

LP3ES have completed their survey work, including the worker and management interviews and other general data collection. The researchers have proceeded to analyze the field data and formulate recommendations, which have been detailed in a series of reports described below.

The following draft reports have been submitted to adidas-Salomon for its review and comment:

- **Survey Report** - summarizing survey findings,
- **Fair Wages Report** - providing an analysis of the survey data, recommendations on fair wage requirements for the survey population, recommendations on revisions (or additions) to the definition for a 'fair wage' and a model approach for the assessment of workers needs.
- **Management Report** - describing wage structures and wage-setting mechanisms used by the participating factories and the relationship to the Government minimum wage levels and apparel and footwear industry norms.

Copies of these reports have also be submitted to an Independent Reviewer, Dr Chris Manning, who has been appointed by adidas-Salomon to critical review the study methodology and findings. Dr Manning, is an economist and a researcher with the Economics Division, of the Research School of Pacific and Asian Studies, Australian National University, Canberra, Australia.

## **2.4 Next Steps – a Fair Wage Workshop**

Before LP3ES finalize their reports, adidas-Salomon have requested that a multi-stakeholder meeting be held in Indonesia to discuss the general findings of the study and obtain feedback from a cross-section of interested parties. The stakeholders will include representatives from government, the major unions, and employers (i.e. top management from the factories participating in the study), as well as local NGOs and academics.

The Fair Wage Workshop is scheduled to be held on 26<sup>th</sup> to 27<sup>th</sup> March 2003, at the Shangri-La Hotel in Jakarta.

The workshop discussions will be by facilitated by Thee Kian Wie from the Economic Research Centre, Indonesian Institute of Sciences, (P2E-LIPI), Jakarta.