

FDRA

FOOTWEAR DISTRIBUTORS AND RETAILERS OF AMERICA





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1. EXECUTIVE SUMMARY

In early 2015, the Footwear Distributors and Retailers of America (FDRA), in partnership with ELEVATE, invited Chinese and global footwear manufacturers to participate in the association's annual survey for the sixth consecutive year. The goal of the survey was to gain insight into the current state of footwear production in China and other emerging manufacturing countries and to develop a better understanding of how factories are managing the various challenges facing the industry. The survey produced the following findings:

- Finding 1: While Women's footwear represents the largest wearer segment, produced by nearly all surveyed factories (92%), kids shoes make up a considerable group of production (15%).*
- Finding 2: Despite the overall growth in production volume, Chinese factories are facing increasing competition from emerging countries.*
- Finding 3: Vietnamese factories tend to be larger factories, whereas the average size of Chinese factories has decreased significantly for three years in a row.*
- Finding 4: In light of increasing overseas competition and operation costs, the 2015 Survey reveals a significant drop in percentage of large Chinese footwear factories, dropping from 47% two years ago to 25% this year.*
- Finding 5.1: Female workers continue to make up the majority of the workforce. The workforce in Vietnam is significantly younger than the Chinese workforce.*
- Finding 5.2: Compared to other sectors, Chinese footwear factories utilize a relatively older worker population with an average age of 34.*
- Finding 5.3: An increasing percentage of factories use retired and juvenile workers, suggesting that Chinese factories are getting "creative" in fulfilling labor needs and such practices are not without risk.*
- Finding 6: Despite the decline in factory size, Chinese factories experienced a stronger seasonal fluctuation than previous years. Small factories with less than 500 workers were hit the hardest by seasonality.*
- Finding 7: Chinese factories, small Chinese factories in particular, tend to use temporary workers to fill the labor gap during high seasons.*
- Finding 8: Labor shortage is reported to be less of an issue this year with only 5 Chinese factories feeling labor shortage is a serious challenge for them.*
- Finding 9.1: Wage level growth is still lagging behind the increase in legal minimum wage.*
- Finding 9.2: Social insurance is particularly acute for the footwear industry given the fact that it utilizes a relatively older workforce than other sectors.*
- Finding 10: While the average weekly working hours remain similar to last year, reported maximum number of working hours is much less.*
- Finding 11: 24% of respondents have not received any worker feedback in the past 12 months. Among those who did, they report that one in every 100 have raised concerns.*
- Finding 12: Small factories are less likely to conduct worker surveys than large factories. Considering the fact that they are the ones that are hit the hardest by seasonal fluctuations, additional support is suggested to help them better manage seasonality and its implications on compliance.*
- Finding 13: Factories report an average of 4% of monthly turnover rate, which is believed to be overestimating the stability of the footwear workforce and not taking into account the turnover of temporary workers.*
- Finding 14: Nearly all surveyed factories indicate that they have dedicated staff for CSR and compliance issues, and 61% of them have full time personnel devoted to this matter.*
- Finding 15: More factories are being audited. On average footwear factories experience at least one audit per every other month.*



Finding 16: 73% of surveyed factories have heard about the FDRA Code of Conduct. Among those who have, the majority find compliance with the Code to be challenging.

In summary, the survey reveals that despite the overall growth in production volume, Chinese factories are facing increasing competition from emerging producing countries. At the same time manufacturers in China are also suffering from continued domestic challenges in regards to production seasonality, labor shortages and increasing labor and material costs. An increasing number of factories cope with some of these challenges by utilizing juvenile and temporary workers as well as workers of retirement age – coping strategies that increase the risk of non-compliance with the social performance requirements of buyers. The social insurance issue, which was highlighted in a series of strikes that took place in 2014 and 2015 at footwear factories, also contributes to the added complexity of wage compliance.

The report shows that pure compliance audits are not enough to tackle these compliance risks, and FDRA members, buyers and suppliers need to realize the importance of diversified compliance management, utilizing a variety of tools, resources and efforts to support footwear manufacturers and elevate their compliance and business performance.



2. INTRODUCTION

2014 was another interesting and challenging year for the footwear industry. While the footwear industry in the United States is recovering, Chinese manufacturers are experiencing increasing competition from other emerging producing countries. Vietnam in particular is capturing a greater share of the footwear manufacturing market. In addition, Chinese factories are also facing growing domestic challenges in terms of labor shortages, increasing labor costs and issues around social insurance.

To better understand the complexity and dynamics of footwear production, in March 2015, the Footwear Distributors and Retailers of America (FDRA), in partnership with ELEVATE, invited footwear manufacturers to participate in the association's annual survey for the sixth consecutive year. As in previous years, the survey aims to gain insights into the current state of footwear production in major manufacturing countries and develop a better understanding of their current challenges and how manufacturers cope with these challenges.

3. SURVEY INFORMATION

The 2015 FDRA Factory Survey consisted of 59 questions, and focused on key social compliance areas such as working hours, wages, and health and safety management. In addition, given the changing social and economic environment in and outside of China, this year the survey also included several new questions on production, recruitment processes and labor shortages, to better understand the challenges in footwear manufacturing and their impact on social compliance.

This survey report presents the aggregate findings of 123 responses. Of the 123, 101 respondents have completed all the questions while the remaining 22 respondents have completed a considerable amount of the questionnaire.

Table 1: Survey Information

Number of Questions	59
Survey Completion Duration	May 18 - Apr 22, 2015
Number of Respondents 100% Answered Survey	101
Number of Respondents Included in Analysis	123



4.WHO ARE THE FACTORIES: LOCATION, PRODUCT TYPE AND FACTORY SIZE

4.1 PRODUCTION HUBS

Previously the annual factory survey was distributed amongst FDRA’s Chinese Member factories and factories that have attended FDRA events in China. This year the survey scope was extended to emerging key manufacturing countries in South-East Asia and the Americas. Table 2 illustrates the respondents’ locations. While the vast majority (87%) of the respondents remain in China, it also covers a considerable number of responses from Vietnam factories (10%). The report will analyze in greater detail how the changing dynamics of global footwear production affect Chinese footwear producers’ practices, and identify differences between China based and Vietnam based manufacturers.

Country	Number	%
China	107	87.0%
Vietnam	12	9.8%
Cambodia	1	0.8%
Philippines	1	0.8%
Mexico	1	0.8%
Guatemala	1	0.8%
Total	123	100%

City	Province	# Responses	%
Putian	Fujian	33	30.8%
Dongguan	Guangdong	15	14.0%
Quanzhou	Fujian	7	6.5%
Fuzhou	Fujian	6	5.6%
Wenzhou	Zhejiang	6	5.6%
Shenzhen	Guangdong	5	4.7%
Other Cities	/	35	32.7%
Total		107	100%

In China, as in previous years, Fujian (40%) and Guangdong (27%) continue to be the most important footwear manufacturing hubs. Respondents from these two provinces together represent two thirds (67%) of factories participating in the survey. Taking a closer look at the city level, Putian and Dongguan are the top two footwear production centers, making up close to half (45%) of responses (Table 3).

4.2 PRODUCT













Respondents of the 2015 survey produce various types of shoes. 66% of surveyed factories make cement shoes, followed by sandal & indoor shoes (46%). About one third of the respondents make boots (Welts) (33%) and athletic shoes (Strobel) (33%). The proportion of high-end shoes grew consistently from 9% in 2012 to 18% in 2014, all of which are currently being manufactured in China. Women’s footwear represents the largest wearer segment, almost all respondents (92%) produce shoes for women, while kids shoes make up a considerable amount of production (15%).

In 2014, a total of 0.47 billion pairs of shoes were shipped by surveyed Chinese footwear factories. This increased from 0.3 billion in 2013 (Chart 2).

Finding 1: While women’s footwear represents the largest wearer segment, produced by nearly all surveyed factories (92%), kids shoes make up a considerable group of production (15%).



Table 4: Production Type

What Type of Footwear Makes Up The Majority of Your Production?		Which Gender do You Cater To?											
													
65.9% Shoes (Cement)	45.5% Sandal & Indoor	91.9% Women's	76.4% Men's										
													
33.3% Boots (Welts)	32.5% Athletic Shoes (Strobel)	73.4% Kid's	15.4% Baby's										
		What Percentage of Your Products Use Following Material Type(s)? <table border="1"> <thead> <tr> <th>Material Types</th> <th>Avg. %</th> </tr> </thead> <tbody> <tr> <td>Leather</td> <td>29.6%</td> </tr> <tr> <td>PU</td> <td>35.1%</td> </tr> <tr> <td>Canvas</td> <td>22.1%</td> </tr> <tr> <td>Other</td> <td>13.5%</td> </tr> </tbody> </table>		Material Types	Avg. %	Leather	29.6%	PU	35.1%	Canvas	22.1%	Other	13.5%
Material Types	Avg. %												
Leather	29.6%												
PU	35.1%												
Canvas	22.1%												
Other	13.5%												
17.9% Shoes- High end (Handsewn)	16.3% Vulcanized Shoes												
													
14.6% Rubber Shoes (Injection molding)	13.0% Special Footwear												

However, despite the overall growth in production volume, Chinese factories are facing increasing competition from emerging countries. Vietnam in particular is capturing a greater share of the footwear manufacturing market. According to the United States official import data, although China remains the single largest footwear supplier, its share decreased by 3% from 2013 to 2014. On the other hand, Vietnam has maintained a two-digit increase for several years in a row, and the share of imports into the US. Imports from Vietnam increased by 2% from 2013 to 2014¹. This is also consistent with the latest official export data from the General Administration of Customs of China. In total, 3.2 billion shoes were exported in 2015, worth 15.45 billion U.S. dollars. While this is up 0.4% from the same period in 2014 in terms of value, it is a drop of 5.7% in terms of volume². The increase in overseas competition, along with continued domestic challenges such as increasing labor costs and shortage put Chinese factories in a tough position going forward.

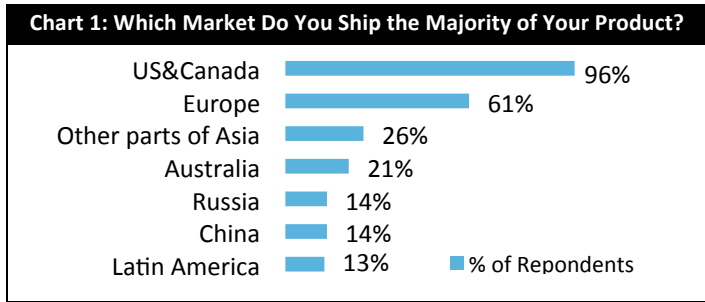
Finding 2: Despite the overall growth in production volume, Chinese factories are facing increasing competition from emerging countries.

¹ "U.S. IMPORTS FOR SELECTED PRODUCTS", U.S. Department of Commerce, Office of Textiles and Apparel, May 5, 2015, accessible at <http://www.otexa.ita.doc.gov/FLT/imports/cat10.htm>

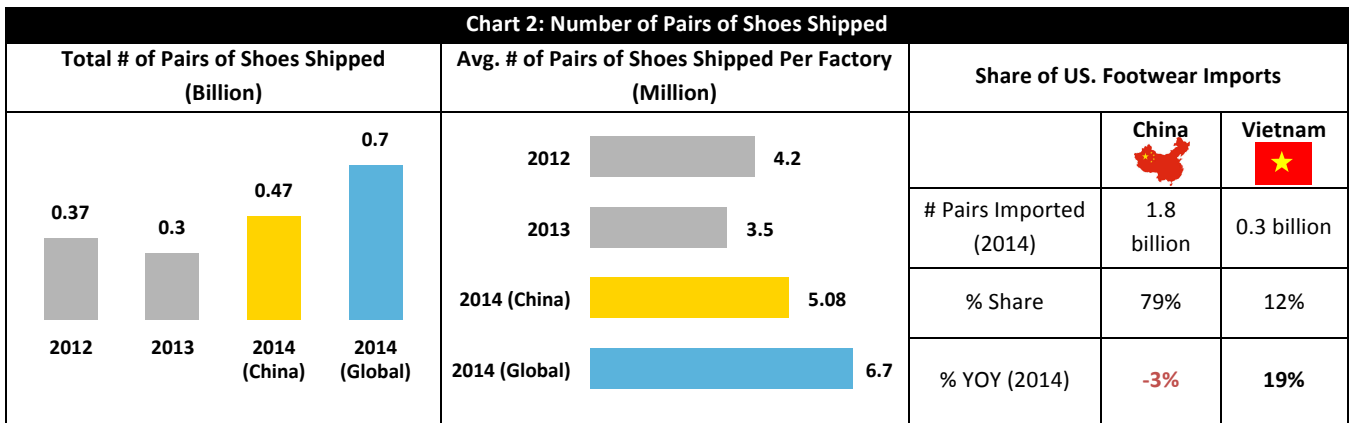
² "Key exports in April 2015", General Administration of Customs of the People's Republic of China, May 21, 2015, accessible at <http://www.customs.gov.cn/publish/portal0/tab49667/info742827.htm>.



The US and Canada markets are still the primary retail market, with 96% of surveyed factories shipping their products to these two countries. This is followed by Europe, attracting exports from over half of the factories (61%) surveyed. In addition, the importance of the domestic Chinese retail market continues to grow for these suppliers. Up from 9% in 2012, China is now the key destination of 14% of these factories' majority products.

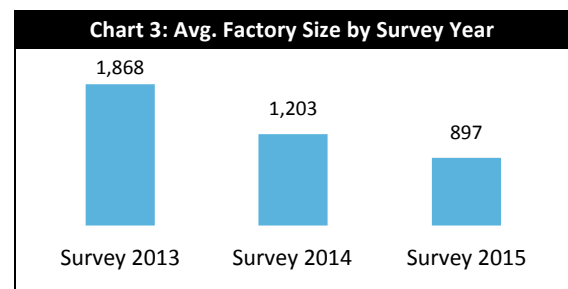


While it certainly reflects the growing significance of the domestic retail market, producing for the domestic market is also a coping strategy taken by many Chinese factories in the light of reduced purchase orders and increasing competition from overseas counterparts.



4.3 FACTORY SIZE

This year's survey data continues to show a great variety in terms of factory size, including factories employing less than 100 workers and factories having almost 80,000 workers. Factories in Vietnam tend to be larger factories with 10 out of 12 Vietnamese manufacturers having over 1,000 workers, whereas Chinese companies tend to be smaller. 76% of footwear factories in China have less than 1,000 workers with an average of 897 workers. Within China, large factories are located in Guangdong, with 1,570 workers on average, whereas factories in Fujian and Zhejiang are smaller in size, employing around 500 workers.



Finding 3: Vietnamese factories tend to be larger factories, whereas the average size of Chinese factories has decreased significantly for three years in a row.

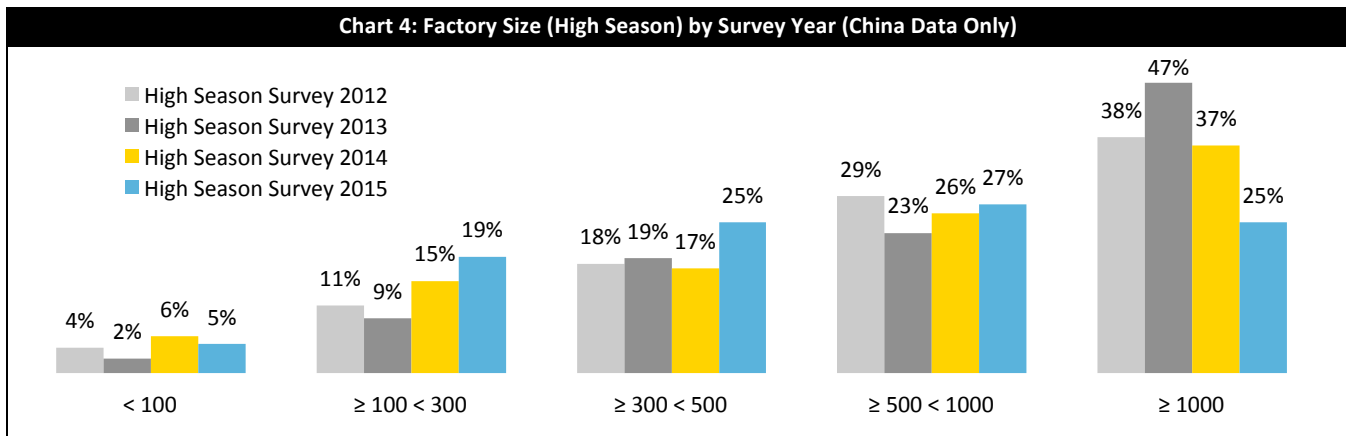
Compared to previous years, average Chinese factory size continues to drop, from 1,868 in 2012 and 1,203 in 2013 to 897 this year (Chart 3), and the percentage of large factories also fell for the third year in a row. In 2013, 37% of Chinese factories had over 1,000 workers, which decreased to 25% this year. On the other hand,



there is an increase in medium size factories with 300 to 500 workers, from 17% to 25%. This is again an indicator of the challenging situation Chinese manufacturers are facing. Factories are not only encountering growing competition overseas, but are also suffering from increasing raw material and labor costs domestically. This has led to a situation in which many factories have made a decision to downsize or even shut down. According to a study conducted by the Southern Metropolis Daily in December 2014, Chinese factories are facing an even tougher period than the economic downturn in 2008. Over two thirds (69%) of the surveyed 150 footwear factories in Dongguan, one of the most important footwear production hubs in China, experienced a decline in profits in 2014, and 23% indicated they would shut down³.

Several corporate footwear giants chose to reduce their production in China, but increase investment in the Southeast-Asian region. For instance, Yue Yuen (Pou Chen) one of the biggest enterprises in the industry, at its height had 50,000 workers in its factory in Zhongshan, Guangdong. Now this has been reduced to a few thousand workers. Similarly, one of the biggest women’s footwear producers in China – Huajian Group reduced its size from 14,000 to around 6,000 workers⁴. We can see that not only have global clients turned to other locations for cheaper production, Chinese manufacturers are also trying to relocate their production somewhere else, including Vietnam, Cambodia and Ethiopia⁵.

Table 5: “Survival Report of Dongguan Footwear Factories, 2014”	
150	Dongguan Factories Surveyed
69%	Experienced decline in profit in 2014
23%	Would choose to shut down
<i>*Source of Data: “Survival Report of Dongguan Footwear Factories”, Southern Metropolis Daily</i>	



Finding 4: In light of increasing overseas competition and operation costs, the 2015 Survey reveals a significant drop in percentage of large Chinese footwear factories, dropping from 47% two years ago to 25% this year.

³ “The Survival Report of Dongguan Footwear Factories”, Southern Metropolis Daily, December 30, 2014, accessible at <http://www.shoeshr.com/designer/log?id=75559>.

⁴ “Despite the depreciation of RMB, Chinese Footwear Factories Turn to Southeast-Asia for Opportunities”, China Business News, February 10, 2015, accessible at <http://www.yicai.com/news/2015/02/4574524.html>

⁵ *ibid*, <http://www.yicai.com/news/2015/02/4574524.html>



5.WHO ARE THE WORKERS: AGE, EDUCATION BACKGROUND AND STATUS

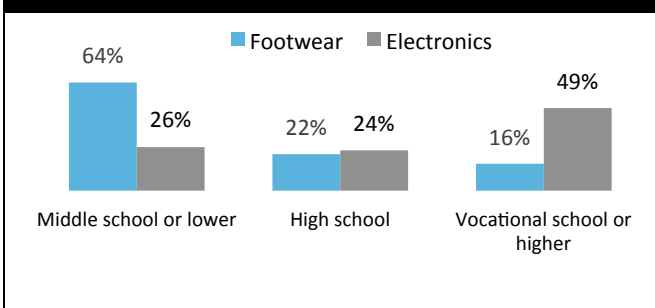
Table 5: Employee Structure

	Average Age	% Female Workers	% Domestic Migrants
Survey 2012	30	58%	67%
Survey 2013	33	61%	69%
Survey 2014	33	65%	62%
Survey 2015 (China)	34	62%	59%
Survey 2015 (Vietnam)	28	75%	40%

When taking a closer look at the employee structure of footwear factories, female workers continue to make up the majority of the workforce, both in Vietnam (75%) and China (63%).

Migrant workers represent 59% in Chinese factories, while a relatively smaller percentage in Vietnamese counterpart manufacturers. In terms of the average age of the labor force, there is a clear difference between Chinese and Vietnamese factories. The average age in Vietnam is 28, whereas in China it is 34 years old. As

Chart 5: Workers' Education Level (ELEVATE Data: Footwear and Electronics Industry)



discussed in the 2014 survey report, this reflects the change in the Chinese labor market. The latest official data reveals that the average age of migrant workers in China increased from 34 in 2008 to 38 in 2014. The percentage of workers below 40 years old dropped from 66% in 2010 to 57% in 2014, whereas the percentage of workers above 40 increased by 28% for the same period⁶.

Finding 5.1: Female workers continue to make up the majority of the workforce. The workforce in Vietnam is significantly younger than the Chinese workforce.

Nevertheless, despite the overall aging labor population, footwear factories tend to attract a relatively older workforce with limited education background than other industries. Based on ELEVATE industrial survey data, the average age of electronic industry workers is

29 years old, 5 years less than the footwear industry. 64% of workers in the footwear sector have a middle school or less level of education, whereas the percentage is significantly less at 26% in electronics manufacturers.

In line with an increased average age, this year's data also shows a continuous use of workers in retirement age. In China, the retirement age for blue-collar female workers is 50, and in the 2014 Survey 60% of respondents utilized female workers at or above this age. This year the percentage of this group increased to 78%. As discussed previously, retired workers who receive government pensions are not eligible for work contracts or social security payments. Therefore, hiring female workers above age 50 often indicates an increased risk of finding workers with no contracts or insurance in the factory. These workers also run a higher risk of being underpaid. The lack of insurance also makes this age group of workers more vulnerable in the case of

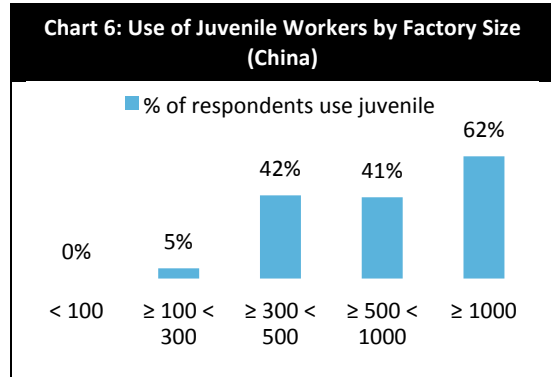
Finding 5.2: Compared to other sectors, Chinese footwear factories utilize a relatively older worker population with an average age of 34.

⁶ National Bureau of Statistics of the People's Republic of China: "Migrant Workers Report 2014", April 29, 2015, accessible at http://www.stats.gov.cn/tjsj/zxfb/201504/t20150429_797821.html.



accidents or illness.

At the other end of the age spectrum, it is evident that an increasing percentage of factories use juvenile workers. While it only represents a small percentage (on average 1% of the entire workforce), 38% of Chinese manufacturers employ workers aged between 16 to 18 to varying degrees. This is 7% more than the percentage obtained in 2013 data. In some factories, juvenile workers make up as high as 15% of the total labor force. It is a more common practice amongst larger factories (Chart 6) with 62% of factories that have more than 1,000 workers utilizing juvenile workers.



It has been discussed in previous FDRA survey reports that the use of these special categories of workers is a coping strategy in light of worker shortages and production seasonality. Factories become “creative” in terms of labor recruiting and management, which raises several non-compliance risks, such as overtime work for juvenile workers, lack of proper protection for retired workers and improper labor contract arrangement.

Finding 5.3: An increasing percentage of factories use retired and juvenile workers, suggesting that Chinese factories are getting “creative” in fulfilling labor needs and such practices are not without risk.

6. BUSINESS CHALLENGES

This year the survey also asked factories to name their top challenges (Table 6). While raw material costs remain the number one challenge for the fourth year in a row, wage and compensation cost comes forward as equally challenging. Labor shortages became less of an issue this year, but business competition for the first time is

Table 6: What Are the Most Significant Business Issues You Are Facing?

	Survey 2015		Survey 2014		Survey 2013		Survey 2012	
Raw Material Cost	1	56.1%	1	59%	1	75.8%	1	76.4%
Wage & Compensation	2	52.8%	3	40%	2	73.6%	3	51.4%
Business Competition	3	30.1%	5	19%	8	9.9%	5	29.2%
Labor Shortage	4	25.2%	2	47.3%	3	67.0%	2	55.6%
Finding Good Management	5	19.5%	6	15.5%	6	13.2%	/	/
Economic Downturn	6	15.4%	8	8.2%	9	6.6%	/	/
RMB Currency Appreciation	7	12.2%	4	26.4%	4	16.5%	4	38.9%
Worker Retention throughout the Year	8	12.2%	7	13.6%	4	16.5%	6	9.7%
Worker Retention around Chinese New Year	9	8.9%	8	8.2%	7	12.1%	/	/
Increasing transportation costs	10	8.1%	/	/	/	/	/	/
Tougher Regulation and Legislation	11	7.3%	8	8.2%	10	2.2%	/	/
Unpredictable energy availability	12	4.9%	/	/	/	/	/	/

chosen as one of the top 3 challenges. This might be explained by the fact that many factories choose to relocate, downsize or close down, and therefore the pool of available workers increases.

6.1 SEASONAL FLUCTUATIONS

Despite the overall decrease in Chinese factory size, they continue to experience seasonal fluctuations, which are even stronger than in previous years. 80% of Chinese factories have experienced low and high seasons, resulting in a fluctuation of 31%. This is up 7% from the 2014 survey. However, this is less of an issue for Vietnamese factories. 33% of factories in Vietnam experienced seasonality of production, and their average fluctuation is 5%. While such seasonal differences are relatively small compared to other industries such as toys⁷, whose fluctuation is as high as 58%, its implication and pressure on human resources and production management is still rather significant and challenging.

For one, small factories are hit the hardest by seasonality⁸ (Chart 8). Factories with less than 300

workers need to hire an additional 65% more workers when the production volume starts to soar. Such fluctuations are much stronger than in previous year's survey data. Considering the fact that small factories often have relatively limited resources for recruitment, the implication of such seasonality is likely to pose significant pressures for management and planning.

Finding 6: Despite the decline in factory size, Chinese factories experienced a stronger seasonal fluctuation than previous years. Small factories with less than 500 were hit the hardest by seasonality.

Chart 7: Seasonal Fluctuation by Industry

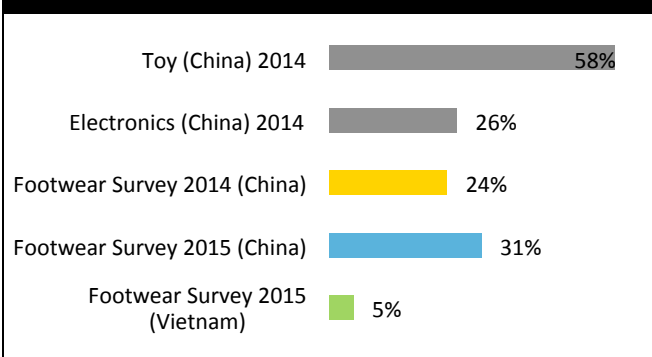


Chart 8: Seasonal Fluctuation by Factory Size (China)

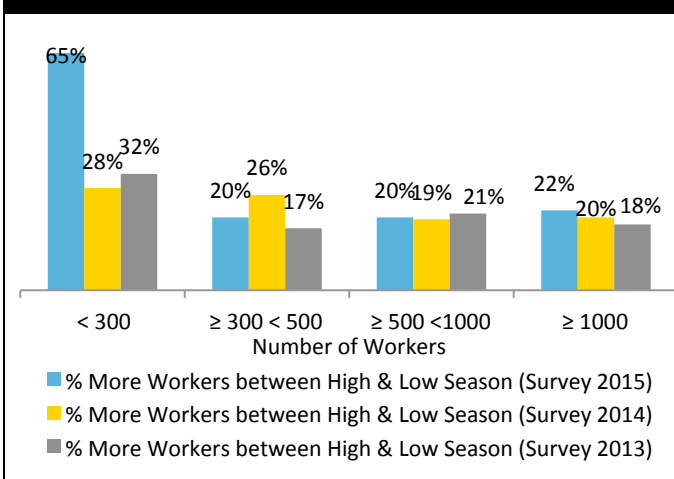
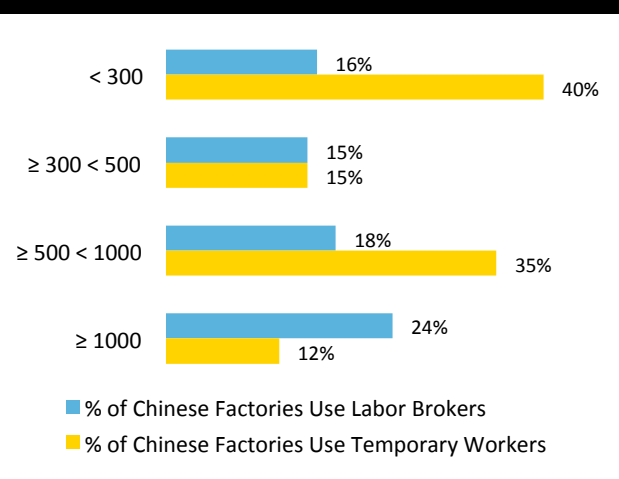


Chart 9: % Factories Use Labor Brokers (China)



⁷ Data of toy and electronics industry comes from ICTI 2014 Factory Survey Analysis Report and EICC 2014 Factory Survey Report.

⁸ One-way ANOVA analysis shows that large factories differ significantly from small factories, in terms of workforce fluctuation between low season and high season, the significance level is 0.000.



Related to the stronger seasonality and growing labor costs and business competition, the survey results show that Chinese factories turn to temporary workers during high seasons to help meet production needs. 25% of surveyed factories in China use temporary workers when production volume is high. This is particularly popular amongst small factories with less than 300 workers, 40% of which utilize temporary workers to fill the labor gap for a short period of time. The percentage of this type of worker is as high as 80% in peak season. In this report temporary workers are defined as workers that have a fixed term of contract for less than 6 months. The practice of utilizing temporary workers is often accompanied with a number of potential non-compliances, including the lack of proper labor contracts, missing complete worker profiles, delays in wage payments or wages not being paid in full and lack of complete social insurance.

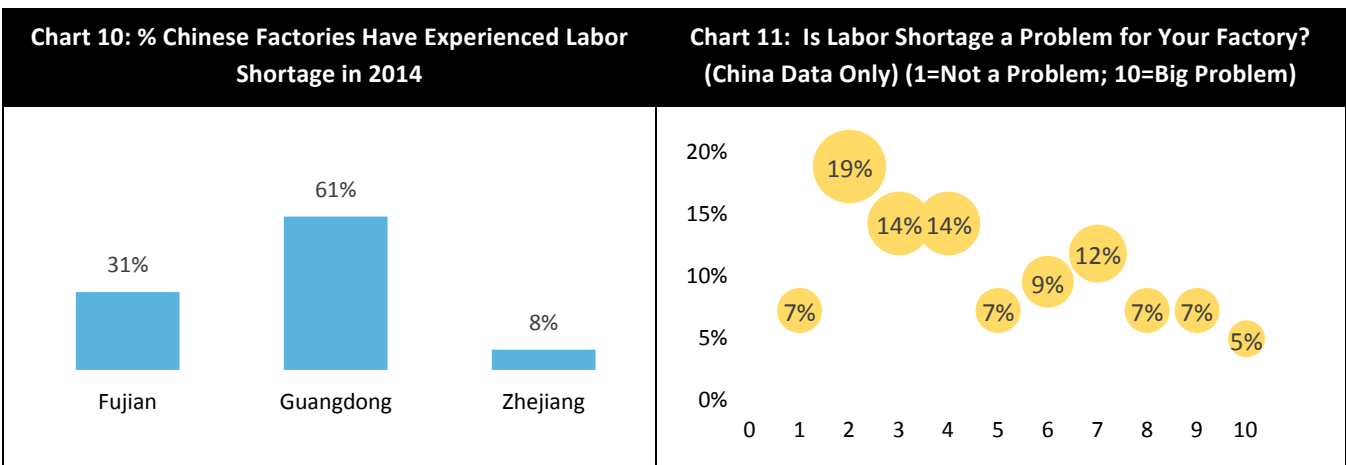
Finding 7: Chinese factories, small Chinese factories in particular, tend to use temporary workers to fill the labor gap during high seasons.

6.2 LABOR SHORTAGE

The 2014 FDRA survey report discussed in detail the background, challenges and potential impact of the labor shortage impacting the footwear industry. This trend is a result of China’s social and economic development, including the one-child policy and economic growth in interior provinces. Coastal provinces (e.g. Guangdong), which employ a large population of migrant workers and where the majority of footwear factories are located, suffer the most from this trend. In Survey 2014, 55% of respondents have experienced labor shortages, and the labor gap was on average 19%. This year a much smaller percentage of Chinese factories (40%) report that they had an issue of labor insufficiency. When asked about the level of severity on a scale of 1 to 10 (1 being not a problem at all and 10 being a very big issue) 50% of respondents gave a score of 5 or lower. 12% (5 Chinese

Finding 8: Labor shortage is reported to be less of an issue this year with only 5 Chinese factories feeling labor shortage is a serious challenge for them.

factories) chose a score of 8 or above feeling that labor shortages are a serious challenge for them. One potential explanation here is that given the less than optimal situation and the wave of factory shutdowns, the pool of available workers is larger and it is becoming less of a challenge to recruit workers.





6.3 WAGES AND COMPENSATION

Wages have long been one of the top business and compliance challenges for Chinese footwear manufacturers. Under the circumstances of labor shortages and a steady increase in minimum legal wages, factories are under

Table 8: Avg. Monthly Wage (China Data)		
	Low Seasons	High Seasons
Survey 2014	2,619RMB	3,214RMB
Survey 2015	2,889RMB	3,458RMB
% of Change	10%	8%
Avg. Hourly Rate (China Data)		
Survey 2014	9.09RMB	11.35RMB
Survey 2015	10.47RMB	11.41RMB
% of Change	15%	0.5%







increasing pressure to be compliant with wage related requirements.

In 2014, 18 provinces and city-states in China adjusted their minimum wage level⁹ with an average increase of 14%. Comparing the data from Survey 2014, the average monthly wages paid by Chinese respondents increased by 10% during low seasons, and by 8% during high season. However, such growth is still to some extent lagging behind the increase in legal minimum wages.

Considering that the self-reported wage data might be a result of long working hours, the given data on wages and working hours was used to calculate how much the factory pays per actual or real working hour. Real hours take into account that weekday overtime hours should be paid at 1.5 times the regular wage, and weekend hours should be paid double at the regular wage¹⁰. In total, 4% of respondents in China (4 factories) are providing a wage level that is below the legal minimum wage in their respective cities and provinces.

Social Insurance

Wage compliance becomes an even more complex and challenging issue due to a series of strikes that took place in 2014 and 2015 at footwear factories around the issue of social insurance. The Chinese Social Insurance Law (2011) requires all employees including migrant workers and dispatched workers to be covered by the social insurance system. Both the employer and employees are required to make contributions (at their different rates). However, as with other laws in China, this law is poorly enforced. Factories often do not make their

Table 9: % of Migrant Workers Covered by Social Insurance in the Manufacturing Sector*		
Accident Insurance  34.2%	Medical Insurance  22.1%	Pension  21.4%
Unemployment Insurance  13.1%	Maternity Insurance  9.3%	Housing  5.3%
Source of Data: National Bureau of Statistics of the People's Republic of China		

⁹ Hebei province adjusted its minimum wage level in December 2014, therefore is excluded in this analysis. Shenzhen adjusted its minimum monthly wage from 1,600RMB to 1,808RMB on February 2014. Wenzhou adjusted its minimum monthly wage from 1,327RMB to 1,490RMB on August 2014.

¹⁰ To account for the working hours and overtime premium, we divide factories into several groups by number of weekly working hours, and estimate overtime hours during weekdays and weekends accordingly. E.g. if the total weekly working hours is 72, it will be calculated using the assumption that workers work four extra hours during weekdays and the rest overtime hours are done over weekends. Similarly, if the total weekly working hours is 54, then it will be calculated assuming 1 overtime hour during weekdays and the rest are done over weekends. This calculation method is in line with common practice in the manufacturing sector. To account for the legally stipulated overtime rate we used the following formula to calculate the average hourly minimum wage: "Hourly Rate= Average Wage/ ((21.75*8 + (Number of Workday OT)*1.5 + (Number of OT during Weekend*2))".



contribution at the required rate or at all. Workers are not sufficiently informed on relevant policy and requirements. In addition, workers do not pay adequate attention to social insurance for a number of reasons. For one, Chinese traditionally have relied on a large extended family to look after them as they enter old age. Moreover, before the reform they relied on the state to take care of everything, therefore the tradition of social insurance is not well established. For another, the social security system is highly localized, and it is not easy to move individual insurance funds from the location where they work back to their hometown¹¹. According to the official data of the China National Bureau of Statistics, migrant workers in the manufacturing sector have the highest degree of coverage, yet even so, only around a third of migrant workers are covered by accident insurance, 22% have medical insurance, and 21% have a pension¹².

Nevertheless, since the retirement age in China for blue-collar female and male workers is 50 and 60 respectively, the first generation of migrant workers is at a stage that they can start receiving pension fund payments soon. Many of them are workers employed in the footwear industry, considering the fact that footwear factories utilize a relatively older workforce than other industries. Therefore this issue is particularly acute for footwear manufacturers, and this is part of the reason why many of these strikes happen in the footwear industry. It goes beyond the scope of this report to fully cover the issue of social insurance, but it will deserve closer attention in the future.

Finding 9.1: Wage level growth is still lagging behind the increase in legal minimum wage.

Finding 9.2: Social insurance is particularly acute for the footwear industry given the fact that it utilizes a relatively older workforce than other sectors.

7. WORKING HOURS AND REST DAYS

Table 10: Weekly Working Hours

	Low Seasons		High Seasons	
	Avg.	Max.	Avg.	Max.
Survey 2014	51 Hours	110 Hours	60.8 Hours	120 Hours
Survey 2015	52 Hours	80 Hours	60.4 Hours	100 Hours
% of Change	2.0%	-27.3%	-0.7%	-16.7%

Workers' Maximum Consecutive Working Days without Rest	
	Max.
Survey 2015	12.4 Days

The FDRA Code of Conduct requires factories not to exceed 60 working hours in a given week and to provide workers with one day off for every seven-day period¹³. This year's survey results show that 91% of factories are able to control their hours within 60 per week during low season,

Finding 10: While the average weekly working hours remain similar to last year, reported maximum number of working hours is much less.

¹¹"China's social security system", China Labor Bulletin, accessible at <http://www.clb.org.hk/en/view-resource-centre-content/110107>

¹² National Bureau of Statistics of the People's Republic of China: "Migrant Workers Report 2014", April 29, 2015, accessible at http://www.stats.gov.cn/tjsj/zxfb/201504/t20150429_797821.html .

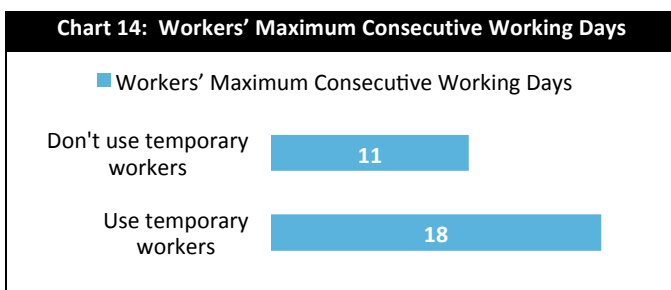
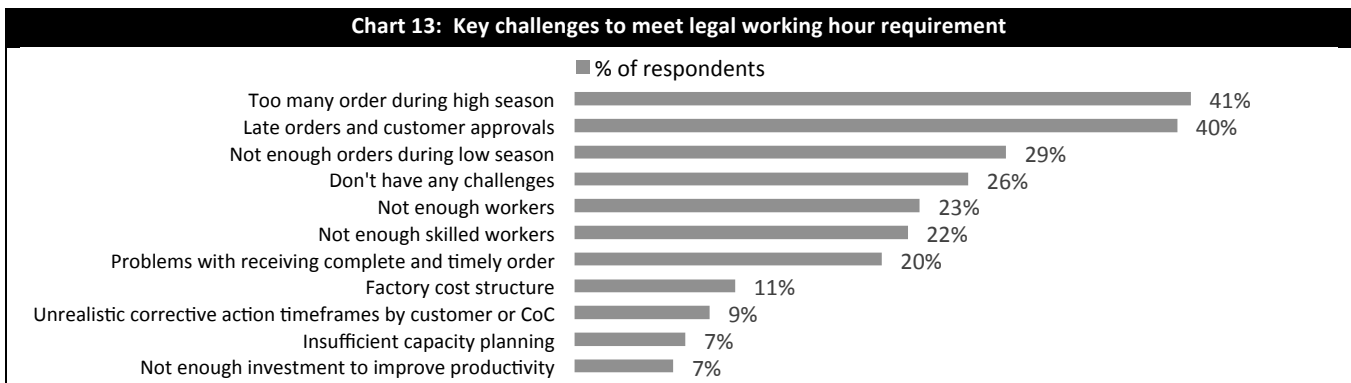
¹³ FDRA factory Code of Conduct (English)



and 64% during high season. Manufacturers have a harder time being compliant with the rest day requirement. In extreme cases, workers work 78 days in a row without a day off.

While the average weekly working hours remain similar from last year, reported maximum number of working hours is much less, decreasing from 120 hours during peak season in Survey 2014 to 100 this year. On one hand, it suggests some progress in reducing excessive working hours at factories in China. However it also reflects the challenging business situation Chinese footwear factories are going through. The increase in competition both overseas and domestically, along with growing material and labor costs, results in smaller demand in working extreme hours.

With regards to key challenges factories have in terms of meeting legal working hour requirements, 26% of respondents indicate that they don't have any challenges. For others, the top three challenges they choose are related to business. The fluctuation of business orders between high season and low season is believed to be the most challenging issue in terms of working hour compliance.



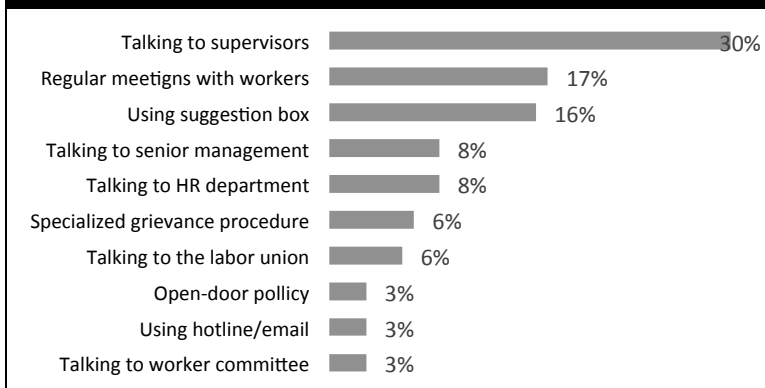
When slicing the data by factory size and employee structure, it is observed that factories using temporary workers tend to have longer consecutive working days than those who do not use temporary workers.¹⁴ This is in line with previous arguments that the utilization of temporary workers is often accompanied by a number of non-compliance risks. Because of their short-term employment by nature, temporary

workers are more vulnerable than regular workers in terms of legal protection.

¹⁴ One-way ANOVA analysis shows that factories who use labor brokers to hire workers, and use dispatched workers or temporary workers differ significantly from other factories, in terms of the maximum consecutive days their workers have worked without a rest day, the significance level is 0.029, 0.047 and 0.036.

8. ARE WORKERS GIVEN A VOICE?

Chart 15: Most Frequently Used Communication Channels



Workers are often seen as a commodity in factories, which are easily replaced, not well educated, not valuable and rarely seem to be invested in the factory's success. However, such belief is losing its popularity in the light of labor shortages, expensive recruitment costs and increasing worker strikes. Chinese factories are learning the importance of giving workers a voice and listening to what they have to say. This is the reason that the FDRA annual factory survey has put a focus on the worker-

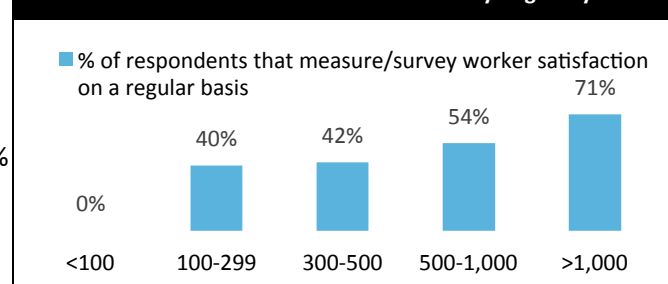
management dialogue in the past 5 years. This year's survey results show while a smaller percentage than last year, the majority of footwear factories (72%) have some sort of worker representative structure in place either in the form of a labor union or worker committee. However, a higher number of factories (71%) than last year indicate that they have worker representatives in place, who are selected by workers. In particular, amongst Chinese factories, 75% out of those that have a labor union or worker committee report that they have elected worker representatives, 12% more than the percentage shared in Survey 2014. This is likely linked to the recent incidents in footwear factories, and factories are realizing the importance of having the means to talk to workers through some sort of formal communication mechanism.

Finding 11: 24% of respondents have not received any worker feedback in the past 12 months. Among those who did, they report that one in every 100 have raised concerns.

However, as in last year, the reported number of worker feedback collected is still limited. In 2014, 24% of the respondents never received workers' complaints/issues/grievances. Among those who have, they have received an average of 15 reports from workers in the past 12 months. 77% of respondents say they received 10 complaints or less during the past year. Taking the factory size into account, this means that one in every 100 workers have voiced complaints/issues/grievances in the past year.

One potential explanation for the limited worker feedback could be that workers' feedback are not properly documented and followed up. When asked about the most frequently used channels by workers, the responses vary significantly. While supervisors are voted the most popular channel, it only represents 30% of the most frequently utilized communication channels. It is followed by regular meetings and the classic suggestion box. These findings are partly in line with ELEVATE data from numerous worker surveys that supervisors are first and foremost the channel workers use in case of questions, complaints and grievances. Yet, supervisors are not always sufficiently trained on

Chart 16: Do You Conduct Worker Survey Regularly?





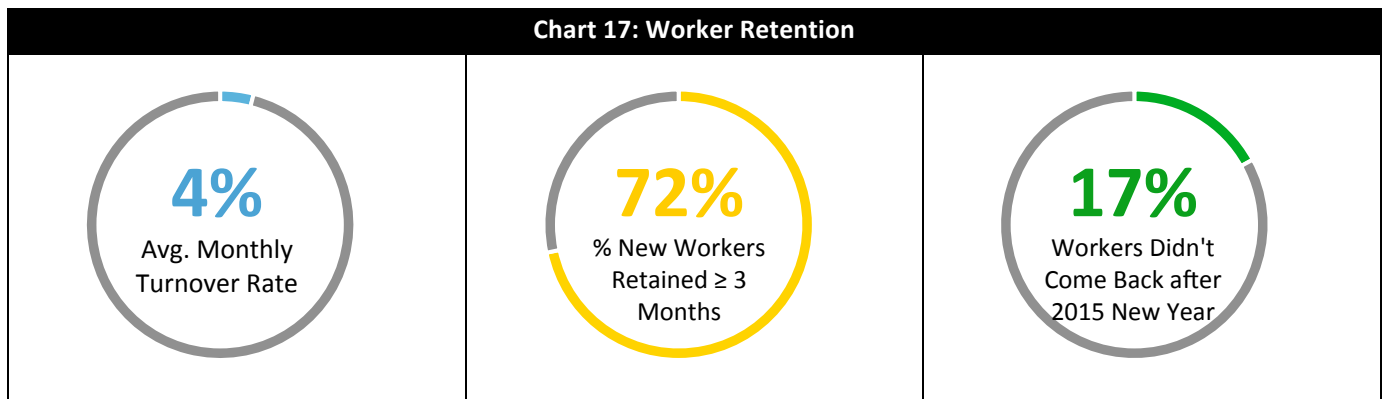
receiving and handling worker feedback. This leads to a situation that worker' grievances and complaints are not documented and followed up on properly, causing negative impact on worker satisfaction.

Finding 12: Small factories are less likely to conduct worker surveys than large factories. Considering the fact that they are the ones that are hit the hardest by seasonal fluctuations, additional support is suggested to help them better manage seasonality and its implications on compliance.

In addition, almost all (90%) of the respondents indicate that they conduct worker surveys to measure worker satisfaction in their factories. Among them, 57% organize such surveys on a regular basis. Data shows that larger factories are more likely to invest in this type of initiative rather than small and medium sized

factories¹⁵ (Chart 16). This could be due to the fact that small factories have rather limited material and human resources. Yet, they are the ones that are hit the hardest by seasonal fluctuations, and they often use temporary workers as short-term solution. Additional support is therefore recommend for these factories to help them plan around seasonality while at the same time remain compliant with relevant requirements.

9.WORKER RETENTION



Worker retention throughout the year as well as around the Chinese New Year is only voted number 8 and 9 in the list of challenges factories face, suggesting that footwear manufacturers are able to maintain a rather stable workforce. The reported average monthly turnover rate is 4%, and even during the most unstable period of time in a year, namely Chinese New Year break, only a small proportion (17%) of workers did not come back.

However, considering the fact that factories lose around 28% of new hires within the first three months and experience a seasonal fluctuation of 31%, the reported 4% is not providing a complete picture of the actual situation. Given ELEVATE's data collection experience in more than 500 factories in the past 6 years, factories do

Finding 13: Factories report an average of 4% of monthly turnover rate, which is believed to be overestimating the stability of the footwear workforce and not taking into account the turnover of temporary workers.

not necessarily have sufficient resources and/or monitoring systems in place to properly track and calculate worker turnover.

¹⁵ One-way ANOVA analysis shows that large factories differ significantly from small or medium factories in terms of whether they measure worker satisfaction on regular basis, the significance level is 0.006.



In addition, as mentioned previously, an increasing number of Chinese factories use temporary workers during high season, and this group of workers is often not taken into account when calculating worker turnover.

10. CSR AND EHS MANAGEMENT

Nearly all respondents indicate that they have personnel responsible for CSR and/or factory compliance performance, and the majority (61%) have dedicated staff working on this issue full time. Vietnamese factories seem to have a higher percentage of factories that have a responsible staff (73%) than Chinese counterparts (60%). Similar to the 2014 survey, this year respondents indicate that the top three environmental requirements are waste disposal (68%), recycling (59%), and waste water (52%).

Chart 18: Issues that Customers Have Specific Environmental Compliance Requirements		Table 15: Existing Procedure to Evaluate Health and Safety Risks		
Waste disposal	68%		Survey 2015	Survey 2014
Recycling	59%	Fire safety	81.3%	92.9%
Waste water	52%	Chemical management and safety	78.0%	88.8%
Energy reduction	49%	Occupational diseases	70.7%	78.6%
Air pollution	38%	Machinery safety	65.0%	78.6%
Package reduction	33%	Electrical safety	64.2%	77.6%
		Building structural safety	44.9%	52.0%
		Confined spaces management	38.2%	41.8%

The majority of surveyed factories report that they have existing procedures to evaluate risks in relation to fire safety (81%), chemical management and safety (78%), and occupational diseases (71%). Comparing the result with Survey 2014, the percentages of factories with relevant procedures declined across the board. This might be related to the fact that this year

Finding 14: Nearly all surveyed factories indicate that they have dedicated staff for CSR and compliance issues, and 61% of them have full time personnel devoted to this matter.

the scope includes responses from Cambodia, Guatemala and other emerging manufacturing countries, which are relatively new in social and health and safety compliance and lacking related procedures¹⁶.

11. AUDIT EXPERIENCE

Data shows that more factories are being assessed or audited for social compliance related violations. In the 2014 survey, 7% of surveyed factories had not been assessed, which decreased to 5% this year. On average, respondents experience 7 external social compliance audits per year, which is at least one audit every other month. 14% of factories have had more than 12 audits, meaning at least one audit each month. This percentage is nearly doubled from last years' survey result. Slicing the data by country, we can see that Chinese factories

¹⁶ One-way ANOVA analysis shows that factories from China and Vietnam differ significantly from factories in other countries in terms of whether they have existing procedure on chemical management and safety, and occupational diseases, the significance level is 0.016 and 0.005.

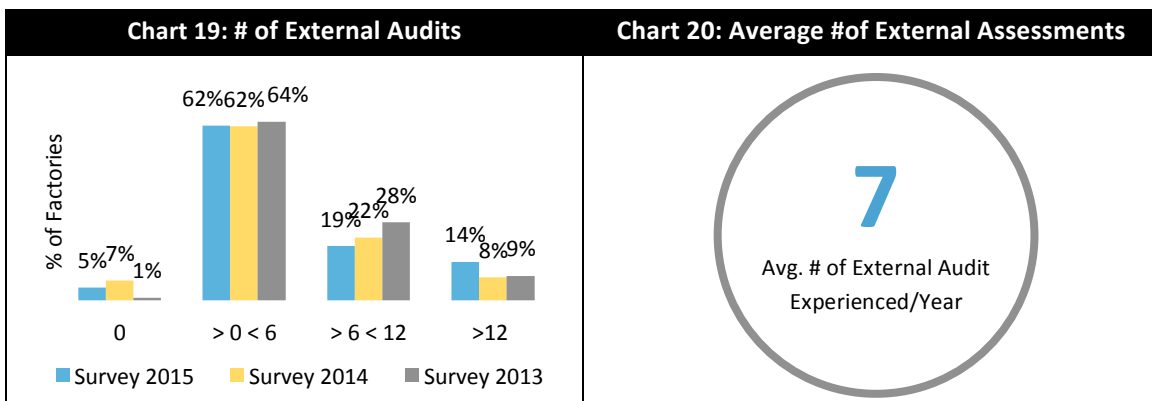


have experienced more audits than manufacturers in other countries¹⁷. Chinese factories on average had 7 audits, whereas it was 4 audits per year for Vietnamese factories.

To better understand the impact of assessment on factories' social performance, the number of assessments factories experience per year is correlated with a number of factors, including communication systems, wage compliance, worker turnover and employee structure. The analysis shows that:

Finding 15: More factories are being audited. On average footwear factories experience at least one audit per every other month.

- Chinese factories that have experienced more audits in the past year tend to have conducted more fire drills than others¹⁸.
- However, factories with frequent audits are not more likely to have a full time staff responsible for CSR and compliance matters.
- Neither are they in a better position in terms of seasonal fluctuation, wage compliance or worker retention. In other words, factories that have been assessed multiple times do not necessarily perform better than those that have been audited less.



12. HOW WELL DO YOU KNOW FDRA'S CODE OF CONDUCT?

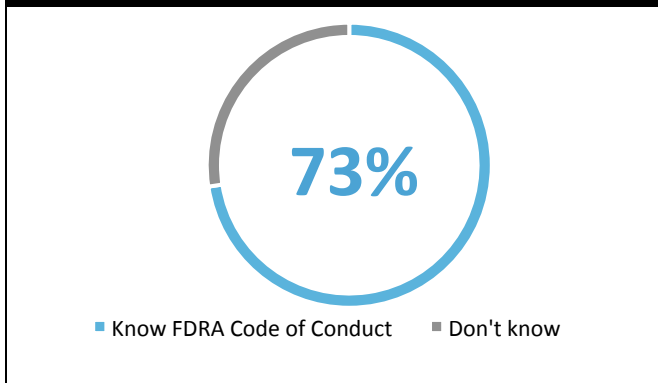
In July 2014, FDRA developed and released a comprehensive Footwear Production Code of Conduct, aiming to establish a common, baseline code that will help drive uniformity within the footwear industry, and help clearly communicate and uphold the social norms and values commonly held by FDRA members. In this context, this year's survey added several questions to assess member factories' awareness of the FDRA CoC and its perception.

¹⁷ One-way ANOVA shows that factories in China and Vietnam differ significantly in terms of number of external assessments they experience, the significance level is 0.014.

¹⁸ The correlation between how many external social compliance audits factories have experienced and the number of fire drills conducted in factory is significant, $r=0.240$, $sig=0.031$.



Chart 21: Do You Know about FDRA's Code of Conduct?



73% of survey respondents have heard about the FDRA Code of Conduct. No difference is observed between Vietnamese and Chinese factories, yet none of the surveyed factories in Cambodia, Guatemala and Mexico are aware of the FDRA CoC.

Among those who know, only 13% think the Code of Conduct is easy to comply with, with the vast majority (87%) feeling it is challenging to meet. Vietnamese factories appear to be more confident than Chinese manufacturers, 29% of them find it

easy to comply with, whereas the percentage is 11% amongst Chinese factories.

Finding 16: 73% of surveyed factories have heard about the FDRA Code of Conduct. Among those who have, the majority find compliance with the Code to be challenging.

13. SUMMARY

The 2015 FDRA factory survey reveals that despite the overall growth in production volume, Chinese factories are facing increasing competition from emerging producing countries. China's share of shoes imported by the US declined by 3% from 2013 to 2014, whereas the proportion of imports into the US from Vietnam increased by 19% during the same period. Manufacturers in China are also suffering from continued domestic challenges in regards to labor shortages and increasing labor and material costs. The survey data observes a decline in the size of Chinese factories for three years in a row. The average number of workers employed per factory decreased from 1,868 in the 2013 survey to 897 this year.

Wages continue to be a top challenge for Chinese factories for a number of reasons. For one, the legal minimum wage level continues to increase, and factories struggle to keep up. The social insurance issue also contributes to the added complexity of wage compliance. This issue was highlighted in a series of strikes that took place in 2014 and 2015 at footwear factories. Given the fact that the footwear sector employs a relatively older workforce, many of whom are first generation migrant workers and who will soon be eligible for pension fund payments, challenges related to social insurance are particularly acute for footwear manufacturers.

As in previous years, 2015 survey results further confirm that labor shortages and strong seasonal fluctuations result in factories becoming "creative" with regards to hiring and recruitment. An increasing number of footwear factories are utilizing retired, juvenile and temporary workers to fill labor gaps. Such practices are accompanied by a number of non-compliance risks, including improper contract arrangements and lack of social insurance and protection for retired and juvenile workers.

The survey further shows that although factories recognize the invaluable contribution workers make to their business and the importance of effective communication with workers, the collection of worker feedback is still limited, improperly documented and underutilized.



Lastly, this survey shows once more what FDRA's Factory Survey has demonstrated for several years now - there are limits to the effectiveness of social compliance auditing. There is no evidence suggesting that assessments have a positive impact on factory performance with regards to working hours, wages, communication and health and safety. FDRA members, buyers and suppliers need to realize the importance of diversified compliance management, utilizing a variety of tools, resources and efforts to support footwear manufacturers and elevate their compliance and business performance.