

The Solidarity Fund and Gildan Activewear, Inc.

In late 2003, officers of the Solidarity Fund, a large pension fund operated by the Québec Federation of Labor (QFL), met to discuss what to do about their investments in Gildan Activewear, a Montreal-based textile and garment company.

Over the previous year, public controversy had swirled around the company's labor practices in its manufacturing plants in Central America. In January 2002, a television documentary aired by the Canadian Broadcasting Corporation (CBC) charged that Gildan's workers in Honduras earned less than a living wage, worked long shifts, had excessively high production quotas, and breathed air filled with fabric dust. Just a few months later, a labor rights group issued a report claiming Gildan had fired Honduran workers who had tried to organize a union. These charges presented the Fund, which owned 14 percent of Gildan, with a difficult dilemma. The textile company had been an excellent investment; its stock had risen in value from just over \$2 (Canadian) per share when the fund first invested in 1995 to nearly \$12. However, if the allegations were true, the company's practices would run counter to the basic values of the Fund. Should the pension fund try to influence Gildan's conduct? Should it sell its shares in protest? Or should it do neither?

The Solidarity Fund

The Québec Federation of Labor (QFL), an alliance of unions in the Canadian Province of Québec representing more than half a million workers, founded the Solidarity Fund in 1983. At the time, Québec was mired in a deep recession. High interest rates had put many small and medium-sized businesses into bankruptcy, and nearly a quarter of the province's young people and more than 14 percent of its workforce were unemployed. In an effort to rethink the role of unions in promoting economic development, the QFL launched a new fund designed to invest its members' retirement savings in local companies. With the unionization rate in Québec above 40 percent (compared with around 30 percent in Canada as a whole and around 13 percent in the United States), the federation believed it could have a significant impact.

The Solidarity Fund had two central goals. Its first goal was to democratize access to professionally managed retirement accounts. A network of volunteer local representatives signed up shareholders who directed savings to the Fund. Unionized workers made up close to 60 percent of the Fund's shareholders (the rest were unaffiliated individuals). Participants typically used the Fund as a supplement to an employer-provided pension.

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Under law, savings invested in the Fund were locked in until retirement, except in special circumstances such as job loss or periods of retraining. The Fund's second mission was to support job growth in Québec, either through long-term investment in small and medium-sized local companies or by investing in outside companies whose activities benefited the province.

Although the Fund sought to give its shareholders a fair return, it also used nonfinancial criteria in selecting investments. Its managers looked to invest in companies with good working conditions, positive relations with local communities, and a commitment to environmental responsibility. It also looked for companies that were open to partnering with institutional shareholders, such as the Fund. The Fund did not, however, have an absolute requirement that a company in which it invested be unionized.

As part of its due diligence, when it first invested in a company—and later when it increased its investment or divested—the Fund prepared a social audit. Between 1983 and 2002, the Fund team prepared nearly 2,000 social audits. Fund specialists would visit a company to gather data, observe working conditions, and meet with company managers and employee representatives. The social audits, which were not made public, sometimes identified issues of concern and made recommendations for improvement, which were often addressed in collaboration with the company's management. Once invested, the Fund played an active role in the company as a shareholder, sometimes by placing a member on the board of directors.

Many of the Fund's 400 employees, particularly its development officers and subscription staff, came from a union background and were loyal to the interests of organized labor. The Fund's financial officers, by contrast, were generally trained in the field of finance and saw their main goal as meeting the Fund's financial goals. Major investment decisions often reflected a creative tension between the unionists and the financiers. The final decision, however, rested with the Fund's 17-person board, 11 of whom were union representatives. The president, general secretary, and other executives of the QFL often came from high positions in QFL-affiliated unions, such as those representing metalworkers, Canadian public service employees, and construction workers.¹

Some two decades after its launch, the Solidarity Fund had 500,000 shareholders and net assets of more than \$4.6 billion, making it a crucial financial player in Québec's economy. (This dollar amount, and all others cited later in this case, are given in Canadian dollars, unless otherwise noted.) It had invested in the start-up, development, and growth of 1,800 Québec companies, some of them leading success stories, such as the transport company Transforce, the pharmaceutical company Biochem Pharma, the travel agency Transat, and the insurance firm SSQ. One of its biggest success stories was Gildan Activewear, Inc.

Gildan Activewear, Inc.

Glenn and Greg Chamandy, two brothers from a family of textile entrepreneurs, and their associate Edwin B. Tisch founded Gildan Textiles, Inc., in Montreal in 1984. (The company later changed its name to Gildan Activewear, or—in French—*Les Vêtements de Sport Gildan*.) The company's goal was "to be the world leader in quality knitwear for the North American and international markets, with the lowest operating costs."² The company's core business was producing low-cost T-shirts and fleece garments that could

¹ Solidarity Fund QFL Board of Directors, www.fondsftq.com/internetfonds.nsf/vWebTAN/AprCon.

² www.gildan.com.

be customized by institutional clients such as schools, universities, and companies with their own logos and designs. Its strategy was to compete on the basis of low prices, good quality, and fast delivery times through vertical integration of its supply chain. In contrast to many textile manufacturers, which relied on subcontractors, Gildan generally owned and operated its own factories. When it did turn to subcontractors, it required that the subcontractor be a dedicated operation, supplying to it alone.

In its early years, Gildan maintained all its operations in Québec, which had been home to a thriving textile industry throughout much of the 20th century. The manufacture of T-shirts required multiple steps: the fabric had to be knitted, washed, and dyed, and then cut and sewn into garments. Gildan operated three factories in Montreal, one each for knitting, dyeing, and sewing, as well as a corporate headquarters; collectively, these operations at their peak employed more than 1,000 workers. But in the early 1990s, in an effort to compete with its main rivals, Fruit of the Loom and Hanes, Gildan began moving some assembly operations, particularly sewing, to subcontractors in Mexico. In addition, the company decided it wanted its own manufacturing capability abroad, and it devised a plan to buy or build several state-of-the-art factories in Honduras, a small country in Central America. This was a risky move in the short term, and several banks Gildan approached for financing turned the company down.

In 1995, Gildan contacted the Solidarity Fund for help in financing its expansion. In reviewing this request, the Fund recognized that Gildan's expansion abroad would likely cost some production jobs in Québec, but thought it would also protect and possibly expand Canadian jobs in design, marketing, finance, and other headquarters functions. Some manufacturing would also remain, it concluded. In early 1996, the Fund invested \$3 million directly in Gildan stock and lent the company another \$3 million.

Gildan's operations, both in North America and Latin America, proved to be extremely efficient, and in the years from 1996 to 2001, Gildan's annual growth ranged from 20 to 30 percent. Very quickly, Gildan took market share from its two leading competitors, Fruit of the Loom and Hanes. Feeling threatened, those companies launched major advertising campaigns to counter their new Canadian rival, but to no avail. Gildan's stack of contracts grew, and in 1998, its sales reached nearly \$200 million with a market share of more than 10 percent.

The same year, Gildan was listed for the first time on the Toronto and New York stock exchanges. Hoping to raise an additional \$60 million in capital through its initial public offering, Gildan was disappointed to obtain only \$30 million. Once again, Gildan turned to the Fund, which provided a loan in 1998 worth \$15 million (on top of \$12 million in 1997). In 1998 and 1999, Gildan purchased two factories in Rio Nance and El Progreso, Honduras, which were equipped with new equipment and modern technology. Gildan began to transfer jobs from Montreal to Honduras and had soon doubled its production and sales volume.

Gildan pursued a vertical integration strategy, organizing different stages of production to exploit the relative competitive advantages of various locales. The sewing was done in Mexico and Honduras, where labor was cheap; the cutting, in the United States to reduce customs duties; and the dyeing and knitting, in Québec where water and electricity were abundant. The company's acquisition in 2001 of a spinning mill in Long Sault, Ontario, which guaranteed a steady supply of cotton yarn, was the final step in its vertical integration strategy.

By the end of 2001, Gildan was producing 14 million dozen T-shirts annually. The company had 8,000 employees in North and Central America. With sales of more than \$500 million, it for the first time surpassed its leading competitor, Fruit of the Loom, which filed for Chapter 11 bankruptcy protection the same year. During the 2002 financial year,

Gildan posted record profits of \$42 million, despite closing its factory on Clark Street in Montreal. The same year, salaries of its three top executives collectively rose from \$1.5 million to \$13.3 million—an increase of more than 800 percent. Gildan's president, Greg Chamandy, earned \$5.8 million (mainly in stock options), going from 110th to 6th on the list of best-paid business executives in Québec.³

Gildan was proving to be an excellent business partner for the Fund; it repaid principal and interest on the Fund's loans in good time, and its stock continued to appreciate. The Fund felt it had contributed to the growth of a Québec company that was undergoing strong expansion and had a solid financial base characterized by limited debt and significant cash flow.

Honduras

Gildan believed that much of its success hinged on its decision to move a large share of its production to Honduras. In the early 2000s, Honduras, a small nation in Central America with a population of 6 million, remained one of the poorest countries in the Western Hemisphere, with a GDP per capita of less than \$1,000 (U.S.) per year. Two-thirds of Hondurans lived below the poverty level, and 44 percent lived on less than \$2 (U.S.) a day. In 2000, Honduras ranked 119th (out of 179) in the world on the Human Development Index (HDI).⁴

In the early 1990s, the government of Honduras began to set up export processing zones (EPZs), designated areas in which foreign companies were exempt from import duties, taxes on equipment, property and capital, and national and municipal taxes on revenues for the first 10 years of operation. Companies could return home with no limits on repatriating profits or capital. In 1998, the government extended those advantages across its entire territory. Some 30 industrial parks were built, most of them private, mainly near Puerto Cortes, the leading Caribbean seaport, and in San Pedro Sula, one of the country's major ground transportation hubs. The industrial parks and the EPZs were considered offshore operations, and duties were charged on products made there for sale in Honduras.

The clothing and textile industry was quick to respond to these incentives and, by 2002, accounted for 90 percent of the companies operating in the EPZs. The garment industry created 100,000 jobs in Honduras between 1992 and 2002. Eighty percent of them were held by women, most between 18 and 25 years of age. During this period, Honduras became the third largest exporter of textiles and apparel to the United States.⁵ In a country where unemployment reached 28 percent in 2001, the *maquiladoras* (foreign-owned factories) and the more than 125,000 jobs they provided had become a vital part of the Honduran economy.

In 2002, the basic minimum hourly wage was 63 cents (97 cents, all costs included), or \$5.58 (U.S.) per day. Under Honduran law, the maximum allowable workday was 13 hours, and the maximum allowable workweek was 44 hours for daytime work. Overtime and night shift work were compensated at a rate that was 25 percent above the regular wage. Employees also received social security contributions, as required by Honduran law, and an extra 13th month's pay (called an *Aguinaldo*), traditional in many Latin American countries.⁶

³ SEDAR, Circulaire de la direction, Gildan, February 9, 2003.

⁴ Panorama de l'espace Caraïbes 2004, INSEE, www.insee.fr/fr/insee_regions/guadeloupe/publi/pano_economie.htm.

⁵ The investment climate in Honduras is described at <http://strategis.ic.gc.ca/epic/internet/inimr-ri.nsf/fr/gr123052f.html>.

⁶ Central American Business Consultants, http://www.ca-bc.com/zip_internacional.

Although unions were permitted in Honduras, they were generally weak. In 1954, a general strike had laid the basis for the Honduran union movement and led to a new labor code that guaranteed workers' right to form unions. But in the early 2000s, only about 20 poorly trained inspectors enforced the labor code. The high turnover of both firms and workers in the *maquiladoras* tended to limit union success. Mounting violence associated with youth gangs (*maras*) established a climate of fear and mistrust that also discouraged union organizing. Within the *maquiladoras*, only about 1 in 10 workers were union members (compared with about 25 percent in Honduras as a whole). Many workers had turned to other institutions for protection, including local development agencies, labor support groups, and churches.⁷

By 2002, Gildan had more than 5,000 employees in Honduran factories that it owned directly. Some of those jobs had been transferred from factories in Montreal, including one on Clark Street that shut down permanently in 2002. At the time of that closing, Gildan's management talked publicly about "problems in finding labor to work in [our Canadian] sew[ing] factories. In the South meanwhile, there is a pool of desperate labor."⁸ The Canadian workers were more productive, but the difference in salary was enormous: an employee in Montreal earned more in one hour than a Honduran did in one day.

■ The Solidarity Fund's Social Audits of Gildan

In 1999, Solidarity Fund's management, concerned about the transfer of jobs from Québec to Honduras, asked Daniel Bourcier, one of the Fund's development officers, to undertake a new social audit of the company.

After visiting the Montreal factory on Clark Street as a basis for comparison, Bourcier left for a week's visit to Honduras, accompanied by Gildan's executive vice president, Edwin B. Tisch. Gildan put a car and driver at Bourcier's disposal and gave him full access to its staff, facilities, and books. During that week, the Fund officer visited three Gildan facilities and three subcontractors in the San Pedro Sula area and another in Tegucigalpa and also met with Gildan's local managers.

During his visit, Bourcier was pleasantly surprised by Gildan's newly constructed factories. Located in closed compounds with armed guards at the gate, the modern buildings were equipped with good lighting and up-to-date sewing machines. However, Bourcier identified three issues of concern. The first was dilapidated facilities and substandard working conditions in plants that supplied Gildan. The audit recommended that Gildan cease all dealings with these contractors. The second issue was the high level of cotton dust in the plants—well above standards acceptable under Canadian occupational safety laws.

The third issue involved the production system in the Gildan factories, under which workers were paid based on the productivity of their team of 12 people. The more each team produced, the higher the pay of each member. Each team was responsible for its own discipline. A quick worker would be given a green flag, and one who was slower, an orange flag. If a worker was much slower than her colleagues, the work team could give her a red flag and send her back to the sewing school, causing her a significant loss of income. The social audit found it unacceptable that Gildan had transferred responsibility for discipline from management to the work team.

⁷ UN Committee on Economic, Social, and Cultural Rights, July 2001.

⁸ Katia Gagnon, "Gildan, les rois du t-shirt (Gildan: the T-Shirt Kings)," *La Presse*, March 24, 2001.

After the audit had been completed, the Fund presented its concerns to management. Gildan's responded that its production system was completely legal, and sending people for retraining was rare. Gildan also insisted that its system gave workers salaries much higher than the minimum wage. Moreover, the company said, the workers could always form a union if they were dissatisfied. The Solidarity Fund decided after this conversation to maintain its investments in Gildan, at least for the time being, but it remained concerned.

Public Controversy

In 2002, the Canadian Broadcasting Corporation (CBC) television program *Disclosure* ran an exposé entitled "Sewing Discontent." The show's producers had investigated allegedly deplorable working conditions in Gildan's El Progreso factory in Honduras. The report mentioned extremely high production quotas, wages that did not cover even basic needs, wages based on productivity, supervised breaks, 11-hour days, poor air quality in the shops, illegal firings, and forced pregnancy tests. In one scene, the program showed young women working at a furious pace in noisy and dusty conditions.

Mackie Vadicchino, Gildan's vice president for corporate affairs, denied these allegations, saying,

We do have excellent working conditions. . . . Many people want to work for Gildan because of our wages, because of our benefits, because of our facilities. . . . One of the visions of [the founders] has always been to prove to the world that this industry can be profitable, and not just profitable but very profitable, and maintain excellent working conditions for their employees. . . . We've become an industry leader in a relatively short period of time. However, there are others that aren't so happy about us having gained that market share. . . . I think that [the employees] lied to you. . . . I think that they were coerced by someone, coached by someone, to say things to you to make us look bad.⁹

After the CBC exposé, the Maquila Solidarity Network (MSN), a North American labor rights organization, and Equipo de Monitorio Independiente de Honduras (EMIH), an independent nonprofit monitoring agency in Honduras, undertook a review of Gildan's practices in Honduras. Several months later, MSN gave Gildan its preliminary report and asked for comments. Their findings included

. . . wages that do not meet basic needs, excessively high production targets, the impact of the 4 × 4 work schedule (4 consecutive 11-hour workdays), and the effects of the intensive pace of production on women workers' health and family life, failure to provide day care and nursing facilities as required by law, lack of freedom of association, and workers' belief that new employees are tested for pregnancy and those found to be pregnant would be fired.¹⁰

That same month, MSN also received reports from Honduras that 38 workers at the company's El Progreso factory had been fired shortly after applying to the Ministry of Labor to register a union. At MSN's request, EMIH interviewed the workers and drafted a report on the circumstances surrounding the firings. When MSN representatives met with Gildan to discuss the findings, the company denied that union activity had been the

⁹ "The Gildan Story," *Disclosure*, CBC, www.cbc.ca/disclosure/archives/0222_gildan/story.html.

¹⁰ MSN Gildan Campaign Updates Gildan, <http://en.maquilasolidarity.org/gildan>.

cause of any dismissals at the El Progreso plant. It also refused to reinstate the fired workers or to contact the Ministry of Labor to determine if the workers had applied to register their union prior to the firings. MSN called on the company to cooperate with an independent investigation into the firings and other workplace issues documented in the MSN/EMIH report.

Gildan's Social Responsibility Initiatives

Gildan itself—as well as some others in government and the community—held a contrary view that the firm was an exemplary employer.

In 2003, Gildan accepted the Award for Excellence in Corporate Social and Ethical Responsibility. Sponsored by the Nexen Corporation, this award was given to companies that had directly helped developing countries or countries in transition to progress socially and economically. In announcing the award, Susan Whelan, Canada's Minister for International Cooperation, praised the company as

a prime example of how a company can combine business success with corporate social responsibility. Gildan's employees and business partners benefit from a code of ethics and behavior that values diversity, dignity, fairness, and equal opportunity for all.¹¹

Whelan referred to Gildan's own code of ethics, which it attached to contracts given to its business partners and subcontractors. Those partners and sources had to comply with the code or risk the cancellation of their contract. The company had introduced an audit procedure to check for compliance. Gildan management described the process of auditing: "The various factories undergo several inspections a month. We make sure they employ no one under 18 years of age, and that the environment is acceptable and safe and comfortable."¹²

In its 2003 annual report, Gildan emphasized that it offered its employees in Honduras

well-paying jobs with attractive benefits. . . . Gildan's Honduran employees work in modern air-conditioned and clean facilities and their wages are generally twice the national minimum wage for the apparel sector. The company provides many benefits, such as access to free medical assistance, subsidized transportation to and from work, subsidized meals, and filtered water. The company also empowers workers by providing them the opportunity to upgrade their skill sets and education levels. School classes are offered so employees can earn their diplomas, and extensive on-the-job training is also provided to employees. In addition, Gildan sponsors family days, where employees are encouraged to invite relatives to visit the facility and share lunch with them at the company's expense, in order to foster employees' pride about their jobs and for their relatives to better understand the type of work they do.¹³

Above all, Gildan insisted, it provided jobs in a country with rampant unemployment, especially among women. At the same time, Gildan highlighted its environmental achievements. According to the 2003 annual report, these included

¹¹ Gildan 2003 Annual Report, p. 23, http://gildan.com/corporate/downloads/annual_report_2003_en.pdf.

¹² Campaign Updates.

¹³ Gildan 2003 Annual Report.

the operation of biological wastewater treatment systems in Honduras, the production of environmentally friendly products, and the use of safe, clean, and energy-efficient manufacturing procedures and inputs. . . . All chemicals, dyes, and materials that are used in Gildan production facilities are selected and monitored to ensure that they have been approved for use by the appropriate regulatory authorities, and that they present no adverse effects to health or the environment. In addition, production processes are controlled to ensure reduced energy and water consumption and to minimize effluent discharge.¹⁴

The Controversy Continues

Even as Gildan touted its own social and environmental responsibility, it continued to attract criticism from NGOs and activists. At the 2003 annual shareholders' meeting, MSN, Oxfam Canada, and Amnesty International publicly accused Gildan of illegally firing employees for union organizing at Gildan's El Progreso factory. They also cited Gildan's failure to give a reason for the firings, threats by supervisors regarding union activities, and failure to respond to three summons from government workplace inspectors. The Solidarity Fund, along with bulk purchasers of Gildan products, including the state of Maine and several universities, joined the NGOs in requesting an independent, third-party investigation of the firings for union organizing, and recommended to Gildan that it speed up its application for membership in the SA8000 (a set of standards developed by Social Accountability International). (Gildan had earlier indicated it planned to do so.)

Under pressure to allow an independent investigation of the allegations at El Progreso, Gildan's management asked the Fund whether, as a long-time partner and investor, it would be willing to conduct the investigation. Although this was not the Fund's preferred approach, it nevertheless agreed to do so. At the end of March 2003, Fund officers Bourcier and Audette left for their week's mission in Honduras. The first few days were devoted to gathering information at meetings with representatives from the union, the main labor federation, EMIH, and the Jesuits (a Catholic religious order), as well as with labor law experts. They collected documentation, including photocopies of the request for unionization filed by the workers with their signatures. The final day was devoted to factory visits and an examination of internal documents, made available by Gildan management. Recalled Bourcier,

In the documents we obtained, we had the list of fired workers and the list of signatories to the request for union accreditation. The names were the same. So we opened the files, and found copies of the severance checks made out to the workers. I could see they all had the same letter of resignation, almost to the letter.

After checking that the productivity of the workers who had been let go was at least as high as the average, the Fund's auditors were convinced that the workers had been fired for trying to form a union.

Pressure on the company grew even stronger in July 2003, when EMIH and MSN released their report, *A Canadian Success Story? Gildan Activewear: T-Shirts, Free Trade and Worker Rights*, which detailed their evidence of bad-faith practices and abuses of worker rights. The report reiterated the request that Gildan apply corrective measures, including rehiring the fired workers.

¹⁴ *Ibid.*, pp. 24-25.

Gildan categorically denied the charges made by both the Fund and MSN/EMIH, explaining that the firings were the result of a downturn in the industry. In addition, Gildan reiterated that it maintained high social standards and directly challenged the investigative methods used by MSN and EMIH, and threatened to sue the two groups. Gildan argued that local unions were unreliable, and it denounced the labor code as antiquated.

The Solidarity Fund and Gildan

In November 2003, three Solidarity Fund officers, Bourcier, Audette, and Laporte, sat down to talk. The intense media focus on the allegations against Gildan had created a serious dilemma for the Fund, which was heavily invested in a company that appeared not to respect the values that lay at the very core of its operations. The officers needed to make a recommendation to the board and top management of the Fund within the next few days on what to do about their investments in Gildan Activewear.

One option was for the Fund to continue doing what it had been doing—to keep fully invested in the company and to continue its regular social audits. Another option was to divest completely—to sell its stock holdings in the company and to call in its loans. Selling would give the Fund a more than 1,000 percent return on its investment over seven years; but that return could potentially be even higher if it stayed invested. A final option was to keep its shares and to step up its efforts to influence the company's behavior. The officers were aware that the Fund enjoyed significant leverage: it was a major shareholder, had a representative on the board, and had worked closely with the company for many years. But it had already been working for many months to influence the firm's practices. In the Fund's officers' view, they had received, at best, mixed messages from the company—and mixed results in their efforts to shape its behavior.

Discussion Questions

1. What is the purpose of the Solidarity Fund? Do you think it represents an example of social investment? Why or why not?
2. Do you believe the evidence in the case shows Gildan Activewear to be a socially responsible company, or not?
3. What evidence do you find in the case of the benefits and of the costs of globalization?
4. In what ways did the Solidarity Fund attempt to use its position as an institutional investor to try to influence Gildan Activewear?
5. What are the arguments for and against a decision by the Solidarity Fund to divest from (sell its investments in) Gildan Activewear?
6. What do you think the Solidarity Fund managers should do now, and why?