
A Business Model for Bangladesh

By [Serguei Netessine](#)

Following the collapse of the Rana Plaza factory building in Bangladesh in April, which caused the deaths of over 1,000 people, many commentators pointed to the absence of building codes, lack of workplace safety rules, and the greed of corporations. But there are business model solutions that can improve supply chain compliance.

Many of the solutions proposed are around paying people more to manufacture in the USA. But however well intentioned the ideas are, this is not the best use of one of the most productive workforces in the world. The true solution, we think, lies in understanding the changed nature of modern supply chains and identifying new business models better suited for managing them. Over the last years, labor intensive production keeps moving to ever-cheaper countries. But producers in many of the newer entrants (such as Bangladesh) tend to be small and highly disaggregated. By some estimates there are over 4,000 garment factories in Bangladesh alone. This has made it increasingly hard, if not impossible, for a global retailer to ensure compliance with standards. In a knee-jerk reaction some firms have decided to just give up and exit the country altogether — [a move that clearly does not serve the interest of the workers and which pulls valuable resources from developing economies.](#)

The need to improve supply chain compliance does not come from moral arguments alone; the business consequences are also increasingly unescapable. Some apparel retailers attempted to deny that they had any connection with the Rana Plaza building that collapsed — but [data at the level of each shipment is increasingly available](#) to both researchers like

us and to the general public. In fact, the press was quick to point out that some of the deniers did, in fact, source from Rana Plaza recently.

Let's do some math to see how expensive the necessary improvements in safety and working conditions would actually be. Non-governmental organisations have calculated that it would cost about \$600 million per year to bring all Bangladeshi factories up to Western standards.

Given that Bangladesh exports \$18 billion worth of clothing per year, we are talking about a 3.3% cost increase for garments. In other words, a T-shirt currently costing \$3 to produce would cost \$3.10 to produce properly. This is a very small price to pay for the ability to claim that no workers producing your clothing were in any danger of dying.

In fact, ecolabeling is known to lead to price premiums of 10-50% and we believe one can expect similar price increases with "safe-workplace labeling". What holds back improvements is thus not direct cost concerns, but the ability to ensure compliance with norms in a supply chain.

We think the answer to that problem lies in the novel business model pioneered by companies like Li & Fung Ltd., a supply chain intermediary that owns no production, transportation or retail facilities, but which is the key link in the sourcing practices of some of the world's best known companies. This firm created a multi-billion dollar business for itself by sourcing "better" in places like Bangladesh than their customers can by going there directly.

Firms like Li and Fung Ltd. have created a new business model that is based on simultaneously providing the flexibility of competitive sourcing and the confidence of long-term relationships that radically increase voluntary compliance even in complex, distributed supply chains. When suppliers and buyers have stable long-term relationships with intermediaries like Li and Fung, their incentives are better aligned, and a small factory in Bangladesh finds it in its own interest to improve workplace conditions that help maintain its long-term relationship with Li & Fung rather than risk losing it all for small gains.

An intermediary of this kind that devoted its energy to ensuring workplace safety could both bring the benefits of free trade to low-income countries and improve workplace conditions without punitive compliance costs or brand damage for the buyer. Such an intermediary organisation (in this case probably an NGO) would collect the extra 3.3%, build relationships with

buyers and sellers and would use the trust of its relationships to have the confidence to certify that clothing was produced according to proper standards.

Find article at

<https://knowledge.insead.edu/entrepreneurship/business-model-bangladesh>

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