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The Market for Labor Standards

Not to sound Pollyannish, but I believe there is a basic decency in the American people that these companies don't understand. We have to try to tap this decency. When we do that, we get a tremendous response.

—Charles Kernaghan (*New York Times*, June 18, 1996, B4)

Brand image, the source of so much corporate wealth, is also, it turns out, the corporate Achilles' heel.

—Naomi Klein (1999, 343)

The role of sweatshops in economic development burst onto the international agenda in the 1990s because activists in advanced countries roused consumer concerns about working conditions and threatened to block trade agreements that did not address their issues. Fearing that consumers might reject products made under poor conditions, major corporations such as Levi Strauss, Reebok, Liz Claiborne, and later Nike decided to address the labor standards problem. They developed codes of conduct for their subcontractors and monitoring programs to verify compliance with those codes. The US Department of Labor initiated a No Sweat program and promoted the multistakeholder Fair Labor Association initiative to improve standards. College students organized the United Students Against Sweatshops to pressure university administrators to set standards for firms making products licensed to bear college logos. The United Nations created the Global Compact to encourage businesses to promote respect for human rights, labor rights, and the environment. And the OECD updated its Guidelines for Multinational Corporations.

Does this surge of concern about labor standards in less developed countries (LDCs) derive from nefarious protectionist interests seeking to reduce imports, as LDC governments and globalization enthusiasts fear? Or does it reflect a genuine desire to help workers in poor countries, as the standards advocates claim? If the latter, why are activists so important in rousing consumer concerns? What determines the response of firms to activist pressure?

Here we examine these questions from the perspective of the economic analysis of markets. Without gainsaying the insights and value of other approaches to studying the labor standards and antisweatshop movement, we treat the demand for standards in the same way as economists treat demand for any other good—as something that consumers want and are willing to pay for. Similarly, we treat the supply of standards as economists treat the supply of any product—as something that producers provide when they can make a profit from it. In our analysis, low standards reflect not moral deficiencies but rational business decision making when the costs of improving standards exceed the benefits. High standards in this analysis reflect normal business behavior when consumers, activists, or governments make it more profitable to produce under good working conditions.[1]

Consumer Demand for Labor Standards

The starting point for a market-based analysis of labor standards is that people care about the workplace conditions associated with the goods they purchase. If consumers were indifferent to those conditions, firms would ignore activist complaints about poor standards. Antisweatshop activists would be found at the Speakers' Corner in London's Hyde Park, next to someone warning about the end of the world, rather than leading a worldwide campaign to which brand-name multinational firms respond.

What gives the antisweatshop movement power is that consumers care not only about the physical attributes of goods and services but also about the workplace conditions associated with them. Consumers are willing to pay higher prices for goods produced under decent conditions because they feel better about consuming such products. This willingness to pay more creates a financial margin for improving conditions or increasing wages in LDCs.

Because economists prize consumer sovereignty over almost everything else, the claim that consumers care about standards has great weight among economists in the debate on standards and globalization. If consumers want improved working conditions for the goods they buy,

1. This analysis also downplays "social responsibility" as a motivation for firm behavior, though we recognize that some owners and managers choose to emphasize personal values with respect to labor conditions and social issues in their business operations. But even socially conscious businesses have to make a profit or go out of business.

the most devoted global enthusiast cannot readily dismiss this demand. After all, it is the job of markets to deliver the products that people want. Globalization enthusiasts also cannot complain about activist campaigns that inform consumers about working conditions any more than they can complain about advertising campaigns that inform consumers about the quality or price of products.

Treating standards as part of the product parallels Adam Smith's and Alfred Marshall's analyses of compensating differentials in the labor market. In *Wealth of Nations*, Smith noted that the "agreeableness or disagreeableness of the employments themselves" affects wages. In *Principles of Economics,* Marshall differentiated between the bricklayer who cares whether he works in a palace or in a sewer and the seller of bricks who does not care whether his bricks pave the palace or sewer. The bricklayer's concern creates compensating wage differentials in the job market: higher pay for sewer work.[2] Modern economic analysis of consumer behavior also recognizes that diverse factors define consumer products (Lancaster 1979), of which the working conditions that produced the product can readily be one.

The evidence that consumers want decent working conditions associated with the goods that they consume and are willing to pay for this comes in four forms:

- surveys of consumer preferences;
- experiments that give individuals the option of behaving in their narrow interest or of taking account of the interest of others;
- the response of shareholders and share prices to allegations that firms produce goods under poor conditions; and
- corporate responses to antisweatshop campaigns.

Survey Evidence

Suppose you are offered two identical T-shirts with your favorite logo. One was made in good conditions in a less developed country. The other was made in a firetrap building by workers paid near starvation wages. Which T-shirt would you buy . . . when the T-shirts cost the same? When the shirt made under good conditions costs a bit more? When it costs much more?

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2. The theory takes as given the options facing a worker, which in some cases may be very limited—e.g., among caste workers in India. It does not predict that low-wage workers have better conditions than high-wage workers, but rather that given a choice, workers who want particular standards can obtain them by accepting lower wages than they could otherwise make (or conversely, that the firm that offers particularly onerous work has to pay more than if that work were less onerous).

Table 2.1 Findings from three surveys on the expressed consumer demand for labor standards

Survey sponsor and question	Period and measure		
	1995	1996	1999
Marymount University Center for Ethical Concerns			
Would avoid shopping at retailer that sold garments made in sweatshop (percent)	78	79	75
More inclined to shop at stores working to prevent sweatshops (percent)	66	63	65
Willing to pay $1 more for $20 garment guaranteed made under good conditions (percent)	84	83	86
Most responsible for preventing sweatshops (percent):			
Manufacturers	76	70	65
Retailers	7	10	11
Both	10	15	19
What would most help you avoid buying sweatshop clothes (percent):			
Fair labor label		56	
Sweatshop list		33	
University of Maryland Program on International Policy Attitudes			
Feel moral obligation to make effort to ensure that people in other countries producing goods we buy do not have to work in harsh or unsafe conditions (percent)			74
Willing to pay $25 for $20 garment that is certified not made in sweatshop (percent)			76
Find arguments for or against labor standards convincing (percent):			
Standards will eliminate jobs			37
Standards interfere with national sovereignty			41
Low standards give unfair advantage			74
Low standards are immoral			83
United States should not import products in violation of labor standards (percent):			
Products made by children (under force or without chance for school)			81
Made in unsafe and/or unhealthy places			77
Workers not allowed to unionize			42
Do not expect workers in foreign countries to make US wages, but expect countries to permit wages to rise by allowing unions and/or stopping child labor (percent)			82
Favor lowering barriers that limit clothing imports (percent):			
Without hearing about costs of protection			36
After hearing costs of protection			53

(table continues next page)

Surveys that ask questions of this form invariably find that the vast majority of Americans *report* that they would choose the garment made under better conditions, even if it cost a bit more. Table 2.1 summarizes the results from three surveys: one by Marymount University's Center

Table 2.1 *(Continued)*

Survey sponsor and question	Period and measure 1995	1996	1999
National Bureau of Economic Research[a]			
Sample A			
Consumers who say they care about the condition of workers who make the clothing they buy (percent):			
A lot			46
Somewhat			38
Only a little			8
Not at all or no response			8
Willing to pay more for an item if assured it was made under good working conditions (percent)			81
Additional amount willing to pay for $10 item (dollars)			2.80
Additional amount willing to pay for $100 item (dollars)			15
Sample B			
At same price would choose alternative to T-shirt that students say is made under poor conditions (percent)			84
Would not buy T-shirt made under poor conditions at all (percent)			65
Would buy T-shirt made under poor conditions at average discount of (dollars)			4.30
Would pay more for T-shirt if came with assurance it was made under good conditions (percent)			78
Average additional amount would pay, including as zeros those who did not offer to pay more or were inconsistent (dollars)			1.83

a. The two samples reflect different people being asked different sets of questions in order to ensure that responses were not dependent on the way the question was asked.

Sources: Marymount University Center for Ethical Concerns (1999); University of Maryland (2000); and for National Bureau of Economic Research survey, Elliott and Freeman (2003).

for Ethical Concerns; one by the University of Maryland's Program on International Policy Attitudes; and one by the National Bureau of Economic Research that was conducted under our direction.[3]

The Marymount surveys were conducted in 1995, 1996, and 1999. In each, three of four consumers said they would avoid stores if they knew the goods being sold had been produced under poor conditions; two of three said they would be more inclined to shop in stores that make an effort to avoid sweatshops. Eighty-five percent of respondents said they would pay $1 more for a $20 item if they could be assured that it had been made under good conditions.

3. This section draws heavily on Elliott and Freeman (2003).

The 1999 University of Maryland Program on International Policy Attitudes survey asked slightly different questions but obtained similar results. In this survey, roughly three out of four respondents said they felt a moral obligation to help workers faced with harsh conditions. A similar proportion said they would pay $5 more for a $20 garment if they knew that it had not been made in a sweatshop (University of Maryland 2000).[4]

The Program on International Policy Attitudes survey also asked about attitudes toward increasing LDC access to US markets in general. Nearly 90 percent of respondents said that "free trade is an important goal for the United States, but it should be balanced with other goals, such as protecting workers, the environment, and human rights," even if this slowed the growth of trade and the economy. Focusing on the apparel sector, where sweatshops abound, the survey asked whether respondents favored lower barriers to clothing imports. Without any information about the costs of protectionism or compensation for those who lose from free trade, only 36 percent favored lower tariffs. But when the survey told them about the economic costs of protectionism (which are almost invariably higher than people expect), the proportion favoring lower tariffs rose to just above 50 percent. Finally, when asked if government assistance for workers hurt by trade would affect their views, the proportion favoring reduced tariffs and greater access to world markets rose to two-thirds.[5]

The Program on International Policy Attitudes survey also tested arguments for and against making labor standards part of the trade agenda. Most respondents agreed with arguments for minimum standards—that harsh workplace conditions are immoral, and that labor standards eliminate unfair advantage through exploitation. By contrast, few were convinced by typical arguments against standards—that they reduce jobs in affected countries and impinge on national sovereignty. However, consumers differentiated among labor standards. Consumers in this survey were more concerned about child labor and job safety than about the right to unionize. More than four-fifths (82 percent) said they did not expect workers in foreign countries to earn US wages. An overwhelming 93 percent of respondents agreed that "countries that are part of international trade agreements should be required to maintain minimum standards for working conditions."

4. Comparing the surveys by Marymount and the Program on International Policy Attitudes, a higher premium on a $20 item, $5 versus $1, reduces the number of people who say they would buy the good made under decent conditions. In this range, moreover, the demand appears to be modestly inelastic. Revenues would rise with the increase in price from $21 to $25, but, because purchasers fall from 85 percent of persons to 75 percent, revenue would still be maximized at the $20 price.

5. For more analysis on public attitudes toward trade, see Scheve and Slaughter (2001).

The results of our National Bureau of Economic Research survey (Elliott and Freeman 2003) show that consumer concern about the working conditions associated with the goods they buy produces a downward sloping demand curve for standards.[6] We asked one set of respondents, Sample A, "how much more would you be willing to pay for items made under good working conditions" for items worth $10 and $100. We asked a second set of respondents, Sample B, if they would buy a $10 T-shirt made under poor conditions if its price were lowered to $9, and then $8, and then $7, and so on, always asking the higher price first. We also asked how much they would pay for the T-shirt if it were made under good conditions.

Most consumers said they were willing to pay modestly higher prices for higher standards but the proportion who said they would pay more was inversely related to the price differential. Among Sample A respondents, consumers said they were willing to pay, on average, 28 percent more for a $10 item and 15 percent more for a $100 item when the items were made under good standards (including as zeros consumers who said that they were unwilling to pay extra for the assurance) (table 2.1). In Sample B, large majorities (84 percent) said they would avoid a T-shirt "with a nice logo" if local students informed them it was made under poor conditions. Nearly two-thirds said they would not buy the T-shirt made under poor conditions at any price. The one-third who said they would buy it wanted a mean discount in the price of $4.30 or 43 percent of the $10 price.

The results from Sample B reveal a fundamental asymmetry in responses to information about good and bad working conditions. Consumers said they would pay an average of $1.83 to know a product was made under good conditions (including zeros for persons who said they would not pay the extra amount, or who refused to answer or were inconsistent in their responses to questions).[7] This is not even half of the discount consumers demanded to purchase a product made under bad conditions. The greater price response to information about bad conditions than to information about good conditions is consistent with prospect theory, which shows that people weigh potential losses more heavily than potential gains (Kahneman and Tversky 1979). The Marymount surveys also show this fundamental asymmetry.

Figure 2.1 shows that both survey designs confirm the asymmetry: a high elasticity of demand for products made under good conditions but

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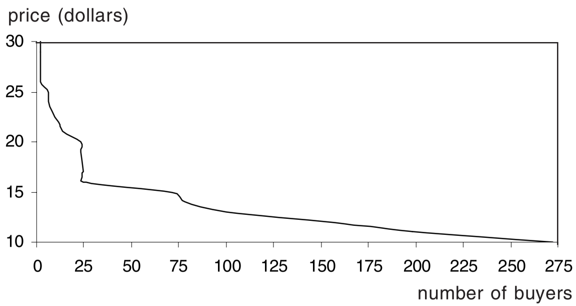
6. The survey of a small number of randomly chosen persons in the United States in fall 1999 was conducted by Springfield Telemarketing. A split sample design was used that posed different questions to different respondents to see whether responses varied with the wording or presentation of questions.

7. Due to a coding problem in the survey, this estimate may be too low. But if we had deleted these observations, our results would be qualitatively the same.

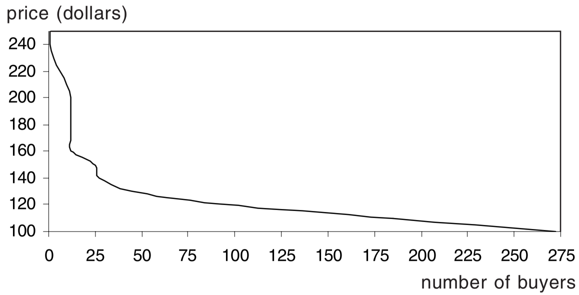
Figure 2.1 Estimated demand curves for labor standards

Sample A question:
What would you pay for an item if assured that it was made under good conditions . . .

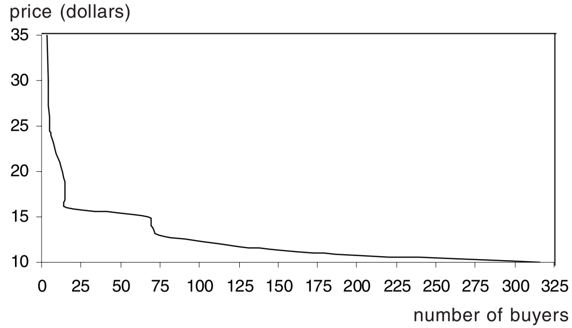
if the initial price was $10?



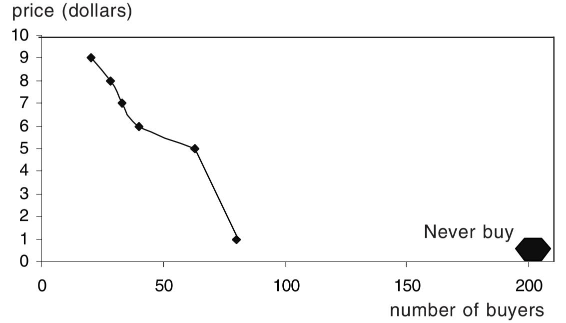
if the initial price was $100?



Sample B questions:
What would you pay for a $10 T-shirt if assured that it was made under good conditions?



What would you pay for a $10 T-shirt if informed that it was made under bad conditions?



Source: NBER Survey, Elliott and Freeman (2003).

a low elasticity of demand for products made under bad conditions. The willingness to pay for items made under good conditions has an elasticity on the order of –3.0 to –5.0. Roughly 20 percent of consumers say that they are unwilling to pay anything extra, and the proportion who said they would buy the product made under better conditions falls sharply as its price rises. The loss in revenue is not recoverable from those willing to pay more. By contrast, roughly two out of three consumers say they would not buy the item made under bad conditions under any circumstance. Among the third who said they would buy the item at a discount, the proportion saying they would make the purchase rises only modestly as the price drops. This produces an inelastic demand for T-shirts produced under bad conditions (the estimated elasticity is just –0.29).

The implication is that firms can lose greatly if their product is identified as being made under bad conditions but they have only limited space to raise prices for products made under good conditions.[8] The varying responses to information about good and bad conditions helps explain, we argue later, the behavior of activists and firms in the market for standards.

Experimental Data: Do Consumers Act as They Say?

I still shop at those brand-name stores, but I feel really guilty about it.
—Founding member of a New York City high school Student Committee Against Labor Exploitation (*Business Week*, September 11, 2000)

What people say on a survey may not accurately presage their behavior, so the survey evidence need not convince the skeptic. People rarely admit that they do not care about anything but themselves, even when this is their true feeling. To see if people actually sacrifice material interests for the sake of others, as they say on surveys, economists and psychologists undertake laboratory experiments. These experiments present subjects with a choice of acting in their narrow self-interest or sacrificing something for the well-being of others. The experiments demonstrate that in actual situations with real money at stake, people act as if fairness toward others is part of their utility function. Because what motivates the demand for standards is a willingness to pay more for the benefit of others, these results suggest that people in fact behave in ways consistent with their statements on surveys.

8. Because we did not specify the conditions under which the alternative product was made, this is an inference from responses to the two sets of questions. The design that would provide a test of this inference would be to ask consumers to compare a product known to be made under good conditions with one known to be made under bad conditions (at varying prices) and a product made under good conditions with one made under unknown conditions. Our analysis compared bad conditions with unknown conditions and good conditions with unknown conditions.

Table 2.2 Experimental evidence on willingness to sacrifice some personal gain for the well-being of others

Game	Predicted behavior of person only by himself or herself	Actual behavior in experiment
Prisoners' Dilemma	Always defect	Often cooperate
Ultimatum Game	Boss takes almost all	Boss usually offers 30 to 50 percent
	Workers accept crumbs	Workers reject highly uneven division of money; prefer smaller amount fairly shared
Dictators' Game	Dictator takes all	Most people give moderate amount to partner
Standards	People buy cheapest product	People pay more for product made under good conditions

Table 2.2 summarizes the findings from the major experiments in economics that underlie this conclusion. The most famous experimental game is the Prisoners' Dilemma. There are two players. If they cooperate, each gains some money; if one defects and the other cooperates, the defector gains more than from cooperating while the cooperator gets the lowest payout. If both players defect, each gets more than if he or she were the sole cooperator but less than if both cooperated or if one defected and the other cooperated. The rational response in a one-period game is to defect. But in fact, players frequently choose the cooperative strategy. It is a stretch from the Prisoners' Dilemma game to the standards problem, because "power" is equally divided between two players in this game, whereas demand for labor standards depends solely on the consumer who can choose the cheap product if he or she so desires. But the outcomes from Prisoners' Dilemma games show that people are more cooperative and less selfish than economic self-interest predicts.

The Ultimatum Game comes closer to the standards problem. It focuses on how individuals react to divisions of a given pie. Player one, the boss, divides a sum of money, say $100, between himself and player two, the worker. If the worker accepts the boss's offer, each gets the amount determined by the boss. If player two rejects the division, the entire amount disappears. If all that matters is the amount that each person gets, the boss will take $99.99 and offer the worker $0.01. Because both are better off, theory suggests that the worker should accept. But no one behaves that way in practice. In response to such a one-sided division of the money, people who play the worker's role will reject the offer, so that no one gets anything. Knowing this, most "bosses" offer workers a greater share of the pie. On average, bosses offer workers 30 to 40 percent of the money, with a modal amount of 50 percent. Workers reject almost all offers that give them less than 20 percent of the amount. In multiperiod versions of the game, where the pie shrinks over time, workers often accept second-period offers that give them smaller absolute amounts of money than they could have had in the first period, as long as the second-period distribution is more even. The "unfairness" of the boss taking the vast bulk of the funds affects behavior. The stretch to the standards problem is shorter.

The Dictators' Game fits our case even better. In this game, whatever the boss decides goes. Two players are selected and given envelopes. One envelope has $100 and the other has nothing. The player with the $100 envelope can keep the $100 and say too bad for you! Yet even in this case, people do not behave in a purely self-interested manner. Only about 20 percent of players keep all the money. Most people share some with their partners, albeit less than if their partner could veto their division. They typically take 60 to 80 percent of the money. In short, even under conditions that allow people to be completely selfish, most give some money to others.

Generous behavior is, of course, not limited to the laboratory. The majority of Americans contribute to charity and many volunteer time for charitable activities as well, often in response to appeals from activists (Freeman 1997). Both in experiments and in the social world, people behave as if they care for more than their own immediate pleasure. Thus, our presumption is that if people say they care about labor standards and that they are willing to pay a bit more for products made under good conditions and would shun products made under poor conditions, they are more likely to be telling the truth than deceiving the surveyor (or themselves).

Ultimately, however, we want direct evidence that consumers reject sweatshop products in favor of a more costly product made under good labor conditions. The ideal evidence would be a "standards experiment" that would offer consumers two identical products for sale, one purportedly made under good working conditions and the other made under bad conditions, at different prices. Instead of asking which item they would buy, the experiment would offer them an actual choice in a retail setting. The sign over one pile of T-shirts might say, Made Under Good Conditions Meeting World Labor Standards; the sign over the second would say, Made by Child Labor in Sleazo's Sweatshop, or more realistically, Made Under Unknown Conditions. Then we could observe how many consumers buy the Good Conditions T-shirt rather than the Child Labor T-shirt at different prices.

There have been a few studies examining consumer willingness to pay for better working conditions in a real-world setting, but they have not yielded definitive answers about the demand for standards. In one analysis, a University of Michigan team placed two stacks of identical socks next to each other in a store, with a sign stating that those in one stack had been made under good working conditions. The socks made under good conditions cost from zero to 40 percent more than the others, but to obtain many sales, both sets of socks had been priced at bargain rates. This study found that at the same price, half of the consumers chose the socks made under the unspecified conditions, which could imply that the average consumer paid no attention to the statements, or did not care about standards. When the price for the socks made under good conditions was increased relative to the price of the other product, the proportion of purchasers that chose the good-conditions socks fell to about a third, but many persons stuck with the socks made under good conditions even at the largest price differential.

The implication of this study is that there is a niche market for socks made under good conditions that could garner a quarter to a third of the sock market and generate enough additional revenue to improve wages and conditions for workers, but that those socks would not sweep the market. Yet because the socks were not visibly branded and were not associated with a campaign to sensitize consumers to the standards issue, the results may not carry over to other situations.[9]

In another case, Occidental University in Los Angeles created a "sweat-free" zone in one corner of the campus bookstore. The zone consisted of a single T-shirt design, produced by a unionized apparel factory in Pennsylvania. But the sweat-free T-shirt was not identical to the comparable non-sweat-free item. It was made of lighter-weight cotton, was available only in white, and sold for $2 less. Sales of the sweat-free T-shirt were double those of the traditional white T-shirt with the same logo, but this could be because the lower price, meant to compensate for the lighter-weight cotton, in fact did more than that.[10]

In the specialty coffee market, Starbucks sells coffee certified by Transfair USA. The Fair Trade Certified coffee comes from cooperatives where farmers earn a minimum price above the commodity market price. The fair trade beans are sold alongside other Starbucks coffees in its company-operated stores and online at a price of $11.45 a pound, which is not the highest-priced coffee sold by Starbucks, but higher than the $10 to $11 a pound charged for most of its other varieties. Starbucks Coffee occupies a premium market niche, with both prices and quality well above the average for the typical commodity coffee sold at the grocery store. It

9. The results have been described to us in a draft that is "for your reference" only, but with permission to cite here.

10. The heavier-weight T-shirt in a more popular gray color remained the top seller overall. This information is based on a private communication with the manager of the bookstore.

is also not clear how customers view the standards associated with uncertified coffee sold at Starbucks since the company paid an overall average price of $1.20 per pound in 2002, compared to an average commodity coffee price of 40 cents to 50 cents per pound (and a minimum fair trade price for nonorganic coffee of $1.26 per pound).[11]

Thus, the Starbucks experience is not an ideal experiment, but it does provide information on behavior. The 2002 Corporate Social Responsibility Annual Report from Starbucks (available at www.starbucks.com, p. 8) shows that purchases of Fair Trade Certified coffee increased sharply from 653,000 pounds in fiscal 2001, the first full year in which it was available, to 1.1 million pounds in fiscal 2002. However, Starbucks also reports that it sold less than half the total purchased in 2002. By contrast, Starbucks reports (p. 9) that it nearly tripled its purchases of Conservation [Shade Grown] Coffee, a result of the company's partnership with Conservation International to protect biodiversity globally, to 1.8 million pounds in 2002, "to meet increased consumer demand." Thus, like the socks, this suggests that higher-standards products can capture a niche market but are unlikely to sweep the field, even among "elite" consumers who are more likely to know about them and be able to afford to pay a price premium.

Still, responses of other retailers to the Starbucks initiative suggest that firms see enough demand for fair trade coffee to change their behavior. For instance, Borders announced in April 2001 that it would offer fair trade coffee at its in-store cafes, and Seattle's Best Coffee signed an agreement with Safeway to sell organic and fair trade coffees at 1,400 stores around the country. In April 2003, Dunkin' Donuts, the "largest coffee and baked goods chain in the world," announced that it would use Fair Trade Certified coffee for all espresso drinks (including cappuccino and latte) offered at its stores nationwide.[12]

As of fall 2002, Transfair USA reported that an estimated 160 importers and roasters, 10,000 retail outlets, and 200 college campuses were offering fair trade coffee. But these are still small numbers in the $18 billion coffee market.[13] In Europe, where fair trade products have been available for longer, the highest-profile fair trade coffees in the United Kingdom and the Netherlands have roughly 3 percent of the market.[14] Overall, the Fair Trade Federation estimates that worldwide fair trade

11. Starbucks Coffee, *Corporate Social Responsibility Annual Report 2002,* www.starbucks.com/aboutus/CSR_FY02_AR.pdf (May 8, 2003).

12. www.dunkindonuts.com/pressroom/press/pressrelease.jsp?id=78 (May 7, 2003).

13. "Fair Trade Update," Fall 2002, www.transfair.org/pdfs/Update_Fall2002.PDF (May 8, 2003); Associated Press, September 24, 2000, available on the Global Exchange Web site at www.globalexchange.org/economy/coffee/ap092400.html (September 26, 2000).

14. Tallontire, Rentsendorj, and Blowfield (2001, 13), www.maxhavelaar.nl.

sales were $400 million annually by the late 1990s, a mere 0.01 percent of total world trade.[15]

Shareholders and Stock Prices

If you owned shares of Nike or Starbucks or some other well-known firm and learned that the firm or its subcontractors were mistreating workers, what would you do? Would you congratulate management for possibly making a few extra cents for you? Or sell the shares because you find such practices offensive? Or sell the shares because you fear that consumers might shun the firm's products and reduce profits? Or demand at the annual shareholders' meeting that the company behave morally?

There is evidence that in the capital market, as in the consumer goods market, people are concerned about how companies treat workers and act on those concerns. In 1999, socially responsible investment funds, which invest in firms that meet some social standard, accounted for about 13 percent of the estimated $16.3 trillion under professional management in the United States.[16] At various times, shareholders have dumped shares in firms that engage in morally reprehensible business practices or have complained about those practices at shareholders' meetings. In the campaign against apartheid in South Africa, many groups divested shares of firms that did business in that country.

These policies or practices will affect investors' portfolios but may have little impact on share prices if enough investors are indifferent to the issues and happy to buy the shares. Antisweatshop campaigns, however, are designed to influence consumers, whose purchasing decisions will determine the profitability of the company. Even investors unconcerned about the social issues may decide to sell shares because they fear the campaign will affect profits, thereby reducing the stock price.

To see if campaigns have this effect, Rock (2003) identified 59 cases in which campaigners claimed that a firm or its contractors operated under poor labor conditions and where nothing else important to the firm occurred that might affect the share price and 12 cases (all Reebok) where the firm received good press for its efforts to improve working conditions. In roughly two-thirds of the cases of alleged poor labor conditions, share prices fell immediately after the campaign generated bad publicity. Nike, which faced a continual barrage of allegations of poor conditions, experienced a cumulative drop in its share price of 19 percent from 1996 through 2000 that was attributable to the bad publicity.

15. "Fair Trade Fact," available at www.fairtradefederation.com/ab_facts.html (May 8, 2003).

16. See www.socialfunds.com/page.cgi/article1.html (May 8, 2003).

Among all the firms examined, there was a 6 percent median drop in share values associated with an antisweatshop campaign. By contrast, the increase in Reebok shares due to good news was 2 to 3 percent. Using the data from this study, we estimate that the share price fell by 1 to 2 percent for each news item reporting sweatshop conditions or protests thereof, whereas the share price rose by less than 0.25 percent for each news item on good conditions. This is the same asymmetry to good and bad conditions found in our National Bureau of Economic Research survey.

More broadly, in a summary of 80 studies comparing the share price of a firm to its social performance, Margolis and Walsh (2001) report that more than half the studies found higher share prices for firms with better measured social performance. Only 5 percent of studies found lower share prices for the firms with better social performance, while the remainder showed no consistent pattern. Studies that analyzed the effect on share prices of anti-apartheid pressures or other human rights violations, however, found weaker results than did the studies looking at other aspects of corporate social performance, suggesting that investors viewed company performance in these areas as less important to them or as having less impact on profitability.[17]

Managers of firms that operate with poor labor standards also face pressures from shareholders at annual meetings. From the beginning of 2002 to mid-2002, shareholders, including major pension funds with substantial ownership stakes, had made 45 proposals to press management to be more attentive to global labor standards. The biggest pressure was at Unocal over its business in Burma, where forced labor was sufficiently common to induce the International Labor Organization to take punitive action against a member government for the first time in the organization's history (see chapter 5). At Unocal, shareholders voted one-third of the shares for a proposition that would have the company adopt a code of conduct that included the core standards of the International Labor Organization.[18] In many other firms, ranging from Sears to Home Depot

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17. However, Margolis and Walsh (2001, 10–11) point out several weaknesses in the studies they review, including in the theory, research design, and quality of data used.

18. A more compelling reason for companies to become interested in "corporate social responsibility" strategies may be the threat of litigation under the Alien Tort Claims Act. In recent years, this 1789 law has been the basis for lawsuits by the International Labor Rights Fund against Unocal over the use of forced labor in Burma, Coca-Cola and Drummond (mining) Company for the murder and repression of union organizers at their operations in Colombia, Exxon Mobil for human rights abuses in Aceh, Indonesia, and Del Monte for repression of union organizing at banana plantations in Guatemala.

Cases have also been brought by others against Shell and Chevron for human rights abuses in Nigeria and against Rio Tinto related to its operations in Papua New Guinea. A Washington-based law firm has also filed a class action suit under the Alien Tort Claims Act on behalf of South Africans seeking reparations from 20 large banks and to Colgate-Palmolive to Stride Rite and Delphi Automotive, substantial minorities of shareholders also supported global standards initiatives.

The Response of Firms

Allegations of sweatshop abuse generally arise in the labor-intensive, geographically mobile, and highly price-competitive apparel and footwear sectors. American multinational corporations in these sectors typically focus on product design and marketing, while contracting out most or all of the actual production. Because the firms that market apparel and shoes have high brand-name recognition and recognizable logos (e.g., Nike and Levi Strauss) and because the retailers that sell the products have a prominent market presence (e.g., Wal-Mart and the Gap), they are vulnerable to activist campaigns. Part of their product is the image the brand carries—the statement the product makes about the person consuming it (Klein 1999).

If activist charges stick to the product, they could reduce sales, particularly to teenagers and young adults whose demand for branded clothing and footwear may be especially faddish. Who wants to buy Nike shoes or Gap jeans if they say to the world that you are indifferent to young women or children slaving in a stifling factory for 12 hours a day? If it becomes gauche to wear a given label's apparel because it was made in a sweatshop, retailers could lose sales quickly.

Faced with a campaign charging that they sell or produce goods made under poor conditions, the first response of firms has been to deny the allegations. But because activist campaigns invariably rest on experiences to which workers or observers will attest, this defense rarely succeeds. Activists proclaim: This firm says its product was not made under harsh conditions? Here is Luisa, who works in the factory 12 hours a day with just 5 minutes to go the toilet and 5 minutes for lunch . . . all for 50 cents an hour. If the multinational manufacturer or retailer claims ignorance that its subcontractors operate under such conditions, they now know. And their previous ignorance shows that they must not have cared about conditions. If activists can uncover such poor working conditions, so could the firm if it tried.

In response to allegations of bad working conditions, firms have developed corporate codes of conduct. These codes specify that their factories and those of subcontractors will maintain good working conditions.

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corporations for "aiding and abetting" the perpetuation of apartheid. International Labor Rights Fund Executive Director Terry Collingsworth believes that this latter case will not be successful unless plaintiffs can prove a direct connection between company actions and specific injuries under apartheid. See "The Alien Tort Claims Act: A Vital Tool for Preventing Corporations from Violating Fundamental Human Rights," at www.laborrights.org (February 12, 2003).

Levi Strauss adopted the first code addressing sweatshop issues in the early 1990s after allegations of abuse among its suppliers in Saipan. Wal-Mart followed after its products were linked to child labor in Bangladesh.

Nike initially rejected responsibility for conditions in its supplier factories but then took steps to improve conditions in order to blunt criticism from activists. By 2001, it had improved the conditions among its suppliers in Indonesia and provided information on conditions in other facilities on its Web site. Reebok avoided being tarred by the same brush as Nike by creating a human rights award to honor activists fighting for democracy and against child labor and other abuses.[19] Critics argued that Reebok had actually done little to upgrade working conditions among its suppliers; but if Reebok's stance was hypocritical, it worked. Activists have not targeted Reebok as they have Nike.

The growing number of corporations with corporate codes and the formation of multistakeholder groups to help firms deal with labor standards problems, such as the Fair Labor Association in the United States and the Ethical Trading Initiative in the United Kingdom, is prima facie evidence that firms believe that some consumers will shun their products if the consumers feel that the products are made under poor working conditions. In 2001, the OECD reported that 246 major firms have corporate codes. The Global Reporting Initiative states that more than 2,000 companies use its guidelines to report on their economic, environmental, and social policies and practices.

Simply developing a code, however, is not enough to assure consumers that a firm's products are made under decent conditions. Factory managers or subcontractors might post the code somewhere obscure in the factory (the boss's office) and proceed as they have in the past. Firms must monitor subcontractors to ensure that they pay attention to the corporate code. Some firms pay for independent monitoring by groups that specialize in assessing and improving labor standards, such as Verité, a small firm created by a former buyer of goods in China who was upset with labor standards in the factories where she placed orders. Many firms have hired PricewaterhouseCoopers to audit their subcontractors. A few firms have agreed to independent monitoring by nongovernmental organizations in LDCs. The Gap spent $10,000 annually for independent monitors at a single plant in El Salvador, plus additional management time for dispute resolution. It estimates that replicating this model throughout its supply chain would cost 4.5 percent of its total profit of $877 million in 2000 (*New York Times,* April 24, 2001, A1).

The pattern of corporate denial, admission of problems, the introduction of a corporate code, and eventually monitoring of the code is typical

19. Not surprisingly, there are consultants who help companies with "cause branding." Cone, Inc., of Boston points to the Reebok human rights award as one its "most impactful programs"; www.coneinc.com/pages/cause_brand.html (November 20, 2002).

Box 2.1 Excerpts from Timberland Statement on its Code of Conduct and Monitoring

We put together a Code of Conduct in 1994, because we believe that everyone we impact with our business deserves the right to a fair, safe and non-discriminatory workplace. . . .

In 1998, we started working with Verité, a nonprofit, non-governmental organization (NGO) to audit factories making Timberland products. This included all footwear and apparel vendors, along with some licensees' facilities.

In 2000–2001, all facilities making Timberland products, including tanneries and major component suppliers, were audited. In 2000, audits of all footwear facilities were performed for health and safety issues, including air quality sampling, noise, and light measurements. In 2001, follow-up audits by Verité were performed on behalf of the vendor base. In addition, we have compliance monitors in Asia that visit factories every 8–12 weeks. These auditing efforts have helped improve worker conditions. . . . We work with factories to make changes by providing training and information. For example, in 2001, we organized Verité payroll training in 24 factories in China. This impacts about 6,000 workers. We choose to use local resources such as NGOs and government agencies, to provide training and programs that are more effective and can make lasting changes.

Source: Timberland Web site, www.timberland.com/cgi-bin/timberland/timberland/corporate/tim_about.jsp?c=global%20labor%20standards (May 8, 2003).

among the major firms that have faced allegations that their products are made under poor labor conditions or that recognized that they could face such allegations. Box 2.1 summarizes how the shoe firm Timberland moved from developing a corporate code in 1994, to employing Verité to monitor its subcontractors, to building training about labor standards into its monitoring process. Because most shoes sold in the United States are produced in low-wage LDCs, where activists might readily find violations of labor standards, it is important for a brand-name firm such as Timberland to avoid becoming the target of an antisweatshop campaign.

Finally, some firms have responded to consumer complaints about labor conditions in subcontractors by dropping their business activities in areas where labor standards abuses are severe. Pepsi withdrew from the Burmese market after protests against human rights abuses, including forced labor, threatened its share of the lucrative college market. Protesting students had convinced Harvard University to reverse a decision switching a $1 million vending contract from Coca-Cola to Pepsi because of Pepsi's Burmese operations. And Stanford University students had collected 2,000 signatures on a petition opposing a Pepsi-owned Taco Bell restaurant on campus over other labor standards issues (*Washington Post,* January 28, 1997, C2).

However, dropping out of a market to avoid charges of operating under poor working conditions can be difficult. In 1993, Levi Strauss announced that it was going to stop producing in China because the human rights situation there was unacceptable. But Levi Strauss never completed the withdrawal, and in April 1998 it reversed course and announced that it was expanding operations in China. The Chinese market and potential as an export platform are so large that few firms are likely to withdraw from China as some have done from Burma.

In sum, the ways firms respond to allegations of worker mistreatment show they believe that consumers will penalize them if they do not undertake corrective action. And consistent with survey findings that consumer demand for good and bad conditions is asymmetric, firms respond largely to negative publicity, improving conditions to avoid losing sales.

The Supply of Standards

In Alfred Marshall's famous analogy, economic markets are like scissors with the two blades, downward-sloping demand and upward-sloping supply. In the market for standards, the demand blade derives from consumers who want decent labor standards and are willing to pay for them; the supply blade derives from firms that improve standards because it is profitable for them to do so. Just as consumer behavior produces downward-sloping demand for standards, producer behavior produces an upward-sloping supply of standards.

Without an antisweatshop campaign that risks costing it money, we assume that a multinational firm cares nothing about labor standards and leaves decisions about working conditions to its contractors. The contractors will balance the costs of improved workplace conditions against the possible gains from higher productivity or workers' willingness to accept lower pay for better conditions. Because consumers have not been informed about conditions, the price the firm receives does not depend on the labor standards followed in producing the product.

An activist campaign changes the economic calculus facing the firm. It creates a new price schedule that depends on labor standards. By galvanizing consumers around working conditions, the campaign reduces the price the firm gets for producing under bad conditions and raises the price the firm gets from producing under good conditions. Given the asymmetry in consumer response, however, the campaign will produce a price curve that is kinked around the minimum level of standards that consumers would accept. Firms suffer large reductions in price for below-minimum standards but gain only modestly from above-minimum standards.

Given the new price schedule, the firm will change its labor standards depending on the cost of doing so. If the cost of improving standards is steep, it may decide against doing so, even though it will suffer price declines and a loss of sales because of its poor working conditions. The campaign will have failed in two ways. It will have failed to pressure the firm to raise standards; and it will have given the firm an incentive to fire workers, reduce their wages, or even to shut down, because it faces lowered profitability.

By contrast, if the cost of improving standards is modest, the firm will choose to raise standards. If consumers are willing to pay much more for the higher standards, the firm may even make more money by adopting high standards than it did before the campaign. The firm can advertise that it has improved standards and position its products differently in the market.[20]

That consumers are more willing to penalize firms for making products under poor conditions than to reward firms for making products made under good conditions explains why activists and firms battle so intensely over transparency and disclosure issues. Information about bad conditions can greatly reduce the price at which firms sell their products, whereas information about good conditions raises revenues only modestly. If consumers responded more to information about good conditions, activists and firms would have common ground on which to work. Instead, the kink in the price schedule facing firms means that information about standards becomes an important battleground in this market.[21]

Activists in the Market for Standards

In the simplest model of a market, consumers and firms interact to determine prices and outcomes. Consumers have perfect information about the attributes of products and buy from businesses that provide the quality with which they are comfortable. For instance, someone who wants super premium gas for their car pays a bit more than someone who

20. In the apparel industry, the move to "lean retailing" and the advantages of quickly responding to changes in consumer preferences, coupled with the tariff advantages of the North American Free Trade Agreement and other hemispheric trade preferences, have led US firms to source more production in Mexico, the Caribbean, and Central America (Weil 2000). Geographic closeness has also made it less costly for activists to uncover abuses and to bring workers from alleged sweatshops to the United States to buttress their allegations. This in turn increases their ability to alter the price schedule facing firms in favor of higher standards.

21. The battle over information became more intense in 2002–03 after a San Francisco man filed a consumer fraud case against Nike in California, claiming that Nike's claims regarding conditions in its factories were misleading. Nike claims that, if upheld, the case would have serious negative repercussions on code monitoring and transparency. Activist groups claim that legal recourse is necessary to prevent "blue-washing." The Supreme Court agreed to take the case and is expected to rule sometime in 2003. See *San Francisco Chronicle,* May 2, 2002, and www.nikebiz.com.

wants regular, and both are satisfied. There are no third parties seeking information about products, organizing consumers against some goods, and altering the price schedules facing firms.

The market for labor standards is different. The major reason is a lack of information about the working conditions associated with products. This information is costly to obtain and unavailable at the point of purchase. Firms will not publicize the information that consumers care about—possible poor working conditions in their factories or those of subcontractors. The incentive is to cover up or distort such information or, better yet, to play a "don't ask, don't know" game.[22] Consumers concerned primarily with using the product cannot be expected to invest in finding out about work conditions by themselves. Thus, the market for standards operates only because there are activist intermediaries who seek out information about workplace conditions and publicize those conditions to consumers.[23]

To rouse consumer interest, antisweatshop activists highlight the evils of low labor standards and stress how far current standards are from the minimum level activists seek. But simply arousing concern is not enough. In the long run, activists need firms that will respond to standards campaigns and will take the initiative to improve conditions. The market for standards is, after all, supposed to produce levels of standards above those that would exist if consumers did not care about working conditions. In addition, once firms respond to antisweatshop campaigns with codes of conduct and promises to do better, there is a further need for third-party groups, including nongovernmental organizations, to monitor how firms implement their promises and to provide this information to consumers as inexpensively as possible.

In the market for standards, the role of activists as intermediaries who verify information and provide it to final consumers is not unique. Financial markets also rely heavily on intermediaries who provide information about the conditions of firms or people. In financial markets, a borrower has no incentive to tell his or her financial problems to potential creditors; a company has no incentive to publicize bad news to the

22. Gathering information is costly for firms, as well as consumers, because of the long and widely dispersed supply chains that characterize many global industries today. Even those at the top of the chain often do not have complete information about conditions in their operations around the world. This creates another disincentive for firms to compete for market share by advertising how good they are to their workers because exposure of violations would cost them credibility with consumers. In addition, because activist groups have limited resources and must focus their muckraking efforts on a handful of market leaders, other firms have an incentive to keep their head down and try to avoid attracting the activists' attention.

23. As pointed out in Freeman (1994), if labor standards have a public goods aspect, then activists would still play a role in pressuring governments and international organizations to provide a minimum level of standards.

stock market. The firm will put as positive a spin on its situation as it can get away with. In turn, banks and other lenders and investors will discount the firm's own claims of creditworthiness and forecasts of future profitability.

In financial markets, given the high costs of acquiring credible information about a firm's true situation and prospects, agencies such as Moody's and Dun & Bradstreet rate creditworthiness and research analysts specialize in particular industries and firms. Antisweatshop activists dress differently and talk a different language than information brokers in financial markets, but they are the labor market counterparts of these Wall Street intermediaries.[24]

24. For a discussion of transparency and disclosure policies in other areas that have been used in lieu of or in addition to direct government regulation, including the role of intermediary groups, see Fung, Graham, and Weil (2002).