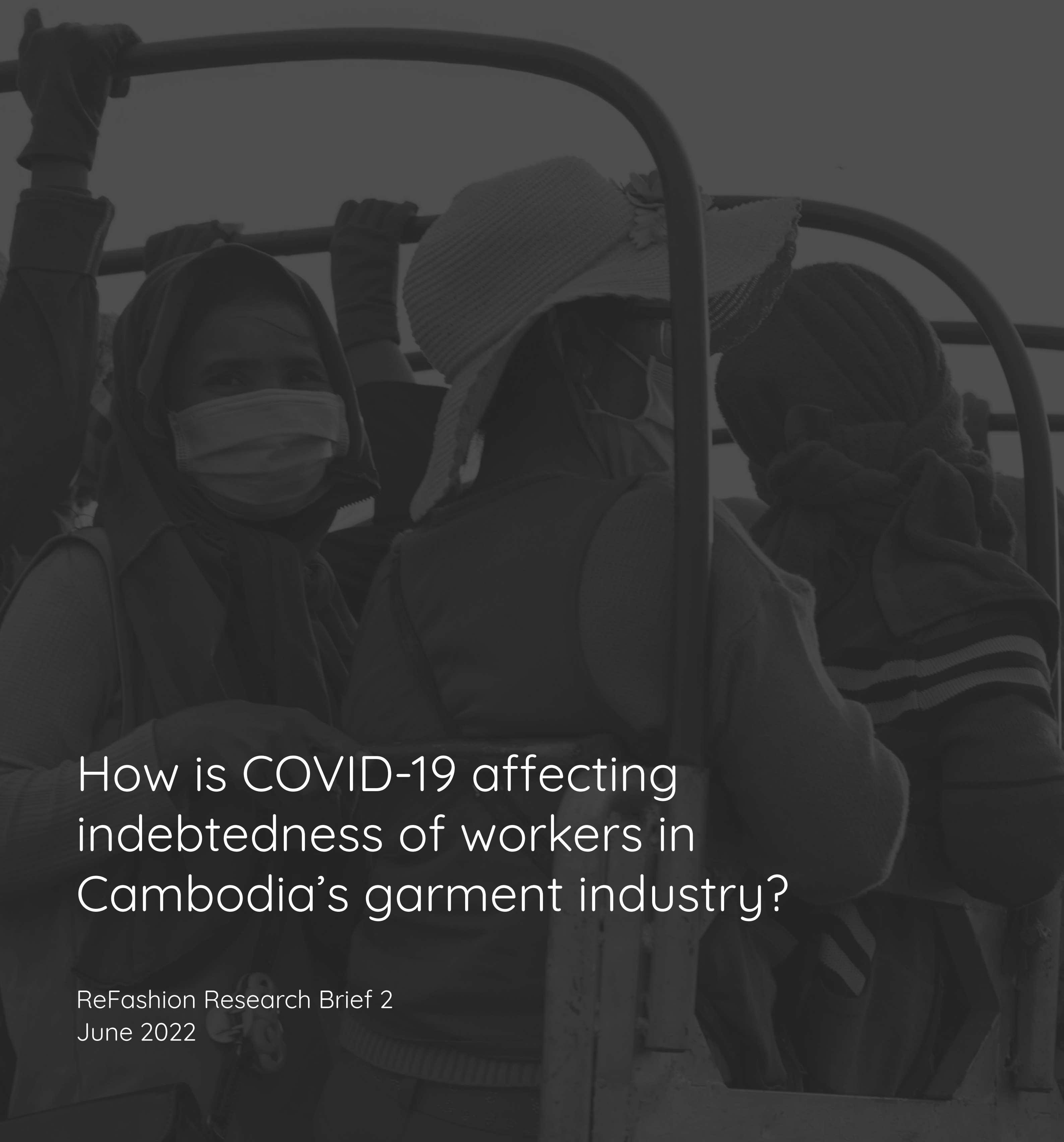
ReFashion



How is COVID-19 affecting indebtedness of workers in Cambodia's garment industry?

ReFashion Research Brief 2
June 2022

COVID-19 has severely impacted employment opportunity and earning potential for workers in Cambodia's garment and footwear sector. The Refashion study is tracking the impacts of the pandemic on a cohort of 200 female workers. Our findings indicate that COVID-19 is exacerbating a crisis of over-indebtedness for workers in the garment industry, with severe consequences for the wellbeing of workers and their families.

"Over-indebtedness is reached when a microborrower is continuously struggling to meet repayment deadlines and has to make unduly high sacrifices related to his or her loan obligations."

World Bank Occasional Paper, 2013

Who we are

ReFashion Study is leading mixed-methods and longitudinal research on the impacts of COVID-19 on female garment and footwear workers in Cambodia. ReFashion is led by a team of UK and Cambodian researchers from Royal Holloway, University of London; the University of Nottingham; and the Cambodia Development Resource Institute.

The study combines a quantitative survey of female workers to measure trends in employment, household finances, and wellbeing, with qualitative interviews to explore emergent themes in greater depth, each repeated with the same cohort of participants at strategic intervals between 2020 and 2022. The research methods are designed to capture an in-depth and long-term understanding of women workers' lives through the pandemic. The experiences of the 203 women in our initial sample are not representative of every garment worker in Cambodia, although corroborating evidence suggests the challenges they highlight are likely widespread. This brief reports on data from 2020–2021 with further publication of later data to follow in our full study report.

The problem

The COVID-19 pandemic is creating significant disruption in Cambodia's garment and footwear industry. Beginning as an economic crisis, the impacts of manufacturing shutdowns and consumer lockdowns around the world continue to slow the garment sector's output. In 2020, Cambodia's garment sector exports fell by 10%. The impacts of this ongoing disruption for the garment industry's workforce are severe. In January 2020, approximately 800,000 people were directly employed in the garment and footwear sector in Cambodia. Around 90% of these workers were women. Although comprehensive data on employment impacts in Cambodia is as yet not available, reliable estimates suggest that, at peak, between one quarter and one half of all factories had suspended production, potentially affecting between 150-200,000 workers (Arnold 2021). By October 2020, already 35-40,000 workers were estimated to have been made permanently unemployed (Arnold 2021).

Before to the COVID-19 pandemic, borrowing money had become common among low-income households in Cambodia, which has one of the largest microfinance industries in the world in terms of borrowers per capita. Between 2000 and 2019, the number of borrowers increased from 175,000 to 2.6 million people (CATU et al. 2020). Garment workers represent a major pool of borrowers, holding 20% of all microfinance loans (Flynn and Mech 2020). In response to the economic disruption posed by COVID-19, the National Bank of Cambodia [NBC] issued guidance in March 2020 to encourage lenders to assist clients "facing actual impacts" from the pandemic. However, its recommendations to lenders were voluntary rather than binding, and had to be agreed with borrowers on a case-by-case basis. Into 2022 there remains urgent concern about workers' continued ability to access support and manage loan commitments on reduced earnings.

COVID-19 and debt: key findings

- The COVID-19 pandemic has exacerbated an existing crisis of over-indebtedness for garment sector workers
- Over-indebtedness occurs when borrowers struggle to make loan repayment deadlines and suffer distress to meet loan obligations
- 63% of garment workers had borrowed money prior to the pandemic, at an average of $4731 per worker
- 61% of these loans were secured against agricultural or residential land holdings
- Between Jan '20 and April '21, the average worker lost 20% of their expected income
- Only 17% of existing loans had been restructured by Oct/Nov 2020, with 72% being repaid as normal
- By Apr/Mar 2021, 68% of workers described loan repayments as one of their main financial worries, second only to daily living costs
- 38% of workers have taken additional loans since January 2020, at an average of $1299 per worker
- 36% of new loans taken to repay existing loans
- Workers are making high sacrifices to met their loan obligations, including reducing food consumption
- Microfinance lenders should act immediately to help borrowers restructure loans and avoid further distress

Key findings

Almost two-thirds (63%) of the workers we surveyed reported outstanding loans borrowed before the pandemic. The average loan portfolio in January 2020 was US$4731. This is more than double the basic annual salary of a garment worker.

The majority of loans were from banks or microfinance lenders (70%) rather than family members (20%) or other private lenders (10%). Very few loans were described as facilitating entrepreneurial potential, through agricultural (2%,) or trade inputs (5%), for example. Instead, they were typically used to support everyday household expenditure. After investments in land and housing (31%); 23% of loans were taken out to purchase transport, including motorbikes; 22% were to support daily living like food and rent; and 16% to cover health or medical care. A further 16% of outstanding loans prior to the pandemic were taken to pay back other existing loans. This signals that, for some workers, debt levels may have already reached unsustainable levels prior to the pandemic.

Indeed, the main financial worries of workers before the pandemic were daily living costs (70%) followed by loan repayments (63%). Being able to make loan repayments is primary concern for workers as most outstanding loans were secured against their main assets, especially land. In our sample, 41% of loans were secured against residential land and a further 20% secured against agricultural holdings. There is considerable risk for workers if they are no longer able to make loan repayments, therefore, as they stand to lose farms and homes.

The COVID-19 crisis has severely impacted workers' incomes and, alongside, their continued ability to make loan repayments. Over 15 months from January 2020, the income of the workers in our sample fell by an average of 20%. As a result, most workers describe themselves as "worse off" than before the pandemic, as reported by 87% of respondents in Nov/Dec '20 and 88% in Mar/Apr '21. Despite facing significant hardship, however, the majority of workers in our sample have not been able to benefit from the loan restructuring recommended by the NBC. Whilst some borrowers had reached an agreement to temporarily suspend repayment (9%) or repay in smaller sums (8%), by Oct/Nov '20 most loans (72%) were still being repaid as usual.

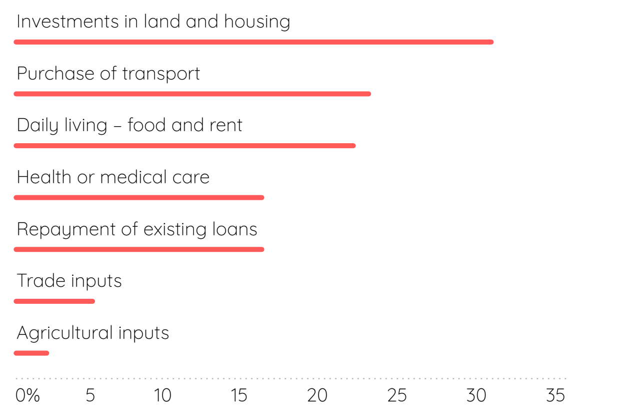
Many workers report taking on additional borrowing to cope with the income shortfall and continue loan repayments. By Mar/Apr '21, at least 38% of workers had taken new loans, at an average of $1299 per worker. This is significantly increasing household debt burdens, pushing the average loan portfolio of the sample in excess of $5000 per worker. The profile of these new loan arrangements is significantly different than before. Only 15% of new loans are from formal lenders such as banks and microfinance institutes, whilst 52% come from family or friends, and 33% from other private lenders. Many workers reported they could no longer access credit from formal sources, as approvals are not granted due to the instability of their employment. The proportion of loans taken to repay existing loans has increased significantly, at 36% of all new loans.

The financial pressures loan repayments are compelling workers to make high sacrifices to their standard of living. As reported in our previous brief, by Mar/Apr '21, 85% of workers who were worse off than before reported that they had reduced daily expenditure on food in response to the pandemic. Most workers now regard their household food intake as inadequate and many report experiencing hunger during the pandemic. Further, at least 28% report selling household assets to raise additional funds.

Our findings align with existing evidence that shows how the COVID-19 pandemic has intersected and heightened existing economic vulnerability of households in Cambodia. A study on the over-indebtedness of garment workers published by civil society groups (Licadho 2020) found that that two-thirds of garment workers were paying off at least one loan. 98% reported that their lives were "much worse" (80%) or "slightly worse" (16%) now compared to before taking out their microloan. Further research (Res 2021) illustrates that loan restructuring has not been made available to all borrowers, with inadequate outreach to households negatively impacted by the pandemic.

This study highlights widespread practices of "credit circulation" – where households borrow money to pay off existing obligations – and emphasises this can be harmful where it increases debt burdens. However, it also highlights that loan restructuring can be harmful too, particularly where, as recommended, interest-only (without principal) repayments are introduced as these increase the total cost for the borrower.

Garment worker loans



In their own words

"I was only suspended for one month, but I still needed to repay the loans to the bank. But how could I repay them? I sold all the assets I could and reduced daily spending. Now, I have nothing left."

Rotha, 45, Phnom Penh

"When I got a small amount of my salary, I had to keep it as saving for the loan repayment. I would reduce my food consumption."

Chanthou, 58, Phnom Penh

"Some banks won't approve loans to [garment] workers as they are afraid whether or not our factories will be closed and workers lose their jobs Before they gave out loans without too much consideration."

Kannareth, 33, Phnom Penh

Recommendations

Most of our field work was conducted prior to the implementation of Cambodia's national lockdown in April 2021. Continued transmission of COVID-19 in Cambodia has since caused further local lockdowns, quarantines, and infections among factory worker populations. We anticipate therefore that the financial situation of workers may have deteriorated since our research was conducted. There is an urgent need for action to ensure workers do not encounter further distress.

Global brands and retailers should act responsibly toward suppliers and workers in their supply chain by making complete and timely payments to suppliers; and establishing emergency funds to guarantee that workers receive full and regular income during the pandemic.

The Cambodian government should mandate that microfinance lenders prioritise client protection and care by introducing greater regulation of the microfinance industry, including enacting legislation to make the NBC's voluntary guidance on assistance for distressed borrowers legally-binding as available to all in need. There must be clear guidance on how the legal obligations of lenders will be implemented, monitored and enforced, including grievance mechanisms for borrowers and sanctions for lenders who fail to uphold their duty of care.

The microfinance industry and its international investors should ensure that client protection and care are prioritised by guaranteeing that loan restructuring or annulment is available to all clients who need it, without impacting on credit histories. This includes conducting sufficient outreach to inform borrowers of loan restructuring options; granting automatic rights to loan restructuring on request; and establishing appropriate grievance mechanisms to provide redress for households who are denied these rights.

Further reading

Brickell et al (2020) Compounding crises of social reproduction: Microfinance, over-indebtedness and the COVID-19 pandemic. *World Development* 136 [open access].

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Contact

This research brief was written by members of the ReFashion Study team. Our research project is ongoing. Find out more about the project by visiting our website, www.ReFashionStudy.org, and keep up to date by following us on Twitter, @ReFashionStudy
For further information about the contents of this brief or the project, please contact us via our website.

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