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AN ANALYSIS OF RISK ASSOCIATED WITH SOURCING SCANDALS

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ABSTRACT

Ethical sourcing scandals have created detrimental consequences and challenges for companies over the past decade. When these scandals arise, companies are exposed in varying degrees to supply disruption, brand detriment, and/or government intervention. Although great progress has been made in recent years regarding supplier auditing, to understand the true nature of the risk posed to supply chains one must understand what strategic factors lead to losses at the bottom line. Outlined in this paper are a series of four case studies, in which an industrial disaster is described, key buyers are identified, and the factors that did or did not lead to financial loss are better understood. As a result, this paper goes beyond confirming the negative public relations that accompany such events to identifying specific factors that lead to financial losses for impacted businesses. Additionally, there are several findings outlined in this thesis that include, but are not limited to, a higher comparative loss experienced by European companies over American companies, and greater fiscal damage from news generated by lawsuits. Overall, these sweatshop scandals rarely occur for companies are currently quite effective at auditing their suppliers and are continuously improving best practices for responsible sourcing programs.
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Chapter 1

Introduction

Off-shoring often times refers to the act of a domestic company sourcing its materials from foreign markets to enable the company to establish a foothold in that country, to take advantage of lower labor costs, or to place them closer to specific expertise or resources. This often times can provide higher margins for the company due to lower costs and growth opportunities globally, greatly contributing to shareholders’ bottom line. This results in increasingly complex supply chains with various import/export procedures, high transportation costs, and challenges that arise when conducting business with differing norms, legal structures, and labor environments that are inherent to foreign cultures.

Many high growth countries such as the BRIC countries (Brazil, Russia, India, and China) have emerging labor, discrimination, and sustainability practices which often times are not up to western ethical standards and practices (O’Neill, 2011). Although these practices may be customary for the country in which a company sources or places operations, there are many consumer awareness groups that will respond with actions that result in a negative perception of the firm. This can result in lower brand perception, significant supply disruption and prompt government regulation to raise worker safety. Ultimately, lower profitability might well be presumed to occur.

Instead of expanding on the literature related to the theoretical application of ethical labor concepts, this research seeks to understand the costs that unethical practices (by western standards) have on the bottom line of the firm in the form of public perception, brand equity, and supply disruption. Such understanding be useful to consumer protection non-profits engaged in
possible unethical practices so they could understand what sort of impact they would have on the bottom lines of these firms, in essence, the leverage they have as the result of their efforts. However, the primary target audience for this paper is industry strategic sourcing and business development professionals in publically traded companies that are potentially subject to ethically related supply chain risk. It would enable them to better understand the factors that lead to ethically related supply chain risk and thus enable them to take strategic preventative measures.

Two metrics that are used in this research. The first useful measure surrounding this type of scandal is financial data in the form of stock price, which would take into account all supply disruption, anticipated government regulation, and tarnished brand image. The second metric involves the conversation in public media, and shows how the public consumers and media view sourcing scandals through its life-span. With cohesive measures of these factors, we can see the effect this perception has on the firm, if any, and if people are willing to, as they say, “put their money where their mouth is,” or whether media conversation is “cheap talk,” having no actual effect on the financial viability of the firm.
Methodology

This research is focused on the effect that sourcing scandals have on large, multinational corporations with simultaneous brand presence in western economies and labor presence emerging and third world economies. Comparisons of the most widely conversed scandals over the previous ten years provide us with the ability to adequately differentiate the effect of widespread sentiment from other factors such as product announcements, management changes, and acquisitions/mergers.

There are two primary measures of conversation that will be used to conduct this research. The first is Google Trends, which measures and compares search terms to one another and will serve to measure time series trends of search terms since 2004. Second, we look to Lexis Nexis Academic (News Sources) to find the amount of “hits” associated with a search term. This measures the amount of times a term has come up in media outlets such as Newspapers, Web-based publications, News Transcripts, Press Releases, Newswires, Magazines, or Journals. This measure of conversation enables the ability to relate news to the instantaneous impact that it has on the stock price.

These measures of conversation will have an effect on stock prices over a certain amount of time, affecting prices both at the initial release of news relating to the topic, as certain aspects of the scandal becomes available, and as brand is tarnished due to high conversation and media attention. To measure these effects, key financial measures will be compared to weekly conversation on a topic and related to stock price to judge whether negative perception is related to stock price. In the special scenario of the pharmaceutical case, each press release resulted in a higher financial loss because they regarded financial loss as opposed to public perception, so the data had to be cleaned of product and quarterly stock announcements.
Chapter 2
Literature Review

Although there has been much research in the field of sustainable supply chains, there has
been no use of the method of analysis used in this research to quantify the value of these ethical
sourcing practices to the public relations value of the firm. Mefford (2011) outlines the cause and
effect involved with sustainable sourcing and the firms associated brand image, citing it as the
single most notable influential factor in determining the financial incentives for incorporating
corporate social responsibility in the supply chain. One point that this paper makes though, is that
information may be incorporated in a stock price over time rather than instantaneously, which
will need to be incorporated into the afore mentioned method of analysis. Likewise, McWilliams
& Siegel (2000) analyzes between whether a company is socially responsible or not and whether
it is associated with profitability provides a backdrop and motivation for us to understand the
risk/return of public image. Auger, Devinney, & Louviere (2003) shows a marketing analysis of
the exact question that pertains to this thesis. It finds that many people feel strongly about ethical
features but are generally ignorant of the origins of the products they consume. Aupperle,
Carroll, & Hatfield (1985) claims that although many studies make claims that there is a positive
relationship between corporate social responsibilities in general and profitability of the firm, the
most empirically rigorous models for assessing these correlations are at best inconclusive. This
paper itself makes the claim that there is an inverse relationship or trade-off between social
imperatives and the profitability of the firm, which they say is surprising because many managers
cite this as one of their highest priorities. Perhaps the most relevant academic paper to this topic
is outlined in Hoejmoso, Grosvold, & Millington (2013) where we see that socially responsible
supply chains are often not solely driven by the ethics and policies of sourcing managers but
rather by relative power with partners in the supply chain and extremely close geographic
distance from one another. It finds that relative power is the driver for companies to bring these
ethics to the bargaining table. Eltantawy, Fox, & Giunipero (2009) has a different perspective by
suggesting that more socially responsible supply chains are positively correlated to strategic
supply management skills, perceived reputation, and supply chain management performance.
This excludes the effect that size and company resources have on supply management. Pedersen
& Andersen (2006) focuses directly on the dimensions of codes of conduct that enable buyers to
enforce ethics. Consequences of Code of Conduct violations can include consumer sanctions,
negative press, capital loss, government interventions, etc. The problem that companies often deal
with is the agency problem, in which buyers must make a supplier vested in the relationship,
through joint partnership or joint strategic goals, and consequently the Code of Conduct. Ki-Hoon
& Ji-Whan (2009) seeks to understand the factors that affect the Korean electronics industry,
through both qualitative and quantitative methods. It also explores CSR adoption and
implementation in supply management in this industry. Locke, Amengual, & Mangla (2009)
focuses on the relative power in a supplier/buyer relationship and motivates the supplier to
comply with codes of conduct and suggests managerial implications for creating incentives and
coaching suppliers for higher performance potential rather than penalties for non-compliance.
Okongwu, Morimoto, & Lauras (2013) investigates the levels of maturity attained organizations
in reporting their supply chain sustainability initiatives. It concludes that the disclosure maturity
level is higher in business to business industries on both environmental and disclosing initiative.
Chapter 3
Bangladesh Fire 2012

Background

“The fire alarm shattered the monotony of the Tazreen Fashions factory. Hundreds of seamstresses looked up from their machines, startled. On the third floor, Shima Akhter Pakhi had been stitching hoods onto fleece jackets. Now she ran to a staircase. But two managers were blocking the way. Ignore the alarm, they ordered. It was just a test. Back to work. A few women laughed nervously. Ms. Pakhi and other workers returned to their sewing tables. She could stitch a hood to a jacket in about 90 seconds. She arranged the fabric under her machine. Ninety seconds. Again. Ninety more seconds. She sewed six pieces, maybe seven. Then she looked up. Smoke was filtering up through the three staircases. Screams rose from below. The two managers had vanished. Power suddenly went out throughout the eight-story building. There was nowhere to escape. The staircases led down into the fire. Iron grilles blocked the windows. A man cowering in a fifth-floor bathroom called his mother to tell her he was about to die. "We all panicked," Ms. Pakhi said. "It spread so quickly. And there was no electricity. It was totally dark." (Manik & Yardley, 2012)

The above quote was taken from a New York Times article published on December 18th, 2012 and regarding a fire on December 7th, 2012 directly outside of Dhkarta, Bangladesh. It is representative of many similar narratives that come from a tragedy like this, and serves as a point for conversation for western news outlets and social media. The factory was owned by Tazreen Fashions Ltd, a subsidiary of the Tuba Group. This particular site supplied retailers such as Walmart, Carrefour, C&A, Gap, Kmart, and Li & Fung. As the story unfolded, the death toll rose,
creating a negative perception for the supply chain partners who allegedly were required to take
responsibility for not properly auditing their suppliers. November 24th the death count was
estimated at 7 and by November 25th, the death toll jumped to 124 people (“Bangladesh fire death
toll jumps to 124,” 2012, “Garment factory fire kills 7 in Bangladesh,” 2012). These people both
died from severe burns as well as jumping to their deaths from the eight story building. This
launched a government investigation of the incidents that led up to the fire, eventually resulting in
the government official auditing the incident to blame the factory owner, Delowar Hossain, for
negligence. Allegedly, Mr. Hossain’s poor management led to nine midlevel managers pushing
factory workers to continue to sew in spite of a fire alarm that was sounding. In addition, a fire
certificate required to run the factory had expired, collapsible gates designed to prevent factory
workers from running down staircases, and lack of training programs for fire extinguishing
equipment all contributed to safety concerns within this factory (Manik & Yardley, 2012).

These events sparked various initiatives from governments, private companies, and non-
governmental organizations meant to increase worker safety and sourcing accountability. As a
result, various news sources generated conversation continuously on this topic, updating trading
partners, customers, and regulators on it. The firms mentioned below are key players in
relationship to this scandal.
Publically Traded Companies Affected by Bangladesh Fire 2012

**Wal-Mart Stores**: The top global retailer that sells a wide range of products to consumers and business, from food and apparel to hardware, household goods, and office supplies. With a market cap of over $240 billion, it is the largest retailer in the world, with retail locations internationally. The majority of Walmart retail locations are focused in the United States (Biesada, 2014h).

**Li & Fung**: A global provider of supply chain services, Li & Fung focuses on the sourcing, production and delivery of soft goods from South East Asian suppliers to western retailers such as Wal-Mart and Target. Western accounts account for 65% of sales. Li & Fung served as an intermediary for western retailers affected by this scandal (Lynett Oliver, 2014).

**Carrefour**: This global retailer operates over 9,700 stores with various strategies including hypermarkets, supermarkets, convenience stores, and cash-and-carry outlets. France is Carrefour’s largest market accounting for 43% of sales, followed by Belgium, Greece, Italy, and Spain, which collectively account for 29% of sales, Latin America, which accounts for 19%, and Asia, which accounts for 9%. This company in recent years has suffered from lackluster sales growth and weak growth markets in Europe. Thus Carrefour has attempted to re-focus its business model by spinning off its less profitable chains in Greece and Thailand to enable it to focus its efforts on domestic market share (Biesada, 2014a).

**Gap**: Gap is primarily a clothing retailer that has a variety of brands that include Banana Republic, Old Navy, Pimperlime and Athleta. Gap clothing is private label merchandise, and controls all aspects of its brand as a casual brand. The company has an expansion plan focused
almost equally on Europe and Asia, followed by growth in Africa, Asia and Latin America. The Gap has about 85% percent of its sales in North America followed by Asia accounting for 8% of sales, followed by Europe which accounts for about 6%. The market cap for Gap, Inc. is over $19 billion (Biesada, 2014g).

**Figure 1: Relationship between Negative News and Stock Price: Bangladesh Fire 2012**

**Conclusion**

The above figure indicates that there is a relationship, which is a .3 correlation or above between negative press and stock price in the case of a scandal, but not for a majority of the companies most mentioned. We expect to see a negative relationship between the stock price of the firm and the press associated with the scandal of their brand, if socially conscious consumers change their buying decisions based on poor ethically related sourcing decisions. In this scandal, we see that Walmart, Li &Fung, and Gap did not have strong relationships associated with stock
price and that Carrefour had a weak relationship with the negative news associated with their brand. We can therefore infer that labor sourcing scandals pose a greater risk to French clothing retailers than American retailers. This makes sense considering France has a more socially conscious consumer base and regulatory environment than does the United States. Regardless, even in France, socially conscious action and rhetoric has a weak relationship to the bottom line of clothing retailers.
Chapter 4
The Foxconn Suicides 2010

Background

Foxconn, is most highly associated with Apple as their Southeast Asian assembler of Ipods, Iphones, and Ipads, is the target of our second example of questionable ethical sourcing behavior. Ho-Hai Precision Corp., or the Foxconn Technology Group, is a Global 500 manufacturer and assembler of technology components, utilizing high engineering expertise and the low cost of the Chinese labor force to position itself as a supplier for European and American technology companies. The company employs over 800,000 workers in China and creates an ecosystem where these employees live in dormitories and work on assembly lines. These dormitories are one of the keys to Foxconn’s success, enabling them to create an environment that minimizes travel time to work, allows Foxconn to motivate workers, and maximizes time and effort put into production on assembly lines (Xu & Li, 2013). The utilization of labor as a resource for Foxconn is extremely high, allowing saving on training more employees, and creating an environment where the primary focus is value creation.

These strategies, workers’ rights group argue, enables the company to make workers work 80-100 overtime hours per month, far above the 36 hour per month legal limit, creating an environment where employees are under inhumane stress around the clock (Xu & Li, 2013). In addition, workers right group claim these laborers are paid about 300 dollars a month, social networks among workers are broken, bottom level management is harsh from lack of management training, and industrial injuries go unreported (Xu & Li, 2013). The assumption of news sources are that these suicides are a form of silent protest, although public reporting from
Foxconn buyers assert that the suicide rate at Foxconn is reduced from the general Chinese suicide rate. Regardless, this holistic approach to labor conditions has put Foxconn at odds with many labor rights activists in both Europe and the United States (Xu & Li, 2013).

As outlined in Appendix A, from January 23rd, to May 26th 2010, reports of twelve suicides from employees came from various sources, coupled with scant explanation from Foxconn. After the first few suicides, Foxconn management denied allegations, eventually taking measures that were seen as reactive, such as putting up suicide nets, and interviewing employees with psychologists to see that their emotional health was taken into consideration (Xu & Li, 2013). Eventually, the company made strategic moves to prevent these suicides, including raising worker wages, and moving manufacturing locations closer to workers’ hometowns (Epperson, 2014).

In addition to reflecting negatively on Foxconn, a publically traded company, many American technology manufactures including Dell Inc, Hewlett Packard, Nokia, Sony, Cisco and, most notably, Apple Inc. were publically chastised for not properly auditing this low cost manufacturer (Xu & Li, 2013). Non-governmental organizations such as “Make it Fair” and “Students and Scholars against Corporate Misbehavior” continuously updated the news media throughout this process and demanded the companies rectify this problem (“Suicides cluster at electronics giant in China: Foxconn - An appalling showcase for the global electronics sector — English,” 2014) (Howcroft & Taylor, 2013). Regardless, western news sources painted low cost suppliers and the American companies in partnership with them in a negative light. The most notable of these instances was an NPR broadcast by Mike Daisey titled “Apple Superfan” which consequentially sparked a flurry of media attention. Jon Stewart followed this broadcast by showing a special called “Fear Factory” (Cosh, 2012). Apple responded by releasing a corporate
social responsibility report detailing the problem, but continues, even to till the publication date of this paper, to deal with this as a public relations problem (Cosh, 2012).

Publicly Traded Companies Affected by Foxconn Suicides 2010

Hewlett Packard’s largest offerings are in PC’s and services which together account for 60% of sales. Printing contributes 20% of enterprise servers. Unlike its competition, this company has poorly adapted to today’s marketplace and is facing stiff competition in the tablet sector from many new entrants. Additionally, their printers are being substituted for digital document storage. HP is a global brand with 35% of sales come from the United States with 65% of sales coming from abroad. Retail sales are through third party resellers, online, in stores and through contracted systems dealers. The company has suffered from lackluster financial performance and decreasing market share. The company is looking to overhaul its strategy in the areas of security, big data, and cloud computing with the company exciting the smartphone and tablet business due to lackluster sales (Cother, 2014).

Dell Inc. is a top provider of PCs focused in four areas, consumer, education, and government, and enterprise. Servers, data storage, displays, and peripherals also provide also are part of Dell’s product offerings. In 2013, Michael Dell took the company private in a partnership with SilverLake Partners to avoid the scrutiny of Wall Street and better compete with PC manufacturers and cloud computing service providers. At Dell, 50% of revenue is generated domestically, the rest abroad. The company is targeting BRIC countries for sales growth (McLellan, 2014).

Nokia is the third leading manufacturer of cell phones, network infrastructure and telecom services, based in Finland with products sold in over 160 countries. European countries contribute
more than 30% of sales, US business contributes less than 5% of sales, with the remaining sales coming from other parts of the world. The company suffered from high competition from larger smartphone manufacturers Samsung and Apple (Huston, 2014).

**Sony** is a large manufacturer of consumer electronics with such offerings as TV’s, PlayStation 4, and audio. For commercial use they offer semiconductors, and computer components. In addition, they have a huge media portion to their business which includes music, film, DVDs and TV. Sony’s primary manufacturing facilities are in Southeast Asia. Sony’s single largest market by sales is Japan, which commands over 30%, with the US, Europe, and China also serving as key markets. Sony’s consumer products account for 45% of sales, despite high competition and decreasing market share. (Biesada, 2014f)

**Cisco** is a networking company that sells routers, servers, and their corresponding security devices. It sells its products primarily to large organizations and communications providers. Although 60% of Cisco’s sales are in the United States, the company maintains large operations in Belgium, China, France Germany, Israel, Japan, Norway, and the United Kingdom. Cisco has dominant economies of scale and high reputation in routing and servers, allowing them to take an aggressive pricing strategy and maintain market share. The company is taking an aggressive growth strategy focusing on next generation data center products (Biesada, 2014b).

**Apple Inc.**’s history has been marked by disruptive technology. It does so by creating an ecosystem that fits seamlessly together including Mac Desktop and Mac Books (laptop), iPods (music player), iPads (tablet), and iTunes (music store). Forty percent of its revenues are realized within the United States, with international markets including Europe, Japan, Africa, the Middle East, and Asia/Pacific. Apple sells its products through 250 retail stores in the United States and
140 international retail stores worldwide. It supports resellers by positioning and providing marketing materials within sellers. It also supports a large online presence, selling much of its product online. The company provides regular updates to its product line with additional features and faster speeds, but is very protective of product design, prompt supply chain delivery, and professional rollout (Anderson, 2014).

Figure 2: Relationship between Negative News and Stock Price: Foxconn Suicides 2010
Conclusion

With as much attention as Apple received in the news with regard to their supplier scandal, it is surprising that Apple’s stock price was not related to the negative press that Foxconn received with regard to the suicide. Likewise, Hewlett Packard, Dell, Nokia and Cisco had no discernable relationship (over/under .3 correlation) with the stock price of the firm and the negative news related to the suicides. We see that the one firm that has a discernable, negative relationship (over .3 correlation) is Sony. Sony has a majority of its sales in Japan, but key markets are also Europe and the United States. We can infer that in the case of technological sourcing scandals, Japanese consumers/regulators are more sensitive to ethically related supply disruption than their United States counterparts. Despite all the conversation relating to these scandals in the news, there is less socially conscious consumerism than conversation and publication surrounding technology scandals than garment scandals.
Chapter 5
Bangladesh Factory Collapse 2013

Background

On Wednesday, April 24 at 9 a.m in Savar, Bangladesh a sub-par working environment led to another tragedy related textile sourcing scandal. The Rana Plaza, was an eight story textile factory that housed more than 2,500 workers. (Saini, 2013) A government panel found after an investigation of the incident that substandard building material along with heavy machinery on the top floors of the building contributed to the collapse. (Al-Mahmood, 2013) The cause of many of the deaths associated with the collapse were buildings that were so close together that they did not allow victims to quickly escape, no emergency exits, as well as locking the main exits. After the tragedy, the building owner Rana, who had government approval to build the five story building but added three additional floors, creating an illegal eight story building. (“Rescuers give up on finding survivors in Bangladesh factory collapse,” 2013) After investigation, this factory collapse should have come as no surprise, as workers were said to have expressed their fears about the safety (“Dhaka tragedy raises calls for better working conditions,” 2013). This event sparked massive worker protests and resulted in the closing of 300 other factories which native workers created use as subject for poor working conditions and low minimum wages (Anonymous, 2013). The owners were among 13 people charged with culpable homicide following the fire, the first time the Bangladesh government has taken action against factory owners following similar fires (“Bangladesh fire disaster factory owners surrender to police,” 2014). The retailers involved in this supplier safety problem ranged from European retailers such as H&M, Carrefour, Inditex, and Mango to North American Retailers such as Walmart, Gap, Children’s Place, and Joe Fresh.
European Union regulators immediately became involved by reviewing its trade tariffs and exemptions and contributing suggestions to improve labor conditions for the production of Bangladeshi textiles (“Dhaka tragedy raises calls for better working conditions,” 2013). After this scandal, many top brands signed a code of conduct called the “Bangladesh Fire and Building Safety Accord,” an opt-in initiative that focuses on improving fire and safety standards. Notably, Wal-Mart and Gap refused to sign the initiative. Walmart claims their own supplier code of conduct and has taken action to inspect all their suppliers and make the results transparent. Gap, on the other hand cited legal concerns with signing such an agreement. All participants in the agreement must pay $2.5m toward the implementation of the initiative (“Bangladesh fire and building safety Accord: What retailers need to know,” 2013). Similarly, the Bangladesh Climate Change Resilience Fund has invested $170 million in infrastructure resilience, as well as preparing 40,000 people for emergency response training (McConnachie, 2013).

Publically Traded Companies Affected by Bangladesh Fire 2013

Hennes & Mauritz (H&M) features a falls in within the line of affordable but modern fashion and Home textiles. Like many European clothing retailers, H&M is growing extremely quickly and maintains a footprint of over two thousand stores worldwide in addition to a strong e-commerce business. H&M operates almost none of its own manufacturing, functioning almost solely as a marketing company. Instead, it outsources all production to suppliers in Asia and Europe to enable the company to focus on branding and retail growth. While 20% of H&M’s retail locations are in Germany, international expansion remains a key part of H&M’s strategy (Biesada, 2014c).
**Marks and Spencer Group** is a retail giant that not only operates department stores, but food stores in the United Kingdom. In addition, they lease over 300 locations in 40 countries around the world focused in Southeast Asia. Marks and Spencer has shown growth in its e-commerce sales, international sales and UK food sales. In recent years, its general merchandise and clothing lines domestically have faltered, with much of its domestic sales saved by its grocery offerings (Biesadsa, 2014).

**Carrefour** operates over 9,700 stores with various strategies including hypermarkets, supermarkets, convenience stores, and cash-and-carry outlets. France is Carrefour’s largest market accounting for 43% of sales, followed by Belgium, Greece, Italy, and Spain, which collectively account for 29% of sales, Latin America, which accounts for 19%, and Asia, which accounts for 9%. This company in recent years has suffered from lackluster sales growth and weak growth markets in Europe. Thus Carrefour has attempted to re-focus its business model by spinning off its less profitable chains in Greece and Thailand to enable it to focus its efforts on domestic market share (Biesada, 2014a).

**Industria de Diseño (Inditex)** focuses on extremely trendy clothing that is both chic and responsive to the fast changing fashion world. Although about a third of the fashion giant’s stores are located in its native Spain, Inditex sells on a global scale. Furthermore, Inditex’s geographic reach includes Asia, the Americas, the Middle East, and Africa even though they only have a small presence in North America. Low prices and high fashion have served Inditex well even in sluggish economies. Inditex’s growth strategies are focused on China and Europe. In all, they have 1,485 stores in over 70 countries and inventory turnover is extremely high as Inditex quickly reacts to changes and trends in the global marketplace. Inditex owns almost their entire supply chain, using this to keep prices extremely low (Biesada, 2014d).
Wal-Mart Stores is the top global retailer that sells a wide range of products to consumers and business, from food and apparel to hardware, household goods, and office supplies. With a market cap of over 240 billion, it is the largest retailer in the world, with retail locations internationally. The majority of Walmart retail locations are focused in the United States.

Gap is primarily a clothing retailer that has a variety of brands that include Banana Republic, Old Navy, Pimperlime and Athleta. Gap clothing is private label merchandise, and controls all aspects of its brand as a casual brand. The company has an expansion plan focused almost equally on Europe and Asia, followed by growth in Africa, Asia and Latin America. The Gap has about 85% percent of its sales in North America followed by Asia accounting for 8% of sales, followed by Europe which accounts about 6%. The market cap for Gap, Inc. is over $19 billion (Biesada, 2014g).

Loblaw Companies Limited is a Canadian brand of supermarket operators, and under its unbrelle it has conventional grocery stores, discount grocery stores, and wholesale food distributor. Additionally, it hosts under its umbrella the drugstore chain Shoppers Drug Mart. In addition, the company hosts the clothing brand Joe Fresh, which offers affordable clothing, cosmetics, clothing and jewelry at Loblaw’s stores. Their growth strategy is focused on consumer segmentation and supply chain improvements. (Biesada, 2014e)

Some Notable Exceptions include following: Mango, Primark, Benetton, Joe Fresh, Matalan, Bonmarché, and El Corte Ingles. These clothing brands are privately owned, and therefore it is impossible to track the financial implications of this factory collapse. Regardless,
all of these private companies signed an agreement to improve working standards and supplier auditing, indicating that these scandals pose risk to the firm.

![Diagram showing the relationship between negative news and stock price for Bangladesh Factory Collapse 2013](image)

**Figure 3: Relationship between Negative News and Stock Price: Bangladesh Factory Collapse 2013**
Conclusion

Contrary to expectation, Walmart had an inverse relationship to the negative news regarding the supplier scandal, experiencing no financial loss. According to LexisNexis News sources, the firms that experienced financial loss during this time were Marks and Spencer and The Gap. This is inexplicable, given that (1) Marks & Spencer signed the Bangladesh Building and Fire Safety Accord and thus might be perceived as socially conscious by its U.K. based customers, whereas (2) The Gap refused to sign the Accord and earns its sales revenue from U.S.-based customers who arguably are less socially conscious than their U.K. counterparts. Wal-Mart also refused to sign the Accord. Although this could risk loss of sales revenue for Wal-Mart, its more diverse range of product offerings (in comparison with The Gap) appears to have enabled it to mitigate that risk with other strategies and/or with possession of a less socially conscious consumer base. (“Bangladesh fire and building safety Accord: What retailers need to know,” 2013).
Chapter 6
Heparin Scandal 2007-2008

Background

Between November 2007 and February 2008, there was an increase in post injection deaths of Heparin, an anticoagulant used to prevent blood clots from forming in people who have undergone certain medical procedures and have certain medical conditions (Hedlund, Coyne, Sanford, & Huddelson, 2013). Heparin, as one of the oldest drugs in widespread clinical use, is administered in the amount of over 1 trillion units each year. Unfortunately, no synthetic process for producing this drug is possible, thus, pharmaceutical grade Heparin is created from porcine intestine. The extraction process involves boiling pig intestines, collecting mucosal membranes, then drying them and reprocessing them (Mintz, 2013). This processes are interestingly run outside of regulatory oversight of the State food and Drug Administration, China’s version of the United States Food and Drug Administration (Mintz, 2013). Consequently, they are not required to be produced within cGMP guidelines (Mintz, 2013).

In November 2007, healthcare workers in St. Louis observed nausea, hypotension, and swelling in children under dialysis. This was the first of many cases, triggering a US FDA investigation which related illnesses to heparin produces manufactured by Baxter Healthcare (Mintz, 2013). In response, Baxter Healthcare recalled 9 batches of Heparin (Hedlund et al., 2013). February 2008 production of the drug stopped, and the FDA investigated the Baxter supply of Heparin, eventually tracing the contaminated supply to a chemical plant in Ghangzhou, China, which was owned by Scientific Protein Laboratories (Hedlund et al., 2013). The FDA listed 62 reports of deaths relating to patients who experienced one or more allergic reactions and were infused with heparin from Jan. 1 2007 through March 2008. The FDA highlighted four main
breaches of cGMP practices were outlined in the FDA warning letter to Scientific Protein Laboratories (Payne, 2008).

- “There was no assurance that processing steps were capable of removing impurities”
- “Systems for evaluating the suppliers of heparin Crude materials, and the crude materials themselves, were inadequate.”
- “Test methods had not been verified to ensure suitability under actual conditions of use.”
- “Equipment used to manufacture heparin sodium USP was unsuitable for its intended use” (Payne, 2008)

Analysis of the contaminated product revealed the presence of over sulfated chondroitin sulfate, a contaminate that is linked to the same problems that patients were reporting (Mintz, 2013). Although this product is close to the chemical composition of Heparin, it is not a bi-product of actual production but rather chemically similar and less expensive, indicating that Scientific Laboratories had intentionally added over sulfated chondroitin sulfate to the drug to cut costs (Mintz, 2013). Regardless, blame regarding actual delivery to market was shared between FDA, SFDA, Baxter and Scientific Laboratories for each organizations alleged oversight. (Mintz, 2013)

The problem began when Baxter did not conduct an audit of the Scientific Laboratories facilities when they started using the supplier in 2004 and instead purchased the results of another company’s audit of the supplier (Mintz, 2013). When Baxter applied to the FDA for approval of this supplier facility, the FDA approved the application without pre-approval inspection ((Mintz, 2013). Even later, when Baxter audited the facility in 2007, they did not inspect the upstream facilities used to extract Heparin (Mintz, 2013). In a similar fashion, during investigation of the contaminated facility, the FDA was also denied access to the upstream supply of the Chungzhou plant (Mintz, 2013).
In relationship to the news break, both Baxter and Scientific Laboratories announced that they were taking accusations seriously, and opened their facilities up to FDA investigation. The Chinese government denied purposely supplying dangerous active ingredients to the market (Japsen, 2011). Following these findings by the FDA, Baxter was hit by numerous lawsuits that required the pharmaceutical giant to pay fines. Although Baxter has created a stricter auditing process for its suppliers, there continues to be high price competition and low regulation among Chinese suppliers, forcing the United States and other wealthy nations to actively work to update Chinese regulation (Mintz, 2013).
**Publically Companies Affected by Heparin Scandal 2007-2008**

**Baxter** is an Illinois based medical equipment and drug manufacturer who makes a wide variety of products through its two divisions. The equipment division of the company accounts for 55% of sales makes such medical products such as infusion pumps and prefilled syringes. The pharmaceutical division accounts for 45% in sales and has large investments in proteins, plasma, and hemophilia medicines. Baxter earns over half its revenues from sales in international markets and markets its products to a variety of outlets, including healthcare centers, physicians, and patients themselves. The company has maintained high growth through two strategic initiatives, the first being a high investment in Research and Development amounting to $1.15 billion in 2012. The second strategic initiative is a restructuring program in which they are streamlining manufacturing facilities and standardizing administration processes (Law, 2014).

![Figure 5: Relationship between Negative News and Stock Price: Heparin Sodium Disaster](image-url)
Conclusion

In the above analysis we conclude that the conversation regarding Baxter and Heparin during the timeframe of deaths caused by Heparin is extremely high, and although this study cannot be compared to other publically traded companies, it still supports the argument that the business environment surrounding pharmaceuticals differs greatly from lower margin businesses. Despite the lack of news generated from a pure publication standpoint, this particular study confirmed that consumer safety was at risk, fear of product use was created, products were recalled, and consequential lawsuits were undertaken as a result of this auditing issue.
Chapter 7
Key Insights, Limitations, and Future Research

It became evident from this research project that there is a disparity between the risk to the financial bottom line of a firm and the actual conversation relating to the topic. One of the reasons that labor safety is such a problem in emerging economies is due to the fact that consumers in western economies are only marginally economically motivated to pursue products and firms they view as socially conscious, creating an environment where firms can often cut more costs. That said European firms oftentimes initiate regulatory environments and consume in a more socially responsible manner, as the firms that had a large percentage of their sales bases in Europe experienced a discernable relationship more often than those that had operations and sales opportunities. Similarly, we see more firms that lead in the creation of improved ethically-responsible supply chains when they have less diversified product offerings associated with their company label. Finally, we notice that when the product poses a danger to the consumer above and beyond a concern for working conditions, we see that there is greater loss to firm from sources such as lawsuits and product recalls.

There were a number of limitations surrounding this work associated with acquiring access to data. There were many opportunities where private companies and investment firms were directly integral to a scandal, and calculating the financial loss to each of these firms would have been useful in understanding the nature these incidents. From a research perspective, in comparison to the amount of publically traded companies in western markets the number of times where these companies were exposed to newsworthy incidents was close to none. This suggests that companies are extremely efficient at mitigating the risk in their supply chains and although the media generates a high amount of newsworthy material surrounding these incidents, they pose very little financial risk to the supply chain.
Appendix A

Foxconn Suicide Events and Foxconn Press Release

Table 1 Timeline of Foxconn crisis and responses

<table>
<thead>
<tr>
<th>Date</th>
<th>Foxconn employee suicides and Foxconn responses</th>
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<tbody>
<tr>
<td>1. January 23</td>
<td>First case (Ma, Xiangqian, male, 19)</td>
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<td>2. January 25</td>
<td>Foxconn held a press release. While expressing sympathy to the victim’s family, the company denied the rumor that the victim was beaten to death during work by management and stated that the police are investigating the incident (Long and Li 2010, January 26)</td>
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<td>3. March 11</td>
<td>Second case (Li, Hongliang, male, 28) Foxconn confirmed the suicide but provided no comments (Ma and Wu 2010, March 12)</td>
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<td>4. March 17</td>
<td>Third case (Tian, Yu, female, 17) Foxconn confirmed the suicide, but provided no further comments (Xu 2010, March 17)</td>
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<tr>
<td>5. March 29</td>
<td>Fourth case (Liu, Zhijun, male, 23)</td>
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<td>6. March 30</td>
<td>Foxconn held a press release confirming the fourth suicide case. Foxconn expressed sorrow for the worker’s death, but provided no further comments, stating that the police’s investigation was ongoing (Enet 2010a, March 30)</td>
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<td>7. April 6</td>
<td>Fifth case (Rao, Shunqin, female, 18) Foxconn management said that this woman jumped because of relationship disputes that had nothing to do with work, but the specific situation needed to be confirmed by a police investigation (Wang 2010, April 7)</td>
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<td>8. April 7</td>
<td>Sixth case (Ning, Yaoqiong, female, 18)</td>
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<td>9. April 10</td>
<td>Spokesperson Liu Kun was interviewed by Yangcheng Evening News. Liu Kun stated that Foxconn should reflect on its management and corporate culture, but also claimed suicide is a societal problem and the company will not comment on the cases before the police completed their investigations (Chen et al. 2010, April 10)</td>
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<td>10. April 12</td>
<td>In response to criticism over Foxconn’s not disclosing the causes of the victims’ deaths, spokesman Liu Kun said doing so would be disrespectful to the victims and their families (Beijing Times 2010a, April 12)</td>
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<tr>
<td>11. April 17</td>
<td>Foxconn donated 30 million yuan (USD 4.4 million) for earthquake survivors in Yushu, Qinghai Province</td>
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<td>12. May 6</td>
<td>Seventh case (Lu, Xin, male, 24)</td>
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<td>13. May 7</td>
<td>Foxconn expressed ‘extreme pity’ on the seventh death and asked psychological experts for help (Dai 2010, May 7)</td>
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<td>14. May 11</td>
<td>Eighth case (Zhu, Chenming, female, 24)</td>
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<td>15. May 12</td>
<td>Foxconn invited monks to conduct a religious rite to dispel misfortune (Chengdu Evening News 2010, May 12)</td>
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<td>16. May 14</td>
<td>Ninth case (Liang, Chao, male, 21)</td>
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<td>17. May 19</td>
<td>Foxconn’s spokesperson Liu Kun told the press that the causes of the suicides lie in the victims themselves (Beijing Times 2010b, May 19)</td>
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<td>18. May 21</td>
<td>Tenth case (Nan, Gang, male, 21)</td>
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<td>19. May 24</td>
<td>Foxconn CEO Terry Guo remarked on the series of suicides for the first time and stated that Foxconn is not a sweatshop (China News Net 2010, May 24)</td>
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<td>20. May 25</td>
<td>11th case (Li, Hai, male, 19) Terry Guo sent two public letters to Foxconn employees after the 11th case</td>
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<td>21. May 26</td>
<td>Terry Guo arrived at the Foxconn Shenzhen factory, starting a series of crisis management efforts, including opening the Foxconn Shenzhen factory to the media and public for the first time (Information Times 2010, May 27)</td>
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<tr>
<td>22. May 26</td>
<td>12th case in the evening (Last name He—first name was not disclosed, male, 23)</td>
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<td>23. June 2</td>
<td>Foxconn declared a base monthly pay raise of 30%, from 900 yuan (USD 135) to 1200 yuan (USD 180)</td>
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<tr>
<td>24. June 6</td>
<td>Foxconn declared another pay raise for qualified employees. The monthly wage was raised by another 66%, from 1200 yuan (USD 180) to 2000 yuan (USD 301)</td>
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</tbody>
</table>

The news items listed in the table are exemplary and not comprehensive. They were selected based on two criteria: (1) they covered one of the 12 suicide cases, and (2) they provided information on Foxconn’s response. (Xu & Li, 2013)
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