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Home textiles being made by one of our suppliers in Shunde, China.





## **Our supply chain**

We partner with our customers and suppliers to create value through the supply chain.

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# Our supply chain

We are reimagining today's supply chains to create a digital end-to-end network, from factory workers to consumers, that helps our customers and supply chain partners future-proof their businesses.

**15,000+**  
SUPPLIERS WORLDWIDE

## TOP FIVE SOURCING COUNTRIES

-  China
-  Vietnam
-  Bangladesh
-  Indonesia
-  India

*\* The ranking is based on sourcing unit volume.*

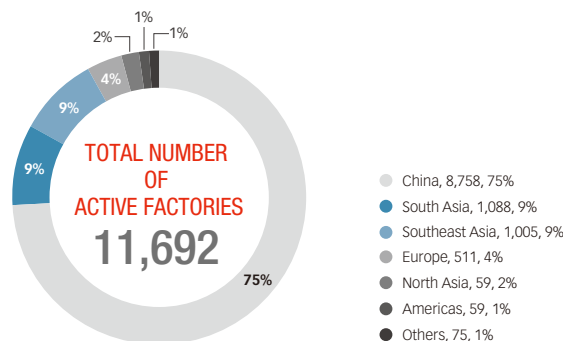
At Li & Fung we manage complex and unique supply chains from a network of over 15,000 suppliers in more than 40 economies around the world for our customers. Over the past 110 years, we have been developing and cultivating this network to help our customers navigate increasingly complex supply chains. Over 80% of our sourcing business by volume is concentrated on a core group of strategic suppliers that we work with over the long term, and where our positioning gives us more leverage and economies of scale.

Beyond this, we continue to work with thousands of other suppliers across major and secondary production countries so we can balance capacity constraints, deliver quick responses close to the end consumer, or respond to unforeseen incidents which may affect certain geographies. Lastly, we continuously search to complement our core network with suppliers who bring us diversity in terms of their specific capabilities, unique technical skills or specific equipment.

Addressing challenges and opportunities in our supply chain is integral to our Sustainability Strategy. Our initiatives focus on three areas:

- Managing risk and furthering compliance in our supply chains
- Sourcing responsibly
- Collaborating with customers, suppliers and other partners to build sustainable supply chains

## Number and Percentage of Active Factories<sup>1</sup> by Region



<sup>1</sup> Active factories had orders shipped within 24 months prior to 31 December 2016. Due to rounding, the percentages do not total exactly to 100%.

## Supply Chain Compliance

We manage supply chain risk through a process involving risk assessment and strategic decision making whereby we direct and develop business with suppliers who have enhanced capability and lower risks, while supporting other suppliers to improve their performance.

Supplier risk assessment starts with Li & Fung's Supplier Code of Conduct<sup>2</sup> that outlines the minimum standards, in accordance with the International Labour Organization's Core Conventions and local laws, for human rights and labor, safety, environment and security, as well as transparency and ethics. All suppliers must accept these minimum standards as a condition of doing business with us. The Supplier Code of Conduct is complemented by Guidelines which offer suppliers advice and practical resources for implementing the Supplier Code of Conduct within their operations.

Performance against the Supplier Code of Conduct is assessed by Li & Fung, external audit firms approved by us or our customers, or independent industry organizations. When non-compliance issues are identified, the factory is required to commit to rectifying the issue through a Corrective Action Plan, with varying timelines from immediately to three or six months, depending on the severity of the issue. We also continually monitor our factory network for one-off incidents that may occur outside of the assessment cycle. Should these occur, we immediately investigate and track remedial actions on an ongoing basis. In every case, our concern is to protect the workers in the factory concerned, reduce the risk, and support the factory for business continuity.

To support suppliers in their efforts to improve performance, we offer tailored programs to meet factories' needs for training and capability building on a variety of topics. Our goal in offering these programs is to equip suppliers with the skills to develop their businesses sustainably and drive their own continuous improvement.



**We are committed to building sustainable and responsible supply chains that are transparent.**

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**Richard Darling,  
Head of Government and  
Public Affairs**

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<sup>2</sup> <https://www.lifung.com/wp-content/uploads/2015/03/CoC2015-English.pdf>

The diagram below illustrates the complete risk management cycle:



The above risk assessment and management process is supported by the continued roll out of our Observer Development Program, which trains and certifies quality assurance and control (QA/QC) teams to identify potentially high-risk safety and labor issues within the factory. The program leverages the fact that the QA/QC teams are in factories on a daily or weekly basis, thus significantly boosting our ability to manage and monitor risk. The teams also engage with factory management on a range of other issues, and their presence as a supplement to our risk assessment process has been beneficial. To date, 43% of our QA/QC personnel have been trained as certified observers.

### Supplier Monitoring Process

To stay abreast of changing industry and regulatory requirements, Li & Fung continually engages directly with policymakers and participates in a number of industry consortiums that contribute to the development of relevant standards and norms. In recent years, we implemented changes to align our systems to the requirements of the California Transparency in Supply Chains Act and the UK Modern Slavery Act. The 2015 enhancements to our compliance process included updated versions of the Supplier Code of Conduct, accompanying Standards and Guidance, the introduction of a new audit tool, rating and grading system, as well as an expanded audit equivalency program and audit scope. Our new process has broken new ground in two key ways:

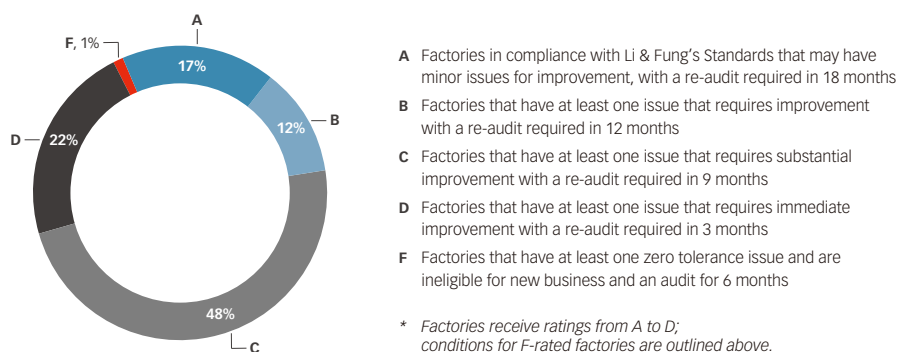
- By outsourcing the majority of onsite audits to four key industry social compliance audit firms, we increased visibility into our active factories
- By rolling out our global equivalency program, over 70% of active factories were able to reduce the number of audits that they were subject to, by submitting a single report to a certified standard (including Better Work, Fair Labor Association and Business Social Compliance Initiative)

This evolving compliance process aims to reduce costs in the supply chain and allow suppliers to focus their efforts on implementing improvements in their operations to achieve sustainable compliance, instead of on repetitive, resource-draining audits. The expanded visibility and information that is available from this new process allows us to assess supply base compliance risk more effectively and establish a baseline from which future improvements and goals can be directed. Response from suppliers to our new process is increasingly positive when they are directed towards one set of requirements and improvements.

Global compliance ratings for factories in our supply chain, as assessed by Li & Fung and external parties, and by our customers' rating processes, are provided below. As critical issues are identified, suppliers are required to remediate for sustained change through awareness raising, training and building management systems to achieve and maintain compliance. Information gathered to date raises similar issues to those found in the rest of the industry, with the top three areas related to: social benefits, safety and working hours.

Our involvement in industry platforms and our collaboration and relationships with our customers and other industry players allows us to leverage greater and unified resources to assist suppliers to make lasting changes to workplace conditions. We will continue our efforts to support our suppliers as developing and working with an accountable and motivated supplier base creates a win-win situation for every stakeholder in the supply chain.

### Factory Compliance Ratings Aggregated Globally<sup>3</sup>




<sup>3</sup> Based on active factories rated by Li & Fung and third parties with orders shipped within 24 months prior to 31 December 2016.

Sustainability Resource Center  
Website Metrics in 2016

 **5,824**  
WEBSITE VISITS

 **33,326**  
PAGE VIEWS

 **3,787**  
RESOURCE  
DOWNLOADS

 **2,338**  
VIDEO VIEWS  
AND/OR DOWNLOADS<sup>4</sup>

### Supplier Capacity Building

We are committed to building capacity across our supply chain to improve general working conditions for workers and enhance efficiency and investment in the supply chain overall. Improving factory operations and performance contributes to our long-term goal of building sustainable global supply chains.

Li & Fung’s assessment, technical support and capacity-building efforts focus on establishing better-managed factories with improved working conditions. We believe that to achieve sustained change in the supply chain, it is essential to support factories to meet compliance standards, and to also ensure that suppliers have the knowledge and training needed to integrate social and environmental best practices into their day-to-day operations.

To further these objectives, we continue to implement training programs for factory representatives and our own employees on a number of topics, including new international requirements, local regulations and customer-specific requirements. In 2016, we held over 630 sessions for more than 8,240 factory representatives and 3,570 of our own employees.

A snapshot of the types of training provided to our employees and suppliers in 2016 is presented in the table below.

Audience	Training Topics
Li & Fung Employees	<ul style="list-style-type: none"> <li>• Conflict Minerals</li> <li>• Greenpeace’s Detox Campaign</li> <li>• Environmental Management</li> <li>• Human Trafficking &amp; Forced Labor (Modern Slavery)</li> <li>• Lean Manufacturing</li> <li>• Observer Development Program</li> <li>• Subcontracting Standard</li> <li>• Sustainable Apparel Coalition (SAC) Higg Index Verification</li> </ul>
<b>No. of People Trained:</b> 3,579 employees	
Li & Fung Suppliers	<ul style="list-style-type: none"> <li>• Achieving C-TPAT Standards</li> <li>• Achieving Sustainable Compliance</li> <li>• Conflict Minerals</li> <li>• Employment Practices &amp; Employee Relations</li> <li>• Environmental Sustainability</li> <li>• Fire &amp; Electrical Safety</li> <li>• Hazards Identification &amp; Risk Assessment</li> <li>• Human Trafficking &amp; Forced Labor (Modern Slavery)</li> <li>• Li &amp; Fung Code of Conduct Orientation</li> <li>• Root Cause Analysis</li> <li>• Social Dialogue</li> <li>• Subcontracting Standard</li> <li>• Worker Management Communication</li> </ul>
<b>No. of People Trained:</b> 8,247 factory representatives	

<sup>4</sup> This includes a total of 16 videos in 14 languages on the topics of good governance, manufacturing excellence, underage labor, managing working hours, worker management relations, chemical safety and electrical safety.

In 2016, we continued to shift the strategic focus of our compliance work from offering audit-based services to remediation and capacity-building services. We provide our suppliers with the education, training and tools to upgrade their operations and comply with industry and international standards.

Examples of the training modules we offer include:

- An orientation program for generally-accepted compliance standards, including our Supplier Code of Conduct and accompanying Guidance
- Introduction to basic principles of safety management in factories, including the most common issues of fire, electrical, building and structural safety
- Tailored programs focused on good practices and management systems to sustain compliance

Our Sustainability Resource Center website continues to evolve and provide suppliers with multilingual compliance resources and tools, industry updates and training schedules designed to help suppliers better understand key compliance and operational issues. Videos on a range of topics and targeted at both management and workers are available on our website. In May 2016, we made these 16 videos in 14 languages publicly accessible on a dedicated YouTube channel. They have since been viewed over 18,700 times.

 Visit our YouTube channel<sup>5</sup> to view our videos in multiple languages.

Toolkits on how to improve key areas of business operations are also available on the website and cover topics such as:



<sup>5</sup> [https://www.youtube.com/channel/UCaIV\\_MGCKl0prY88YHpEaLg](https://www.youtube.com/channel/UCaIV_MGCKl0prY88YHpEaLg)



In 2016, we also conducted a total of 2,304 training sessions in 15 countries across our global supply chain, including Bangladesh, Cambodia, China, Guatemala, India, Indonesia, Korea, Mexico, Pakistan, Philippines, Sri Lanka, Taiwan, Thailand, Turkey and Vietnam, on material issues related to compliance and performance improvement, as outlined below:

**TOTAL NUMBER OF TRAINING SESSIONS: 2,304**



<sup>6</sup> "Others" cover a variety of topics ranging from HERproject workshops in Bangladesh to customer-specific compliance training sessions.

### Social Dialogue Program – Bangladesh

To raise awareness of and improve the relationship between factory management and workers, we launched a social dialogue program for our supply base in Bangladesh (outside the Export Promotion Zones). We are among the first in the industry to launch a program targeting middle management in Bangladesh with a focus on freedom of association, participation committees, safety committees and grievance handling. The program was developed in partnership with Just Solutions, a UK-based organization with extensive experience in improving industrial relationships in Bangladeshi factories.

Since the launch of the program in February 2016, we have conducted four, half-day introductory sessions covering 96 suppliers across 152 factories and 185 members of factory senior management.

Following the introductory sessions, we conducted a further 20, three-day sessions attended by 360 participants from 106 factories. The training raised awareness among factory management of the advantages of actively engaging workers in constructive workplace dialogue and of best practices in successful social dialogue from other factories. Participants gained deeper insight into the increasing importance of the ability of factory owners and managers to lead the development of mature social dialogue and engagement with workers. The program is expected to continue into 2018.

### Worker-management Communication Program

We recognize that improving worker-management communication is the basis of a sustainable enterprise and positive working conditions. Without effective two-way communication, workers and management do not have a foundation to raise concerns and effect change. To bring this value into our supply chain, Li & Fung engaged the Swiss training and coaching consultancy Equiception to train our own employees on worker-management communication and facilitation skills that can be deployed in our supplier training programs.

The program was initially launched in China, where a number of factories are now engaged through training, and has been expanded to other markets in our global supply chain.



## Sustainable Sourcing

Our approach to sustainable sourcing is to work with our customers, suppliers and industry partners to further the adoption of standards and best practices. We also provide our customers with sustainable design, manufacturing, product and packaging options, to meet customer requests for sustainably-sourced materials and products with reduced environmental impact from well-managed factories.

Some of the ways we helped customers source products and packaging with sustainability attributes include:

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### Apparel



- Garments that comprise:
  - > Cotton from certified organic sources, such as the Global Organic Textile Standard
  - > Cotton that meets the Better Cotton Initiative standard, Fairtrade standards, the Organic Content Standard 100 or Blended and/or has been produced by mills that have joined Cotton LEADS™ as partners
  - > Cotton from traceable sources with country of origin certificates
  - > Linen from certified organic sources
  - > Recycled yarn, polymers, leather and shearling
  - > Wool from traceable sources that meet non-mulesing declaration requirements
  - > Fur-free materials and/or responsibly-sourced angora wool or down feathers
  - > TENCEL®, a Lyocell fiber produced from sustainably-harvested wood in a closed loop, water-efficient process
  - > Teflon EcoElite™ water-repellent, a non-fluorinated fabric treatment that is manufactured with 60% renewably-sourced raw materials
  - > Hangtags made of recycled paper
- Garments that are shipped in polybags from recycled materials and/or are shipped in a “flat pack” without the use of hangers
- Textiles that are independently tested and certified to meet the Oeko-Tex® Standard 100 criteria, REACH requirements and/or are produced in factories certified under the bluesign® system
- Textiles and shoes sourced from suppliers that are phasing out hazardous chemicals in production for customers committed to Greenpeace’s Detox campaign
- Leather for shoes, wallets, covers and pouches produced from tanneries that are audited against the environmental responsibility practices of the Leather Working Group

**Beauty Products**



- Items that are biodegradable, not tested on animals and free of silicones, sulphates, parabens and colorants
- Products that meet industry standards and incorporate ingredients such as community trade olive oil, shea butter and brazil nut oil, RSPO-certified<sup>7</sup> palm oil derivatives and organic babassu oil, fine sugar and rosehip oil in formulation design. Our manufacturing facility in Trowbridge uses raw materials certified to the Soil Association's organic standard and its usage of organic and community trade ingredients increased from 71 tonnes in 2015 to 74 tonnes in 2016
- Product packaging and carton board that is Forest Stewardship Council<sup>TM</sup> (FSC<sup>TM</sup>)<sup>8</sup>-certified
- Wet wipes that comprise 100% cellulose fabric and are dispersible and biodegradable
- Toothpaste that was the first to be certified as organic in the world under the Oregon Tilth certified organic (OTCO) program; our manufacturing facility in Tonawanda also is a member of Oregon Tilth and is a FDA-registered manufacturing facility. The facility manufactures a variety of products with OTCO Certification Acknowledgement, which are declared by Oregon Tilth to be in compliance with the NSF/ANSI 305 Organic Standards program, as well as products that meet the Natural Products Association (NPA) Natural Standard, certifying that they contain natural/biodegradable ingredients, are manufactured with appropriate processes to maintain ingredient purity and have environmentally-responsible packaging
- Additionally, we are working with a customer to develop a dedicated product stewardship program to assess and improve the sustainability of products, packaging and manufacturing processes

<sup>7</sup> Palm oil derivatives certified under the Roundtable for Responsible Palm Oil (RSPO)'s mass balance or segregated models.

<sup>8</sup> FSC license number FSC-C113132.

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**Household and  
Other Items,  
Furniture and  
Packaging**



- Household items, furniture and packaging made from wooden/paper materials that are FSC<sup>9</sup> or Programme for the Endorsement of Forest Certification (PEFC)-certified, and meet the chain-of-custody requirements of the European Timber Regulation (EUTR) where applicable
- Household items, utensils and furniture made from natural materials and fibres ranging from bamboo, roots and branches of organic teak wood and wood from spent rubber trees, to banana bark and water hyacinth
- Gadgets made of recycled plastic and photo frames comprising recycled polystyrene foam, with recyclable packaging
- Packaging, luggage and other items using polyethylene terephthalate (PET) instead of polyvinyl chloride (PVC), polypropylene (PP), polycarbonate (PC) or acrylonitrile butadiene styrene (ABS), as well as PVC-free packaging material for polybags, clips, gum tape, strings, collar inlays and zippers
- Reporting to customers on the processes in place and supplier compliance in meeting legislative requirements related to chain-of-custody requirements for wood products<sup>10</sup> and components containing reportable minerals<sup>11</sup>, and required testing standards, such as BIFMA<sup>12</sup> for furniture. This includes conducting product risk and traceability assessments for customers by raw material categories

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<sup>9</sup> FSC license numbers FSC-C113132, FSC-C114681, FSC-C116575 and FSC-C129309.

<sup>10</sup> As per the United States' Lacey Act of 1900.

<sup>11</sup> As per the United States' Dodd – Frank Wall Street Reform and Consumer Protection Act of 2010.

<sup>12</sup> Business and Institutional Furniture Manufacturers Association (BIFMA).



## Industry Collaboration

Li & Fung is involved in key industry initiatives that bring our customers and industry partners together to effect change. Our collaboration efforts are focused on implementing programs that address the particular challenges of our industry and specific production countries where we operate.

### Bangladesh

We remain actively engaged in key collaborative efforts in Bangladesh, working with governmental and non-governmental organizations, industry partners and suppliers to improve factory conditions.

As advisors to the Boards of both the Alliance for Bangladesh Worker Safety (Alliance) and the Bangladesh Accord on Fire and Building Safety (Accord), we fund and engage with both programs at the highest level. In 2016, both initiatives focused on education and the remediation of safety issues that surfaced through in-depth safety audits. We jointly organized a number of activities and reviewed progress over the course of the year, all of which contributed to continuous improvements being made by suppliers:

- Li & Fung representatives participated in 459 factory visits and 199 meetings with factories to support the Alliance and the Accord
- Two training sessions were held and attended by over 180 factories with a total of 246 participants
- Li & Fung arranged 24 joint meetings with other signatories/brands of the Accord and the Alliance for 65 common factories to expedite remediation

In addition to our support of the Alliance and Accord initiatives, we continued to conduct training sessions on fire, structural and electrical safety for factory management and workers, and to strengthen the capability of our own QA/QC and merchandising teams in Bangladesh on these same compliance issues.

### Cambodia

Since 2014, we have engaged with the Government of Cambodia to raise awareness of building safety. This effort led to the establishment of an inter-ministerial Working Group to develop Cambodia's Building Safety Code, comprising the Ministries of Land Management, Urban Planning and Construction, Labor, Industry and Handicraft, Health, Interior and Environment. The International Code Council was appointed as the technical advisor to the Working Group to assist in drafting the Building Safety Code. The draft Code has been submitted to the inter-ministerial Working Group for review and is currently undergoing intensive discussion and finalization.





### Better Work

Li & Fung continues to be an active Buyer Partner of Better Work. In 2016, we specifically supported the program in Bangladesh, Cambodia, Indonesia, Jordan and Vietnam.

### Business for Social Responsibility (BSR)

We continue our partnership with BSR to implement the HERproject, with the support of the Fung Academy. The project uses impactful peer-to-peer training and a local partner network to empower primarily female workers through education on nutrition, health and finance, and on improving workplace interaction, harmony and efficiency. Since 2015, indications of positive impact from the project show reduced absenteeism and sick leave and improved workplace communication.

Country	Program	No. of Factories	No. of Workers
Bangladesh	HERhealth	41	87,000+
Cambodia	HERhealth + Nutrition	11	17,000+
India	HERhealth + HERfinance	20	43,000+
Vietnam	HERhealth	15	31,000+
<b>TOTAL</b>		<b>87<sup>13</sup></b>	<b>178,000+</b>

▶ Visit our YouTube channel<sup>14</sup> to view a video of how we make an impact with the HERproject in Cambodia.

### Center for Child Rights & Corporate Social Responsibility (CCR CSR)

Li & Fung participates in the Hong Kong working group focused on the prevention and awareness raising of underage labor in the supply chain. In 2016, our teams in China and Southeast Asia also participated in a survey conducted by CCR CSR to identify key aspects related to underage labor and standard processes in place for remediation. The survey data informed the 2016 Connors report<sup>15</sup>, "Insights on Child Labor Response Practices in Asia Pacific."

<sup>13</sup> As the HERproject continues over annual reporting periods, some factories complete and others join the program during the reporting year. In 2016, the program reached over 4,000 more workers than in 2015.

<sup>14</sup> <http://www.youtube.com/watch?v=eGWYP0fF5u8>

<sup>15</sup> <http://www.ccrsr.com/resource/548>

### **Mekong Club**

We established a partnership with the Mekong Club on a focused initiative around modern slavery. The first step was to hold a workshop in September 2016 on how to raise internal awareness on the issue of modern slavery, and to start the joint development of a risk assessment tool. We will continue to partner with the organization on sustainable solutions to address modern slavery.

### **Sustainable Apparel Coalition (SAC)**

#### **Higg Index**

We continue to be actively involved in the development of the Higg Index, a suite of sustainability tools to help organizations standardize measurement and evaluation of the environmental performance of apparel products at the brand, product and facility levels.

In 2016, Li & Fung participated in the SAC's regional and global meetings, provided input on the Higg Analytics platform and worked with a key customer and the SAC to pilot Advance Analytics for Higg Index data. As SAC makes further updates to the tool, we will support further pilot testing in a number of factories in 2017. Additionally, Li & Fung was certified as a preferred service provider for environmental training and onsite verification activities for factories as recommended by SAC and its members. In addition, we also continue to support the SAC's partnership with the Natural Resources Defense Council to implement Clean by Design, an initiative to reduce environmental impacts from manufacturing, in several textile mills in China.

#### **Social and Labor Convergence Project**

Li & Fung is a signatory to the SAC Social and Labor Convergence Project, an industry collaboration project launched in 2016, which seeks to develop a simple, unified and effective industry-wide assessment framework. In this project, we participate in the working groups for tool development and verification to provide valuable contributions through both our customer and supplier insights and our experience with creating a convergence tool for our diverse customer and supply base.

