



# Fast Fashion: Why Brands Need to Consider ESG to Slow Down

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## Fast Fashion Facts

**93%** of fashion brands aren't paying their garment workers a living wage

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**3 out of 5** fast fashion garments end up in a landfill within a year of purchase

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It takes over **1800** gallons of water to produce a pair of jeans

Source: <https://wearzeitgeist.com/blogs/hearsay/fast-fashion-statistics>

## Key Takeaways

- The Boohoo scandal highlights the importance of labour practice management in the supply chain, particularly for the fashion industry
- ESG risks can have a negative impact on a company's share price and reputation
- Companies should proactively integrate ESG into their business models, as stakeholders are increasingly evaluating a company's supply chain from an ESG perspective.

**100 billion** items of clothing are produced each year

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The fashion industry is responsible for **8-10%** of global greenhouse gas emissions





## The Backstory

From generation to generation, as societies have evolved and the world has changed, one thing has remained the same: our need for clothes. A few generations ago, it was a common and wholesome practice for people to wear hand-me-downs, which increased the longevity of garments. But in the 1990s, consumer behaviour changed and hand-me-downs started to go in the bin.

When fashion retailer Zara opened its first US store in New York in 1989, the New York Times coined the term “fast fashion” to describe the store’s mission, emphasising that it only took the brand 15 days for a garment to go from a designer’s brain to being sold in stores.<sup>1</sup>

Fast fashion made the latest trends available at lightning speed and at extremely cheap prices. Who even wanted to consider the negative implications this business model had for the environment or human rights when the clothes looked this good?

## The Birth of the Conscious Consumer

Fast forward to 2021 and consumers have woken up. Last year, as the world was hit by a global pandemic, lifestyles and priorities changed, which resulted in a heightened social and environmental consciousness amongst consumers. For the fashion industry, Environmental, Social and Governance (ESG) factors became the “new management approach”.<sup>2</sup>

The pandemic also gave ESG the opportunity to prove its merit – companies with ESG considerations embedded in their business strategy were less impacted by the pandemic.<sup>3</sup> Mara Hoffman, a brand rated ‘great’ for its environmental considerations,<sup>4</sup> decided to scale back and not produce its already-designed Fall 2020 collection – a move the brand was applauded for. Instead, the brand repurposed its existing inventory, committing itself to working with what they had as opposed to “creating newness to pile on to an already existing mountain”.<sup>5</sup>

On the contrary, fast fashion brands that were using sweatshop labour to churn out orders found themselves in hot water.

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1 <https://fashionista.com/2016/06/what-is-fast-fashion>

2 <https://wwd.com/business-news/financial/esg-fashion-beauty-retail-management-finance-disclosures-1234582913/>

3 <https://www.ft.com/content/50eb893d-98ae-4a8f-8fec-75aa1bb98a48>

4 <https://directory.goodonyou.eco/brand/mara-hoffman>

5 <https://fashionista.com/2020/11/sustainable-fashion-brands-covid-19-pandemic-strategy>



## The Boohoo Case

Fashion e-tailer Boohoo's reputation took a beating when the flaws in the company's supply chain were brought to the surface last year. The factories in Leicester (UK) producing clothes for the brand were accused of paying workers less than the UK minimum wage and having poor standards of health and safety.<sup>6</sup>

Post the allegations of worker exploitation within its supply chain, Boohoo published a statement in July 2020: "We will not hesitate to immediately terminate relationships with any supplier who is found not to be acting within both the letter and spirit of our supplier code of conduct".<sup>7</sup> The company also highlighted in its statement the measures it had taken to strengthen its teams, procedures and processes. Some of the actions taken included appointing its first Sustainability Director in 2019 with a focus on developing the company's sustainability initiatives and supply chain governance.

However, in September 2020, the findings of an independent review commissioned by Boohoo were published. The review identified many failings in the Leicester supply chain and recommended improvements to Boohoo's related corporate governance, compliance and monitoring processes.<sup>8</sup> Following the publication of the independent review, Boohoo CEO John Lyttle commented that the group had to go "further and faster" to improve its processes, adding that the company planned to implement necessary enhancements to its supplier audit and compliance procedures, and increase the board's oversight of these matters.<sup>9</sup>

Though the company has made efforts to reassure the market it will take the necessary steps to strengthen its governance and internal processes, it is difficult for any company to undo the damage of serious allegations of misconduct. Good On You, the world's leading source for fashion brand ratings, highlights in its evaluation of the company that Boohoo "is not taking adequate steps to ensure payment of a living wage for its workers" and has also given the brand a 'not good enough' environment rating, on the basis that the brand "does not use eco-friendly materials. There is no evidence it has taken meaningful action to reduce or eliminate hazardous chemicals. It measures and reports greenhouse gas emissions from its direct operation but not its supply chain. There is no evidence it implements water reduction initiatives".<sup>10</sup>

6 <https://www.theoxfordblue.co.uk/2020/09/22/has-the-boohoo-scandal-changed-the-tide-on-fast-fashion/>

7 <https://markets.ft.com/data/announce/full?dockey=1323-14603695-4IIAJFC8RMFFDE1OI86EUM1VNV>

8 <https://www.essentialretail.com/news/boohoo-responds-review-supply-chain/>

9 ibid

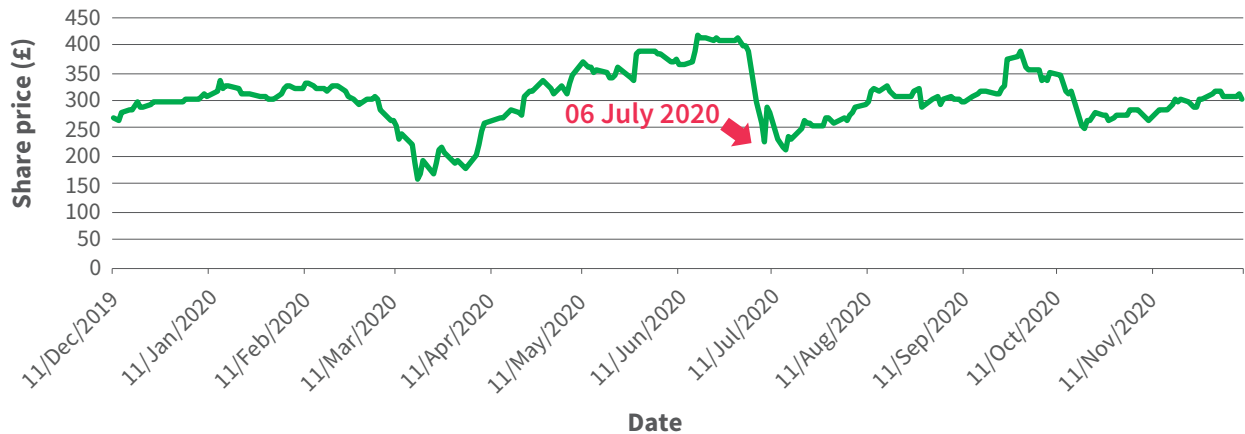
10 <https://directory.goodonyou.eco/brand/boohoo>



## Market Reaction Post the Scandal

Given the negative media attention gained by the Boohoo scandal, the share price of the company was inevitably impacted. In the below graph we took a look at how the company's share price plunged. On July 6, Boohoo's share price dropped by approximately 23% (from £387 to £296 per share), a day after an article was published highlighting worker exploitation at the Leicester factory.

Share price of Boohoo (LSE listed)



The share price seemed to pick up in August 2020, but still did not recover fully, with another significant drop in mid-October, soon after news was published claiming Boohoo's suppliers were being investigated on suspicion of money laundering and VAT fraud.<sup>11</sup> Boohoo's stock price volatility is high, meaning institutional investors such as passive asset owners would have less motivation to invest in a company such as Boohoo, as they would not be able to exit investments immediately after controversies. Less long-term investment means less capability to create sustainable financing, therefore disadvantaging shareholders.

<sup>11</sup> <https://www.thetimes.co.uk/article/boohoo-suppliers-investigated-for-money-laundering-and-vat-fraud-9k5vgbkpc>



## ESG – How Does Boohoo Measure Up to Its Peers?

To understand the material ESG issues at Boohoo, and how the company measures up to its peers, we conducted a peer analysis in which we compared Boohoo to its key competitor ASOS plc. We chose ASOS as the main peer, as its business model and market capitalisation is similar to that of Boohoo, and we identified both as having a similar level of governance risk.

### Here's what we found:

#### **Supply Chain: Cause for Concern**

Post the Leicester factory controversy, ratings agencies were heavily criticised for previously giving Boohoo good ESG ratings for its labour standards, and failing to identify the inadequacies in its supply chain.

In terms of management system, Boohoo has disclosed its Supplier Code of Conduct, covering crucial topics such as forced labour, child labour, working hours and minimum wage. However, we have identified best practices in terms of management system by analysing ASOS, which has elaborated on each topic in detail and also provided a glossary at the beginning of the document to aid suppliers' understanding of its requirements. ASOS has also taken overtime payments for workers throughout its supply chain into consideration, while Boohoo did not touch upon this topic.

Furthermore, effective due diligence across the supply chain allows timely identification, measurement, mitigation, and prevention of labour-related risks, and fosters transparency that strengthens corporates' reputation and social license to operate. In order to overhaul its supply chain transparency, Boohoo engaged a third-party specialist to conduct supply chain tracking and auditing. However, no concrete findings or remedial action plans were provided. On the contrary, ASOS has showcased best practice among its peers in terms of supply chain auditing, by disclosing detailed audit methodology and quantitative data (i.e. number of audits and non-conformances).

#### **Product Carbon Footprint: Plenty of Room for Improvement**

Carbon footprinting paves the way for waste and cost reduction which in turn enhances sales and a company's reputation. Boohoo has already begun its journey towards product carbon reduction.

As well as taking steps to reduce energy use in its own operations, Boohoo has partnered with third-party specialists to explore opportunities reducing indirect footprint in the value chain.

Compared to its peers, Boohoo's main gaps exist in target setting and energy management in the transportation and logistics stages. Whilst its peers have made considerable progress in carbon emission reduction target setting which in turn helps them to better evaluate performance in terms of carbon management, Boohoo is lagging behind. ASOS, as a signatory to Sustainable Clothing Action Plan (SCAP) 2020 Commitment, aims to reduce the carbon and water footprint of ASOS Brands clothing by 15% by 2020 and is using SCAP's assessment tool to measure and report on its progress.<sup>12</sup>

Moreover, we observe that Boohoo's peers have already realised the significance of carbon impact originating from deliveries and returns. ASOS works closely with international carriers to support and foster sustainable and low-carbon innovation. Using alternative fuel vehicles, increasing vehicle efficiency and route optimisation are some of the ways in which a company can reduce its carbon footprint from deliveries and returns.

### **Pay Issues: Some Red Flags Identified**

Increasingly, investors are interested in the effectiveness and transparency of remuneration plans. A profound and transparent remuneration plan can motivate an executive to work harder and raise the credibility of the company.

Remuneration has been a contentious issue at Boohoo even before the Leicester factory scandal: ahead of the 2020 AGM, proxy advisor Institutional Shareholder Services (ISS) recommended a vote against the company's remuneration plan prior to the Leicester factory scandal, which influenced the voting of its clients invested in Boohoo.<sup>13</sup> As a result, there was significant dissent for the remuneration report at the company's 2020 Annual General Meeting (AGM), amounting to 34.08% against votes.<sup>14</sup> In addition, ISS' against recommendation was likely a contributing factor to asset managers and advisory firms publicly criticising Boohoo's pay actions.

The significant dissent and criticism regarding Boohoo's remuneration shows two things:

- 1) Companies should be more transparent in aligning executive pay with business performance
- 2) Increasingly, stakeholders are seeking the rationale for companies' incentive compensation plans.

### **Gender Diversity: Need for Monitoring**

Gender board diversity is another factor stakeholders are taking into consideration when assessing a company's governance. Ideally, the Board should be majority independent, consisting of directors who are not affiliated with the company other than in their capacity as a director. Diversity and independence levels are good indicators of a company's cultural advancement and its proactiveness when it comes to inclusion. As of 16 July 2020, Boohoo's board failed to achieve majority independence, and there was only one female director on the board. In order to mitigate governance risks and increase credibility, Boohoo should aim to increase gender diversity and independence at board level.

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12 <https://www.asosplc.com/corporate-responsibility/our-products/sustainable-sourcing-programme>

13 <https://www.thetimes.co.uk/article/boohoo-faces-city-tantrum-over-1m-payout-to-john-lyttle-dpsff6bfr>

14 <https://www.boohooplc.com/sites/boohoo-corp/files/all-documents/agm/2020/agm-2020-results-table.pdf>

## Lessons Learnt from the Boohoo Scandal

It is easy to think that E, S and G issues are distinguishable when, really, they are closely interlinked. The environmental and social issues often occur due to the lack of a carefully considered governance system. Bad top-down decisions are often the direct result of a lack of diversity, expertise and independence at board level.

There are some very important lessons to be learnt from the Boohoo scandal for corporates in the fashion industry and other capital market participants:

- Never underestimate the importance of supply chain management and ethical labour practices
- An independent and diverse board with a reasonable remuneration plan is risk management in action
- Investors and stakeholders should seek to monitor not only a company's financial performance, but also key ESG issues, utilising peer comparison and market best practice to do so efficiently
- Keeping in mind a reason the Boohoo scandal shocked the market was due to the company's exemplary ratings prior to the supply chain controversy, there is a need for ESG raters to develop analysis methods that enable them to find lurking risks in a company's supply chain.



## What Boohoo's Key Investors Expect With Regard to ESG

By using the IHS Markit investor relations platform BD Corporate, we identified Boohoo's top 5 institutional investors based on data captured from April-October 2020: Jupiter Asset Management, T. Rowe Price, Invesco, Baillie Gifford and Eleva Capital.

To have a better understanding of Boohoo's top 5 institutional investors' general expectations on ESG and how it will influence Boohoo response to such expectations. We conducted an analysis of the ESG approach of these institutions by analysing publicly available information such as the in-house stewardship code and ESG policy.



ESG Expectations	Top 5 Investors & Holdings				
	Jupiter Asset Mgt 123.5M shares as of 22/09/20	T. Rowe Price 70.3M shares as of 30/10/20	Invesco Advisers 61.3M shares as of 30/09/20	Baillie Gifford 53.2M shares as of 02/04/20	Eleva Capital 35.1M shares as of 02/04/20
<b>Environmental</b>					
Biodiversity	●	●	●	●	●
Natural resources, water and waste management	●	●	●	●	●
Disclosure of climate-risks in accordance to TCFD	●	●	●	●	●
<b>Social</b>					
Employees' welfare	●	●	●	●	●
Supply chain management	●	●	●	●	
Consumers	●	●	●	●	●
Community engagement	●	●	●		
<b>Governance</b>					
Board structure, independence, diversity and election	●	●	●	●	●
Remuneration	●	●	●	●	●
Audit, reporting and transparency	●	●	●	●	●

Based on the above analysis of Boohoo's top 5 investors' ESG expectations, we'd like to highlight the below points:

- Boohoo's top 5 investors believe companies should report on climate risk in line with the Task Force on Climate-related Financial Disclosures (TCFD) framework. Hence, climate change and GHG emissions-related considerations would be key areas of focus for these institutions when making investment and voting decisions
- Issuers are likely to receive increasing pressure from these institutions to raise labour standards within the supply chain (e.g. improving health and safety, complying with minimum wage requirements), particularly in light of the global pandemic and the Boohoo scandal. T. Rowe Price, for example, treats labour issues in the supply chain as a risk indicator when assessing a company's ESG profile
- In terms of board management, these institutions are likely to emphasise on board oversight of ESG issues, and board ethnic and gender diversity.

## Case Study: Jupiter AM's Active Engagement With Boohoo Post the Scandal

### What was Jupiter AM's response to the scandal?

Jupiter AM, one of the largest investors of Boohoo, stood by the brand when a prominent UK Member of Parliament called for the removal of the company's CEO and chair.<sup>15</sup> Instead, the investor agreed for Boohoo to publish the list of suppliers and bring in two new board members for ESG oversight.

### How has Jupiter AM been engaging with Boohoo post the scandal?

The investor has escalated their engagement with Boohoo's board post the scandal. Due to pressure from Jupiter AM, Boohoo eventually published an independent review of its supply chain in September 2020. The review highlighted that the company was aware of the underpayment of workers prior to the scandal, but failed to take action.

### How does Jupiter AM integrate ESG factors into its investment process from a supply chain perspective?

The investor's stewardship code states that their fund managers will consider risk factors in the supply chain's social impact (i.e. labour practices), as well as risks related to environmental and climate-related impact.

The Boohoo scandal highlights how ESG risks, particularly when neglected, can have a negative impact on a company's share price and reputation.

Company business models are constantly evolving to reflect stakeholder expectations and market pricing. The move from the shareholder value model to shared value and emerging regenerative models, is an area where the fast fashion industry may have to reinvent itself. Sector competitive advantage can be defended and obtained by reacting to "new ways of working", embracing new ESG opportunities and by using ESG as a risk barometer.

Companies should proactively assess and monitor their ESG profile, as stakeholders increasingly evaluate a company's supply chain from an ESG perspective. This is where the ESG Advisory team at IHS Markit can help.

## Helping to Tell Your ESG Story

IHS Markit understands the importance of ESG storytelling for a company: a good story founded on good-quality and relevant quantitative data will resonate with different stakeholders, engage them, and in turn drive change.

We offer diverse ESG advisory solutions to help companies tell compelling ESG stories to the right audience.

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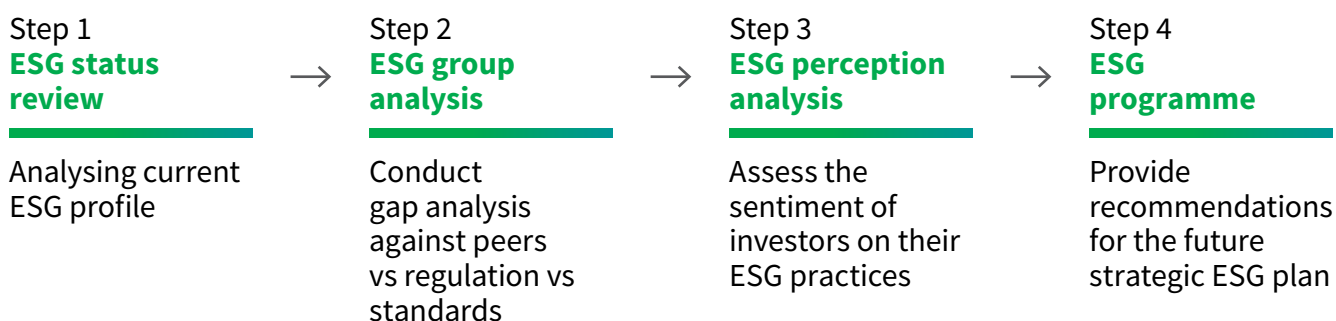
<sup>15</sup> <https://www.business-humanrights.org/en/latest-news/uk-mp-calls-for-removal-of-boohoo-ceo-after-evidence-of-illegal-supply-chain-working-conditions/>

## How We Add Value

Our team will tailor the solutions so that companies can:

- Understand the ESG sensitivities of key investors
- Advise, plan and facilitate ESG-focused investor engagement
- Assess market sentiment with regard to ESG
- Target potential ESG-focused investors
- Understand the influence of a particular ESG rating and disclosure framework
- Implement a climate transition programme in line with the Paris Agreement

## Our Strategic ESG Advisory Solutions



### Step 1: ESG Status Review

Our team analyses the client's ESG profile through publicly available information such as the ESG report, annual report and additional information that may be available on the company's website.

### Step 2: ESG Gap Analysis

Following the initial steps of identifying a client's ESG status, we closely benchmark their ESG profile against different regulatory requirements, reporting standards and peers.

By using IHS Markit's unique datasets and platforms, such as BD Corporate and ESG Reporting Repository, we are able to systematically identify reporting gaps, risks and opportunities in communication and ESG ratings.

### Step 3: ESG Perception Analysis

To understand the sentiment and factors driving investors' investment decisions, we conduct an in-depth assessment of different capital market stakeholder groups to keep our client informed of current market risk and opportunities.

### Step 4: ESG Programme

After having a strong understanding of our client's ESG position, we tailor recommendations for their future strategic ESG plan.

The IHS Markit ESG Advisory team looks forward to assisting current and prospective clients in telling powerful ESG stories.

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## About IHS Markit

IHS Markit (NYSE: INFO) is a world leader in critical information, analytics and expertise to forge solutions for the major industries and markets that drive economies worldwide. The company delivers next-generation information, analytics and solutions to customers in business, finance and government, improving their operational efficiency and providing deep insights that lead to well-informed, confident decisions. IHS Markit has more than 50,000 business and government customers, including 80 percent of the Fortune Global 500 and the world's leading financial institutions. Headquartered in London, IHS Markit is committed to sustainable, profitable growth.

