7 La Laguna and the ‘outside world’: bi-national export production networks and the domestic market alternative

The preceding chapters have pointed to the exceptionally strong export orientation of the local garment industry in La Laguna. During the 1990s the Laguna region became a major foothold in US-Mexican production networks of blue jeans, orchestrated by US buyers.

In La Laguna there is cluster-wide resignation to the limited depth, stability and cooperation in local intra-cluster linkages (see Chapter 6). By contrast, there is much more attention for the linkages between local producers and US buyers. Garment producers in La Laguna emphasise the importance of vertical linkages with their buyers and stress the need to cooperate more closely with these buyers. Chapter 3 discussed how US branded manufacturers and retailers, and the differences between their sourcing strategies and networks, occupy centre stage in the current literature on the Mexican garment export industry. Basically, the succession of branded manufacturers by US retailers as main buyers of Mexican garment producers is thought to reflect and/or stimulate the upgrading of these producers in the direction of full-package production.

This chapter deals with the network links between garment firms in La Laguna and US branded manufacturers, designers/marketers and retailers in the US. The aim is to uncover the structure of different networks, the governance exercised through network links and the way a position in these networks may influence the development of local firms. In export networks, SMEs run the risk of becoming locked into the role of assembly subcontractor. Therefore, the opportunities offered by the domestic market for SMEs are also briefly explored.

This chapter is divided into five sections. The first introduces the most important buyers for the Laguna region. It sketches the expansion of the region’s buyers base over the 1990s. The next section discusses the various types of buyers – branded manufacturers, designers/marketers and retailers – and their sourcing and networking strategies in greater detail. Differences in emphases and network structures are discussed; the most notable is the role played by intermediary firms in retailer-centred networks. Attention will also be paid to the contrasting perceptions local contractors and their buyers have of each other and their business relationship. Though subjective in nature, these opinions are informative and may affect the configuration of networks as well as the content of the sourcing linkages. The position of local SMEs is discussed in section 7.4. As shown in the previous chapters, most SMEs depend on subcontracting work. Only a few work directly for small US buyers, brokers or a combination of both. The position of SME subcontractors is examined to see how local subcontracting relations differ from the relations between buyers and local manufacturers. The final section of this chapter shifts the attention to domestic market networks as a SME alternative to exporting and contrasts their structure and governance with those of export networks.
7.1 General trends with regard to La Laguna’s buyers

NAFTA has impacted the geography of global garment trade and production as it caused many US buyers to shift their attention from the East Asian apparel industry to Mexico as a nearby and relatively cheap sourcing country. More than attention alone was shifted: the impact of NAFTA is reflected in the increasing prominence of Mexico in the strategies of US fibre and textile producers, apparel firms and retailers. The number of US-Mexican alliances in apparel production has grown, a larger and increasing number of Mexican apparel producers are incorporated into the production networks of US buyers and some of these Mexican producers have replaced Asian or Caribbean producers (Gereffi & Bair, 1998; Gereffi, 1997; see Chapter 2).

From the perspective of La Laguna, the most notable changes since the passages of NAFTA are the quantitative boom in production, an incremental change in the organisation of production in the direction of full-package production (see Chapter 8) and the arrival of new US buyers.

Table 7.1: Main US clients of the Laguna garment cluster

<table>
<thead>
<tr>
<th>La Laguna early 1990s</th>
<th>La Laguna 2000</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Main clients</strong></td>
<td></td>
</tr>
<tr>
<td>Marketers/designers</td>
<td>Marketers/designers</td>
</tr>
<tr>
<td>Old Navy/Gap</td>
<td>Old Navy/Gap</td>
</tr>
<tr>
<td>Tommy Hilfiger</td>
<td>Tommy Hilfiger</td>
</tr>
<tr>
<td>Eddie Bauer</td>
<td>Eddie Bauer</td>
</tr>
<tr>
<td>The Limited</td>
<td>The Limited</td>
</tr>
<tr>
<td>Polo Jeans</td>
<td>Polo Jeans</td>
</tr>
<tr>
<td>Mudd</td>
<td>Mudd</td>
</tr>
<tr>
<td><strong>Branded manufacturers</strong></td>
<td></td>
</tr>
<tr>
<td>VF**</td>
<td>VF**</td>
</tr>
<tr>
<td>Levi Strauss</td>
<td>Levi Strauss</td>
</tr>
<tr>
<td>Savane</td>
<td>Savane</td>
</tr>
<tr>
<td>Sara Lee/Hanes**</td>
<td>Sara Lee/Hanes**</td>
</tr>
<tr>
<td><strong>Retailers</strong></td>
<td>Retailers</td>
</tr>
<tr>
<td>Kmart</td>
<td>Kmart</td>
</tr>
<tr>
<td>Wal-Mart</td>
<td>Wal-Mart</td>
</tr>
<tr>
<td>Target</td>
<td>Target</td>
</tr>
<tr>
<td>JC Penney</td>
<td>JC Penney</td>
</tr>
<tr>
<td>Sears</td>
<td>Sears</td>
</tr>
<tr>
<td><strong>Intermediaries</strong></td>
<td>Intermediaries</td>
</tr>
<tr>
<td>(brokers/vendors)</td>
<td>(vendors/hybrid)</td>
</tr>
<tr>
<td>Sun Apparel</td>
<td>Sun Apparel**</td>
</tr>
<tr>
<td>807</td>
<td>807**</td>
</tr>
<tr>
<td>Kellwood</td>
<td>Kellwood</td>
</tr>
<tr>
<td>Aalfs**</td>
<td>Aalfs**</td>
</tr>
<tr>
<td>W. Stevens*</td>
<td>W. Stevens*</td>
</tr>
<tr>
<td>Easy Wear Group</td>
<td>Easy Wear Group</td>
</tr>
<tr>
<td>A &amp; A Consultants</td>
<td>A &amp; A Consultants</td>
</tr>
</tbody>
</table>

Source: Baseline survey, 1998-1999

* These US intermediaries are also involved in retailing through licensing or own brand production.

** These US companies have FDI production facilities in the region.
start with the latter development, Table 7.1 gives an overview of the main clients of the Laguna garment cluster in the early 1990s and in 2000. During and before the early 1990s, La Laguna was producing primarily standardised blue jeans for the low-end segment of the market through mass merchandisers such as Kmart, Wal-Mart and Target, but also better positioned branded manufacturers such as VF Corporation and Levi Strauss. A few intermediaries also played a role; they channelled mostly work for department stores to the region. Over the course of the 1990s new buyers entered the Laguna apparel arena, especially since the passage of NAFTA (see also Gereffi & Martínez, 2000; Bair & Gereffi, 2001). The table also shows that the new buyers have joined rather than replaced the cluster’s former buyers. As a consequence, the buyer base of the region has expanded quite dramatically to include clients new to garment production in the region, and even in Mexico.

Table 7.1 shows that on the whole, the cluster served the lower segments of the US market and works for many lower-mid end clients. Illustrative is the sourcing pattern of Gap Inc., a highly important buyer in La Laguna. Gap Inc. primarily sources garments under its Old Navy brand, which is positioned in the low-end segment of the market, from La Laguna. Much smaller volumes of the higher quality Gap-branded jeans are sourced from the region. Banana Republic – Gap Inc.’s best positioned brand, in the mid- to high-market segment – is not sourced from La Laguna at all.

The table also illustrates not only the growth in the number of clients of the cluster, but also that new and different types of buyers have begun to source from La Laguna. A comparison of the clients in Table 7.1 with the listing of garment buyers in Table 1.3 reveals that during the 1990s La Laguna’s production began to penetrate the mid- and the upper-mid-end market segments. This is indicated by the increase in the number of designers at the top of Table 7.1. In general, these new buyers are more demanding than clients such as Wal-Mart, Kmart and – in some ways – Levi Strauss, which traditionally produced in the region. On the whole, however, these designers still manage small volumes in La Laguna and deal with a more selective group of local manufacturers than do the other buyers in the list. As will be further discussed later in this chapter, designers deal only with the most capable, full-package local giants. The increase in number and importance of higher-end retailers and designers causes a diminishing relative importance of branded manufacturers. Though in itself hardly a surprising shift (see also the discussion of industry trends in Chapter 1), this is thought to have great implications for the development dynamic of the cluster (see Gereffi et al., 2002b). Also noteworthy is the importance of intermediary firms, many of which channel the work of the lower-end retailers to the cluster. In most of the literature, limited attention is paid to intermediary firms in US-Mexican garment production networks.

7.2 Buyers: sourcing and networking strategies

This section sets out to examine the bi-national production networks between La Laguna and the US market in greater detail. As mentioned in Chapter 1, the garment industry has gone through a process of hybridisation: retailers have gone vertical, manufacturers have diversified into retailing, and some are even retreating from manufacturing in order to focus on marketing. The different types of clients are becoming more and more alike, so much so that the literature tends to group them together under the common denominator ‘buyers’. But are they really so alike? Are their production networks and sourcing strategies identical? In some ways they are: all types of buyers mention product quality, acceptable cost and punctual delivery as prerequisites for a good sourcing relationship and most have codes of conduct or a
contract of compliance specifying the minimal labour and facility conditions local contractors
have to provide (see Annex 2). On the other hand, recent literature on the development of the
Mexican garment industry also stresses the differences in sourcing strategies between branded
manufacturers and retailers and their impact on local upgrading processes (see Chapter 3). To a
large extent this was confirmed by interviews with different buyers which showed that their
practical involvement with these aspects as well as the structure of their networks can be
markedly different. Even if many buyers are doing something of everything, their background
as manufacturer or retailer appears to work through in the expertise and focus they bring into
their current network linkages, as well as in the structure of their networks. For this reason,
this section focuses on manufacturers, designers, retailers and intermediaries separately. It aims
to shed light on the structures of the production networks as shaped by the various types of
extra-regional buyers. Moreover, it seeks to highlight the varying strategies of these clients
with regard to their local manufacturers and contractors through a focus on the information
and knowledge content of production linkages.

7.2.1 Branded manufacturers
The main concern of many branded manufacturers in the face of the general shift of power to
retailers (see Chapter 1), is to maintain their market share. To do so, most have complemented
their traditional product lines of commodity jeans, tee-shirts or other basic garments, which
traditionally were the backbone of their business, with higher fashion content product lines.
Examples of such new product lines in pants/bottoms are the ‘Engineered Jeans’ and ‘Dockers’
by Levi’s, and Timbercreek casuals and camouflage combat-pants by Wrangler. This product
duality is also reflected in the production networks of these companies, in which FDI,
traditionally the main production vehicle for these companies, is now flanked by extensive
international sourcing. The production of basic commodity garments occurs in very large
volumes, is relatively stable and predictable, and can be highly automated. It is in this segment
where, through decades of production experience, specialisation and technological innovation,
branded manufacturers have built a competitive advantage. The FDI facilities of branded
manufacturers generally manufacture precisely these traditional, basic product lines. The more
changeable, fashion-sensitive and new product lines are primarily produced through sourcing
linkages. Sourcing is generally coordinated and controlled by a separate sourcing division
integrated into the corporate structure. Even though sourcing is becoming an integral part of
the production strategies and networks of branded manufacturers, their tradition of
manufacturing is still reflected in both the structure and the content of sourcing network
linkages.

Thus in relation to the Laguna region, branded manufacturers as a group play a double role: as
buyers they are external actors exercising control over local contractors through their sourcing
linkages, and as manufacturers they have a local presence through their FDI facilities. In
general the impact of their presence on the region should not be underestimated. Together
they are estimated to absorb approximately 15% of those employed in the industry in their FDI
factories; a further large number are indirectly employed through sourcing relationships with
local contractors. A few branded manufacturers combine both these functions in the region:
Wrangler and uniform manufacturers RKI and Aramark have contracting linkages and FDI
facilities in La Laguna. By contrast, Hanes, for example, has FDI facilities but no local
contractors, while Levi Strauss works with a few local contractors but does not have own
facilities in the region. Both the FDI and the sourcing sides of the production networks of
branded manufacturers will be examined here, starting with strategies with regard to FDI facilities in the region.

Intra-firm network linkages/strategies with regard to FDI facilities
In line with the general patterns described above, the FDI facilities of branded manufacturers in La Laguna generally produce basic, standardised products that are produced in predictable, large batches. In this way, applied technology developed in-house can be fully exploited to reach very high production efficiencies.

In general, local subsidiaries are relatively tightly leashed to their US headquarters, where the business strategies are formulated. Subsidiary guidelines and objectives are rooted in a strict corporate framework. The overall corporate strategy of branded manufacturers with regards to their FDI facilities is very much focused on production efficiency. Many cite ‘control’ – with regard to quality but also production planning – as the reason for channelling a large part of total production through FDI facilities. These considerations are reflected in the content of linkages between US headquarters and FDI facilities in the region. Headquarters do not get involved in local matters beyond the level of general guidelines, but are very much involved in production planning and organisation. Local production has to fit within the overall corporate production aims based on sales and market projections.

The management of several foreign-owned subsidiaries in La Laguna had been directly responsible for the precise site selection within the region, and sometimes even for the selection of the region as production location within Mexico. This great strategic involvement in the pre-production stage stands in contrast to more limited local decision-making once local subsidiaries were up and running (see also Figure 7.1). Essentially, the only area in which subsidiaries are largely autonomous is the recruitment of personnel. Beyond that, decision-making in most areas is concentrated in the hands of either divisional or corporate headquarters.

However, there is more nuance to the actual situation than this short introduction suggests. There are grey areas in decision-making – and shifts in and stretching of these areas. Also, the sharing of responsibility and information differs from case to case and from company to company, and even between divisions of the same corporate company. In many companies there appears to be room for some strategic manoeuvring at the local level, certainly if a factory has been running successfully for some time. Whether grey areas in decision-making are exploited by local FDI subsidiaries depends on the local management of the facilities. Local managers are the company’s experts on the local business environment and the business opportunities embodied in it. For instance, investment and expansion decisions are ultimately taken at the US headquarters, but information, advice and ideas are mostly provided by subsidiary managers in the field. Several managers of FDI facilities in La Laguna indicated they had been involved in the further expansion of their company’s interests in the region. Several local managers also felt they were in a position to make recommendations in areas such as domestic suppliers, while admitting little progress had been made in this field. Few had successfully pushed for changes in the organisation of production or existing linkage patterns. This may be explained by the fact that the development of productive linkages to the surrounding cluster and local manufacturers or suppliers does not form part of the tasks of FDI facilities: contracting as well as supply relations are controlled at higher levels of the corporate hierarchy (see Figure 7.1).
Formally, local decision-making is only significant with regard to purely local matters. Informally decisions are ultimately taken at headquarters outside the region, but the decisions can to a greater or lesser extent be ‘pre-cooked’ by local management.

In short: production linkages of FDI facilities are bi-directional and dense in information: information on local business matters and opportunities is communicated from the region to the headquarters, while information on business strategies, market developments, etc. is communicated to and implemented at the local level by (divisional) headquarters. Linkages between the local subsidiaries and headquarters in the US are mostly of an immaterial nature. As mentioned in the previous chapter, material flows to and from local FDI facilities are mostly extra-regional and maintained with production facilities and distribution centres in the US.

Sourcing by branded manufacturers
How are the sourcing linkages between US branded manufacturers and local contractors in La Laguna shaped? And, more importantly, what is the content of these linkages? Are they mere flows of orders, material and finished garments, or is knowledge exchange and learning also part of these sourcing networks, as is asserted by the literature?

Many branded manufacturers in the region still obtain a relatively small part of total production through sourcing linkages. Sourcing networks for these companies may be relatively small, not only in relation to total volume but also because of a preference for a small number of contractors with relatively large capacities. Traditionally, as explained in Chapter 3, branded manufacturers sourced mostly pure assembly work under production-sharing provisions such as the 807/HTS 9802 Program. Their concern is principally with quality rather than with factory size (see Figure 7.2). Currently, most branded manufacturers that source from the Laguna region prefer to work with medium or large contractors who can do more than pure assembly – preferably ‘CMT+laundry’ (cutting, assembly, finishing and laundry) – so that any confusion about responsibility for mistakes or non-compliance can be avoided. For the same reasons and as part of a general quest for greater control, branded manufacturers do not allow subcontracting by local contractors. As the contractors of branded manufacturers become more capable, they assume responsibility for the procurement of material inputs.
Several branded manufacturers indicated their general intention to have a long-term working relationship with contractors because such a commitment is seen as a win-win situation, as it leads to stability, mutual familiarity and trust. In effect, in La Laguna most branded manufacturers have worked with the same contractors for a couple of years. Branded manufacturers engage a large share of the production capacity of their local contractors. Many are quite protective of their good contractors: if they are producing a style that is not selling as projected, it may be replaced by basic garments. The focus on product quality and efficiency evident in their FDI facilities is also reflected in their sourcing linkages: branded manufacturers share knowledge that can lead to reductions in cost or increases in efficiency in their contractors with these contractors. In most cases this concerns general adjustments to the organisation of production on the shop floor, which can lead to considerable cost reductions in plants in the region. In addition, some branded manufacturers apply their knowledge by teaching contractors hands-on about the construction of new styles and the efficient and

Figure 7.2: Production network of a branded manufacturer, Savane
proper performance of certain operations. Sharing knowledge about technology and machinery is much more restricted. Especially branded manufacturers with a R&D centre to develop new production technology for their own plants are protective of their in-house technological knowledge, which is the basis for their competitive advantage.

Information regarding market developments and business strategies, if shared with contractors, is shared informally. There is no formalised, regular medium for the sharing of such information, and it appears largely dependent on the interpersonal relationship between sourcing managers and contractors.

7.2.2 Retailers

The general shift in market share and power from manufacturers to retailers in the garment industry is reflected at the local level in an increasing importance of retailer-centred networks. Many of them, especially the department stores, have a relatively short history of sourcing from the Laguna region when compared to branded manufacturers. Yet they are rapidly gaining ground on the manufacturers.

Mass merchandisers (e.g. Kmart, Wal-Mart, Target) and department stores (e.g. JC Penney, Sears) are producing large volumes of their private label jeans in La Laguna. Mass merchandisers were amongst the first retailers to source from the region and are still sourcing large volumes there. The sourcing networks that connect these buyers to suppliers in La Laguna appear to be two-pronged. On one hand, the bulk of their sourcing is carried out, coordinated and controlled by US-based intermediary firms, such as Kellwood, W. Stevens, Flyn and Sun Apparel. These firms bear full responsibility for all the planning, coordination and logistics of the sourcing network, and network relations are centred around these intermediaries. To most intents and purposes they function as the clients or buyers of local suppliers. On the other hand, especially in the case of basic commodity items or collections, retailers may work directly with very large local suppliers of full packages. In most cases local suppliers are allowed to subcontract work to local subcontractors. This practice turns them into the central point of local production networks and may be the first step in the direction of becoming a key or core supplier.

It may hardly be a surprise that, compared to branded manufacturers and designers, retailers have a more distant relationship with both their products and the firms that produce them. Many do not have their own design department but rely on vendors or other types of intermediary firms, to whom they also assign the responsibility for the actual production or the coordination thereof. It is rare to find representatives of retailers in La Laguna. Thus hardly any direct links of primary importance exist between department stores or mass merchandisers and local contractors. In contrast to branded manufacturers and designers, retailers do not maintain links with all their subcontractors/contractors. Instead, governance concerning codes of conduct, specification of trim items and quality, cost and delivery is formalised and communicated through the intermediaries or core suppliers. These intermediaries or core suppliers bear responsibility for the structuring, control and coordination of the lower tier of the production network and the network-wide implementation of the retailer’s code of conduct.
The role of intermediaries in retailer-centred networks

Importers, vendors, brokers, supply chain managers – the diversity in nomenclature reflects the diversity in the roles played by intermediary firms. Intermediary firms occupy a pivotal position in the sourcing networks that connect many US garment retailers to producers in Mexico. However, their position and responsibilities vary widely and may be contested by different firms in the networks. One of the most obvious changes with regard to the position of intermediaries in the 1990s was the virtual disappearance of the traditional brokers, many of which were located in the US border region. Brokers owed their position to their extensive knowledge of and connections with garment manufacturers (with access to quotas) in Mexico. Their business was built on the ability to connect demand for garment production capacity to available and suitable supply sources in Mexico. This was a unique and highly important asset, certainly in the times when Mexican production capacity for export was tied to quota bureaucracy. The opening up of Mexico has eroded the position of such traditional brokers, so much so that brokers have been forced to consider a strategic realignment of their business in order to validate their continuing position within the bi-national production networks. Now that bi-national trade is liberalised and the most competitive Mexican manufacturers are striving to extend their command over the production chain (and are succeeding in doing so), the functionality of brokers and other intermediaries in the bi-national production networks is no longer a given. Many intermediary firms see themselves forced to secure their position by either assuming the more strategic role of supply chain manager or by becoming a core supplier through investing in in-house production capacity. The first option is relatively less viable in Mexico than in Asia because of geographical proximity and the liberalisation under NAFTA, which simplify logistics and administrative or customs management. The direct involvement in garment manufacturing with the aim to become a core supplier with local facilities has been a more common response, despite some hesitance and resistance on the part of vendors. The increasing direct involvement of intermediary firms in production appears in many cases to be the result of pressure to this effect from buyers. Behind this pressure lies the need to justify the value added of intermediaries, as well as a search for increased and direct control over delivery and quality.

Meanwhile, many intermediaries have acquired licenses for existing brands or have developed own brands in an effort to also develop the retailing end of their business. This allows intermediaries to differentiate themselves from new core suppliers in LMICs and reduces their dependency on their buyers. Repositioning and realignment in this segment of the production network has contributed to the general hybridisation trend noted in Chapter 1. The number of intermediaries performing different combinations of activities in the logistics, service, management, design and production segments of the production chain has grown. Within different production networks, they may assume different roles.

Thus, even within the context of NAFTA liberalisation and the development of full-package capabilities in the region, intermediary firms play a central role in retailer export networks in La Laguna. Focus is on strong intermediaries that organise the entire production process/supply chain.

Three configurations appear to be common. One is where US intermediaries coordinate the supply chain without being directly involved in manufacturing. Local manufacturers are usually involved on a CMT+laundry basis, while production planning, procurement of fabric, import and distribution and sometimes design are done by the intermediary. On the other
Box 7.1: El Paso and La Laguna: predecessor and heir?

Apart from New York, Los Angeles and San Francisco, where many buyers have headquarters or sales offices, El Paso figures quite prominently in the production networks that connect La Laguna to the US market. La Laguna can be seen as the inheritor of El Paso’s former position as ‘Jeans Capital of the World’, and in many ways the existing links between El Paso and La Laguna appear to affirm this status. El Pasoan garment entrepreneurs and other experts play varied and important roles in the local garment industry in La Laguna and in the production networks that connect it to the US market. This has especially been the case since the demise of the El Paso garment industry in the mid to late 1990s. Some of the city’s garment entrepreneurs still cling to their shrinking factories in El Paso hoping to stay in business until retirement, but many have flocked out of El Paso in the footsteps of ‘their’ industry. As the garment industry boomed in Mexico, many went across the border to Mexico. In doing so, they cemented a tight link between El Paso and Mexico, and especially with the Laguna region – El Paso’s successor as Jeans Capital.

The El Paso-La Laguna link is based on a number of different strategies. Several of La Laguna’s large and very large factories are owned by companies based in El Paso. Such companies as Border Apparel, Onsite and Sun Apparel have shifted their entire production base from El Paso to La Laguna. Other El Pasoan companies are sourcing from La Laguna, in a few cases as buyers, but most commonly they have found a niche in the intermediary role. Especially in the early to mid 1990s a disproportionate number of brokers from El Paso channelled work for US buyers to La Laguna. Though in general the growth of El Paso-based brokers may have been short lived, a few built a steady business on connecting mostly smaller buyers in the US to SME contractors in La Laguna.

Furthermore, companies in La Laguna have also built a direct link in the other direction, viz. from La Laguna to El Paso (see also Chapter 5); this mainly occurred in the pre-NAFTA period. Many of the large exporting companies have an office and a warehouse in El Paso. Finally, industry-specific suppliers also downscaled their El Paso offices and complemented their El Paso business by opening new offices and warehouses in La Laguna or by cementing supply linkages to La Laguna from El Paso.

Clearly, many garment companies in El Paso have seized the new business opportunities in La Laguna, and vice versa. Many El Paso industry experts have found their way into La Laguna, either by moving with their company or independently. Consequently, several managers of the foreign-owned and locally owned companies in La Laguna, as well as sourcing directors and managers of intermediaries or buyers sourcing in La Laguna, have previously worked in El Paso. The local expertise in El Paso with regard to jeans production is applied in Mexico through independent consultants and individual entrepreneurs who are no longer directly involved in production, but have built a business on the wheeling and dealing surrounding it.

Especially at the time of the explosion of garment capacity in La Laguna during the mid 1990s, the expertise coming from El Paso was highly valuable to the local industry. Many of the garment entrepreneurs in El Paso grew up in the ‘needle trade’ and have extensive hands-on experience. They started out as employees of one of the larger companies and pride themselves in the fact that the garment industry is in their blood. They have the technical experience and know the US garment industry and its key players. This is exactly the kind of experience that was needed in La Laguna,
By the turn of the century, El Paso’s expertise was proving footloose again or possibly even outdated. First, as soon as the ice between US buyers and intermediaries and Mexican producers was broken, a large part of the El Paso-based brokers disappeared. Later, many managers, consultants and other experts from El Paso also moved away. This is not surprising: though numerous parallels between the former and the current Jeans Capital can be drawn (see also Chapter 3), the market and the industry as a whole have changed dramatically over recent decades. El Paso was able to build a large industry on contracting work of standardised, mass production for mostly branded manufacturers (van Dooren & van der Waerden, 1997, van Dooren & Verkoren, forthcoming). La Laguna faces a changed business environment of different types of buyers with new strategies, and the concomitant challenges and opportunities. Recent dynamics may create new and great opportunities for local manufacturers. The most urgent question now concerns the local response needed to reap the full benefits of these opportunities. The El Paso garment industry and its experts have provided La Laguna with valuable practical expertise in the area of production. They may be less able to serve as an example or guide for the increasingly urgent strategic response, especially with regard to increased flexibility, local companies need to make to changes in market and industry.

Table 7.2: Mapping linkages between El Paso and La Laguna

<table>
<thead>
<tr>
<th>Ownership linkages</th>
<th>7</th>
<th>Several of these companies are large or very large and have large facilities in La Laguna. They are generally manufacturers that have positioned themselves as intermediaries or core suppliers in the networks of US buyers; they form the local hub of their subcontracting network.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Managers</td>
<td>5</td>
<td>Most El Pasoan managers work in the FDI facilities of US branded manufacturers; a few work for local giants.</td>
</tr>
<tr>
<td>Intermediaries/Brokers</td>
<td>6</td>
<td>El Paso-based intermediaries are involved with production in La Laguna. In most cases they coordinate the production in Mexico for smaller US buyers; in La Laguna they generally work with SMEs.</td>
</tr>
<tr>
<td>Local companies with offices in El Paso</td>
<td>14%</td>
<td>Most offices in El Paso take care of customer relations and shipping of material inputs to factories in La Laguna, as well as border-crossing procedures of finished garments into the US; some also have/had a cutting room.</td>
</tr>
</tbody>
</table>

Source: Estimates based on interviews and Baseline survey, 1998-1999

On the other hand, it is very common for the central intermediary to have established production facilities of its own (in the Laguna region, the US or elsewhere), in which it occupies a position similar to what in Chapter 1 was called a ‘key supplier’. In La Laguna, approximately half of the FDI facilities belong to such US intermediaries. In these cases, part of the production is carried out in its own facilities, but the intermediary is also responsible for the contracting out of work to a sourcing network. Local examples of such arrangements are the production of jeans for JC Penney through the US-Mexican joint venture Aalfs-OMJC, and the production of Wal-Mart [191]
jeans by and through US-owned Sun Apparel, which has several production facilities in La Laguna under the name of Pami. Finally, part of the local Old Navy/Gap production, mostly children’s wear, is produced by and through the 807 Company, which is based in El Paso and has a factory in Gómez Palacio.

Finally, direct sourcing linkages have developed between mass merchandisers and a few department stores and very large, capable, locally-owned producers in La Laguna. However, by the turn of the century very few local contractors had acquired a position of core supplier: most still worked through US intermediaries. This limited direct involvement appears less a matter of lagging capabilities of local producers as of the still limited ability of the US retailers to deal directly with local suppliers. Especially department stores still have little know-how and an infrastructure that is not well adapted to dealing directly with Mexican contractors.

Most intermediary firms active in La Laguna in retailer-centred networks are US owned and US based. Many are based in or connected to traditional garment production regions in the South and Northeast of the US and on the US-Mexico border. Though not a location for headquarters of US buyers, many garment companies are in one way or another connected to El Paso. This is partly based on the concentration of small intermediaries in that city. However, Box 7.1 shows that building on El Paso’s unique position as former Jeans Capital, there are multiple linkages between that city and La Laguna.

7.2.3 Marketers/designers
The newest buyers in La Laguna are the buyers/marketers of designer labels. In some ways, the network strategies of designers and marketers are a mix of those of branded manufacturers and retailers. Like branded manufacturers, they have direct and exclusive involvement with the product at the pre-assembly stage of production. However, unlike branded manufacturers but akin to retailers, their direct involvement stops after the design of the garment and specification of trim and fabric: all productive activities beyond designing are sourced out. In other words, designers and marketers depend fully on their sourcing network for actual production as they have no production capacity of their own.

Designers such as Tommy Hilfiger, The Limited, Liz Claiborne and Eddie Bauer have a short local sourcing history and maintain sourcing relationships with a few very large, full-package suppliers. They generally do not work with less all-round, assembly or CMT contractors. Besides (the potential to supply) large volumes and established full-package capabilities, designers demand high quality from their suppliers. The direct preoccupation of designers with the final product, its appearance and quality and with corporate images comes to the fore in overall tight governance of sourcing linkages. An example is the fact that all types of trim items as well as their certified suppliers are specified, a practice also noted in relation to the strategies of branded manufacturers. Designers source their basic bottoms from La Laguna. Yet, on the whole these are more sophisticated than the bulk of other products produced locally as more emphasis is placed on product quality. Emphasis on fashion also applies to their basics: regular changes in styles are common. Like branded manufacturers, several designers have a staff of industrial engineers who visit contractors’ factories to evaluate and improve production efficiency and quality. Especially at the beginning of the relationship, links are dense with information on production techniques and –organisation and a marketer’s engineers commonly work with supervisors, auditors and shop-floor personnel. A technical director of one of the designers that works in La Laguna observed:
'They [producers in La Laguna] are proud and tell us they've worked for Gap for a long time. To us that just means there's a lot of work to be done. We need to tell them Gap is not the best and that their standards may not be not good enough for us. We need to work with them to make them lose their bad habits and teach them about our demands and our ways.'

Furthermore, many designers are trying to streamline communication and data exchange so as to have production respond to sales as closely as possible. Flexibility on their contractors' shop floors (in adapting sewing lines to shorter runs of garments with a higher fashion content) is highly important. But this is not all: flexible management and an emphasis on service to the buyers is of increasing importance. Many designers are quite vocal about the need for local manufacturers to provide full packages and to improve their services if they want to secure a future position within their international garment networks. Most designers involved in the cluster have truly global sourcing networks and are constantly weighing the advantages and disadvantages of sourcing locations. Benchmarking between their producers is sometimes communicated to the local manufacturers in La Laguna, possibly to pressure them into a certain direction. Information about market and industry trends appears to be shared quite extensively. According to one designer, this was done to make local suppliers understand the system they were feeding into and 'to make them understand what they're up against'. Network relations between designers and local suppliers in Mexico are generally direct. Rather than using an intermediary firm, several designers have a buying or support office in Mexico to take care of emergencies, quality control, administration and logistics.

Buyer succession (see Chapter 2) and the active involvement of new, higher-end buyers with new demands may be a highly important motor behind the upgrading of the cluster. Designers may indeed push the cluster to close the gap between local capabilities in the mass production of basic jeans and the new demands for smaller runs of more sophisticated jeans. This would align the cluster with the general trends in the industry. However, while the involvement of these new buyers is significant and challenging, it has been neither fast paced nor cluster-wide. The volumes sourced by designers in La Laguna are considerably smaller than those sourced by mass merchandisers and branded manufacturers. Most designers have only initiated small pilot programs with local manufacturers and appeared to be testing the water. Over all, very few local full-package giants had secured a stable relationship with designers: most designers discontinued their sourcing from certain suppliers or from the entire region. This may well be due to the immaterial demands of designers. Few problems appeared to arise with regard to product quality. However, business mentality, service-mindedness and management appear to be the main trouble areas, and the main upgrading challenges for local entrepreneurs wanting to improve and deal with higher-end buyers appears to lie in these areas. What is more, their higher demands are an important reason why work for designers is only sparingly subcontracted in La Laguna. When it is, it is reserved for the best subcontractors. The quality risks are higher and very few subcontractors live up to the standards of designers. Most local giants are unable or unwilling to pass on the necessary know-how and skills. This is significant because it means that the upgrading impetus that originates from the recent involvement of designers benefits the cluster to a limited degree and in a highly selective manner.

Figure 7.3 is a schematic representation of the network structures La Laguna is engaged in; it is an adaptation of Figure 3.3 based on the findings outlined above. Figure 7.3 distinguishes not
only between branded manufacturers and retailers but also presents marketers as a separate group. Branded manufacturers work through FDI facilities as well as sourcing linkages. Several branded manufacturers increasingly demand CMT or even full-package capabilities of their contractors and as a consequence work with or are working with larger (and more capable) contractors than before. In relation to retailers it is important to note the role of intermediaries, which in La Laguna take much of the upgrading along the chain (in the direction of full-package production) incentive away from local producers. The sourcing linkages of marketers, especially designer label marketers closely resemble those of branded manufacturers. Designers appear more demanding: they want full packages but also flexibility and service, which so far few local manufacturers offer.

Appendix II provides illustrations of the position of local companies in bi-national production networks.

7.3 Buyers and producers: contrasting perceptions
As mentioned in the introduction, most garment entrepreneurs assert the need for close cooperation with their buyers. In general, strategic partnerships or joint ventures with US buyers or branded manufacturers are seen as better options than local cooperation. Some form of integration with US buyers is believed to help secure a future position within their production networks. In the face of volatile markets and international competition, and bearing in mind the important role of buyers noted in the previous chapter, this focus is understandable. As noted in Chapter 1 and 2, from the perspective of buyers this may also be desirable: the forging of tight links with a select group of large and capable ‘core suppliers’ is a common element in buyers’ strategies. This is confirmed by several of La Laguna’s buyers who

Figure 7.3: The structure of US-Mexico garment production networks, La Laguna
express an interest in maintaining long-term linkages with their most capable core suppliers. In practice, however, joint ventures and/or other types of formalised partnerships between local producers and US partners are rare in the Laguna region. Buyers prefer and are able to exert governance through subcontracting links. Diverging and sometimes conflicting interests and even mutual antagonism appear to be the main reasons for the lack of formal cooperation. From interviews with local contractors and US buyers it is clear that the expectations and opinions that the two sides have of their sourcing relationship and their respective roles within it often do not coincide. As a consequence, a fair amount of tension and friction may be part of these relations.

Local producers most commonly complain about the prices they are being paid. Buyers tried to maintain prices for particular products at ‘price point’ during the late 1990s. Worse than virtually stagnant prices may be the buyers’ underlying attitude that the local manufacturers perceived behind it. In reference to this, several local respondents mentioned how a number of the cluster’s main buyers had teamed up just after a peso devaluation to apply downward pressure on the prices. In doing so, they were able to appropriate the windfall profits that resulted from exchange rate change, something that local manufacturers felt they had a right to. From the local perspective, contractor’s margins were being squeezed by ‘inconsiderate, greedy clients’. Worse still, local manufacturers felt they were being sandwiched as the tight labour market, high turnover rates and inter-firm labour poaching exerted upward pressure on wages throughout the late 1990s. In addition, there were sharp increases in electricity and telecommunication costs. Thus, costs rose but as buyers were insensitive to the problems of their suppliers, prices remained stagnant.

Also, initially the increasing fashion content of garments caused some tension in the buyer-supplier relationship (see also Chapter 8). Many local producers have only limited awareness of the features of and changes in the US market. This made it difficult for them to relate their clients’ demands to larger trends in the market and hampered mutual understanding. While limited market awareness persists in local subcontractors, it has diminished over time.

Buyers’ perceptions of their sourcing linkages to La Laguna vary somewhat according to the type of buyer, but fall into a few general categories. Buyers complain about unsatisfactory production planning and punctuality on the part of their contractors in La Laguna. Especially for designers, for whom, based on the paramount importance of lead time considerations in the configuration of their networks, the geographical proximity of the Laguna region constitutes its main attraction. It is hardly surprising, therefore, that the unnecessary lengthening of lead times through the bad planning of and late deliveries by local contractors is an important aggravation. Buyers commonly also point to the inefficiency of many local suppliers. According to them, increasing production efficiency would allow contractors to deal with cost pressures.

More importantly, local business mentality in La Laguna is perceived as passive and unresponsive to market changes and buyers’ demands. Related to this, many buyers condemn the lack of service offered by their contractors. In comparison to, for example, Asian manufacturers, contractors in La Laguna are characterised as ‘arrogant’ and unwilling to think with their clients or to see things from their clients’ perspective. Several buyers acknowledged they might be spoilt by their Asian suppliers; indeed their opinions do appear slightly prejudicial (see Egan & Mody (1992) for a discussion of opinion-making amongst buyers). In reference to differences between Asia and Mexico, one buyer made the following observation:
'If, for example, you tell an Asian supplier he has to sew a pant, put on the button, dye the pant, take off the button, wash it and then put the button back on, he will do as specified without questions or comments. The contractors in Mexico will protest, will try to convince you that taking the button off makes no difference. Some may simply not do it.'

A manager of a high-end buyer with recent contracting experience in various parts of Mexico, including La Laguna, stated that the company was determined to take advantage of the opportunities – of NAFTA, geographical proximity and potential reductions of turn-around times – of sourcing in Mexico. Without going into great detail, he said:

'We will work in a different way from what we had planned. After trying a great number of Mexican garment firms, and asking for help and advice from institutions, agencies and consultants, we just had to give that up. Recently we ended up asking one of our main Asian suppliers to come to Mexico and do it for us. He's now in Yucatán, but we're trying to persuade some others to establish a factory in Mexico. It will allow them to continue to work for us and we will benefit from the short distance and flexibility...'

A final concern for buyers with regard to the Laguna cluster, is one they share with their local contractors. They are worried about the developments in the local labour market, turnover rates, labour poaching and wage cost. Especially smaller buyers that have a direct relationship with local producers and travel to the region expressed worries in this regard. A few buyers and brokers in El Paso even mentioned these problems as the main reason for moving their production from La Laguna to other regions in Mexico. Instead of blaming workers, most buyers place the fault with local industrialists. In the words of an El Paso-based intermediary:

'They [local industrialists and the chamber] need to get a handle on labour poaching. It has to stop. I know that the chamber has tried but has been unsuccessful. Business will be hurt if prices go up and productivity and quality suffer.'

A sourcing director of a large manufacturer drew his conclusions in late 1999. The company pulled all its work out of La Laguna and he explained the decision as follows:

'We do not see any future in La Laguna anymore. We don’t think they can solve the labour market problems, and ultimately prices will go up and quality is jeopardised. Central Mexico offers better opportunities, large firms are not all packed together there.'

### Table 7.3: Insertion of local SMEs in export networks

<table>
<thead>
<tr>
<th></th>
<th>Small</th>
<th>Medium</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct exports</td>
<td>1</td>
<td>6</td>
</tr>
<tr>
<td>Export through local intermediary</td>
<td>8</td>
<td>13</td>
</tr>
<tr>
<td>Export through non-local intermediary</td>
<td>0</td>
<td>6</td>
</tr>
<tr>
<td>Export through intermediary + direct exporting</td>
<td>1</td>
<td>5</td>
</tr>
<tr>
<td>Total</td>
<td>10</td>
<td>30</td>
</tr>
<tr>
<td>Purely domestic market</td>
<td>2</td>
<td>2</td>
</tr>
</tbody>
</table>

Source: Baseline survey, 1998-1999
This latter observation points to one of the potential downsides of clustering that is a real threat to the development of La Laguna where the disadvantages of an excessively tight labour market outweigh the clustering advantages.

Despite their ultimately subjective nature, these general perceptions can be assumed to affect business relations and the content of individual sourcing linkages. At a higher level of scale, even the configuration of production networks may be impacted as perceptions of business in La Laguna are juxtaposed with perceptions of other Mexican regions or even other countries.

7.4 Export networks and the insertion of SMEs

Notwithstanding their structural differences, the various types of networks discussed above have one thing in common: buyer-producer linkages are concentrated in the large and very large and only sometimes – in the case of branded manufacturers – medium-sized garment companies in the region.

How and where do local SMEs fit into these export networks? Most networks outlined above appear to offer limited (if any) opportunities for SMEs: the work of branded manufacturers and designers, for example, is either not at all or only to a very limited extent subcontracted. Through subcontracting linkages, retailer centred-networks do extend to include medium-sized and small subcontractors in La Laguna. Does this mean SMEs rely fully on retailer-centred networks and the intermediaries through which their work is distributed and controlled? Or do SMEs also produce for smaller buyers in the US? Table 7.3 illustrates the insertion of local SMEs into the export networks.

At first glance the table confirms the image created by the first sections of this chapter and by previous chapters: very few SME have a direct link to the export market. Those that do export directly, commonly work for branded manufacturers such as Savane and JanSport (part of the VF Corp.) but also for smaller buyers. Generally in these networks SMEs perform a limited role (assembly or CMT), while other production activities are subcontracted locally or performed or coordinated by the buyer. The large majority of the local SMEs export indirectly; their connection to US buyers is mediated through local contractors or non-local intermediaries. In line with findings in the previous sections, most work that is channelled through intermediaries to SMEs bears the private labels of large retailers. Route 66 and High Sierra by Kmart, Faded Glory by Wal-Mart and Chic by His are examples of the labels produced in local SMEs. These are the lower-end, bulk produced garments at the bottom of the local product range. However, Table 7.3 also shows that some SMEs have room to manoeuvre in choosing export channels and positioning themselves in the export networks. Several companies combine a subcontracting role in retailer-centred networks with direct exports. Typically, direct exports are for smaller, less well-known buyers such as Motherhood, which specialises in maternity clothing, or Cavaritzi, a Los Angeles-based fashion buyer.

Over all, medium-sized firms are in a better position to develop a direct exporting relationship. Larger company size is an explanatory factor in itself, but machinery and facility conditions may also play a role. Large production capacity allows some of the medium-sized companies to work for up to three customers at one time. Small companies are unable to do that, as their entire capacity is usually filled by one local client. In fact, small company size is a severe barrier to direct export production, because the minimal production capacity that even smaller US...
buyers require often exceed the capacity of small firms in the region. In addition, the facilities of many small companies do not meet the standards of most buyers, who in turn do not want to invest in upgrading these small companies. Finally, the perspective of most small companies in the garment industry does not extend beyond the local cluster boundaries. In other words, they work for one of the local giants and have little notion of the US or the domestic market, the main buyers and their market position, how and where to contact them or the standards they require from their contractors.

The companies in Table 7.3 that export directly stand out from the other SMEs in the region. While many SMEs are managed on a day-to-day basis and appear to lack a well-defined, articulated business strategy, these few more diversified companies are exceptional. Their position is in most cases the result of a proactive attitude. Some of them have spread their risks by broadening their buyer base and by producing for the domestic market as well. Others have put particular emphasis on the quality of their products and/or the conditions of their facilities. In general, the managers or owners of all of these more all-round companies have a better understanding of their industrial environment and its trends than their local peers do. In some cases they, or their family, have been in the business for a relatively long time.

Most but not all local SMEs function as subcontractors and depend on local contractors for their insertion into export networks. The critical question with regard to local SMEs concerns the differences and advantages/disadvantages of direct exporting compared to indirect exporting, and vice versa. If, as is the case for several of the more diversified SMEs, their position is the result of strategic decisions, what is the aim of such strategies? Diversification of the buyer base or diminishing the dependence on one single client may be an aim in itself. However, when asked to elaborate on any differences between local contractors and US buyers as clients, a more subtle difference was also revealed. One respondent explained the difference between the relationship with his US intermediary and that with his local contractor (through both of which he worked for the same buyer):

‘After six years of working for our client, we had a relationship built on trust. Our factory was treated as a socio, a partner. We were more strategically involved and we knew what was going on – with the intermediary, its clients and in the market. On several issues, the buyer and our factory communicated directly, without interference from the intermediary. We had our own responsibilities, including practical responsibilities; we bought all the trim and printed the barcodes, for example. We did not have an auditor from the intermediary or buyer in our factory.’

This contrasts with the company’s relationship with a local contractor through which it exports indirectly, which was described as follows:

‘[the local contractor] … treats us like an employee. We are not involved, consulted or even informed on matters of planning or organisation. We are like a babysitter; everything [trim and fabric] is delivered to us, we assemble and deliver when we are told to. All contact with the buyer is through the local contractor, but all responsibility is also theirs. Procedures and products are checked strictly by their auditors.’

Interviews suggest that this pattern can be generalised to a difference between a direct and an indirect export position. Respondents indicated that when working for local intermediaries or contractors, prices were reasonable and the products largely the same, but the responsibilities of the subcontractor were very limited. Fluctuations in work were fairly frequent so it was hard
to build up a long-term relationship, especially because the business relationship in many cases was rather distant and dispersed over several departments and personnel. This system of fluctuating, unstable sourcing relationships requires tight governance but little investment in the relationship and limited transfer of knowledge and information (see Chapter 8). This is facilitated by subcontracting work of the lower-end buyers, who first of all, allow subcontracting but also generally have lower quality standards. In the relationship with US buyers the physical distance often meant more responsibility for the local firm and also more learning because the responsibilities were broader and not always clearly defined.

For many local SMEs, positioning themselves in a direct exporting position may be complicated and difficult because of the minimal capacity requirements and limited knowledge of potential buyers. Furthermore, if standards and requirements increase, as is suggested by the literature (see Chapter 1), then the window of opportunity for SMEs wanting to break out of a pure subcontracting role is closing. On the other hand, the majority of local SMEs appeared to be fairly content with their indirect insertion into export networks, which implies a limited but straightforward, surveyable role as subcontractors. Only a few companies broke away from the subcontractor role, by seeking access to direct export channels or by getting more deeply or structurally involved in the domestic market.

7.5 Domestic market networks: an alternative for SMEs?

For a local garment SME that wants to break away from its pure subcontractor’s role, production for the domestic market may be an easier option than entering into a direct exporting relationship with a US buyer. As mentioned in Chapter 2, generally there is a large capability gap between standards in domestic markets of LMICs and those in export markets. By contrast, barriers to penetration of the Mexican domestic market are so low that some companies occasionally do some domestic market work ‘on the side’ (see Chapter 4). This ease of entry and exit is due to the fragmented nature of the Mexican domestic market (Mendoza et al., 2002; see also Chapter 3). First, it is fragmented geographically: many domestic market producers sell their products on the regional market. More importantly, the retailing of clothing is fragmented organisationally, as formal large-scale, formal small-scale and informal small-scale distribution channels each account for about one-third of total clothing sales in Mexico (Mendoza et al., 2002). This contrasts with the situation in many Western countries, where formal large-scale channels, most notably department stores, take up a relatively larger share, while informal small-scale retailing is of more limited and declining importance. Other

<table>
<thead>
<tr>
<th>Distribution channel</th>
<th>No. of companies</th>
</tr>
</thead>
<tbody>
<tr>
<td>Nation-wide department stores/ tiendas de autoservicio</td>
<td>6</td>
</tr>
<tr>
<td>Formal small shops:</td>
<td></td>
</tr>
<tr>
<td>• Own shops</td>
<td>3</td>
</tr>
<tr>
<td>• Wholesale</td>
<td>2</td>
</tr>
<tr>
<td>Informal: tianguis/aboneros</td>
<td>2</td>
</tr>
<tr>
<td>Total</td>
<td>13</td>
</tr>
</tbody>
</table>

Source: Baseline survey, 1998-1999
key characteristics are of domestic production networks (formal as well as informal) are variation and opportunities.

This section examines whether and if so how local producers in La Laguna feed into the various domestic market distribution channels and how these channels are structured. Table 7.4 shows which distribution channels garment firms in La Laguna use to sell their garments on the Mexican market.

Possibly the most surprising feature of Table 7.4 is the fact that few local producers sell their products through informal channels of *tianguis* or street vendors who use vouchers, the *aboneros*. One might expect such local markets to sell local products, but in La Laguna *tianguis* and informal markets sell primarily garments from places in the centre of Mexico, such as León and Irapuato, as well as cheap imports bought in the US. Although informal, small-scale channels are of limited importance to local producers, the limited occurrence in the table may also partially be due to the clandestine, hidden and/or possibly incidental nature of these activities. However, as mentioned in Chapter 5, no evidence was found of sizeable underground garment trade and production in the region, and therefore the general trend in the table seems fairly accurate.

Thus, generally domestic market garment producers in La Laguna feed into formal distribution channels. Their garments are sold through nation-wide buyers with stores throughout the country or in small shops, in most cases in the region. In a few cases these shops are owned by the producers; often, however, they are independent. The connection between local producers and formal marketing differs in two ways from those in the export chains. First, garments are designed and owned by the manufacturers and the relationship with buyers is mostly a market or arms-length relationship. Generally, buyers, including the *tiendas de autoservicio*, are not involved with product development or with production organisation. Most of these stores do not have a focused private label line; in fact, in many cases the garments sold bear the label of the producer, even if it is a small producer and the business relationship is temporary. Governance is not part of domestic retailer-producer linkages and producers are the pivotal point of the production network. In some cases, especially for companies that are predominantly oriented towards the domestic market, fairly large numbers of subcontractors are engaged. Since the retailer’s interference in and governance of product and production matters is limited, facility and labour conditions are hardly a matter of their concern. Commonly, conditions found in subcontractors of manufacturers that supply domestic large-scale retailers approach sweatshop standards.

Secondly, the chain feeding into the formal channels is short. In the Laguna region most producers produce autonomously and sell directly to the retailer or are themselves responsible for retailing. Most export companies that produce for the domestic market sell their garments through small shops. Their production is carried out in-house as a complement to or back-up for export production (see Chapter 4). Though some have their own shops, only a few companies in the region use domestic-market production to create a focused brand or label image. The latter is a reflection of the Mexican market, where very few Mexican brands or labels have established a strong market position for themselves.

In general the Mexican domestic/regional market is marked by instability and it offers plenty of opportunities to adventurers, opportunists and fly-by-nights. The fairly large number of small, specialists cutters, laundries, etc. in the region (see Box 7.2) are both evidence and
Box 7.2: Bits and pieces of domestic market production

In La Laguna, domestic market garment production is dwarfed by the export-oriented segment. Yet it can not be ignored. Within the region, the entire domestic market value chain is represented mostly by comparatively small-scale, often somewhat run-down facilities with basic and sometimes truly outdated technology. Barriers to entry are low and the presence of specialist cutters and laundries allows for the occasional production of small batches, especially since fabric and trim leftovers of the export segment may be obtained at much reduced prices. A number of representatives of this domestic market chain are introduced below.

A shadow economy in fabric and trim supplies

Between calls on his cellphone – from managers who urgently need a certain type of thread or who want to sell elastic or another kind of leftover – in his small ‘warehouse’ of which every millimetre seems to be occupied by one type of trim or another, Sr. Pedro Gonzales explained his business. Gonzales has made the trade in leftover trim and thread of the garment companies in the region his main source of income.

After many years of performing different jobs in the garment industry, both on the border as well as in the Laguna region, Gonzales set up shop in Torreón in 1998 and bought a small house in a hidden corner in the centre of the city to serve as a warehouse. At that time, his business was relatively straightforward and local: it consisted of the buying and selling of thread and trim leftovers of the companies in the region. In the days when US buyers still sent the necessary trim for their garments to their manufacturers, over-estimation of trim was such as to give rise to fairly extensive tradable volumes of leftover zippers, thread, elastic, pocketing and buttons, et cetera. Since these leftovers were a burden on the limited storage space of most of the companies and their future use mostly a matter of coincidence, Gonzales could buy them at relatively low prices. On the other hand, there was always a demand for these goods in the cluster (from exporting as well as domestic market producers) and since Gonzales was a known figure in the business, he had no problem selling his goods.

Recently, however, since the establishment of a very wide array of suppliers in the region and the increasing responsibility of local manufacturers for supply procurement, the amount of leftovers in the factories has been pushed down to a bare minimum, forcing intermediate traders such as Gonzales to travel extensively in search for cheap tradables. He now regularly travels throughout the North of Mexico, covering the states of Chihuahua, Durango and Sonora. Local demand, as evidenced by his constantly ringing phone, is still very high. Especially the domestic market producers are good clients. Gonzales: ‘...acceptan todo, especialmente lo barato’ (‘...they’ll accept anything, especially the cheap stuff’). Indeed, the warehouse did not show serious signs of a slowing supply: there was barely any room to move between the ceiling-high piles of boxes of thread, elastic, zippers and buttons.

While Gonzales’ business is well-known and formal, informal, underground trade often of stolen fabric, trim items and other goods, has grown over the past years. Local sources reported informal traders who turned up at factory gates trying to sell different sorts of trim and fabric at very low prices. Generally the origin of these goods is ‘unknown’ and the sale is unregistered.

Second-hand machinery and parts

In the region is a lively business between local companies in second-hand supplies of machinery and parts, as well as in machinery coming from auctions of closed down companies in the US. The latter
may appear to be of a more ad hoc nature, though some people have made the contrary development in the garment business between the US and Mexico their core business by trucking second-hand machinery from the US to Mexico. This is Mr. Jones’ business: he buys equipment at auctions throughout the US, loads it onto his truck and drives it to and through Mexico, where he sells equipment to Mexican garment manufacturers. Generally, the Laguna region is his first stop in Mexico.

Besides these specialist traders, local industrialists in La Laguna may from time to time also visit auctions—which are advertised widely—in the US in search for good, cheap equipment. This applies especially to automated or highly specialised sewing machines or cutting room or laundry equipment. More ordinary second-hand machinery can quite readily be found in the region. Many machines are ‘handed down’—at a fair price—from contractors to their subcontractors. This type of recycling of machinery within the cluster is quite extensive and facilitates the establishment of small companies. On the other hand, as noted by some US clients, quality may well be less consistent in companies using what sometimes appears to be ‘pre-colonial’ machinery.

The cutting edge

A garage-type space, just outside the centre of Gómez Palacio, houses the cutting room of Sr. Palma: on one side there are endless heaps of cut fabric and rolls of fabric, and on the other are Palma’s cutting tables. The cutting room was established in 1996; until that time Sr. Palma had worked in many different garment factories from Tijuana to La Laguna. Most importantly, he helped set up the cutting room of a very large garment company in La Laguna in 1993. This cutting room was closed soon after it was opened due to a lack of demand based on trade regulations that imposed duties on garment cutting in Mexico. However, his involvement in the project gave Sr. Palma the necessary skill, experience and contacts for the establishment of his own cutting business. Moreover, in the peak export season, Sr. Palma is hired to cut all the domestic market production for this very large company (that re-opened its cutting room as soon as duties on cutting were lifted). For this task, which is an important (up to 70%) but fluctuating part of his business, he temporarily hires extra personnel to work in the cutting room of his client.

Meanwhile, in his own cutting room he currently has several manual cutting machines and besides Sr. Palma there are five full-time employees. In 1999 the cutting room had a maximum capacity of 15,000 garments a week, up from 5,000 three years earlier. It does work for various local companies that find him through word of mouth. The lion’s share of his work is for the domestic market. The domestic market business is informal in character: clients come and deliver the fabric and a pattern, and arrange an approximate date for collection of the cut pieces. Generally, for domestic market garments, markers are made in the cutting room on the basis of provided patterns and the specification of the numbers and sized to be produced. Sr. Palma occasionally also has larger clients that produce for export.

*Ivan’s sewing shop*

Ivan’s sewing business is located on the third floor of a five-storey building in the commercial centre of Gómez Palacio; the business is unidentifiable from the street, other than from the small ‘Se solicita costureras’ sign on the wall. These all but modern surroundings contrast sharply with the working environment found in the better exporting companies: there is no marble and mirror covered entrance hall, and the shop floor has few of the amenities commonly found in the export sector. There is no air-conditioning—‘fresh’ air enters through the windows on the street side of the building—or
canteen, and the toilets are two floors down, but the music is loud and thirty sewing machines are buzzing away.

The sewing business has a weekly production of 1,500-1,800 jeans or carpenter trousers, which are destined for the local market. Ivan works for two large local-market clients and fills seasonal gaps in demand with his own products – which just happen to be exactly the same models as the ones his clients use. He intends to increase the volumes of his own products.

The business employs 35 people, most of whom are from the neighbourhood and who prefer to work in this business because of the higher flexibility, more relaxed and less demanding atmosphere compared to conditions in the exporting companies. However, just like the exporting companies, Ivan has problems with high labour turnover and absenteeism rates.

A laundry in a garage

Laísa – a small industrial laundry working for both the export and the domestic market – is located behind the petrol station at the entrance of Cd. Lerdo. Between one- and two-thirds of the 30,000 weekly capacity is destined for export (through an assembly factory owned by a family member of the laundry-owners); the rest is filled with domestic-market production. Laísa has approximately seven domestic-market clients, who deliver their orders (500-5,000 garments each) to the laundry during the second half of the week and pick them up the following week.

The building is a large garage with hardly any laundry-specific infrastructure. Most of the very old, and sometimes wooden, machinery is placed almost randomly in the space and in some cases the discharge is a virtually ad-hoc arrangement of hoses and flumes. Containers filled with chlorine and other chemicals are placed close to the equipment and the floor is wet with a blue liquid (the discharge from the washing machines).

On one side of the existing laundry a new and more modern laundry building is being constructed. As in the case of the existing laundry, most of the equipment for the new laundry has been bought second-hand in the US or in the region. The new building will include a recycling installation – which is now obligatory in Cd. Lerdo – and a finishing department. The present facility has neither of these.

Domestic ‘marketing’

Umberto Jaidar has an oversized and apparently luxurious factory in Gómez Palacio, in the vicinity of a number of large exporting factories. This is Jaidar’s only production facility, although he controls a fair share of the domestic market production of piratería jeans in the northern states of Mexico through his subcontracting network. All Jaidar’s jeans bear the ‘Ranchero’ label, while the models bear a striking resemblance to the basic models of VF’s Wrangler jeans. The labels, tags, buttons and even rivets are attached in his own factory, all other production activities are organised through subcontracting arrangements within the region. Jaidar works with a large number of subcontractors, many of which are small sweatshops producing volumes from a few hundred to a few thousand jeans a week. Many of his contractors are located in the small villages surrounding Cd. Lerdo.

Jaidar distributes his garments widely in North and Central Mexico and has managed to consolidate his position over the years through a number of devaluations that put his less cash-rich competitors out of business. The Ranchero jeans are sold through wholesalers, at ‘tianguis’ and in small independent shops in cities in the north of the country. As the model is recognisable, cheap and popular in this part of the country, no active promotion or marketing is required.
facilitative of it. Their presence makes it possible for small producers to occasionally produce small batches of own 'private label' garments, or counterfeits for the domestic market.

No data could be obtained on the financial situation of domestic market production, but with the exception of subcontractors working for the large-scale tiendas de autoservicio, many domestic market entrepreneurs were quick to state that they were doing well. This may well be the case: Mendoza et al. (2002) for example, estimate the average mark-up over the entire chain feeding into Guadalajara’s garment market at over 100%. In the short supply chains feeding into the small shops that the local producers in La Laguna are involved in, much of this mark-up may accrue to them. It is therefore somewhat surprising that so few export companies see in the domestic market a worthwhile alternative to export. The limited interest in the domestic market is surprising for a number of reasons: the production of finished products for the domestic market can be done in small volumes against limited risk and with comparatively large profits, involvement in the domestic market spreads risk as it diminishes the dependency on the US market and, finally, it allows exporters to experiment with full package production.

Similarly, there is little enthusiasm for export production amongst domestic market producers. There have been attempts to incorporate domestic market producers as subcontractors into export production networks. However, few domestic market manufacturers are willing to accept export work. Prices for assembly differ little from one sector to the other; however, timeliness and quality demands are much higher and stricter in the export sector. Several domestic market assemblers reported that they do not believe they could live up to export standards and that they know they would be penalised severely if they failed. This can be understood in the light of the general capability gap between the Mexican domestic market producers and export standards. Moreover, it confirms the limited role local subcontracting linkages play in closing that gap. Since generally local export firms looking for new subcontractors do not, or only to a limited degree, get involved in the upgrading of domestic market producers to export standards, many domestic market manufacturers consider export production too risky.

Nevertheless, some often somewhat hidden interrelations were found. As mentioned, prices paid by US buyers have been stagnant and the profit margins of manufacturers in the region have been negatively affected. Exporting companies are trying to bring down costs and some do so by contracting domestic market cutting rooms and laundries, which charge rates significantly below those of the export cutting rooms and laundries that are certified. In both the cutting room and the laundry presented in the box in the previous section, export work was being done for a local export company.

7.6 Conclusion
Over the past few years the buyer base of the Laguna garment cluster has broadened: besides the branded manufacturers, which used to dominate the local industry, the number of retailers and designers that source from La Laguna has increased since the passage of NAFTA. Different types of buyers not only structure their networks differently, but their expectations of participants and governance exercised over the network linkages may also differ.

One important observation in this regard is the fact that generally retailers are not replacing branded manufacturers but are joining them: branded manufacturers have not left La Laguna and their networks and strategies remain important elements in the cluster. Several US branded manufacturers are directly involved in the cluster through local FDI facilities, which
have limited linkages to the rest of the cluster. These and other branded manufacturers also source from contractors in La Laguna; sourcing linkages run through international sourcing departments in the US and operate largely in isolation from local FDI facilities of the same companies. In La Laguna, several branded manufacturers have worked with a stable group of contractors for several years. Most of their contractors are large- and medium-sized companies that dedicate a large share of their total production to branded manufacturers. Much emphasis is placed on product quality and production efficiency. Most branded manufacturers do not allow the subcontracting of their work.

Mass merchandisers also have worked in La Laguna for a long time. They have been joined more recently by department stores. Both types of retailers have started to develop direct linkages to local giants, but the bulk of their work is still channelled to La Laguna through US-based intermediaries. Several intermediaries have factories in the region. In most cases the intermediaries supply their buyers with full packages by relying on a local subcontractor network of mostly pure assemblers and by centralising either cutting, laundry, finishing and/or other more specialist, higher value-added activities in their own production facilities. In other words, the intermediaries orchestrate and govern the entire production process and are headed for direct competition with local producers. In general, linkages between them and local subcontractors appear distant and formal and transmit limited learning opportunities, certainly with regard to extending capabilities along the chain. Upgrading of subcontractors by extending their capabilities along the chain is not in the interest of intermediaries as it would create competitors. Only a few local producers have bypassed intermediaries and established a direct relationship with a retailer. The few local companies with a direct link to a retailer are very large full-package suppliers.

Finally, marketers of designer labels have recently also started to source from the local full-package giants in the region. So far, they are only working with a select group of the largest local companies that can deliver high-quality full packages, potentially in large volumes. Especially in the early stages of the sourcing relationship they are directly involved with their suppliers and with communicating, teaching and enforcing their upgrading to the demanded quality levels. They require flexibility and service from their suppliers. Designers have not become firmly embedded in the cluster, but are still working with small volumes and pilot programs and a select group of local giants. Several have already discontinued their sourcing from their local suppliers or even the cluster at large, apparently because they were not satisfied with the service and flexibility on offer.

In line with observations in the literature with regard to the role of buyers in upgrading LMIC suppliers, buyers have played an important role in setting and improving the standards of local contractors in La Laguna (Egan & Mody, 1992; Gereffi, 1999; see Chapter 2). In the case of La Laguna it appears especially important because local experience with jeans production, especially amongst the new companies, was limited and their frame of reference to the US garment market was either very limited or non-existent. In this light, the assistance, interference, support and other forms of involvement of US branded manufacturers and of jeans manufacturing experts, many of which are from El Paso, have been very important. By the end of the 1990s, the Laguna cluster was a firmly established source for large volumes of good quality jeans sold by US branded manufacturers and retailers in the low and mid segments of the US market. Upgrading impetuses appear to emanate from the arrival of new buyers to the
cluster; the following chapter will examine whether this has resulted in an upgrading process, which companies are engaged and with which aim.

One observation with regard to upgrading can already be made here: the findings presented in this chapter suggest that the dependence on buyers for upgrading stimuli may be cause for concern with regard to local SMEs. The large majority of SMEs does not maintain direct network linkages with buyers. While in general subcontracting linkages have been found to facilitate learning in SMEs (CEPAL, 1998), in La Laguna there are clear limits to learning through subcontracting. The unstable nature of local subcontracting linkages based on pure assembly may limit the knowledge and information transmitted down the subcontracting networks and this in turn may hamper the upgrading of local SMEs. All the more so because SMEs are mostly incorporated in the networks of mass merchandisers and department stores, while the more sophisticated products of designers are only rarely subcontracted out.

The dependence or narrow focus on buyers as the main and often single source of market information is also somewhat worrisome. Information on the market and on market conditions is principally obtained through buyers: it is rare to see industry magazines in the offices of local factories and few local entrepreneurs appeared to have a well-informed, broad outlook on the industry or the US wearing apparel market and its principal buyers. At the turn of the century, new challenges were facing the Laguna cluster. Increasingly, enhanced market awareness, service, flexibility and a proactive business attitude are needed if local producers want to be able to respond adequately to new challenges. In order for them to secure a future for themselves, local producers will need to develop these qualities/attitudes independent of their buyers and will need to base them on a solid understanding of the global garment market and industry.

In this light, the virtual neglect of the domestic, regional market can be considered a missed opportunity that represents valuable upgrading opportunities. Product quality may not be so high on the agenda of the domestic market, but involvement in the domestic market may allow exporters to spread risk while teaching them how to take risks and act on opportunities. In short, the domestic market appears to be better at fostering entrepreneurial qualities than the export market.

Notes

1 It is difficult to compile a detailed list of final clients of the complex for the beginning of the 1990s, because of the dominance at the time of brokers and other types of intermediary firms. In many cases, there was no direct contact between the final client and the local contractor, and in some cases this may have obscured the identity of the final client.

2 In studying the impact of US buyer strategies and power shifts in retailing on manufacturers in Mexico, business relationships are often simplified by putting aside the role played by intermediary companies. As will be discussed in this chapter, this remains far removed from the experiences of garment producers in Mexico. The impact of shifts in retailing are in practice often still indirectly passed on to them through intermediary firms. This chapter departs from a functional division of downstream actors: branded manufacturers, retailers – including mass merchandisers, department stores and designers – and intermediary firms.

3 A number of intermediaries involved in production in La Laguna have followed this strategy by either developing or buying (a licence to) an existing label or brand. For example, the 807 Company based in El Paso has acquired the Long Horn brand, W. Stevens has its Zena Di label and Sun Apparel (now part of the Jones Apparel Group) has the exclusive rights to the Polo Jeans label.
The most important marketer for La Laguna is Gap Inc., which has a sourcing strategy that differs from other designers. Gap started sourcing in the region several years ago and mixes different kinds of sourcing strategies: part of its production is channelled through intermediaries, and part is direct and in the form of full packages.

When asked about the opportunities in the domestic market, export producers in La Laguna mentioned a number of problems. The comparatively large investment in fabric and the ownership of the garments is seen as both a risk and a barrier. The instability of the market and the underground nature of parts of it were also mentioned. In general, risk avoidance is highly prevalent among exporters. In contrast, many domestic market subcontractors indicate their interests in operating directly (i.e. with full packages) on the domestic market. In many cases they are barred from doing so on a structural basis by insufficient cash flow and access to credit, but may be quick to take advantage of occasional opportunities.
Appendix II
Illustrations of bi-national production networks

In this appendix the structure of the local production networks of local multi-plant companies that were illustrated in Appendix I are extended to show how the work of different US buyers is contracted out to local subcontractors (through mediation of local contractors).

Roman works for four different clients: Duckhead, Chic by His, Savane and Wrangler. With the exception of the relationship with Duckhead, that goes through a broker in El Paso, all relationships with clients are direct. For Wrangler, Roman does only the laundering and perming of Wrangler’s Timbercreek casuals, for the other clients it does assembly and laundering. The work for both Savane and Wrangler is done in Roman’s own facility; nothing is subcontracted as Savane nor Wrangler allow subcontracting of their work.

![Diagram of bi-national production networks](image)

Source: Baseline survey, 1998-1999

Figure II.1: The structure of the bi-national production network, Roman
Figure II.2: The structure of the bi-national production network, Casolco

Casolco USA
location: El Paso, Texas
employees: 30
activity: distribution

Casolco
location: Gómez Palacio
employees: 355
activity: headquarters, administrative offices, assembly

Casolco El Huarache
location: Cd. Lerdo
employees: 220
activity: assembly

Casolco Durango
location: Durango
employees: 175
activity: assembly

Casolco Corte
location: Villa Juárez
employees: 125
activity: cutting

Casolco Finish
location: Villa Juárez
employees: 400
activity: laundry and finish

Casolco Villa Juárez
location: Villa Juárez
employees: 125
activity: cutting

United States
Mexico

Dayton Hudson
Chic by His
intermediary, US
Kmart

Casolco

source: Baseline survey, 1998-1999
By contrast, a large share of the casuals for Chic by His – which are sold in US mass merchandisers such as Wal-Mart, Kmart and Target, under the Chic by His brand or the store’s private label – are assembled by Roman’s subcontractors. Also, one subcontractor assembles Duckhead casuals.

At the time of the survey, Casolco worked for three different clients; all three serve the low- to mid-segment of the US market and work with very large volumes. The work for Kmart is

![Diagram of the bi-national production network, Lajat]

*Figure II.3: The structure of the bi-national production network, Lajat*

Source: Baseline survey, 1998-1999
obtained through a US-based broker, who does cutting and finishing; Casolco (and four of its subcontractors) does pure assembly.

For Chic by His Casolco does CMT. Finishing, including perm press, is done by Chic by His, because Casolco does not have a perm press facility/oven. Three subcontractors also assemble for Chic by His because subcontracting is allowed and quality requirements (and thus risks) are comparatively low.

Finally, the work for department store corporation Dayton Hudson is full-package work that is all done in Casolco’s own facilities.

In 1999, three clients were filling most of Lajat’s production capacity: Liz Claiborne, Gap Inc. and Kmart, while a few smaller clients would come and go and change regularly. The relationships with Liz Claiborne, Gap Inc. and Kmart are direct. Volumes of Gap Inc. and Kmart are very large, but Liz Claiborne has just started to work with Lajat and works with smaller volumes and pilot programs. Compared to Gap and Kmart, the quality standards set by Liz Claiborne are high and this is why the work for Liz Claiborne was only subcontracted to Maquilas Tauro – a subcontractor that could deliver the required quality. Tommy Hilfiger had also worked with Lajat, but the relationship was terminated. The work of both Gap Inc. and Kmart may be and is subcontracted, the precise mix at any point in time depends on order sizes and production planning.