

Labour standards in Pakistan's surgical instruments sector: a synthesis report



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About The Ethical Trading Initiative

The Ethical Trading Initiative (ETI) is a leading alliance of companies, trade unions and NGOs that promotes respect for workers' rights around the globe. Our vision is a world where all workers are free from exploitation and discrimination, and enjoy conditions of freedom, security and equity.

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About Pakistan Institute of Labour Education and Research (PILER)

The Pakistan Institute of Labour Education and Research (PILER), established in 1982, is a not-for-profit, citizen sector organization engaged in research, education, policy advocacy and networking in the areas of labour rights, social justice, human development, regional solidarity, and peace. PILER, as a resource centre, facilitates the labour movement in building a wider social consensus on core labour rights through advocacy and linkages with local, national, regional and global partners.

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INTRODUCTION

Pakistan is a major exporter of high-quality surgical instruments, produced in the Sialkot region, that are used in public and private health authorities in Europe and the USA. Over the past decade a number of in-depth studies have highlighted instances of severe labour exploitation and child labour within the industry.¹ There have been some improvements in compliance with international labour standards from exporting factories in Sialkot. However, there is little visibility or oversight of the lower tiers of the supply chain where exploitation is known to be prevalent.

In order to continue to successfully participate in the global market, it is vital that ongoing due diligence on child labour and abusive practices is undertaken in the Sialkot surgical instruments industry and that meaningful steps are taken to address these risks. New legislation and regulations in Europe, Australia, and the USA require due diligence to be included in procurement and contracting procedures. Failing to comply with the contracting and procurement requirements of international buyers puts the industry at risk of losing business and causing damage to Pakistan's trade and export reputation and capabilities. In order to mitigate these risks and improve labour

standards and compliance, companies across the entire value chain need to work collectively to understand their respective roles and responsibilities in improving workers' lives in this sector.

This report builds on existing knowledge of the sector and its challenges. It set out to understand the root causes of poor labour standards and to identify the actual and potential roles and responsibilities of all of the key stakeholders in the global value chain. The aim was to identify recommendations that could deliver long-term solutions to these complex, endemic problems.

The research study involved a wide range of key stakeholders in order to benefit from their knowledge, to ensure it reflected their own understanding of the issues in the sector, to establish ownership and buy in to the findings, and ensure that those most affected would be integral to identifying the solutions. Two multi-stakeholder steering committees were established to oversee the research – an International Advisory Committee and Sialkot Steering Committee – both of which met over an 18-month period to provide critical inputs and advice on the research. These stakeholders included government officials at national and local levels (trade and commerce as well as labour departments), international public procurement bodies, international companies supplying public bodies, surgical instruments industry associations, manufacturing businesses in Sialkot, trade unions, NGOs, international and Pakistani experts and academics. These partners were consulted on the terms of reference for the research, the questions and focus of the due diligence study, and reviewed findings and drafts throughout the process.



1. See detailed long report for literature review.

ABOUT THE STUDY

The study was undertaken by 4 senior independent Pakistani researchers. PILER was responsible for contracting and overseeing the researchers in Sialkot and also provided a Secretariat function to the Sialkot Steering Committee. ETI led the study overall and convened the International Stakeholder Advisory Committee meetings. The study comprises four components:

1. A literature review (academic & grey literature), providing an overview of labour standards in Sialkot, reviewing production processes and business operations, the influence of cultural norms and traditional values and the prevalence and determinants of child labour
2. An analysis of labour standards (field research), including risks and incidence of child labour and other labour rights abuses (such as forced labour), business practices and prevalent contracting systems. The fieldwork included visits to 4 large factories (150-200 workers) and 1 medium sized unit (20-30 workers) in the formal sector, and 3 medium-sized workshops (20-35 workers) and 8 small workshops (4-10 workers) in the informal sector. In-depth, structured interviews and focus groups were held with 18 employers/owners, 12 state officials, 28 adult workers, 12 child workers, 8 subcontractors and 8 civil society representatives, during February and April 2019
3. A map of the supply chain of 2 categories of surgical instruments – Mosquito Artery Forceps and Dressing Scissors (both disposable and reusable kinds) – from procurement of raw materials to finished products and point of sale in Pakistan. Field investigation included unstructured interviews with 6 manufacturers (3 from the factories involved for producing reusable surgical instruments, and 3 for disposable instruments), interviews with 8 medium- to large-sized vendors (owner-workers) and 7 home workers

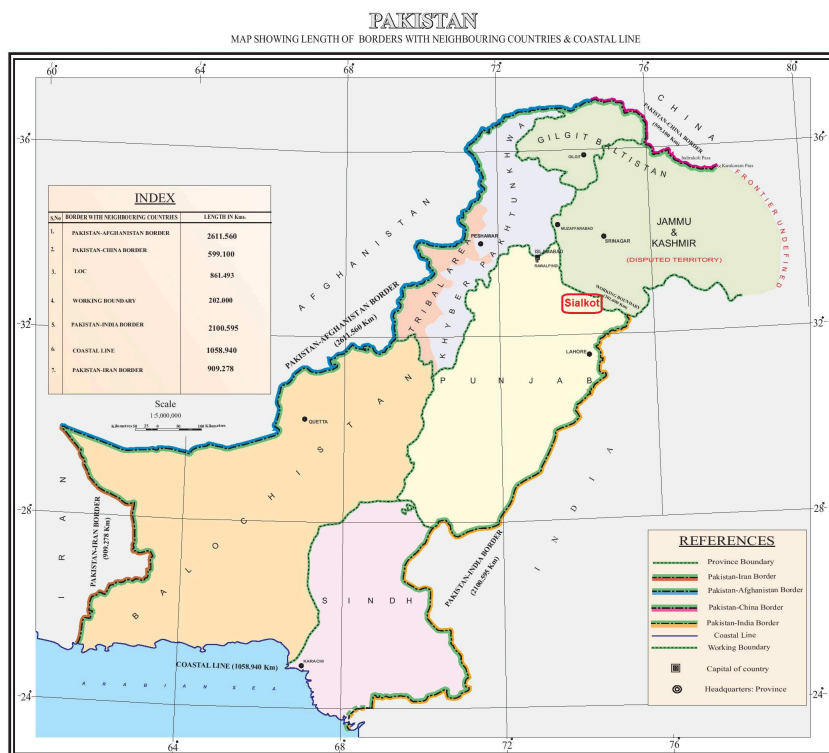
4. A mapping of the organisations and initiatives in Sialkot that may feature in identifying solutions and interventions. This report was based on visits, reviews of official documents, other materials, one-to-one interviews with local stakeholders, state institutions, NGOs, trade unions and other relevant bodies operating in Sialkot district. The map assesses their capacity, highlights local and national legislative frameworks and analyses the gaps in state labour welfare institutions and inspection mechanisms. A number of recommendations were made on how to strengthen the existing local platforms, enhance connectivity and collaboration and activate the relevant state mechanisms to eliminate child labour and unfair labour practices.

Ethics

A context-appropriate research ethics protocol was agreed and implemented. The stakeholders (employers and the management, state officials, adult and child workers) interviewed and consulted were informed about the aims and objectives of the scoping study. Oral consent to participate was obtained from each stakeholder. Confidentiality was assured and the names of companies and individuals have been anonymised.

Research constraints

Several constraints, including limited time for field work, prevented the team from more fully exploring the issues, including child labour, and access to some stakeholders was difficult. Child labour was the most sensitive subject and some stakeholders refused to acknowledge it. Focus group discussion with 6 children did not provide enough credible or generalisable information to draw clear conclusions on its nature or prevalence. The presence of child labour, at some sites, was difficult to witness – either because it was not present, or because children were told to disappear when advance notice was given of the visit. Due to the paucity of time and the watchful eyes of adult workers, the team was not able to develop a rapport with younger workers they encountered, and on-site interviews remained brief.



This map is adapted from the *Survey of Pakistan* website to show the general location of Sialkot.

SIALKOT SURGICAL INSTRUMENTS SECTOR

Overview

The Sialkot surgical industry produces 10,000 different types of surgical instruments and an average of 150 million pieces annually with an estimated value of PKR 40 billion (USD 255 million).²

Sialkot’s surgical instrument global production and value chain is labour-intensive and highly complex. It involves the import or local production of raw materials (including recycled steel imported from Germany and Japan) multi-tiered manufacturing centres, registered factories (“formal sector” workplaces), vendor-operated large, medium and small informal workshops, traders and suppliers of semi-finished and finished products, intermediary agents and international buyers.

Formally registered factories employ both permanent staff as well as workers on temporary or agency contracts. Their terms and conditions of work are generally understood to meet Pakistani as well as international labour standards. However, it is estimated that over 95% of production is outsourced to the informal sector (where worksites are unregistered and

work is carried out in small units and family homes). The informal sector is largely unregulated, and there is evidence of child labour, unsafe working conditions, excessive working hours, low wages, discrimination and vulnerability to abuse and exploitation.

Sialkot surgical instruments cluster

The Sialkot cluster started as a cottage industry, based on social and familial networks. Skills have been transferred from one generation to another and businesses handed down from fathers to sons. The export of surgical instruments is said to have originated in historical relationships between these businesses and family-run skill-based businesses in Tuttlingen, Germany.

The industry underwent significant change from the 1970s onwards, following successive legislative reforms. There was a steady increase in sub-contracting by factory owners, beginning with key production processes.

Today Sialkot has over 9,000 manufacturers registered as members of the city’s Chamber of Commerce and Trade across a variety of sectors. The surgical instruments cluster is considered the key SME export sector in Pakistan. The sector contributes 0.13% to the national GDP³, engages 100,000 to 150,000 workers in direct employment and creates indirect employment for 300,000 to 400,000 workers.



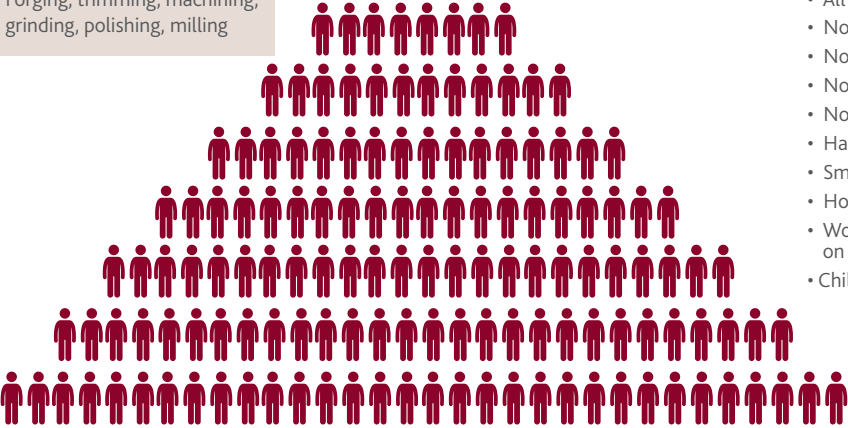



2. UK Department for International Development and Punjab Skills Development Fund (2014), Sector skills study: Cutlery, Utensils, Hunting Equipment and Surgical Instruments and Manufacturing [https://www.psd.org.pk/wp-content/uploads/2018/11/Cutlery-Surgical.pdf]
 3. Cluster Development Initiative, (Jointly implemented by United Nations Industrial Development Organisation (UNIDO) & Punjab Small Industries Cooperation (PISC) (2018), Diagnostic study report of surgical cluster Sialkot. [http://www.cdi.psc.gov.pk/reports/pscpublications/diagnostic_study_report_of_surgical_cluster_sialkot.pdf]

In 2018 the Cluster Development Initiative⁴ identified 3,600 surgical industry manufacturing units, the majority of which outsource significant percentages of their production processes. Three types of production units were identified:

- 20 large firms employ 250 to 350 workers and outsource 10 to 15% of their production
- 50 medium firms employ 50 to 250 workers and outsource 40 to 50% of their production

- 3,530 small firms/vendors employing 10 to 50 workers. It is estimated that 70 to 80% of the products made in these units use semi-finished materials made by home workers or outsourced from other sub-contractors.

The industry lags behind technologically and faces a sustainability crisis; the work is dirty and dangerous, and increasingly unpopular as a profession. Skills and training bodies in the region have not succeeded in building the skills base the sector needs to survive, and while there have been ad-hoc initiatives to improve skills, there has been inadequate coordination and a lack of any long-term strategy.

PRODUCTION PROCESS	FORMAL SECTOR	
Administrative, Packing, checking, cleaning	 Salaried	<ul style="list-style-type: none"> • Have employment contracts • Paid regularly or piece rate
Die making, polishing, heat treatment	 Contract workers	<ul style="list-style-type: none"> • Some registered for employment benefits • Independent trade unions generally not present
	INFORMAL SECTOR	97% OF PRODUCTION
Forging, trimming, machining, grinding, polishing, milling		<ul style="list-style-type: none"> • All workers paid on a piece rate • No contracts • No guarantee of minimum wage • No access to stable benefits • No access to trade unions • Hazardous working conditions • Small crowded 'vendor' workshops • Home-based workers on piece rates • Workers are often indebted to employers on 'peshgi' advance payments scheme • Child labour, although rare, can occur
	Helpers/apprentices: Unskilled workers helping on odd jobs or those who are training earn as little as 5,000 PKR a month. Legally apprentices should be paid 50% of minimum wage, however training is rarely formal.	
	Home Workers: Vendor workshops outsource some processes to home-workers because they will work for less. Little is known about the piece-rate paid to workers but it is likely very low as it is deemed more cost effective than workshop labour.	
		Traders/agents: They operate as fixers across all tiers of the supply chain. They take product specification from buyers, identify vendors and orders are met. They are often registered and vetted by foreign buyers.

4. The Cluster Development Initiative is jointly implemented by the United Development Industrial Development Organisation (UNIDO) and the Punjab Small Industries Cooperation (PISC) and was set up in 2017 to improve the capabilities of high growth potential industrial clusters through operational improvements, linkages to lead firms/export markets and product development.

International market – competition and resilience

The surgical instrument industry is growing alongside increasing demand in high-income importing countries. Sialkot's market share of the global surgical instrument industry is significant but under-reported. Many products are routed through Germany and badged as "made in Germany", which obscures more accurate trade figures.

Britain is the third-largest buyer of surgical instruments from Pakistan. In 2018 a report found that 80 to 90% of all instruments purchased by the public health procurement body, NHS Supply Chain, were made in Pakistan. The UK market represents 10% of Pakistan's exports.⁵

China, producing low-quality cheap products appear to have increased their market share – mainly to emerging markets such as Africa, South East Asia and Russia. China's share increased from 2.8% in 2007 to 4.9% in 2016.⁶ Historical drivers of competitive advantage, namely skilled knowledge and established relationships are of decreasing relevance in some markets where price trumps quality. In some markets, demands for greater volume, more advanced and specialised equipment has brought new competition, and technical compliance specifications have increased.⁷

The surgical cluster, save a few exceptional manufacturers, generally lack the resources and organising capabilities to diversify and keep up with new competition and market demand. The Cluster Development Initiative reports that profit margins of 62.5% of companies have decreased due to price competition among the cluster companies, as well as increased costs in the price of production.⁸

Quality

The quality of instruments produced depends on the materials and processes used, as well as the quality of the workmanship. Most manufacturers in Pakistan have internal processes to ensure products meet international quality standards such as the Association of British Healthtech Industries.⁹ However, there is no evidence that this standard is applied in all locations in Pakistan or locations outside of Pakistan. In most cases, the location of each stage of manufacture is not documented. This raises critical questions about quality assurance.

Peer-reviewed medical journals have highlighted the impacts of poor quality of instruments on health. This is particularly in an increasingly hazard-conscious environment, where there are concerns over instrument sterilisation, surgical glove puncture and the potential for transmission of blood-borne and prion diseases.¹⁰

There are a number of reports of poor-quality instruments manufactured in China, with first-hand accounts by surgeons.¹¹ The quality of instruments from countries such as China may not match those from Pakistan. Production of instruments is a highly skilled task, so cannot be easily taken over by newcomers to the field. One surgeon interviewed in the study said that the quality of Chinese manufactured instruments being used in Ethiopia was the worst he had ever seen.

Production processes

It is estimated that out of the total number of surgical instruments manufactured in Sialkot, 60% are disposable items and 40% reusable instruments (see Figure 1, Annex 1 diagram).

For reusable instruments, expensive, high-grade steel, mostly imported from Germany, is used. Reusable instruments are produced with (mostly) a 5-year warranty on rusting, corrosion and precision. The final product involves up to 40 production processes. For disposable instruments, local low-grade stainless steel is used and only about 20 processes are carried out. The production process is labour-intensive and uses low- to medium-tech equipment and specialized workmanship skills. The majority of the work is done manually by subcontracted piece-rate workers. There are often multiple units (and often a mix of formal and informal) engaged at different stages for the completion of a single product.

Formal factories are normally based in the city of Sialkot or on its outskirts. They are able to manufacture 200,000 instruments a month. Most have modern equipment and some equipment is custom-built. Management systems are in place and they employ permanent staff who have access to social security benefits. They may also hire on-site subcontractors to meet certain orders.

5. <https://www.theguardian.com/global-development/2018/jan/29/nhs-admits-doctors-may-be-using-tools-made-by-children-in-pakistan>

6. Cluster Development Initiative, (Jointly implemented by United Nations Industrial Development Organisation (UNIDO) & Punjab Small Industries Cooperation (PISC)) (2018), Diagnostic study: Surgical Cluster Sialkot. [http://www.cdi.psic.gov.pk/reports/psicpublications/diagnostic_study_report_of_surgical_cluster_sialkot.pdf]

7. Hamrick, D. & Bamber, P. (2019), Pakistan in the medical device global value chain, Duke Global Value Chains Centre

8. Cluster Development Initiative (2018), Diagnostic study: Surgical Cluster Sialkot

9. Surgical Instrument Purchase and Care Guide, ABHI <https://www.abhi.org.uk/media/1430/abhi-si-sis-16pp-booklet-v4-singles.pdf>

10. Brophy, T; Srodon, PD, Briggs, C, Barry, P, Steatham J, Birch MJ "Quality of Surgical Instruments" <https://www.ncbi.nlm.nih.gov/pmc/articles/PMC1964625/>

11. <https://www.lifebox.org/instruments/#3>

Some factories, despite having the required equipment and technical capabilities to carry out the entire production process themselves, still choose to subcontract work to vendors as it is far cheaper to do so.

One factory owner explicitly stated this, saying ***"It is better to outsource some processes to workers sitting in villages because they do it on lesser wages. Hence some companies stop in-house processes even though they have acquired the machines"***.

Informal workshops are primarily based in villages surrounding Sialkot city and vary in size. They normally have one to two poorly lit rooms with three to five workers in each room being paid at a piece rate. Most of the work is carried out manually. However, researchers did report some vendor workshops having process-specific machines, but they appeared to be underutilised. Sometimes workshops outsource part of the production processes to home workers.

THE GLOBAL VALUE CHAIN

Price pressures

The large formal factories are captive to international buyers. They are expected to respond to buyers' demands around pricing and product specifications. Producers reported downward pressure on prices from many buyers with unit prices declining over the last few years.

The study found that there is limited profit for Pakistani manufacturers compared with profits made on the international market. Because of fierce local competition between manufacturers, some international buyers (public bodies and their key suppliers) continue to place downward pressures on prices, while still expecting the suppliers to meet their requirements on quality and social standards.

Compliance and auditing

Suppliers are expected to shoulder the burden of increasing compliance costs.¹² There is also a problem of quality and verification of data in relation to monitoring compliance. International buyers and suppliers are often barred from travel to Pakistan on security grounds, and are wholly reliant on third-party auditors. In Pakistan, few auditors are internationally certified, the audit industry is not regulated, and auditors may be subject to bribery.

Branding

Pakistani companies are limited in the profit they can extract from the surgical instrument value chain. Very few companies have the ability to brand and export their own products directly without going through intermediary agents and suppliers. Branding usually takes place in Europe or USA, after export. Intermediaries therefore often sell Pakistani products at a significant mark up.

Value chain dynamics

The study found that some products were being sold in the UK with a mark-up as high as 400% on the export price (see figure 2), but this includes the cost of marketing and distribution. Governments and public health services are key clients of distributors. Public procurement teams, facing pressures to provide the taxpayer with good value for money, often weight price heavily when awarding contracts. This, however, is often at odds with expectations of good labour standards and working conditions. Most buyers are reported to make their final decision on pricing, although there are some exceptions. Some public buyers are now changing their tendering contract specifications and are reviewing suppliers against criteria that include due diligence, transparency and mitigating risks of child labour and modern slavery.

Smaller contract manufacturers that supply to export factories are even more squeezed, as the formal factories pass on these pressures through their subcontracting processes. Invariably, because of fixed minimum production costs and quality standards for these commodities, labour costs are the only "elastic" element and the most vulnerable, exploitable workers end up paying the cost of these price pressures.

"The buyer only requires quality at the lowest price. He is not concerned with labour. If I ask him to raise the price from 25 cents to 30 cents so that I can increase wages and make the workplace comfortable for my workers the buyer says, 'why should I buy from you? I would rather get it from your competitor at a lower price'."

12. Hamrick, D. & Bamber, P. (2019), Pakistan in the medical device global value chain, Duke Global Value Chains Centre

Figure 1, below, details the pricings of the two instruments studied. It shows that the majority of the profit goes to companies outside of Pakistan, and that the manufacturer itself is able to make minimal profit.

Instrument		Cost of Manufacture	Avg. Export Price	Avg. Sale price (UK)	% Mark-up post-export
Mosquito Artery forceps	Reusable	0.91 GBP	1.53 GBP	5.31 GBP	247
	Disposable	0.43 GBP	0.54 GBP	1.08 GBP	100
Dressing Scissors	Reusable	0.77 GBP	1.38 GBP	6.95 GBP	404
	Disposable	0.34 GBP	0.45 GBP	0.99 GBP	120

Figure 2: Value chain analysis,



WORKING CONDITIONS

Child labour

In 2016 the Government of Punjab raised the minimum employment age to 15 years in most sectors, and to 18 years in hazardous occupations, including the manufacturing of surgical instruments.

In the formal sector (large and medium-size factories) persons under 18 years of age are not employed. Some large factory owners conduct checks that their off-site vendors are not using child labour, but very few are doing this. However, anecdotal evidence during the study points to a box-ticking paper-based exercise, and many of the audits, if they are conducted, are unlikely to be reliable.

Although the incidence of child labour is declining, it is still present in the informal sector, hidden in congested neighbourhoods on the outskirts of the city, and in nearby villages. Child workers are aged between 11 and 17, employed in small workshops. In one instance the team came across 9 children aged 11 to 15 in a drop hammer workshop in a village 25 km outside of the city centre.

Poverty remains the core driving factor pushing children into the workforce. Many people working in this sector cannot afford to send their children to school, and many say the quality of education available is poor. The poorest families living in and around Sialkot are desperate to earn

money to put food on the table and pay for healthcare and other basic costs.

In spite of this, in recent decades, although poverty levels have changed little, child labour levels have gone down. This is primarily due to enhanced legislation against child labour, awareness-raising interventions carried out by various stakeholders, and pressures from international bodies, including buyers.

Health and safety

A limited number of large formal sector firms have clean, healthy and safe environments. Working conditions in the informal sector are generally unhygienic and hazardous both to workers and their employers.

The premises of many small vendor units, particularly forging shops, were found to be dirty, cramped and poorly lit, without ventilation or health and safety equipment. Forging, cutting, grinding and polishing by hand expose workers to harmful dust and debris, and many workers have cuts or burn injuries to their hands, arms or faces.

Few workers seem to wear face masks, gloves or eye goggles. Even in formal sector factories where health and safety instructions and equipment are provided, workers may often not use them, because they feel the equipment is uncomfortable to wear, and slows them down. There is limited awareness of the value and importance of personal protective equipment by workers and employers.



Wages

Pakistan's national minimum wage increased from PKR 13,000 to PKR 15,000 in 2017, and in turn contributed to increased production costs. But in the face of increased competition for market share, businesses have increasingly out-sourced parts of the production process to workers in the informal sector. The result has been wage stagnation as most workers in the informal sector are paid on a piece-rate basis, and are not subject to minimum wage laws. These labour market dynamics have in turn contributed to the shortage of skilled labour in the surgical instruments sector. More workers, particularly younger people, are now seeking jobs in other industries that pay more and involve better types of work.

The earnings of skilled workers in the formal sector vary from PKR 20,000 to up to 70,000, inclusive of overtime. Some regular workers in the formal sector are registered and can access employment-based benefits such as social security and old-age support. However, a 2016 assessment of labour standards in formal factories across the entire manufacturing industry in Sialkot, found that less than half (44%) of workers were registered with the Punjab Social Security Institution. In the surgical instrument sector specifically, only 29% of formal workers were registered with the Employees Old-Age Benefit Institution.¹³ None of the piece-rate workers in the informal sector, which comprises around 97% of the production processes, are registered or able to access these benefits. They often do not know that they exist. It can therefore be concluded that the total percentage of workers in the surgical instrument value chain receiving employee benefits is extremely small.

Most people interviewed in this study reported that unskilled workers (those involved in packing, loading) and skilled workers (involved in various stages of the production process) in factories receive at least the minimum wage of PKR 15,000 per month. In 2017 the Asia Floor Wage estimated that a living wage for Pakistan as a whole to be PKR37,886 with regional variations.¹⁴ The Global Living Wage Coalition Report in 2017 put living wages at PKR20,000 for urban Sialkot and PKR18,000 for rural Sialkot.¹⁵

In the informal sector, incomes vary between PKR 15,000 and 30,000 per month, depending on the types of work and volume produced based on piece rates. The situation of "apprentices" is less clear. Regulations stipulate that apprentices should earn half the minimum wage while they are training. Some stakeholders that were interviewed reported apprentices to be earning as little as PKR 5,000 per month.

Freedom of association

Pakistan has ratified ILO core labour standards, including the right of workers to freedom of association and collective bargaining. However, very few workers in the country as a whole access these rights in practice: many workers are prevented from joining an independent, democratically elected trade union or may be threatened if they do so.

The Pakistan Workers Federation is the officially recognised national trade union federation that participates in tri-partite forums and international meetings. According to their representatives, only 2 large factories have a PWF-affiliated union in the surgical sector. A decade ago, union density was higher.

Nowadays it is common for employers to establish and register their own "yellow" unions to meet audit requirements, and de-register legitimate unions to prevent them from organising in the factories.



13. GSP Plus and Labour Standards in Pakistan, Interim Report 2016, Pakistan Workers Federation: <https://library.fes.de/pdf-files/bueros/pakistan/13924.pdf>

14. Pay Check - Pakistan, Wage Indicator Foundation: <https://paycheck.pk/salary/wages-in-context> [Accessed 18th November 2019]

15. Update: Living Wage Report Sialkot Rural and Urban Pakistan Football Manufacturing Industry - Updated to December 2017, Global Living Wage Coalition (2017) <https://www.globallivingwage.org/wp-content/uploads/2018/05/Pakistan-LW-Update-Report-final.pdf>

Working hours

Formal sector workers have contracts based on a standard 48-hour working week, with an additional provision for overtime hours. This is in line with the ETI Base Code. Informal sector workers were reported to be doing longer hours, but the scope of this study did not provide for independent verification of this.

Regular work and contracts

Most workers in this sector do not have permanent employment contracts. Piece-rate work is common in both the formal and informal sector. Due to competition and high levels of unemployment in the area, piece rate workers often find themselves in a "take it or leave it" situation, unable to negotiate higher rates of pay. Sub-contracted or agency workers operate on a precarious basis, with no certainty about the duration of their work, and unable to negotiate their wages.

Gender discrimination

There is gender discrimination in the labour market throughout Pakistan, and this industry is no exception. It is considered inappropriate for women to enter the surgical instruments sector. Social norms as well as the types of work prevent many women from accessing employment opportunities or advancement in this sector. However, there are some instances of women in senior or skilled roles in a few leading export manufacturing factories.

Loans - the "peshgi" system

The informal practice of advance payments or *peshgi* (in the form of interest-free loans) in the surgical instruments sector is common. Employers provide loans to workers to pay for health crises, education, funerals, weddings or other household costs because workers have no savings or ready access to loans.

Whilst the loan binds workers to their employer, it is different from other forms of debt bondage. The *peshgi* is commonly granted with no interest or deadline, nor is the repayment of the loan systematically deducted from monthly wages. The worker can repay the interest-free loan at their own discretion and, should they wish to leave their employer, they can seek to transfer this advance to their new employer.

The practice of *peshgi* is reflective of low wages and the fact that those who work in the sector tend to come from extremely poor and disadvantaged families. The practice exposes the financial insecurity and vulnerability of workers who spend their entire working lives under the burden of a loan. The debts are passed from one generation to another, and families are unlikely to be able to pay off the loan unless they are able to derive another income from elsewhere. When workers are so dependent on their employer, they are vulnerable and it is less likely that they will raise concerns, grievances, or join a trade union for fear this may risk losing their jobs.

Skills shortages

There is a growing skills shortage in the surgical sector. Families that have worked in the industry for generations – passing skills from father to son - are getting older and are not being replaced. The harsh working environments of the surgical instrument sector are not attractive to younger people. Those with an education and greater awareness of alternative job opportunities leave Sialkot to look for jobs in the IT and service sectors.

While there are a number of training organisations and institutes in the Punjab Province, they are not organised or coordinated effectively to deliver the skills needed to sustain the surgical manufacturing industry. There is a risk that the industry itself is under threat as greater investment in skills training, integrated industrial strategies, new technologies and innovation emerges from competitor countries.



The cross-cutting effects of informality

A key feature of the surgical instruments sector in Sialkot is the large number of very small, unregulated employers. Large numbers of workers are employed in small workshops, without formal contracts or social protections. This generates a range of cross-cutting impacts on key actors in the global value chain.

Vendors: In the informal economy, there are few, if any, records of commercial transactions. Many people working in the sector have had little formal education. In a highly competitive environment and with minimal profit margins and an absence of management systems, vendors don't have the time, incentive or know-how to consider the benefits of formalisation. This may limit growth and innovation. Small-scale vendors with low profit margins are focused on the day-to-day business of securing and delivering orders. They, like many others in Pakistan, tend to be sceptical of engagement with state institutions out of fear of increased taxes and regulatory burdens. They do not have the resources or capacity to invest in new technology or to expand their work to cover additional production processes. This current model benefits those higher up the value chain.

Workers: Just as vendors themselves have little motivation or capacity to change the status quo, workers do not have the knowledge or resources to fight for their employment rights. The majority of the labour force is poor and semi-literate. Piece-rate workers have no leverage to negotiate wages with their employers, and without the support of functioning trade unions lack the capacity to do so anyway. The lack of formal work environments limits opportunities for training and development and keeps workers in precarious financial situations. This creates a vicious cycle in which workers have neither the time nor the money to invest in education or training opportunities that could help to lift them out of poverty.

Innovation: The surgical instruments cluster has lagged behind in technological development, research or innovation. On the whole, there has been little upgrading of technology or streamlining of production processes, with a few exceptions. The up-front costs of modern machinery, combined with high electricity costs and unpredictable power outages deters small, informal vendors from shifting away from outdated manual manufacturing methods. Small vendors also tend to specialise in one or two processes only. As vendors do what they can to protect their specialised workstreams, there are few incentives to streamline production processes, use resources more efficiently or increase productivity in the sector.

RECOMMENDATIONS

1. Build Pakistan's reputation in the international surgical instruments market

Issue: There is a lack of visibility and oversight of working conditions in the manufacture of surgical instruments below Tier 1 export quality factories in Sialkot. However, Pakistan also has a proud tradition of producing high-quality instruments using highly skilled workers. The industry is at risk of losing market share if it cannot demonstrate that it can meet growing international expectations to meet higher quality as well as labour standards.

Action: Sialkot is well positioned to utilise its position within the market to produce a line of high quality, ethically produced, and inexpensive instruments, which could be regulated and supported from within Pakistan, and sold to ethically approved international suppliers and directly to public health purchasing authorities.

2. Collaborate and mobilise against child labour

Issue: Despite a huge reduction in child labour across the industry, and its eradication from the formal sector, child labour can still be found in the informal sector where most production takes place.

Action: It is recommended that the Labour Department, SCCI, SIMAP, CSOs and trade union federation should collaborate to identify families at risk and develop interventions. The District Government could ensure children of poor families are enrolled in government primary schools, and continue secondary education until 15 years of age as per the Punjab Free and Compulsory Education Act 2014.

3. Increase wages and access to benefits

Issue: Workers involved in over 97% of the surgical instrument production processes do not have any guaranteed monthly income or any access to state and employment benefits. In order to meet compliance regulations and to maintain a workforce at a time of a skills shortage in more hazardous work companies need to play a greater role in improving wages and benefits for workers.

Action: Supply chain stakeholders could develop collaborative institutional mechanisms to improve wages for workers, in line with the actual cost of living. SCCI and SIMAP could coordinate with the state-run welfare institutions for labour (ie PESSI, EOBI) to drive universal registration of workers in the sector so that they can access social security benefits. There could be improved governance, accountability and monitoring mechanisms regulating the roles and responsibilities of employers and public bodies.

4. Tackle informality

Issue: The informal nature of the sector is one of the biggest constraints not only on the growth and development of the cluster, but to the status of workers and their ability to access rights and benefits. The Pakistan Bureau of Statistics undertakes a 5-yearly census of manufacturing industries, but surgical instruments manufacturing has never been included.

Action: SIMAP and SCCI could advocate for a census of the surgical instruments cluster to map the exact size of the sector, the number of formal firms and informal workshops and their categories based on revenue generation and workforce. This would help pave the way towards universal registration of workers with labour welfare institutions

5. Change international procurement practices

Issue: While not directly within the scope of the research, there is strong evidence that the procurement practices of international buyers contribute significantly to the conditions that result in poor labour practices. Buyers that drive a race to the bottom on prices are responsible for forcing Pakistani companies to sub-contract parts of the production to smaller vendors with low labour costs. This is the only way exporters will be able to meet the costs and quality requirements of the customers.

Action: International buyers and suppliers should agree to common minimum standards for working conditions in the sector, recognising that this will have cost implications. Increased transparency on the labour costs should be included in the price agreed for particular products, and buyers could include higher labour standards in tenders to improve commercial incentives for businesses that demonstrate responsible practices. Capacity building and guidance will be needed.

6. Increase freedom of association

Issue: The importance of freedom of association and collective bargaining (ILO conventions 87 and 98) in the global supply chain is recognised as crucial to improving working conditions and ensuring living wages. But a lack of trade unions is hampering the ability of workers in the Sialkot surgical instruments sector to claim their legal right to negotiate for improved working conditions through collective action.

Action: Consultations between employers and trade unions should be held to improve the lack of trust between them and to increase opportunities for workers to be organised and collectively represented. The advice of the ILO and ITUC could be sought to improve the

reach and capacity of the Pakistan Employers Federation, including workers' training programmes. An equivalent scheme to the Labour Standards in Global Supply Chains (LSGSC) Project recently implemented by the ILO in the garment sector supply chain in Pakistan should be considered.

7. Build skills

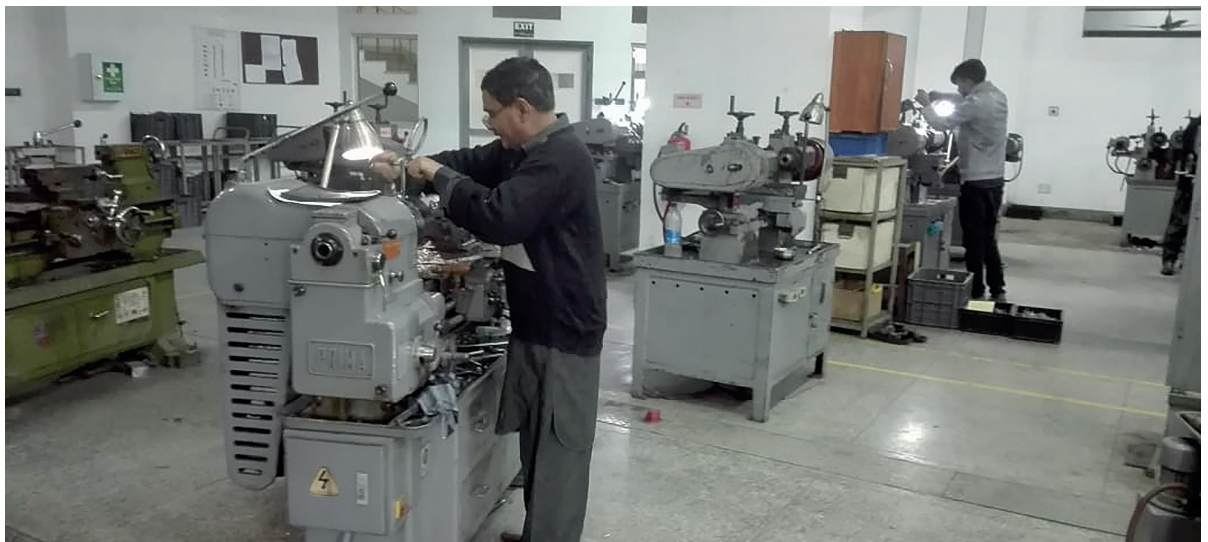
Issue: The workforce needs upskilling and renewing. This could be done through regulated apprenticeships and vocational programmes for both young men and women, to facilitate the professionalisation of skills and knowledge. Sialkot has a number of institutes which can be strengthened to produce skilled and qualified workers in the surgical manufacturing industry that meet international standards.

Action: A committee of experts led by SCCI and SIMAP should undertake a mapping exercise of existing institutions, engage with them, design appropriate curricula in consultation with appropriate stakeholders. They should urgently seek investment in research, development and the professionalisation of the industry.

8. Alternative financing mechanisms

Issue: The practice of advance payment (*peshgi*) that is used to tide over workers in the event of household emergencies – could be replaced with alternative financing mechanisms, such as (potentially) soft loans or microfinancing.

Action: A feasibility study should be conducted on alternative loan institutions to replace the *peshgi* system. SCCI and SIMAP could consult with existing microfinance operations within the country and consult on the possibility of a financing programme targeted at workers in the surgical instruments industry. Workers should be consulted on this and their own views sought for alternatives to *peshgi*.



CONCLUSIONS

Sialkot is well positioned to utilise its position within the market to produce a line of high quality, ethically produced and inexpensive instruments. It could be regulated and supported from within Pakistan, involving the government, industry bodies and other key stakeholders. Instruments from Pakistan could be sold to international suppliers that can demonstrate ethical practices or sold direct to public health purchasing authorities.

There are both challenges and huge opportunities to improve working conditions, business practices and Pakistan's competitiveness in trade and export. The report sets out some recommendations for making sector-wide sustainable changes to the surgical instruments manufacturing sector to improve both its commercial success as well as reputation on ethical standards.

The next stage of the process will be the development of a roadmap, identifying specific actions, resources and responsibilities for all actors in the supply chain. All stakeholders will have a critical role to play in ensuring that the goods they produce, export or procure from Sialkot are not produced at the expense of exploiting and abusing workers.

A number of policy and system changes will be needed:

- An agreed set of ethical standards for the surgical instruments industry, involving independent stakeholders to verify compliance and ensure alignment with international good practice
- Changes in international public purchasing practices – tendering, evaluation and review criteria to reward ethical performance rather than a race to the bottom on prices

- Improved governance oversight and regulation – involving government, industry associations, manufacturers, civil society, trade unions and international bodies.
- Increased transparency throughout the global production chain
- Multi-stakeholder monitoring of standards
- Incentivising responsible business practices

There is a critical need for government bodies, particularly for labour and trade authorities to regulate and monitor labour standards as a condition for export trade. In addition, there should be strong legal and financial consequences for non-compliance. The industry should be supported and held accountable for demonstrating both quality and ethical standards.

- Capacity building will be needed to effect these changes – top-down and bottom-up: Building awareness and technical changes in procurement processes for international public buyers and private sector suppliers sourcing from Pakistan;
- Increasing investment and capacity in industry bodies such as the Sialkot Chamber of Commerce, the Surgical Instruments Manufacturing Association to comply with commonly agreed labour standards and responsible business practices;
- Increasing capacity of manufacturers in Sialkot, intermediaries, informal SMEs, vendors to streamline efficiencies and increase productivity, improve and professionalise skills;
- Building the monitoring and technical advisory capacity of civil society organisations
- Improving the capacity and access of trade unions to represent the interests of workers.

With the right level of commitment, a shared sense of responsibility and a willingness to build trust between all parties, a multi-stakeholder approach to improving the surgical instruments sector in Pakistan could provide a global model of good practice.