

GAP

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Introduction -

- Gap Inc. was founded in 1969 by Donald and Doris Fisher in San Francisco, California, with a single store and a handful of employees.
- They originally began operations by selling Levi's, records and tapes (eight-track).
- Today, the Gap is one of the world's largest specialty retailers with three of the most recognized brands in the apparel industry — Gap, Banana Republic and Old Navy.
- Gap Inc. has more than 150,000 employees supporting about 3,000 stores in the United States, United Kingdom, Canada, France and Japan.
- In 2004, the Gap boasted fiscal revenues of \$16.3 billion.

Introduction, cont'd.

- World headquarters are located in San Francisco, product development offices in New York City and distribution operations and offices coordinating outsourcing activities are located throughout the globe.
- One of the original mottos of the company was "Levi's for Guys and Gals." The Gap began creating its own private label clothing in 1982 and had stopped carrying other labels altogether by 1991.
- The name came from the growing differences between children and adults, called "the generation gap", which reached its peak with the hippie movement.

"Fisherisms" -

- Fisher says in his self- published book that he came to see the entire planet as "a world full of potential Gap customers" and himself as a man with the rare entrepreneurial prowess to clothe them.
- "I just wanted to take the nightmare out of buying Levi's, to offer an easy and well-organized shopping experience that would appeal to a guy like me."
- "I viewed things with the eyes of a real estate man, not a retailer. I always looked for ways to get the most out of square footage, to go beyond the floor space. So I created a honeycomb of cubicles on the walls. . . . I had never seen this done before, but it seemed so logical, I wondered, why not?"

Industrial Organization -

- Contestable Markets - Gap began dominating the apparel market as a result of its ability to fill what it perceived as “gaps” before anyone else could enter.
- Economies of Scale - As an early entrant, Gap was able to take advantage of economies of scale within the industry.
- Economies of Scope - By expanding its market within the apparel industry, Gap was able to reduce its manufacturing costs.
- Product Differentiation - Increased sales have resulted primarily from the Gap’s ability to expand into specialty markets, i.e., Banana Republic, Old Navy, babyGap, etc.
- Vertical Integration - Although the Gap began by selling Levi’s exclusively, its ultimate growth and dominance began once it started to manufacture products under its own label. Vertical integration also allowed Gap to lower transaction costs and reduce supply threats created by Levi’s.
- Branding - The Gap’s multiple brands have become some of the most recognizable labels within the apparel industry.

Vertical Integration -

- Levi Strauss & Co.'s jeans gave birth to Gap, but that relationship grew rocky. In 1978, Fisher and Robert Haas traded unfriendly words in an argument focused on Levi's trademark.
- By that time, Gap had opened more than 300 stores and was selling its own, increasingly popular brand with the Gap label.
- Gap stopped selling Levi's in 1991, according to press accounts, though Fisher puts the year at 1992. These days, Gap Inc. has roughly four times the sales of Levi's. Gap has more than 3,000 store locations among its Gap, Old Navy and Banana Republic brands.
- Fisher portrayed Haas as saying: " 'We don't want to sell you product anymore. We're not making any deliveries after the first of December.' "

Vertical Integration, cont'd -

- "I had a suspicion that something big was up," Fisher recounts of the meeting. "(Haas) continued for about an hour, complementing (sic) our stores, and how we're the best at what we do. Then his tone suddenly changed."
- At the time, both companies said publicly that they agreed to the termination of their relationship, which to many industry observers seemed inevitable. Gap, with about \$2 billion in sales compared with Levi's \$5 billion at the time, had weaned itself gradually off Levi's sales in favor of its own Gap label.
- "I don't know if Bob realized what a great compliment he had paid us by cutting us off. We represented a lot of money to his company," Fisher writes. "Yet, he wanted to take away any advantage we might gain by our association with the number one brand in our category. I clearly understood how much he feared the Gap label as serious competition to the Levi brand."

Mergers and Acquisitions -

- **Banana Republic** - known for casual luxury, with high-quality apparel for men and women and sophisticated seasonal collections of accessories, shoes, personal care products, intimate apparel and gifts for the home.
- **Old Navy** - famous for the best in denim, graphic tees, cargos, Performance Fleece, plus the Old Navy Item of the Week — each and every week, a special item at a special price.
- **Forth & Towne** - a unique shopping experience and destination for women. Forth & Towne will offer fashionable apparel and accessories.
- In addition, Gap brands include babyGap, GapKids and Gap Maternity.

Strategies and Conduct -

- Overall corporate real estate strategy is focused on optimizing store fleet and more aggressively allocating square footage across all brands to better serve customers.
- Closures reflects underperformance and the company's determination that it was no longer financially beneficial to keep that store open. Information regarding individual store performance is not available.
- Stores are evaluated from a market perspective, and a closing is based on various criteria including how many stores are located in that market, where the stores are located and how the store is performing.
- As of fiscal 2004, Gap Inc. reports only store locations (not concepts), which the Gap feels is a more useful and clearly defined measure.

Growth / Shrinkage -

- As of Jan. 29, 2005, Gap Inc. operated 2,994 stores, compared with 3,022 stores last year. For fiscal 2005, the company expects to open about 170 store locations, weighted toward Old Navy, and close about 135 store locations, weighted toward Gap brand.
- Net square footage is expected to increase 2 percent for fiscal 2005.
- **2005 Expected Store Activity (As of April 21, 2005)**

	Expected Store Openings	Expected Store Closings	Expected Net Openings / (Closures)
Gap North America[^]	30	95	(65)
International[^]	20	5	15
Old Navy	75	25	50
Banana Republic	40	10	30
Forth & Towne	5	0	5
Gap Inc. Total	170	135	35

- * Gap North America includes Gap stores in the U.S. and Canada. International includes our stores in the U.K., France and Japan.

Critical Milestones -

- **1976** Gap goes public, offering 1.2 million shares of stock on the New York and Pacific stock exchanges.
- **1977** The Gap Foundation, Gap Inc.'s charitable arm, is established.
- **1983** Gap Inc. buys Banana Republic — then a two-store safari and travel clothing company with a thriving catalog business.
- **1986** GapKids opens its first store.
- **1987** Gap goes international, opening its first store outside the U.S. in London.
- **1990** babyGap is born.
- **1994** Gap Inc.'s newest brand — Old Navy — debuts. Gap Outlet opens its doors. GapScents is introduced in Gap stores.
- **1995** Millard Drexler is named CEO of Gap Inc. The first Banana Republic store outside the United States opens in Canada.

Critical Milestones, cont'd. -

- **1996** Banana Republic introduces gift and home accessories collections.
- **1997** Making shopping even easier for U.S. customers, Gap opens its Online Store at gap.com. Old Navy achieves \$1 billion in annual sales in less than four years of operation.
- **1998** GapKids and babyGap launch their Online Stores. Gap Inc. launches its formal ethics code, the [Code of Business Conduct](#).
- **1999** Banana Republic goes online at BananaRepublic.com.
- **2000** Gap delivers GapMaternity in an online-exclusive debut. Old Navy launches its Online Store at oldnavy.com.
- **2001** Old Navy makes its debut outside the U.S. — opens 12 stores in Canada.
- **2002** Paul Pressler named CEO of Gap Inc. Millard Drexler retires after 19 years of service.

Sweatshops...?

- In December of 1995 the Gap became the first major North American retailer to accept independent monitoring of the working conditions in a contract factory producing its garments.
- The Gap has received mounting criticism over working conditions in its factories. During the spring of 2003 The Gap, along with 21 other companies, was involved in a class action lawsuit filed by sweatshop workers in Saipan.
- The allegations included "off the clock" hours, where workers were not paid for working overtime, unsafe working conditions, and forced abortion policies.
- A settlement of 20 million dollars was reached but The Gap contends that the allegations were without merit, saying that lumping the companies together in one lawsuit was unfair.

Our Code of Vendor Conduct outlines eight categories of labor and operating standards. All new garment manufacturers must be pre-approved before orders are placed. Once approved, factories are monitored on an ongoing basis. The chart below illustrates the regional distribution and frequency of code violations documented by Gap Inc. VCOs in approved factories in 2003. ■

2003 Code Violations

REGION*	GREATER CHINA	NORTH ASIA	SOUTHEAST ASIA	INDIAN SUB-CONTINENT	PERSIAN GULF	NORTH AFRICA & MIDDLE EAST	SUB-SAHARAN AFRICA	EUROPE (INCLUDING RUSSIA)	U.S. & CANADA	MEXICO, CENTRAL AMERICA & THE CARIBBEAN	SOUTH AMERICA
No. of active factories	464	200	671	592	42	91	116	277	186	298	68
No. of factories reworked for compliance violations	42	1	42	31	6	1	4	9	0	0	0
GENERAL PRINCIPLE											
Lacks full compliance with local laws	■	■	■	■	■	■	■	■	■	■	■
Restricted access of Gap Inc. representatives	■	■	■	■	■	■	■	■	■	■	■
ENVIRONMENT											
Lack of environmental management system or plan	■	■	■	■	■	■	■	■	■	■	■
Insufficient notification procedures in case of environmental emergency	■	■	■	■	■	■	■	■	■	■	■
DISCRIMINATION**											
Employment	■	■	■	■	■	■	■	■	■	■	■
Wages & benefits	■	■	■	■	■	■	■	■	■	■	■
FORCED LABOR											
Use of any kind of involuntary labor, including prison labor, debt bondage or forced labor	■	■	■	■	■	■	■	■	■	■	■
For foreign contract workers, non-payment of agency recruitment fees and/or requiring workers to remain in employment against their will	■	■	■	■	■	■	■	■	■	■	■
CHILD LABOR											
Workers are not 14 years old or do not meet minimum legal age requirement	■	■	■	■	■	■	■	■	■	■	■
Not in full compliance with child labor laws	■	■	■	■	■	■	■	■	■	■	■
Failure to advise migrant workers to attend night classes and/or participate in educational programs	■	■	■	■	■	■	■	■	■	■	■
Poor age documentation	■	■	■	■	■	■	■	■	■	■	■
WAGES & HOURS											
Pay is below minimum wage	■	■	■	■	■	■	■	■	■	■	■
Overtime pay rates are below legal minimum	■	■	■	■	■	■	■	■	■	■	■
Work week in excess of 60 hours	■	■	■	■	■	■	■	■	■	■	■
Workers cannot refuse overtime without threat of penalty or punishment	■	■	■	■	■	■	■	■	■	■	■
Workers do not have at least 1 day off in 7	■	■	■	■	■	■	■	■	■	■	■
Violation of local laws on annual leave and/or holidays	■	■	■	■	■	■	■	■	■	■	■
Unclear wage statements	■	■	■	■	■	■	■	■	■	■	■

*For a list of countries in each region, please see the inside back cover of this report.

Our Program Today

GLOBAL COMPLIANCE EVOLUTION

YEAR	MILESTONE
1992	<ul style="list-style-type: none"> Gap Inc. develops Sourcing Guidelines outlining general labor standards for vendors to follow. Quality Assurance employees oversee this initiative.
1995	<ul style="list-style-type: none"> Labor conflict at Mandarin International factory in El Salvador (see Page 20) increases company's awareness of factory conditions and the need to ensure vendor commitment to Sourcing Guidelines.
1996	<ul style="list-style-type: none"> In the wake of Mandarin incident, Gap Inc. partners with three outside organizations to form the Independent Monitoring Working Group, which pioneers the industry's first independent monitoring program in El Salvador. Gap Inc. forms internal compliance organization, hiring first Vendor Compliance Officers, and begins to separate compliance from Quality Assurance function. Sourcing Guidelines replaced by comprehensive Code of Vendor Conduct.
1999	<ul style="list-style-type: none"> Gap Inc. is one of many apparel retailers named in Saipan lawsuit (see Page 9), an experience that highlights the need to refine and better articulate requirements for foreign contract garment workers. To further strengthen compliance function, Gap Inc. separates compliance from sourcing, establishing independent Global Compliance department reporting into company's Chief Administrative and Compliance Officer.
2000	<ul style="list-style-type: none"> Journalist alleges child labor violations at Cambodian garment factory. Gap Inc. requires additional age verification in that country (see Page 24). Gap Inc. becomes second corporate partner of Global Alliance as part of multiyear commitment to identify garment worker needs, develop training for workers and management and provide community-based services.
2001	<ul style="list-style-type: none"> Gap Inc. implements guidelines to help protect rights of foreign contract garment workers, including freedom to return to their home country (see Page 9).
2002	<ul style="list-style-type: none"> Gap Inc. supports formation of Public Reporting Working Group (see Page 28). Gap Inc. pilots program to rate factory compliance (see Page 16). Global Partnerships group formed within Global Compliance department to focus on stakeholder dialogue and engagement. Gap Inc. supports Cambodian Labor Training Coalition on an initiative to improve factory conditions and relations between workers and management (see Page 25).
2003	<ul style="list-style-type: none"> Gap Inc. strengthens external engagement by joining SAI's Corporate Involvement Program and the United Nations' Global Compact (in April 2004, Gap Inc. joined ETI).

More than 90 full-time employees work in Global Compliance. Most are Vendor Compliance Officers (VCOs) who work to improve labor conditions among the garment manufacturers that produce our apparel and operate approximately 3,000 garment factories in about 50 countries.

Most VCOs are from the region or country they oversee. They represent about 25 nationalities and speak as many languages. Some have worked in factories as managers or on the production line. Others have experience in education and government or with NGOs. Still others were local labor organizers or lawyers. We believe this diversity and localized approach greatly enhances the team's commitment and effectiveness. A profile of one of our VCOs, VannChhai Leng, is included with the Cambodia case study on Page 25. Other profiles can be found at gapinc.com.

OUR PROGRAM SCOPE

Headed by Dan Henkle, Vice President of Global Compliance, our Global Compliance department is separate from and independent of our sourcing organization and focuses on improving factory working conditions and labor standards.

While factory monitoring is an important part of our program, we know that it isn't enough to support sustainable change. Most garment manufacturers work with many customers. Our influence on a given manufacturer's practices is limited when we represent only a fraction of its production. So, in 2002, we initiated a strategy to collaborate with partners worldwide in an effort to foster longer-term solutions.

