Competitiveness and Corporate Social Responsibility

Laszlo Zsolnai

CSR PAPER 2.2006

DECEMBER 2006

CSRM – Corporate Social Responsibility and Sustainable Management

Laszlo Zsolnai, *Business Ethics Center, Corvinus University of Budapest*

The special issue on *Corporate Social Responsibility Papers: The potential to contribute to the implementation and integration of EU strategies (CORE)* collects a selection of papers presented at the Marie Curie Conference CORE organised by FEEM.

The CORE conferences Series addresses the question of the goals achievement of the EU strategies. The main EU strategies (Lisbon, Sustainability, Integration) can be successful if their implementation involves adequately and effectively the business sector, non-profit partnerships and networks, local communities and civil society. In this setting CSR holds the potential to stimulate corporate contributions to the implementation and integration of the mentioned EU strategies and can be tested as a policy tool.

This batch of papers has been presented at the first Core Conference: *The potential of CSR to support the implementation of the EU Lisbon Strategy.*

CORE is financed by the European Commission, Sixth Framework Programme and it is co-ordinated by Fondazione Eni Enrico Mattei (FEEM).

Further information is available at www.core-project.net

Conferences:

- **The potential of CSR to support the implementation of the EU Lisbon Strategy.**
- Milan, June 22-23, 2006
- **The potential of CSR to support the implementation of the EU Sustainability Strategy**
- Milan, June 14-15 , 2007
- **The potential of CSR to drive integration in an enlarged Europe**
- Nottingham, June19-20, 2008
- **The potential of CSR to support the integration of core EU strategies**
- Darmstadt, 15-16, 2009

Partners of the CORE network:

- Fondazione Eni Enrico Mattei, Milano, Italy
- Oeko Institut, Freiburg , Berlin, Darmstadt, Germany
- University of Nottingham, Nottingham, UK

Competitiveness and Corporate Social Responsibility

Summary

The paper addresses the problem of the relationship between competitiveness and CSR, and analyses the reasons why the opportunistic use of CSR is counter-productive. It attempts to establish how ethical behaviour can survive in highly competitive markets, and tries to find the new meaning of competitiveness in the light of CSR. The final section of the paper describes how a number of progressive, socially responsible firms have prospered in competitive environments by forming commitments among owners, managers and employees and by establishing trust relationships with customers and sub-contractors.

Keywords: Competitiveness, Corporate Social Responsibility

JEL classification: Z1

Keynote Presentation at the CORE First Conference: The potential of CSR to Support the Implementation of the EU Lisbon Strategy at Fondazione Eni Enrico Mattei, Milan, 22-23 June 2006.

Address for correspondence:

Laszlo Zsolnai
Professor and Director
Business Ethics Center
Corvinus University of Budapest
Veres Pálné 36H
H-1053 Budapest
Romania
E-mail: laszlo_zsolnai@interware.hu

Competitiveness and Corporate Social Responsibility

The paper addresses the following problems: (1) What is the relationship between competitiveness and CSR? (2) Why is the opportunistic use of CSR counter-productive? (3) How can ethical behavior survive in highly competitive markets? and (4) What is the new meaning of competitiveness in the light of CSR?

1. Competitiveness versus CSR

The responsible competitiveness approach developed by *The Copenhagen Centre* and *AccountAbility* and supported by the *Employment and Social Affairs DG* of the *European Commission* explores the conflict between competitiveness and corporate social responsibility. (Zadek, S. et al 2003)

Zadek and his colleagues state that there are inherent limitations to the “business case” that provides an economic rationale for companies to invest in improving their environmental and social performance. They say, “Some of the measures demanded of companies in the name of corporate responsibility are incompatible with current business models and markets. Pharmaceutical companies cannot alone provide affordable drugs to the poor, and the footwear companies cannot just decide to pay workers in Mexico or Vietnam a wage comparable to that earned by workers in London or New York. The challenge is not so much to ‘find’ profitable opportunities in today’s markets, as to create markets (in societies) that systematically reward responsible practices.” (Zadek, S. et al 2003: p. 1)

In the responsible competitiveness approach corporate responsibility is required to be consistent with and mutually reinforced by national and regional competitiveness strategies. “Business can compete effectively across the responsibility spectrum, spanning the investment in environmentally-friendly technology and raising productivity by improving their employees' work-life balance, through to cutting corners on environment and labor standards and engage in corrupt relationship with government." (Zadek, S. et al 2003: p. 2)

The conclusion is that

(i) Scaling up corporate responsibility can be more effectively achieved where it supports, and is supported by national and regional competitiveness strategies.

(ii) Public policy aiming to scale-up corporate responsibility practices should be established within broader competitiveness strategies.

(iii) Competitiveness strategies, similarly should reflect the potential for corporate responsibility to support 'responsible competitiveness'.

(iv) 'Corporate responsibility clusters' offer a pivotal mechanisms for scaling up corporate responsibility practices through their effective integration into national and regional competitiveness strategies. (Zadek, S. et al 2003: p. 3)

The basic problem with responsible competitiveness is that in this approach corporate responsibility is subordinated to and used as an instrument for economic competitiveness. Responsible competitiveness remains captured by the dogma of "Economic Man" which allows economic players to consider the interest of others only if it serves their own interest. But this self-interest based, opportunistic approach to ethics and corporate social responsibility fails.

2. Opportunistic CSR is counter-productive

Luk Bouckaert's criticism on the "Green Paper of the European Commission Promoting a European Framework for Corporate Social Responsibility" is relevant here. The Green Paper published in 2001 and its follow-up consultation process, put business ethics and corporate social responsibility (CSR) on the political agenda in Europe. It gives a regulative, political framework for an ethically driven economy, which goes beyond the logic of the social market economy. Though the dynamics of the social market economy rested on a clear separation between economic and social institutions operating in national boundaries, the new regulative structure is built on voluntary partnerships among business, government and civil society. (Bouckaert, L. 2002)

The Green Paper defines CSR as “a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis.” This definition contains the credo of business ethics, which can be summarized in three points: (i) the need to integrate the economic, social and environmental impact in all business operations to create sustainable economic growth, (ii) a focus on stakeholder management and manager's accountability to all the stakeholders, and (iii) a commitment to go over and above explicit legal requirements to respect the implicit social contract between business and society so that the firm’s “license to operate” goes with social responsibility to create sustainable value for all its stakeholders.

Many business leaders, policymakers and other stakeholders agree today on this definition of CSR because it is the expression of a long-term rational management perspective. It is a necessary condition to remaining a trustworthy company for investors, for highly skilled and competent employees, for potential partners in a joint venture and so on. It is part of good reputation and communication. So CSR has a rational and instrumental function in a set of accepted goals and objectives. The only remaining question is how to make it operational. A list of actions is proposed in the paper and in the follow-up documents, of which the most important may be the launching of a “Multi-stakeholder Forum” at the EU level. This forum has the aim of promoting transparency and convergence of all CSR practices and tools (ethical codes, audit systems, labels, participation schemes, etc.). Another important step is the integration of CSR into the other policies of the EU such as trade, development agreements, public procurement policies, public administration and so on.

By reducing ethics to a functional and instrumental management concept we lose something vital – argues Bouckaert. We are crowding out genuine moral feelings and genuine moral commitment, substituting them for rational and technocratic management tools. This substitution fails. Although business ethics took off in the late 1970s and has flourished for decades, ethics management has failed in recent times to overcome the new, more sophisticated and hidden forms of opportunism in business. It is important to understand the nature and limits of ethics management to prevent new irruptions of irresponsibility. We must be aware of the unavoidable paradox of ethics management.

The core idea of this paradox is the following: By creating new regulations to temper opportunistic behavior in and among organizations, we may temper the symptoms but often reinforce the underlying roots of opportunism. We introduce economic incentives like benefits, such as premiums or tax relief for those who respect the new regulations, but by doing this, we substitute economic calculations for moral feelings. Preaching moral concepts such as trust, responsibility or democracy based on calculative self-interest or as conditions of systemic functionality is ambiguous. It opens the door for suspicion and distrust because calculations and systemic conditions can easily be manipulated. When the fox preaches, guard your geese.

It is fascinating to see how trust, value-driven leadership and democratic stakeholding have become part of Western management theory. Bouckaert's point is that the more economic democracy can be sustained by a rational and economic discourse, the more it risks crowding out the spiritual and moral commitment, which is a necessary condition for sustaining genuine entrepreneurship and stakeholding. We must put forward not only the question of how to make business ethics operational, but also the question of how to make it genuinely ethical. (Bouckaert, L. 2002)

To promote corporate social responsibility on the basis of the pure economic logic of the market and to use it solely as an instrument for improving economic competitiveness is not a sufficient strategy to address the unsustainable and irresponsible growth strategies of today's business. (Zsolnai, L. 2003)

3. The Benefits of Social Responsible Behavior

Robert Frank's book "What Price the Moral High Ground?" represents a real breakthrough in business ethics literature because it treats ethics as an endogenous factor in economic life. (Frank, R. 2004) Moral considerations are not externally forced upon economic agents but internally chosen (or not chosen) by them.

Frank challenges the central view of our era that competitive pressure makes naïve to expect that people (and organizations) restrain themselves for the common good. Both economic theory and evolutionary theory suggest that human agents are willing to make sacrifices for the common good only if society confront them with significant penalties. Both on empirical and theoretical results Frank shows the emergence of pro-social behavior independently of external rewards and sanctions.

One of the main arguments developed by Frank is that people who are intrinsically motivated to adhere to ethical norms often prosper in competitive environments. It is a paradoxical phenomenon that people can often promote their own narrow ends more effectively by abandoning the direct pursuit of self-interest.

According to Frank there is a closer link between rationality and morality than many economists believe. A rational individual will often be unlikely to achieve his or her material ends if the moral emotions are missing from his or her character. An interesting corollary is that the ultimate victims of opportunistic behavior are often those people who practice it.

Frank also shows that socially responsible firms can survive in competitive environment because social responsibility can bring substantial benefits for firms. So it might be a good business to sacrifice in the name of ethical concerns.

Frank developed five distinct types of cases when socially responsible organizations are rewarded for the higher cost of caring. (Frank, R. 2004: p. 67)

(I) Opportunistic behavior can be avoided between owners and managers.

(II) Getting moral satisfaction employees are ready to work more for less salary.

(III) High quality new employees can be recruited.

(IV) Customers’ loyalty can be gained.

(V) The trust of sub-contractors can be established.

Caring organizations are rewarded for the higher costs of their social responsible behavior by their ability to form commitments among owners, managers and employees and to establish trust relationships with customers and sub-contractors.

Ernst Fehr and *Simon Gaechter* were able to demonstrate experimentally the virtuous circle between responsible behavior and positive stakeholder response. (Fehr, E. and Gaechter, S. 2000)

They designed a gift exchange game in which employer makes a wage offer with a stipulated desired level of effort from the worker. The worker may then choose an effort level, with costs to his or her rising in effort. The employer may fine the worker if his or her effort level is thought to be inadequate. The surplus from the interaction is the employer’s profits and the worker’s wage minus the cost of effort (and the fine, where applicable).

Self-regarding worker would choose the minimum feasible level of effort, and, anticipating this, the self-regarding employer would offer the minimum wage. But experimental subjects did not conform to this expectation. Employers made generous offers and workers’ effort levels were strongly conditioned on these offers. High wages were reciprocated by high levels of efforts.

4. Beyond Competition

The chance to improve the ethical quality of economic activities can only be taken if the motivation of the agents is genuinely ethical; that is, only if they want to realize ethical conduct for its own sake. Ethics could bring material benefits only for those individuals and companies who use it not to produce material gains.

Companies should fit into the ecological, social and cultural niche within which they are functioning. The most competitive companies are so unique in serving their stakeholders that their products and services have no substitutes, and they therefore have no real competitors at all.

Progressive companies like outdoor clothing company Patagonia, retail business firm Ishka, natural health care company Blackmores, skin care specialist Jurlique, and organic food company Whole Foods are good illustrations of doing successful business beyond competition. (Pozzi, D. 2006, Nocera, J. 2006)

Patagonia is an outdoor clothing company started by a group of climbers and surfers in the sixties. The company branched, from selling climbing equipment into clothing in the 1970s. Company founder Yvon Chouinard's vision of long-term sustainability and minimum impact on the environment has become a reality for Patagonia and its customers. This has been realized through producing quality clothing that outlasts fashion, and a business ethic, which values the environment and its employees over rapid growth and the bottom line.

Patagonia shows a strong commitment to the environment, donating a large percentage of the company's profits to environmental campaigns and an ongoing accountability to the environment, demonstrated by constant monitoring of the effects of its manufacturing. In 1996 the company shifted its entire cotton line to organically grown cotton: grown without the use of chemical pesticides, herbicides or defoliants. They say: “Given what we now know about conventional cotton, there is no going back regardless of the decision's impact on the company's sales or profit. It's an ethical choice we have made and hope other companies will follow.”

Acknowledging the impossibility of zero environmental impact, Patagonia also has a strong commitment to research into producing durable fabrics. They are at the forefront of technology, having been the first to introduce such fabrics as Capilene in 1985, Polyester fleece in 1977 and Post Consumer Recycled Polyester fleece in 1993. Durable fabrics, coupled with durable and versatile designs, ensures that Patagonia's customers mirror the company's own philosophy of reduced consumption.

Nor does the company compromise on the care for its employees. Heavily subsidized in-house and external child-care programs, available to women and men, a commitment to employee training and pleasant working facilities are deemed important to simultaneously provide for the employees and to retain valuable people for the business.

The company’s broad vision considers how Patagonia impacts on the environment, its employees and the community at large. The simplicity is their philosophy. They believe that “Going back to a simpler life based on living by sufficiency rather than excess is not a step backward. Rather, returning to a simpler way allows us to regain our dignity, puts us in touch with the land, and makes us value human contact again”.

A retail business that takes its business ethics seriously is Ishka: the chain of handcraft shops founded by Michael Sklovsky and which has been operating successfully for 25 years. His business follows Buddhist philosophy in which ethics play an important part.

Most of Ishka's products are manufactured in villages across 48 countries, including India, Thailand, Nepal and Indonesia. In villages greatly needed income is generated through Ishka buying locally crafted products. The purchasing of local handcrafts provides work for people in their own village.

Exporting arts and crafts is a way that families can break out of the poverty cycle. To become a crafts-person or artist can mean a well-paid profession for life. Ishka have direct dealings with most of the artisans from whom they purchase handcrafts. The company investigates the workshops of suppliers and examines the working conditions of the artisans. Moreover, Ishka ensure they do not deal in products of exploitation such as the popular 'Persian' rugs copied in Pakistan by children in slavery.

Another important ethical issue considered by Ishka is the use of environmental resources. Wherever possible, Ishka make use of recycled products; and the company is always aware of the need to preserve natural habitats. Ishka are also regularly involved with Amnesty International and Unicef, and have been acknowledged as Unicef's biggest Victorian fundraiser.

Natural health care company Blackmores extends its vision of drug free health care to encompass a more widespread respect for nature and the environment. Environmentalism has been a distictive feature of Blackmore's corporate philosophy as evidenced by its environmental committee. This committee enforces Blackmore's environmental policy, which is about “more than just recycling and pollution control; it means integrity, quality and pride, not only in the way the company's products are manufactured, but with everything with which the company is associated”. Blackmores is proud that its products are manufactured without causing suffering to animals, and that it features among the 'cruelty-free' list of beauty products promoted by animal welfare groups, proving that cosmetic safety can be achieved without the use of testing on animals.

Adelaide-based skin care specialist, Jurlique, has successfully integrated spirituality into its corporate philosophy. Built around the three principles of 'purity, care and integrity', the organization believes that incorporating these values into all aspects of the production process enhances the final product, and the well being of the company and its staff.

'Purity' is observed in Jurlique's practice of organically growing, at their Jurlique Herb Farm, 85% of the herbs the company requires. The company ensures that only natural, non-chemical, unpolluted, organically and bio-dynamically grown raw materials are used in its products. Care for the environment, for oneself and others forms the Jurlique philosophy. Staff are encouraged to embrace change, energize others, and break down barriers, and to be customer focused, responsible and accountable, to strive for excellence and to face reality.

Co-founder of Jurlique, Dr Jürgen Klein considers consumer education vital in helping the public to be aware of the processes involved in “natural cosmetics”. In line with this view, Jurlique offers open days at the farm and factory, cosmetic ingredient listings, education and seminars covering skin and health care, aromatherapy and herbal medicines.

American organic food company, Whole Foods is characterized with rapid expansion, double-digit growth and a business model that no competitor seems able to touch. Its stock has returned more than 2,700 percent since it went public in 1992. Wall Street analysts could not speak enough good things about Whole Foods. John Mackey, the co-founder of Whole Foods and his executive team make no bones about the fact that shareholders rank low on their list of priorities. They speak instead about the importance of keeping customers happy and employees engaged and sticking to the company’s core values. Mackey says that they consciously work for the common good rather than depending solely on the ‘invisible hand’ of the market to generate positive results for the society.

References

Bouckaert, L. 2002: *Humanity in Business*. Paper presented in the European Ethics Summit in August 29-30, 2002, in Brussels.

Fehr, E. and Gaechter, S. 2000: *Do Incentive Contracts Crowd Out Voluntary Cooperation?* CEPR Discussion Paper no. 3017. Centre for Economic Policy Research. London,

Frank, R. 2004: *What Price the Moral High Ground*? *Ethical Dilemmas in Competitive Environments.* Princeton University Press, 2004. Princeton and Oxford.

Nocera, John 2006: “The whole truth” International Herald Tribune July 15-16, 2006. p. 17.

Pozzi, D. 2006: Business Can Have Soul. Available at http://www.livingnow.com.au/soul/s1soulstories3.htm

Zadek, S. et al 2003: *Responsible Competitiveness. Corporate Responsibility Clusters in Action.* The Copenhagen Centre and AccountAbility, 2003. Copenhagen & London.

Zsolnai, L. 2003: “The Paradox of Business Ethics”, *European Business Forum*, Spring 2003, pp. 90-94.