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BUSINESS ETHICS

Best Practices in Corporate Social Responsibility

by Alison Kemper and Roger Martin

TABLE OF CONTENTS

Executive Summary

- Business leaders throughout the world are under increasing pressure to make socially responsible decisions comply with legal requirements and generate sufficient profits.
- Corporate social responsibility (CSR) decisions demand new skills: managers must understand not only the demanded of all firms, but also the opportunities they introduce.
- While the marketplace does not reward all good deeds, thoughtful strategies can increase the likelihood that their value while creating positive outcomes for society.
- In this essay, we review the complexity of the issue, the opportunities CSR presents, and one approach to id opportunities.

Managing in Complexity—Civil vs Strategic

As business has become increasingly global, the values and principles that guide managers are no longer local. from Canada and Indonesia are transformed by manufacturers in India and Brazil under contract to firms in the U and Germany. Social activists, investors, accountants, workers, politicians, environmentalists, regulators, and cus each and every location work to influence management's decisions. Normal business practices in one location ca objectionable to customers and investors in other areas, while labor and environmental principles in one region a protectionist to businesses in other regions.[1] Companies would like to do the right thing but seldom have reliable choose a direction or level of investment.

For most companies, CSR presents complex problems and great opportunities. CSR allows companies to engag sophisticated nonmarket strategies that can influence customers, regulators, and employees. It also can reveal fi weaknesses. There are no global laws. There is no single right way. Firms must distinguish the legitimate deman governments, assess the claims of diverse groups, and identify the significant problems they can best resolve.

What Works?

Many researchers have looked for the elusive factor that will turn a firm's good deeds into profits, searching in vai magic. The right answer to the question "Does doing result in doing well?" is "It depends." Firms that select a spe social or environmental opportunity consistent with their identity and strategy will reap rewards. Firms which make based on the most recent request for help or on a particular manager's enthusiasm will likely not.

The most critical factors in the success of any firm's CSR strategy are not about CSR. A successful CSR strategy basics. First, a firm must be viable in order to create an effective, valuable approach to society and the environme unlikely that a good CSR strategy will reverse bad business decisions. Second, firms must meet their legal and re commitments. Compliance is essential. Enron's ethics policies were widely admired, but the company was nevert violation of the law. Third, firms must meet basic expectations of their industry and the communities in which they company known for spilling toxic effluent is unlikely to make gains from sponsoring a children's sports team. This responsibility is illustrated in the CSR value curve IBM has described (Figure 1).

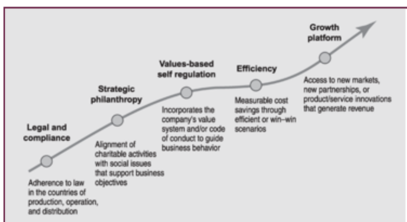

Figure 1. CSR value curve. (*Source*: IBM Institute for Business Value)

IBM recommends that firms ask their employees, suppliers, and customers what kind of CSR strategy would be c Engagement with these groups helps managers identify their best strategies in many settings. The IBM report su consulting these groups will also help identify good CSR strategies. This is consistent with recent economic theor the case for strategic approaches not only to financial gains, but also to social output.[2]

Meeting the demands of disparate social agents disperses the energy and creativity of the firm. Deliberate, strate maximize social effectiveness and firm opportunities.

The Role of Financial Firms

Financial institutions can choose to play another, powerful role: increasingly often, they determine whether new ir more social and environmental risks than potential economic benefits.[3] Good analysts will be able to see the way future growth prospects are enhanced or reduced by the social and environmental characteristics of the firms anc finance.

Financial analysts and investors now recognize that a firm's ability to work with indigenous people and their prope critical to the success of new mineral extraction projects. Corporate finance professionals in companies like Proct know that their sustainability principles must be factored into their investment decisions and growth forecasts.[4]

The special role of the financial industry is apparent in the appearance of two CSR codes focused solely on finan *Equator Principles* and *Principles for Responsible Investment* both offer guidance to finance professionals who ar projects of great potential value and risk. Financial professionals who identify a broader set of risks and rewards v effective.

Case Study

Thomas the Tank Engine Runs Off the Rails

The spring of 2007 was promising for the global toy industry. In early June 2007, RC2 (RCRC), the manufacturer Friends Wooden Railway Toys, was trading at over $45 per share, the highest level it had ever reached. Mattel's reached historic highs in spring 2007. In May, a trade journal announced that "China's coatings industry is benefi country's thriving consumer goods market, to which it supplies almost 4.5 M tonnes/y of paint… In the electronic a computerized toys segment, coatings suppliers will be hoping to tap the country's 290 M children."[5] Painted toys v segment of China's manufacturing sector, and the global demand for colorful, inexpensive toys seemed insatiable

In 2007, China's manufacturers accounted for approximately 80% of the world market for toys and employed mor million workers.[6] Their business depended on the tight ties in the value chain: the links between consumers, the b their personalities, the toy company giants, the Hong Kong brokers, and the Chinese manufacturers were close a

Everything changed in mid-June, when RC2 recalled 1.5 million Thomas toys that had been sprayed with lead pa share price dipped below $40 on the news. The markets began to discount other toy companies: Mattel dropped $26 in June, and eventually to $22. Hasbro went from historic highs of $32 in June 2007 to $28 for the remainder

The toys were pulled from shelves throughout Asia, the European Union, Canada, and Australia as well. It was no such recall: Of the 24 US recalls earlier in 2007, all were of Chinese manufacture. Once lead had been found in tl RC2's Thomas trains, parents, politicians, and retailers began to search through the toy aisles for more. By early had found it. Mattel recalled two batches of toys costing in excess of $30 million.

Chinese and US officials battled over the issue: were there enough safeguards on Chinese exports? Which gover fault?

The Hong Kong industrialists were devastated. Companies were banned from exporting goods. One toy manufac Shue Hung, committed suicide.[9] The industry was in disarray from shop floors in Guanyao to retail shelves in Tor

Good intentions had failed. In spite of all the safeguards, millions of lead-contaminated toys were sold to families world. Toy companies lost millions of dollars of capitalization. Cheung was dead. It was time to move up from goc effective action.

How Would *You* Have Responded?

Imagine that on September 1, 2007 you were one of the following:

- A financial analyst in New York focusing on the global toy industry;
- A banker reviewing loan applications for coating process machinery in Shanghai;
- Plant manager of a coating factory in Guanyao;
- Chief of manufacturing export regulations in Beijing;
- Regional manager of Toys“R”Us retail operations in California;
- Global brand manager of Thomas & Friends Wooden Railway Toys;
- Research director at Al Tawfeek, a leading provider of *shariah*-compliant investment funds.

From the perspective of the person whose position is most similar to yours, first list the strategic opportunities anc in the situation you face. Then consider these issues:

1. What do governments require? Do you need to ensure that these requirements are being met?
2. What do consumers and other groups expect of businesses in this situation? Does your work meet their ex
3. Where are the opportunities for a single firm or brand to gain advantage over its competitors? Can you ide harness them?
4. Where is there no likelihood of profit but a great likelihood of harm? Is this impossible to resolve by firms th profits? Can your organization contribute to a resolution?
5. From your professional standpoint, do you support a market solution based on competitive dynamics? Do y voluntary industry codes will work? Would you support increased regulation?

What are the issues here? Why did the Chinese toy debacle happen? Why did the incentives allow this to happer What can prevent its recurrence?

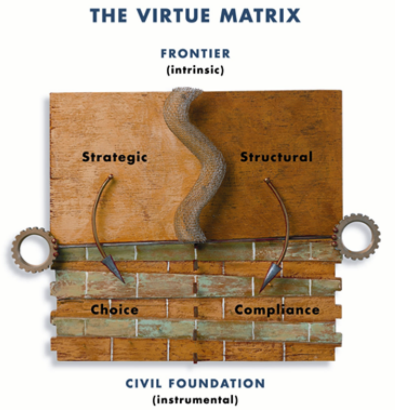

Figure 2. The virtue matrix

Making It Happen

The Virtue Matrix[10] as an Action Framework

By distinguishing four types of "virtue," companies can approach CSR effectively. When a firm recognizes the spe social activity demanded, it can respond optimally. Roger Martin's "virtue matrix" maps out these four kinds of virt which demands a different decision-making logic.

To identify and enact CSR strategies, a broad-based working group of managers can ask:

- *Compliance:* What are the firm's legal and regulatory requirements?
- *Choice:* Which codes of conduct and other expectations govern the choices of business in this context?
- *Strategic:* What problems can be tackled that will enhance the value, brand, or profits of a specific firm?
- *Structural:* What are the problems that no business can solve alone?

The best business opportunities lie in the area where a firm's unique resources and skills match social and envirc or needs. Competitive advantage does not emerge from compliance with the law, from tackling systemic issues s handedly, or from meeting the demands of civil society. Each of those must be addressed as distinct ways of doir

This need not be a mysterious process. Mapping the demands and opportunities requires environment scanning capacities that businesses use daily. IBM suggests asking employees and suppliers to make recommendations. I there are likely to be many more opportunities to do good than there is capacity

Having gathered a planning team and a list of options, a firm might then match each idea to a quadrant in the virt assign a priority

- Compliance issues are the most straightforward: Noncompliance is too risky for most businesses.

- Choice issues are more complex. What are the social norms? Are there any rankings or indices that give firm about their competitive position with regard to the issues? What kind of identity does the firm wish to project? afford?
- Structural issues demand the alignment of firms, governments, industries, and/or civil groupings. Each struct identified demands the formation of a working group or coalition. A firm can then ask if the potential benefit to warrants participation in such a group.
- Finally, strategic opportunities can be evaluated for their potential benefit to the reputation, position, or profits Their implementation can be assessed through the same processes as are used for other business strategie

By categorizing each type of CSR, a firm can make better decisions.

Notes

[1] Kline, 2005.

[2] Husted, B. W., and Jose De Jesus Salazar, "Taking Friedman seriously: Maximizing profits and social performa *of Management Studies* 43:1 (2006): 75–91.

[3] See the Equator Principles: www.equator-principles.com

[4] Procter & Gamble. "P&G 2007 Global Sustainability Report." Online at: www.pg.com/company/our_commitment/pdfs/gsr07_execsum.pdf

[5] "China has enormous potential in paint and coatings for cars, electronics and computerized toys." *ICIS Chemic* (May 21, 2007). Online at: www.icis.com/Articles/2007/05/18/4502632/China-has-enormous-potential-in-paint-and cars-electronics-and-computerised.html

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[7] Dee, Jonathan. "A toy maker's conscience." *New York Times* (December 23, 2007): magazine section. Online a www.nytimes.com/2007/12/23/magazine/23Mattel-t.html

[8] Chen, Shu-Ching Jean. "Subcontractor at heart of Fisher-Price toy recall is apparent suicide." Forbes.com (Aug Online at: www.forbes.com/2007/08/13/mattel-subcontractor-suicide-face-cx_jc_0813autofacescan02.html

[9] *Ibid.* 2007.

[10] Martin, Roger L. "The virtue matrix: Calculating the return on corporate responsibility." *Harvard Business Revi*
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Further reading

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