Corporate Responsibility and the Competitive Advantage of Nations

Tracey Swift & Simon Zadek
July 2002

The Copenhagen Centre

AccountAbility
institute of social and ethical accountability

Authors & Acknowledgments

This pamphlet is the product of a collaboration between The Copenhagen Centre and AccountAbility, and the authors are particularly grateful for the key contributions from Helle Dossing, Niels Højensgard and Jens-Erik Lund. Comments by Hannah Jones, Robert Madelin, Ed Mayo, Jan Noterdaeme, Nigel Twose and Kim Møller of Oxford Research are also greatly appreciated.

Dr Simon Zadek is the Chief Executive of AccountAbility. He sits on the Board or advisory groups of the Global Alliance for Workers and Communities, the World Bank's Business Partners for Development. The Copenhagen Centre, and the Nordic Partnership. He has until recently represented AccountAbility on the Steering Committee of the Global Reporting Initiative. He has been a Visiting Professor at the Copenhagen Business School and was previously the Development Director of the New Economics Foundation and Founding Chair of the Ethical Trading Initiative.

Tracey Swift is AccountAbility's Director of Research. She has published widely on corporate responsibility and related topics in academic journals such as Business Ethics: A European Review, European Accounting Review, and British Journal of Management. She joined AccountAbility in March 2002, from the University of Cambridge where she was Deputy Director of Sustainability Education in the Programme for Industry.

The Copenhagen Centre - New Partnerships for Social Responsibility (TCC) is an autonomous, international knowledge centre established by the Danish Government in 1998.

Focusing on social cohesion, TCC strives to promote voluntary partnerships between business, government and civil society in order to provide opportunities for the less privileged to be self-supporting, active and productive citizens. TCC serves as an intermediary for governments, businesses, social partners, NGOs and civil society organisations in developing forums for innovative activity and debate.

AccountAbility is the pre-eminent international, professional institute active in the field of social and ethical accountability. Its mission is to enhance social, ethical and overall organisational performance by developing and promoting effective tools and professional expertise, and by advocating an effective enabling environment for organisations to embrace the accountability dimensions of sustainable development.

Preface
Corporate Social Responsibility – Beyond Buzz Words

Today's global economy provides opportunities for increased international trade and thus for the creation of economic wealth. Equally, it raises new challenges in how best to develop trading relationships that deliver in support of the UN's Millennium goals of reducing poverty and ensuring greater environmental security.

This is the context in which 'corporate social responsibility' in its diverse forms has emerged as a key framework within which business operations are being re-examined and further developed. How does this tie in with the quest for competitiveness? Indeed, and beyond commonly "received opinions", the experience I gained through my current function as EU Trade Commissioner showed me that there is a positive link between social and environmental principles of behaviour of a company and its competitive advantages and performances.

Corporate social responsibility is one of the responses to the imbalances resulting from the acceleration of the globalisation process:

- Imbalance between the ever increasing pace of liberalisation (more pronounced for finance than for trade) and the time necessary to elaborate the international regulatory framework for these exchanges;

- Imbalance between the advanced governance systems in industrialised countries, who dispose of a highly sophisticated set of economic and social regulation, and the lack of such governance in developing countries as well as at international level.

- Imbalance between the highly developed economic pillars of global governance (IMP, World Bank, WTO) and the almost embryonic state of the social and environmental pillars of such a governance system.

Against this backdrop, voluntary social and environmental practices of business, going beyond companies' existing legal obligations, can play a major role in filling the governance gap in a creative and innovative way. CSR is thus not a substitute, but a complement to hard law. As such it must not be detrimental to public authorities' task to establish binding rules, at domestic and/or at international level, for the respect of certain minimum social and environmental standards. The focus of the debate in this respect has certainly moved on from a simple dichotomy between voluntary and binding instruments, towards the overarching challenge of devising reporting tools and verification mechanisms to ensure proper compliance with CSR commitments.

I think, however, that the societal benefits of CSR practices will remain limited unless they can be integrated into broader strategies, and public policies certainly have a role to play in this respect.

What role can Europe play in this respect? In early July, the European Commission adopted a policy paper, "Corporate social responsibility, a business contribution to sustainable development", suggesting, inter alia, the establishment of a "European Multistakeholder Forum" for all players (social partners, business networks, civil society, consumers and investors) to exchange best practices, to consider principles for codes of conduct and to seek consensus on objective evaluation methods and validation tools such as social and environmental labels. The strategy seeks to complement existing initiatives by companies themselves and by public organisations such as the OECD and the UN.

In my view, these discussions should explore the possibility of developing a European approach to CSR, which would complement the ones already developed at international level. Through centuries of economic development, European countries have developed a particular balance in their social contract between governments, citizens and markets. We need to reflect this balance also in our approach to CSR.

Until now, the debate has largely focused on what individual companies can do to enhance sustainable development goals. This pamphlet represents, I think, a significant step forward, by exploring some of the challenges, dilemmas and tensions surrounding the CSR debate and notably the link between CSR and the competitive advantage of nations, the role of partnerships between business, civil society and the public sector, and the contribution public policy could make to strengthening the links between corporate responsibility and competitiveness. I hope it will find the wide readership it deserves.

Pascal Lamy, Commissioner for Trade,
European Commission

Policy Challenges

Effectively addressing today's social and environmental challenges depends on the world's communities, nations and regions creating economic wealth in ways that are consistent with the tenets of sustainable development. This depends in turn on their ability to build development strategies based on *appropriate* forms of economic competitive advantage in globalising markets marked by ever-increasing competitive pressures. This challenge is illustrated by the strategic goal adopted at the Lisbon Summit in March 2000 for the European Community to become by 2010, "*the most competitive knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion*".

The European Commission's recent communication concerning 'corporate social responsibility' (CSR) seeks to establish how CSR can contribute to this strategic goal.[1] The Commission rightly frames CSR in the broader context of globalisation and the emerging debate about the role of business in society. The Commission's communication largely focuses on how best to encourage voluntary business activities and associated outcomes within an institutional framework of stakeholder dialogue. It therefore highlights the need to develop micro-level management skills, tools and standards.

The potential of a *significant macro-level* shift in the role of business in society remains to be adequately explored, as do its policy implications. In particular, there has been practically no consideration to date of whether CSR could shift the basis of a nation's economic competitive advantage.[2] CSR practitioners and analysts have been largely unconnected from, and uninformed about, the functioning of the broader competitive environment. The 'business case' for CSR has remained a fundamentally micro-affair.[3] Similarly, mainstream analysts and architects of the foundations for international competition have in the main ignored the possibility of a nation's economic competitive

1 European Commission (2002) Communication from the Commission Concerning Corporate Social Responsibility: A Business Contribution to Sustainable Development, Com (2002) 347 Final, European Commission, Brussels

2 'Nations' will in this document be taken to cover communities and regions.

3 J. Weiser and S. Zadek (2001) On-Going Conversations with Disbelievers, AccountAbility, London (www.accountability.org.uk).

advantage being grounded in the social and environmental performance characteristics of the business community itself.[4]

AccountAbility and The Copenhagen Centre have moved to close this gap by initiating an exploration of how shifts in the role of business in society might underpin new forms of international, economic competitive advantage. The intention at this stage has been to stimulate much-needed debate by setting out some of the issues, challenges and dilemmas for policy-makers from public bodies, business and civil society institutions. The initial work suggests that:

- Societal benefits from changes in the role of business in society will remain limited unless such changes support local, national and regional economic competitiveness strategies and outcomes.

- Such strategies and outcomes can and should be developed, and can be most effective if rooted in partnerships between business and civil society and public sector organisations.

- Public policy could productively strengthen the links between such partnerships and the competitive advantage of nations.

4 A notable exception to this has been the work of Michael Porter and others on 'inner city competitiveness': see for example M. Porter (1995), 'The Competitive Advantage of the Inner City' Harvard Business Review and P. Ramsden et al (2002) The Competitive Inner City, New Economics Foundation, London (www.neweconomics.org).

Competitive Paradoxes

The impact of globalisation on social and environmental outcomes is a topic that solicits varied and conflicting views. Just as many point to seeming gains from international investment and trade, so do others highlight the apparent downsides.[5] The relationship between economic growth and social and environmental outcomes has, similarly, long been hotly contested. Clearly the starkest issues concern the fate of over one billion people, mostly living in economically-poorer nations, who live on less than a US$1 per day.[6] Yet the paradoxes of economic growth are equally, if not more apparent in so-called developed countries. Economies traditionally thought of as 'Anglo-Saxon',[7] for example, are not only those that rate amongst the most competitive, but also lead the developed world in levels of economic inequity between their citizens.[8] In Europe as a whole, the significant economic growth of the last decades has been accompanied by growing inequalities rooted in an unequal access to work.[9] Indeed, the meaning of access to work is itself transforming, as teleworking, part-time and casual work portfolios become the norm. By the mid-nineties, for example, 25% of all UK jobs were part-time.[10]

There are growing calls on national, regional and international public institutions to reinvent public policy to provide the checks and balances required to guide how economic processes create social and environmental outcomes. The Lisbon declaration is a clear example where the European Community has acknowledged its responsibilities, and affirmed its commitment, to becoming the most competitive knowledge economy in the world whilst securing and nurturing social cohesion. The Government of South Africa has, in different words but a similar vein, clearly established policies and practices that are intended simultaneously to make the economy 'fit' for international competition, whilst driving through an explicit programme of black economic empowerment across the nation's labour and financial markets.

5 See for example, Weisbrot, M., D. Baker, E. Kraev and J. Chen (2001) The Scorecard of Globalisation 1980-2000, Centre for Economic and Policy Research, Washington DC.

6 World Employment Report 200: Life at Work in the Information Economy, ILO, 2001.

7 Notably Ireland, the UK and the USA.

8 Nelson, J., and S. Zadek (1999) Partnership Alchemy: New Social Partnerships in Europe, TCC, Copenhagen

9 Gray, J. (1998) False Dawn: the Delusions of Global Capitalism, p74.

10 World Employment Report 200: Life at Work in the Information Economy, ILO, 2001.

These national and regional policies are as much reflections of deeply-rooted tensions as they are manifestations of coherent strategies. Every aspect of publicly-funded, social welfare expenditure across Europe is challenged by the seeming imperative of creating lean economies. This, despite the fact that a knowledge-based economy can certainly breed inequality in a world where at least 15% of adults have only elementary literacy skills in 14 out of 20 OECD countries,[11] or in the UK where it is estimated that 25% of the population are unable to read or understand basic government documents.[12] Black empowerment initiatives by the Government of South Africa are criticised by some, accused of undermining the country's economic competitiveness and so, ultimately, the very basis on which black economic empowerment might be achieved. These criticisms are made despite the broad acceptance that social unrest arising from unequal development is a strong disincentive to potential inward investment.

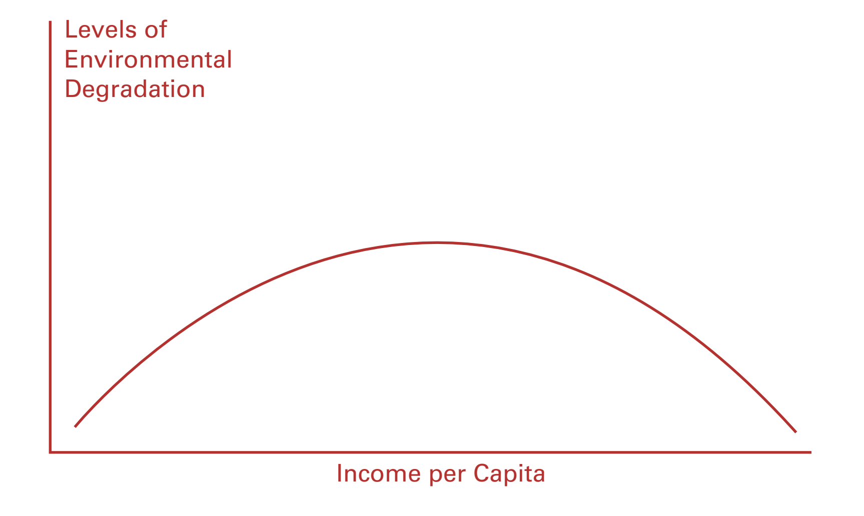
These policy tensions are reminiscent of the debate in the 1990s over the extent to which developing countries needed to 'catch up' with developed countries before addressing growing environmental problems. Those opposed to direct intervention to raise environmental standards based their arguments on the so-called *Environmental Kuznets Curve*. This inverted U-shaped curve suggested that pollution levels will only fall after a sufficient level of economic wealth had been created to enable countries to spend money on environmental protection (see Figure 1). The economist Francis Cairncross, for example, argued that, 'as poor countries grow richer – and trade is a powerful source of wealth – their environmental standards will rise'.[13]

11 Taking Literacy Seriously, UNESCO, 2001.

12 Ibid.

13 Zadek, S. (1995) "Dangerous Trading: Trade and Growth Pose a Threat to the Environment Unless Care is Taken", in New Economy Summer 1995: 142-146

Figure 1: Environmental Kuznets Curve



This application of the Kuznet's Curve has been recycled in the current policy debate about the apparent tension between social cohesion and economic competitiveness.[14] Those favouring unfettered free trade argue for letting economic growth rather than codes or regulation drive up labour standards and human rights. Whether right or wrong, the very real policy paradox clearly remains as to how to drive international economic competitiveness *in ways that secure the requisite social and environmental outcomes in the short as well as the longer-term.*

14 The continued currency of the Environmental Kuznet's Curve is apparent in that it provides the basis for the European Commission's most recent report on competitiveness analysis of 'sustainable development' and growth EC (2002) 2002 European Competitiveness Report, Commission Staff Working Paper [COM(2002) 262 final], EC, Brussels.

Conventional Wisdoms on Economic Competitiveness

The economic competitiveness of nations is traditionally judged using a variety of indicators of productive factors that demonstrate market flexibility, technological and organisational dynamism and innovation, and social and political stability. There are many indexes of competitiveness. Each has a different emphasis, but all in the main cover the same territory. The IMD, a leading European business school, for example, uses 314 criteria in creating its economic competitiveness ranking covering 49 countries (see Figure 2). These criteria are grouped into four broad areas: economic performance, government and business efficiency, and infrastructure.

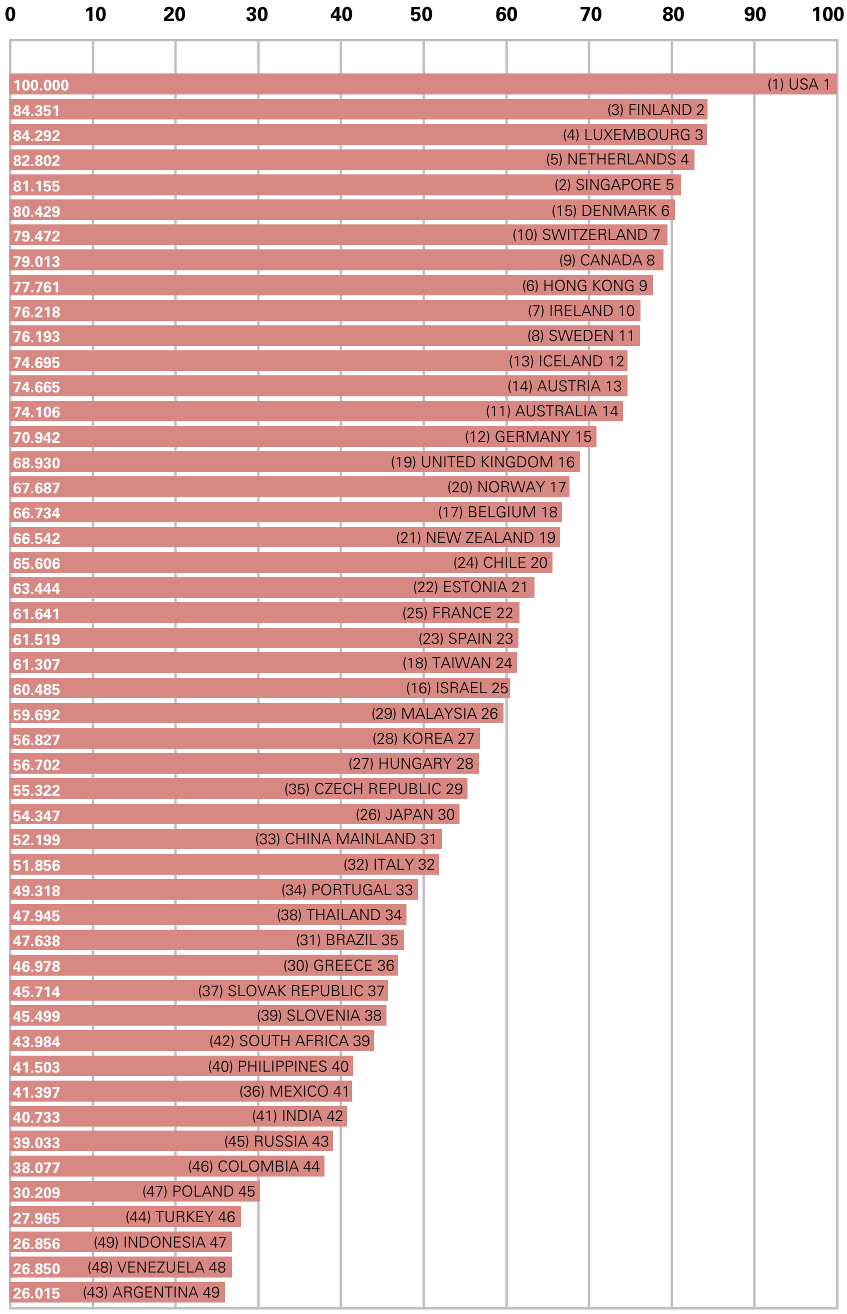
Corporate responsibility is not part of the IMD's analysis. However, many of the precepts of corporate responsibility are embodied in the IMD's handling of so-called 'soft' issues, such as 'values-in-society', and attitudes towards gender and other aspects of discrimination. Notable is that most of these issues are located within the IMD's fourth category, 'infrastructure', a simple indication that the IMD does not consider these to offer any direct contribution to business productivity.[15] Indeed, they are, in the main, not even seen as providing any *indirect* contribution to business and overall productivity in that these criteria are framed largely in the negative, i.e. scoring positively towards economic competitiveness if they do not constrain market flexibility or productivity. In some instances this borders on tautology. The criteria 'environmental laws', for example, is understood to mean "Environmental laws and compliance do not hinder the competitiveness of businesses".[16] There is, in short, little indication in the IMD approach of the view that responsible behaviour might contribute towards competitive advantage, for example through its positive impact on workforce motivation, innovation or brand recognition.

The World Economic Forum (WEF) has also contributed its thinking to the analysis of economic competitiveness. The WEF's competitiveness index is calculated using five categories of criteria and associated data: the country's level of GDP per capita in 1992; the Economic Creativity Index; the Finance Index; the International Index; and the Economic Crises Index. Although framed differently, the majority of the underlying criteria used in these five categories are broadly similar to those

15 Although some social aspects of economic competitiveness also appear in the third category, i.e. 'business efficiency'.

16 http://www02.imd.ch/wcy/criteria

Figure 2: The World Competitiveness Scoreboard 2002.[17]



(2001 rankings are in brackets)

17 IMD (2002) World Competitiveness Yearbook
http://www02.imd.ch/wcy/ranking

used by IMD. Not surprisingly, therefore, its Global Competitiveness Report provides a country competitiveness ranking strikingly similar to that of the IMD.[18]

The conventional wisdom about economic competitiveness, in short, treats societal issues in one or more of the following ways:

- *Inputs to business (often externally developed and delivered)*, rather than a part of business strategy and outcomes;

- *Enabling economic competitiveness* where they build human capital or other inputs at minimal cost;

- *Neutral (at best)* where they do not undermine market flexibility and the overall dynamics of the social economy.

These perspectives, whilst perhaps not wrong, are certainly incomplete. At the micro-level, emerging corporate responsibility practices suggest that broader social and environmental outcomes are increasingly intertwined with businesses' financial performance. What is less clear, however, is how these emerging practices relate, if at all, to the broader process by which economic competitiveness is formed and sustained.

18 WEF (2002) Global Competitiveness Report (http://www.weforum.org/pdf/gcr)

Corporate Responsibility

The role of business in society is a hot topic amongst public policy makers, NGOs, trade unions and the business community itself. Increasing numbers of corporations are expressing the aspiration of addressing the 'triple bottom line' in their policies, strategies and practices. This growing business group has mainly been led by global corporations with retail premium brands. More recently, this group has been joined by increasing numbers of hitherto less visible corporations that have been directly or indirectly impacted, often negatively, by rising public concern and anger.

The changing role of business in society has come to mean many things. Corporate sustainability, corporate social responsibility, and corporate citizenship are but a few of the new terms that have emerged to describe this period and process of challenge and change. There is, however, an emerging consensus that the scope of the challenge is not confined to philanthropic activities, and moreover extends beyond the more obvious legal responsibilities to include for example labour standards in supplier factories, the accessibility by poor people to life-saving drugs, and the basis by which and transparency of how management decisions are made[19] (See Figure 3 for examples).

Figure 3: Dimensions of Corporate Responsibility

- Human rights
- Working conditions
- Equality and diversity
- Consumer protection
- Environment and health impacts
- Economic development
- Ethical business practices
- Lobbying and political influence
- Businesses' role in conflict zones

The shifting role of business in society does, however, have a complex relationship to the matter of law. The European Commission, for example, has identified 'CSR' as where companies "*integrate social and*

19 The new Global Reporting Initiative Sustainability Reporting Guidelines illustrate just how broad the scope has become. (www.globalreporting.org).

environmental concerns in their business operations and in their interaction with their stakeholders on a ***voluntary basis****".*[20] This rightly reflects the perspective that compliance with the law is a given in terms of responsible behaviour. At the same time, it is equally clear that the matter of what constitutes appropriate law governing business behaviour is within the scope of the field of corporate responsibility. The ongoing debate in Europe and elsewhere about voluntary versus regulated social reporting and labelling is a case in point, as are the topics of the regulatory role concerning pension fund policy disclosure and corporations' foreign direct liability.

This pamphlet has adopted the more general term 'corporate responsibility' to cover the topic of why, when and how business can, should and does consciously address social, environmental and economic (including financial) dimensions of its performance and impact. Consistent with the Commission's definition of CSR, 'corporate responsibility' clearly focuses on where businesses have real options and therefore choices to make and justify to their stakeholders. Beyond this, however, 'corporate responsibility' covers the environmental and economic, and embraces the business community's powerful role in shaping public policy and regulations, as well as its relationship to existing law where public institutions are unable to enforce straightforward compliance.[21]

20 European Commission (2002): 5 (emboldened for emphasis)
21 Which we would take to particularly concern the international dimensions of corporate responsibility.

Corporate Responsibility & Economic Competitiveness

Corporate responsibility in its multitude of different forms will continue to face challenges as it moves beyond the margins of business activity and enters the mainstream realm of public debate and policy. And rightly so. The evidence to date that it makes a significant and lasting contribution in addressing poverty and inequality is, to say the least, weak. Certainly, there are many examples of positive social outcomes from businesses' good deeds.[22] But these do not add up to a macro effect.

Key questions need to be addressed in understanding the potential benefits and pitfalls in using corporate responsibility to meet wider societal goals:

- Can corporate responsibility be scaled-up beyond the level of individual businesses in order to make a real difference as a productive factor in economic competitiveness?

- What is the relationship between corporate responsibility and main stream public policies in addressing poverty and inequality, many of which focus on strengthening the underlying economic development process?

- Might corporate responsibility be, as some would claim, part of the problem for smaller businesses and economically weaker communities? It is in this context that the relationship between corporate responsibility and economic competitiveness becomes so important. Yet this relationship has hardly been imagined to date, let alone systematically explored. Figure 4 highlights the under-explained relationships between public policy, economic competitiveness, corporate responsibility strategies and practices and social outcomes.

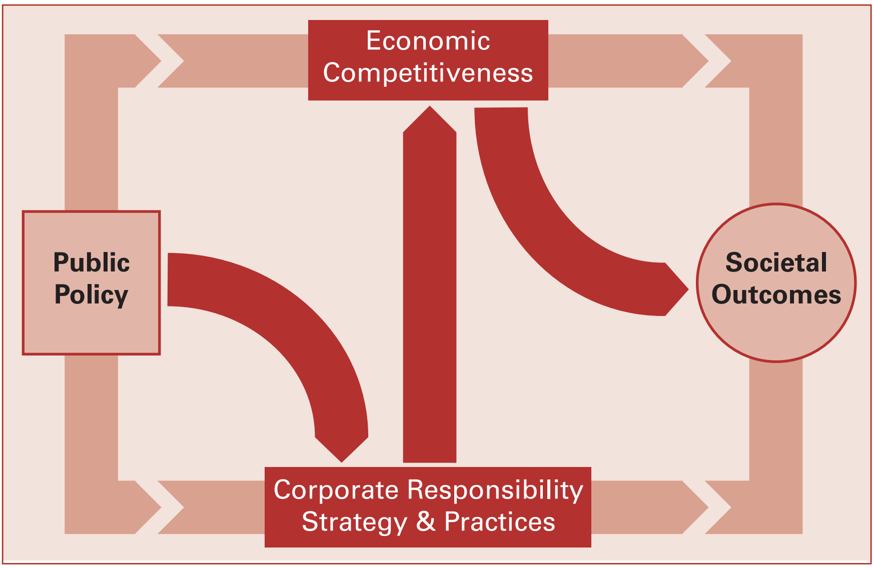
In examining these questions, AccountAbility and The Copenhagen Centre have identified several strands of thoughts that have a bearing on this emerging debate.

- Is being good for business good enough?
- If it's good for business, is it good for the economy?
- Is corporate responsibility good for all business?
- How does corporate responsibility impact on trade opportunities?
- How does corporate responsibility relate to market flexibility?

22 See for example the annual Business in the Community Awards (www.bitc.org.uk).

- Can corporate responsibility underpin the development of competitive clusters?

Figure 4: The Core Policy Question



None of these *alone* can answer the central question of whether and how corporate responsibility might impact on and underpin economic competitive advantage in ways that facilitate economic wealth creation and greater social inclusion. Individually and collectively, however, they throw light on some of the key dynamics that need to be better explored, understood and, where appropriate, guided. In focusing on these dynamics, it becomes possible to move beyond the consideration of direct impacts of corporate responsibility on societal outcomes that, whilst important, are likely to be dwarfed by the broader, indirect, impacts.[23]

23 That can be analysed through more straightforward social impact analysis.

'Can Good For Business Be Good Enough?'

The business case for 'doing good' is the holy grail of the corporate responsibility movement. In fact, the view that 'win-wins' exist that allow profit to be made from doing good is the movement's single most important proposition about the way business and markets do, *or at least might*, work. There is a proliferation of work going on to research, test, and prove the proposition. And the evidence does seem to suggest that money can be made by doing all manner of good things, from increasing employee volunteering to backing mandatory disclosure of social and environmental performance data.[24]

But rhetoric on the 'business case' has without doubt outstripped understanding, let alone practice.[25] Most businesses active in driving forward visible approaches to corporate responsibility are focused primarily on avoiding short-term reputation-related risks, making very small expenditures as an extension of their traditional corporate philanthropy, or merely re-branding good business practices (e.g. engaged and sensitive human resources management). These practices should be welcomed, since they can and do make a difference to people's lives and might support overall good business performance. But these are not the substance of meaningful shifts in the basis on which a nation's competitive advantage can be built and sustained.

A growing number of companies are seeking to go beyond this low-level business case to the 'second generation' of corporate responsibility (see Figure 5 below). For these companies, corporate responsibility is becoming more closely integrated into key aspects of their business strategy and practice. Corporate responsibility, for example, is becoming important for companies seeking to recruit and retain people with the best talents who will increasingly discriminate between potential employers with better social credentials. Financial analysts are more

24 For a discussion of these arguments, see J. Weiser and S. Zadek (2001) Conversations with Disbelievers: Persuading Companies to Address Social Challenges, Brody Weiser Burns and the Ford Foundation, New York. Also see AccountAbility's new 'Conversations with Disbelievers Initiative' in association with The Centre for Corporate Citizenship at Boston College (www.conversations-with-disbelievers.net).

25 Zadek, S. (2002) 'Exploring the Business Case', in Ethical Corporation, May 2002: 9, 33

willing than before to factor in a company's ability to handle the intangibles that drive business success. Successful business strategies, from pharmaceuticals to toys, are expected to be grounded in a clear understanding of society's changing demands, both now and in the future.

Figure 5: Generations of Corporate Responsibility[26]

	Tools & Processes
3rd Generation Remolding Competitive Advantage	Multi-stakeholder standards and partnerships, institution building, CR-oriented advocacy and public policy.
2nd Generation Strategic Corporate Responsibility	Product and process innovation, new business and corporate governance models, long-term sustainability.
1st Generation Low-Level Business Case	Philanthropy, short-term risk management, industry standards.
Legal Compliance	Regulation covering tax, health and safety, workers rights, consumer rights, environmental regulations.

It remains uncertain as to whether these 'second generation' companies will deliver qualitatively different business models and outcomes. It is too early to see what are the real implications of BP's commitment to go 'beyond petroleum', or the Ford Motor Corporation's vision of being a provider of mobility. But even if these visionary statements prove accurate, the successful transformation of one company, however large, cannot by itself shift the basis of a nation's competitive economic advantage. Such a quantum shift requires that corporate responsibility moves beyond the exceptional behaviour of individual companies.

26 Adapted from S Zadek, M. Fostater and P. Raynard (2002) Social Development and the Role of the Private Sector: Corporate Social Responsibility, Unpublished Working Paper, United Nations Department for Economics and Social Affairs: Division for Social Policy and Development, New York.

This is not a matter of driving 'compliance' with acceptable responsibility standards (although compliance may prove to be one element in an overall strategy). It is more a matter of making corporate responsibility a pervasive resource base and opportunity on which many businesses strategies and practices can be based.

This challenge has been referred to elsewhere as the 'third generation' of corporate responsibility. At this stage, public policy objectives are addressed by moving beyond individual company initiatives and driving the underlying principles of corporate responsibility into the very fabric of the economy.[27] The challenge is, of course, how to move beyond the simple business-case and make this third generation a reality.

'If It's Good For Business, Is It Good For The Economy?'

The simplest argument that links micro-level corporate responsibility practices with macroeconomics (albeit indirectly) is the view that 'if corporate responsibility is good for business, then it must be good for the economy'. Reminiscent of the old adage, 'what's good for General Motors must be good for the US', this perspective is all too often put forward corporate as a *sine qua non* of corporate responsibility.

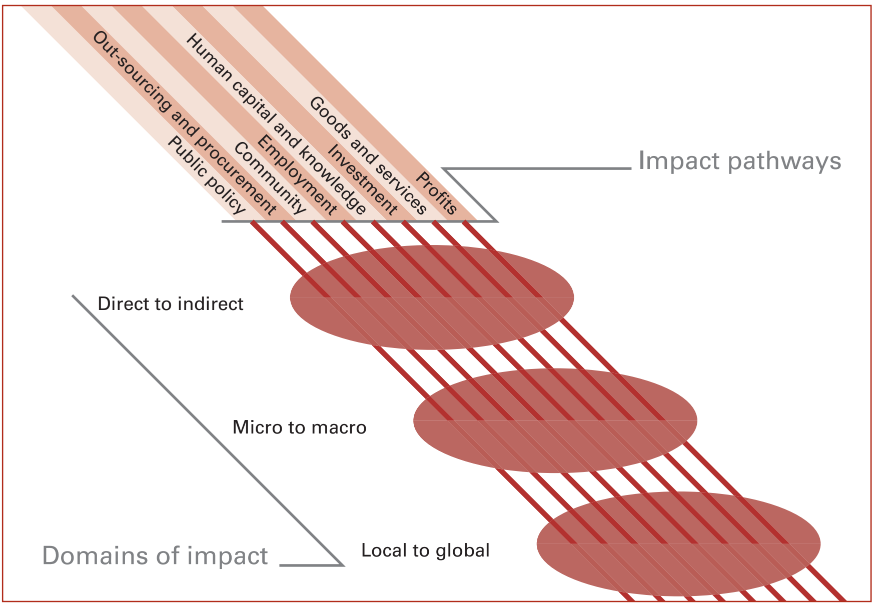
Clearly there are many instances where it *can* benefit the broader economy for a business to enhance its performance on the back of corporate responsibility practices. Increased employment, taxes paid, and spend on domestic supply chains are but a few of the channels through which business success can positively impact the broader economy within which it operates.

At the same time, there are equally convincing arguments that what is financially good for one company may not be good for a particular economy. The continued commitment by Levi Strauss to be responsible in its sourcing strengthens its financial performance by protecting its reputation, but may not be good for the US economy if it is linked to a shift of production out of the US into Asia. Similarly, a progressive approach by a telecommunications company to the 'global divide' may enhance its reputation, but might be bad for the economy within which it operates if it is part of its strategy for securing high prices to its business customers.

27 Zadek, S. (2001b) Third Generation Corporate Citizenship: Public Policy and Business in Society, London, Foreign Policy Centre in association with AccountAbility, London (www.accountability.org.uk).

Figure 6 illustrates this need to understand key direct and indirect economic impacts across micro and macro, local and global levels.

Figure 6: Economic Impact Pathways[28]



We can be confident that corporate responsibility practices that damage financial performance are unlikely to support any economy, and that enhanced financial performance is likely to directly benefit the economy within which a business operates. But indirect effects are crucial, both positively and negatively and we cannot assume what form they will take. We can conclude that positive financial performance is therefore necessary, but not sufficient, in enhancing the impact of corporate responsibility practices on a nation's economic competitiveness.

Can Corporate Responsibility Be Good For All Business?

Global corporations have dominated the corporate responsibility headlines, both in terms of challenges against them, and visible good practices. There are good reasons for this. Global corporations deeply penetrate the political economy of both developing countries and super-powers. Their investments underpin the capital base of many emerging economies, and their donations have until now been essen-

28 S. Zadek and C. Tuppen (2001) Adding Values: the Economics of Sustainable Business, BT Occasional Paper, BT, London

tial to ever-more-costly political campaigns. Global corporations have the broadest reach and impact on the largest number of people, through their supply chains, research and development activities, investments, pricing policies and tax payments. These business institutions are crucial because they will shape tomorrow's markets and set the stage for the rules and norms for the entire business community.

This focus on the responsibility of global corporations has, however raised concerns as to the implications for small and medium-sized enterprises (SMEs). SMEs are clearly the engine-room of economic wealth generation in every economy across the world, not least developing countries. The concern for some is that SMEs might be competitively disadvantaged if corporate responsibility primarily benefits larger corporations. Such a disadvantage might occur if corporate responsibility practices give large corporations a competitive edge in lowering their cost of capital, consolidating their brands and reputation, or enhancing their position in the market for labour and talent. Furthermore, 'business-to-business' SMEs can face additional costs where their corporate customers adopt new social and environmental policies, using their market muscle to externalise associated costs into their supply chains.

Whether a bias exists that benefits larger corporations is both an empirical and a strategic question. Many argue that SMEs' roots within communities makes them almost inherently 'responsible' because of the mutual dependency that exists between them and the people they employ and serve.[29] Yet the most visible approaches to corporate responsibility today are increasingly formalised and validated through the application of costly standards. Moves to implement these more generally, for example through 'level-playing field' regulatory processes, could seriously disadvantage SMEs.[30]

A nation's economic competitive advantage has many possible sources. For some, particularly poorer developing countries, competitive advantage is often rooted in the (actual and potential) strength of its SMEs, if only because few have large corporations. If indeed a bias exists in which

29 Raynard, P & M. Forstater (2002) Corporate Responsibility: Implications for Small and Medium Enterprises in Developing Countries, UNIDO, Vienna

30 Utting, P. (2000) Business Responsibility for Sustainable Development, UNRISD, Geneva

types of companies tend to benefit most from corporate responsibility, there is the real possibility that some nations will benefit more than others as a result, and indeed some might actually suffer in economic terms.

How Does Corporate Responsibility Impact On Trade Opportunities?
A broader question concerns the impact of corporate responsibility practices on international trade. Advocates of trade liberalisation in support of export-led development have voiced concern at the potential for corporate responsibility to create non-tariff barriers to trade, disadvantaging nations that are unable to meet social and environmental process standards in the market. Unlike regulatory barriers that can be challenged under current World Trade Organisation (WTO) rules, these barriers (if they existed) would be non-statutory, created by the media power of NGOs, and in time happily reinforced by corporate advertising as a means of consolidating their premium brands.

Such concerns must be balanced by the potential for corporate responsibility to become a conscious basis for evolving a nation's competitive trading advantage. The South African wine-industry, for example, has invested in responding to European consumer demands for improved standards for farm labour. This investment will certainly place them well in facing cheaper competition, or in confronting potential erosion of their markets to suppliers that do not have to overcome historical legacies comparable to apartheid. Countries basing their economic advantage on cheap labour now find their exporters subject to increasing scrutiny by private social auditors commissioned by premium brand buyers. This has raised the possibility that public policy focused on securing labour standards could act to strengthen competitive advantage by simultaneously reducing audit-related costs and reputation-related risks of potential international customers.

There are major challenges raised by these two related issues. First is the possible bias of corporate responsibility-related business gains to larger companies. Second is the potential for corporate responsibility to confer relatively more benefits to those nations that can extract an 'intangible' premium for their products, often based on how they are produced. From an international trade and development perspective, these two related issues are critical in forming a view as to the potential positive and negative aspects of corporate responsibility.

How Does Corporate Responsibility Relate To Market Flexibility?

Free market proponents have long argued that the best way to overcome poverty is to liberalise markets, thus unleashing the dynamism of capital effectively applied by profit-seeking business entrepreneurs. From this camp has emerged a potentially significant critique of corporate responsibility, best represented by the work of the ex-OECD Chief Economist, David Henderson.[31] Henderson argues that societal ills are best addressed through liberal markets in which the remit of business is to make profit and where the role of government is the redistribution of wealth through the collection of taxes and provision of public services. He argues that in voluntarily accepting responsibility for broader social and environmental outcomes, business incurs significant costs, which in turn hampers the effectiveness of markets, reducing the potential for wealth creation that could otherwise alleviate poverty and social inequality.

Demonstrating the many business cases for corporate responsibility goes some way to undermining this argument. However, most business cases are still rooted in first generation, short-term reputational and financial benefits. It remains plausible that a company could find it profitable in the short-run to embrace aspects of corporate responsibility practices, whilst still suffering as a result from reduced competitiveness in the longer-term. Some would argue, for example, that the demise of Ben & Jerry's and the poor financial performance of The Body Shop were intimately related to their 'misguided' focus on aspects of corporate responsibility that over time eroded their competitive thrust. There is little doubt that the efforts of companies such as Nike to improve labour standards in global supply chains cost real money that is not directly recovered through increased sales and profits. Addressing labour standards thoroughly does not automatically bring its' just rewards! Reduced reputational risk, although real, does little to level the cost-based playing field with what John Elkington calls the 'stealth companies' – organisations that remain under the radar of public scrutiny whilst investing little or nothing in progressive change.

The very notion of market flexibility has become so ideologically charged that some advocates of progressive corporate behaviour reject it outright as a worthy challenge. This is a mistake, and potentially a lethal one.

31 Henderson, D. (2002) Misguided Virtues: False Notions of Corporate Social Responsibility, Institute of Economic Affairs, London (www.iea.org.uk).

Economic competitiveness certainly needs a dynamic and enterprising business community. This is nurtured and enabled in large part by markets that encourage and reward innovation, minimise unnecessary costs, and allow business to focus on the challenges of securing viability and success. The desire for corporate responsibility must go hand in hand with the need for appropriate flexible markets. There is therefore clearly a challenge in ensuring that corporate responsibility practices do not damage the dynamism of the broader economy by becoming, for example, overly bureaucratic.

Corporate Responsibility Clusters As Drivers Of Competitive Advantage

The initial research by AccountAbility and The Copenhagen Centre suggests that the dynamic, relational aspects of corporate responsibility practices may well provide the key to understanding its links to a nation's economic competitive advantage, and so its ability to provide significant support in addressing public policy goals. This resonates with the idea of 'clustering' as a basis for analysing economic processes that has gained considerable credence amongst economists and business leaders alike since it was first put forward by Michael Porter of Harvard University.[32] The term cluster refers to collectives of organisations that are not only linked through buyer-seller relationships, but through a broader set of interactions. These connections allow for a collective, but self-organising development process across the business community.

In terms of corporate responsibility, common issues such as labour integration, social investment strategies, lifelong learning for the workforce, gender and ethnic minority representation and participation in decision-making face all industries and sectors in varying degrees. They are likely to have the same stakeholder groups in common and by working with them in collaboration, groups of businesses can significantly and collectively address issues that are of pressing importance to local and regional communities and the wider array of societal interest groups. Similarly, in terms of environmental stewardship, clusters of businesses are likely to be drawing upon the same pool of finite resources and be subject to the same pressures to demonstrate responsibility, be affected by the same regulation, be levied by the same taxes and be subject to the same public policy environment.

32 Porter, M. (1990) The Competitive Advantage of Nations, MacMillan, Hampshire

The idea of 'corporate responsibility clustering' takes the model of synergies between competing companies to an altogether different level, and into largely unexplored territory. It may be, for example, that companies based in countries with unusually intensive NGO climates, such as the UK, become more knowledgeable about civil society, more able to handle NGOs around the world, more effective in managing reputation, and even more dynamic in identifying new product and process opportunities associated with social and environmental dimensions of performance. It is very likely that companies that have invested in partnerships with NGOs, trade unions and public bodies in addressing anything from 'conflict diamonds' to bribery to labour standards will be more competent in identifying and building profitable business partnerships.[33] Service providers from auditors to PR advisors will build specialised skills and networks in the field of corporate responsibility, which can be a source of international business opportunities in the future. Public bodies that learn to thrive in environments where corporate responsibility practices are more visible and debated are perhaps more likely to develop productive relationships with the business community. Such governments that are also active on the international stage, moreover, will tend to promote corporate responsibility in international markets, thus providing an additional foundation for such practices to underpin their own business community's competitive advantage.

'Corporate responsibility clustering' is a multi-faceted affair. It extends beyond the business community, and can include relationships as diverse as partnerships and law-breaking confrontations. The over-arching competitive advantage that such clustering might deliver is rooted in many possible learning mechanisms and processes, ranging from viral forms (e.g. NGO campaigns spreading across sectors) through to antibiotic variants (e.g. companies investing in learning and change to prevent potential problems in the future). From this perspective, NGOs can and do provide an extraordinarily cost-effective consultancy service to business, accelerating their learning, sensitising them to new issues, and creating more responsive, agile organisational cultures.

Corporate responsibility will support social inclusion at national and regional levels if we can move it beyond ad-hoc initiatives and stand-alone business cases. The dimensions described above provide food for thought, and some signposts to guide much-needed exploration of the facts of the matter.

33 Zadek, S. (2002) Working with Multilaterals, Business for Social Responsibility, San Francisco (www.bsr.org).

The Next Steps

The point of corporate responsibility for public policy is to enable social and environmental challenges to be more effectively addressed. That it is hopefully good for business is no more or less than the means to this end. Governments, NGOs and trade unions should assess corporate responsibility from this perspective. Indeed, businesses should also apply this litmus test. For if corporate responsibility fails in this basic aim, its financial return to the business community will be undermined as its stakeholders' frustration, disappointment and ultimately cynicism, take hold.

A little is not enough. Corporate responsibility will have no future unless it is clearly part of a broader process through which the more daunting social and environmental challenges are effectively addressed. That does not mean that business has to do everything, which is clearly as ridiculous as viewing the role of business as being merely to make a profit. But it does mean that corporate responsibility has to be a credible, significant and consistent element of strategies to alleviate poverty, overcome unacceptable forms of inequality and achieve environmental security.

Economic wealth creation is clearly a key element of any such strategy. Corporate responsibility must therefore at least be consistent with the process by which nations secure their economic competitiveness. Better still, of course, is if responsible business practices, designed and implemented together with Governments and civil society organisations, can help in remoulding the basis on which economic competitive advantage is achieved.

The jury is out. We have outlined some of the key ways in which corporate responsibility relates to social cohesion and economic competitiveness. Clearly there is powerful potential for corporate responsibility to make a positive contribution to addressing the needs of disadvantaged communities. Equally, however, there are ways in which corporate responsibility could, whether by mistake or design, damage the same communities.

The public policy challenge is, of course, not to *discover* but to *create* the relationship between corporate responsibility, social inclusion and economic competitiveness. The work by AccountAbility and The Copenhagen Centre is designed to help in doing just that. One starting point is clearly the challenge facing the European Community in addressing the Lisbon Summit Declaration of sustaining and growing international competitiveness together with social cohesion. But the challenge underlying the work programme of AccountAbility and The Copenhagen Centre aims to contribute to a more international agenda that spans the public interests from Beijing to Johannesburg to Sao Paulo. This public interest concerns how best to mould the basis on which business can compete and prosper in ways that benefit society. This in turn ultimately requires that the basis on which nations compete are underpinned by responsible business practices.

Designed & Typeset by Ethical Media
www.ethicalmedia.com

"Until now, debate has largely focused on what individual companies can do to enhance sustainable development goals. This pamphlet represents a significant step forward by exploring the link between CSR and the competitive advantage of nations, and the contribution public policy could make to strengthening this link".
Pascal Lamy, Commissioner for Trade,
European Commission

Effectively addressing today's social and environmental challenges depends on our ability to create economic wealth in ways that are consistent with the tenets of sustainable development. This depends on the ability of nations to build development strategies based on appropriate forms of economic competitive advantage.

Corporate Responsibility and the Competitive Advantage of Nations breaks new ground in exploring how changes in the role of business in society might underpin new forms of international, economic competitive advantage. It argues that this is a pre-requisite for corporate responsibility becoming more than an exciting side-event in driving global social and environmental outcomes.

AccountAbility and **The Copenhagen Centre** have initiated this work to stimulate much-needed debate between policy-makers from public bodies, business and civil society institutions. Forthcoming research will explore in greater depth the potential for rooting nations' competitive advantages in corporate responsibility practices, and how best this can be supported through public policy and practice.

www.copenhagencentre.org
www.accountability.org.uk