CORPORATE
SOCIAL RESPONSIBILITY

Martin Wolf

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Martin Wolf

Martin Wolf is associate editor and chief economics commentator at the *Financial Times*. He was awarded the CBE (Commander of the British Empire) in 2000 for services to financial journalism. He is a visiting fellow of Nuffield College, Oxford University, and a special professor at the University of Nottingham in the United Kingdom.

Mr Wolf was joint winner of the Wincott Foundation senior prize for excellence in financial journalism in both 1989 and 1997 and won the RTZ David Watt memorial prize in 1994. He was the winner in the United Kingdom of the 2003 Business Journalist of the Year Decade of Excellence Award and won the Newspaper Feature of the Year Award at the Workworld Media Awards in 2003. He has been a forum fellow at the annual meeting of the World Economic Forum since 1999.

Martin Wolf obtained a Master of Philosophy in economics from Oxford University in 1971. Following that he joined the World Bank, where he became a senior economist in 1974. In 1981 he became director of studies at the Trade Policy Research Centre in London. He joined the *Financial Times* in 1987 as chief economics leader writer and became chief economics commentator in 1996.

Mr Wolf is the author of the book *Why Globalization Works: The Case for the Global Market Economy* published by Yale University Press, New Haven, Connecticut, in 2004.

Introduction by Malcolm Johnson

member, Institute of Directors in New Zealand Inc

We are most fortunate to have Martin Wolf here to speak to us. Some of you will know that he is in New Zealand to deliver the New Zealand Business Roundtable's flagship address, the 2004 Sir Ronald Trotter Lecture, in Auckland on 2 September. Martin is the associate editor and chief economics commentator at the *Financial Times*. He is also a visiting fellow of Nuffield College, Oxford, and a special professor at the University of Nottingham.

Phrases such as corporate social responsibility, corporate citizenship, sustainable development, triple bottom line reporting, and putting people before profits are now in widespread use. But what do these terms really mean and how can business people, in particular company directors, best understand their implications for the firms that they govern? Our guest speaker promises to strip away the jargon surrounding these ideas and put corporate social responsibility, the title of his address, into an understandable economic context.

Ladies and gentlemen, would you please give a warm Wellington welcome to our guest speaker, Martin Wolf.

CORPORATE SOCIAL RESPONSIBILITY

Nobody would wish to defend corporate irresponsibility or suggest that businesses should behave antisocially. It is little wonder therefore that corporate social responsibility (CSR) is a popular notion. To attack it is like assailing motherhood. Yet the idea is not merely problematic but, in some respects, dangerous.

Hostility to markets is sour old wine. What changes are the bottles into which it is put. The collapse of communism destroyed the illusion that abolition of private property would create a paradise. However, this failure barely touched the enemies of the market. What it has changed is their means. Today's aim is not to eliminate private business but to transform the way it behaves. This, argued David Henderson, former chief economist of the Organisation for Economic Cooperation and Development, in a thought-provoking study for the New Zealand Business Roundtable and the London-based Institute of Economic Affairs, lies behind the vogue for corporate social responsibility. This increasingly accepted idea represents a response to critics, many in activist groups, who are "... with few exceptions ... hostile to, or highly critical of, multinational enterprises, capitalism, freedom of cross-border trade and capital flows and the idea of a market economy. One might expect, and indeed hope, that the business community would effectively contest such anti-business views. But ... the emphasis is on concessions and accommodation".[1]

Mr Henderson argues that the idea of corporate social responsibility is today more than a merely defensive one. It is positive and broadly focused, amounting to a transformation of the objectives of the company and so of the market system. It is not enough, in this view, for companies to pursue profits within the constraints of law and the principles of honest dealing. Companies are seen as having a leading role as agents of social, environmental and economic progress. Business should enthusiastically embrace and adopt the notion of 'corporate citizenship'.

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1 David Henderson, *Misguided Virtue, False Notions of Corporate Social Responsibility,* New Zealand Business Roundtable, Wellington, 2001, p 35. I wrote on this subject in 'Sleep-Walking with the Enemy', *Financial Times*, 16 May 2001.

Largely in response to the pressures upon them from groups who often describe themselves as 'civil society', companies have adopted codes of conduct, at individual and industry-wide levels. In the process, companies often negotiate performance standards with non-governmental organisations (NGOs) that include some form of monitoring. The NGOs arrogate to themselves, in this way, functions that belong to governments.

At its limits, the notion of social responsibility takes the form of the 'triple bottom line', which corresponds to the three facets – economic, social and environmental – of sustainable development. Implementation of the triple bottom line involves a transformation of how businesses operate. Shell, which has taken this idea far further than most, has stated that the adoption of corporate social responsibility "demands a deep shift in corporate culture, values, decision-making processes and behaviour".

The arguments for corporate social responsibility can be reduced to the following propositions: first, there exists a well-defined and generally agreed notion of the wider public interest for companies to follow; second, this notion of the public interest can be identified with the pursuit of social and environmental objectives – the triple bottom line; third, the 'soft regulation' of corporate social responsibility serves as a way of inducing corporations to promote the public interest; and, finally, this body of soft regulation of companies should be developed much further.

Powerful objections can be made to such a broadening of corporate objectives: it accepts a false critique of the market economy; it endorses an equally mistaken view of the powers of businesses; it risks spreading costly regulations worldwide; it is as likely to slow the reduction of global poverty as to accelerate it; it requires companies to make debatable political judgments; and it threatens a form of global neo-corporatism, in which unaccountable power is shared between companies, activist groups, international organisations and a few governments.

To elaborate this position, I will now try to set out my view of the role, limits and dangers of CSR.

First, behind the pressure to adopt corporate social responsibility too often lies hostility to the profit motive itself. What is needed, critics argue, is to put 'people before profits'. The truth is the opposite. It is by seeking out opportunities for profit that business contributes to economic and social development. Competitive businesses are forced to seek new markets and employ previously under-used resources. In so doing, they benefit customers, employees and the countries in which they operate. The twentieth century could be regarded as the century of the modern joint-stock corporation. It was also the most economically successful century in human history – the world's population rose four-fold and world output per head rose six-fold. This is no accident. The private limited liability company has proved to be the world's most powerful engine of innovation, large-scale organisation and transmission of know-how across frontiers. It is a responsibility of business to make this case clearly and powerfully.

Second, in its pursuit of profit the corporation has the same moral obligations as individuals. The precise content of moral behaviour is controversial. However, most people would accept the golden rule – 'do unto others as you would be done by'. From this follow principles of honest dealing and voluntary obedience to the law even where it may be possible to evade it. Because companies are institutions set up to serve the interests of their owners, they also have an obligation to be transparent in what they do. Morality means, among other things, neither offering nor receiving bribes.

Third, in some senses companies are more powerful than individual employees or customers. They have an obligation to take that imbalance of power into account. Companies should not use the resources of their shareholders to lobby for narrow sectional interests. When companies lobby in this way, they undermine the legitimacy of the political process and the market system. Critics of capitalism confuse corporate competitiveness with political power. Businesses should not encourage that confusion.

Fourth, the profit-seeking corporation will also often find it in its interests to accommodate pressures for what people believe to be socially responsible behaviour, even if these demands are misconceived. Reputation is an important corporate asset. What its own employees, customers, governments and the public think of the corporation is a determinant of its viability as a business. By placing CSR explicitly within the objectives of the company it may also allow the company to focus better on long-term concerns relevant to its success. Thus, CSR may sometimes be a genuine contribution to long-term corporate profitability and success and, as such, be something companies should adopt, in their own interests.

Fifth, companies will find it particularly difficult to decide how to behave in countries with weak, corrupt or brutal governments. Sometimes, they will have to provide governmental services – education and health, for example. Often they will have to make difficult judgments about whether to invest in such countries at all. There are no simple answers. A good general rule is to ask whether the company could defend its behaviour if it were splashed all over the newspapers. Companies cannot make up for the absence of good governance, but they should do what they can to avoid making bad governance worse. Proposals to publish revenues paid to governments should, for these reasons, be welcomed, not resisted.

Sixth, the behaviour of CSR-driven companies may not serve the public interest. Let me give just a few examples of behaviour that advocates of CSR might consider to be in the public interest, but could well not be.

Corporate social responsibility advocates might recommend that a company stays in a given locality, even if it is not the most profitable place in which to produce. But what would such behaviour mean for the ability of up-and-coming regions and countries to attract investment? What would such an obligation do for the willingness of companies to invest in the first place?

Corporate social responsibility advocates might recommend that multinational companies pay workers in developing countries above the opportunity cost of their labour. But what would be the benefit if these companies ended up employing fewer people than they would otherwise do?

Corporate social responsibility advocates might recommend that multinational companies should not employ children in very poor, developing countries. But what would be the alternatives for such children – school, prostitution or starvation?

Corporate social responsibility advocates might recommend that activities be ‘sustainable’. But how can any resource-extraction industry ever be sustainable, and what would happen if we stopped all such activities?

Seventh, even if the public interest could be defined, why would a process of bargaining between publicity-seeking, single-issue NGOs and profit-seeking companies necessarily reach the right outcome? The process that generates the commitments to CSR is, let us be blunt, one of blackmail and concession. This may produce the socially optimal outcome. But why would one expect this?

Eighth, to the extent that companies feel obliged to operate with the same environmental standards and terms and conditions of employment worldwide, for reasons of reputation, they may harm the development of less economically advanced countries by ignoring differences that should operate in favour of them. Similarly, to the extent that companies accept excessively costly operating practices, they are likely to be less competitive and less profitable, and so make a smaller contribution to the economy. Should a company feel obliged to accept costly responsibilities, it will need to impose those costs on its competitor. If those costs are incurred in pursuit of socially worthwhile goals, that is no problem. But if the costs are not justified by the gains, then the result will not be an improvement in overall social welfare but a reduction in it.

Ninth, political processes are the only effective and legitimate way to determine what the public interest is and how to enforce it. Neither companies nor pressure groups are entitled to define the public interest. True, political processes do not exist at the global level. But this is a reflection of the reality of national sovereignty, itself an important value.

Tenth, the notion of CSR coincides with the strange idea that activist groups represent 'civil society'. Because elected governments are wrongly deemed powerless, it is suggested, instead, that only concerted action by companies, activist groups and governments can achieve the global goals on which every right-thinking person is supposed to agree. But this is global neo-corporatism. As such, it is subversive of individual freedom and democratic accountability. Behind the demands lies the oft-stated view that governments are impotent before modern, multinational businesses. The truth is the opposite of what critics allege. Governments remain potent local monopolists of coercion. Meanwhile, international economic integration has reduced corporate monopoly power, by enhancing competition.

Eleventh, while companies may be willing to achieve objectives that support profits, there is a strict limit on what they can do at the expense of profits. This is truer the more competitive is the industry in which they operate. A competitive company cannot afford costs that are not also borne by its competitors. The move towards a more competitive economy is, for this reason, incompatible with the ability of companies to pursue costly social goals. The old AT&T monopoly had, in Bell labs, one of the most significant research establishments in the world. The competitive AT&T can no longer afford this. For that very reason, there will be great pressure from 'socially responsible' businesses to impose the costs they have accepted voluntarily on their competitors, willy nilly. The chief executive of an Australian mining company described a conversation with another chief executive. The latter said: "Don't you understand? My organisation is run by Greenpeace today and it is my job to ensure that Greenpeace is running yours tomorrow."

Twelfth, business may well find that failure to implement the obligations whose legitimacy they have accepted will lead to mandated corporate social responsibility. An approach taken to ward off increased regulation by governments at the behest of so-called civil society is consequently likely to lead to increased regulation. This is because business will already have accepted these social and environmental objectives. If so, how can it object to legislation that imposes those objectives on all businesses?

To conclude, I strongly agree that private companies should behave morally. I also agree that companies may find it in their interest to promote what is deemed socially rewarding behaviour. I also agree that such behaviour may further the public interest where that can be satisfactorily defined.

Yet I would also argue that the public interest is, in fact, difficult to define and may conflict with generally accepted views of CSR. Furthermore, profit-seeking companies in competitive industries will be unable to achieve social goals that undermine profitability, even where to do so would be in the public interest. Corporate social responsibility would even be counterproductive – that is, reduce social welfare – if companies forced or persuaded to adopt CSR tried to impose the costs on their competitors.

Companies cannot save the planet by voluntary action. They should not pretend they can. Making it richer is quite good enough.

Questions

You talked about ethics and moral values in companies. The same issues arise in governments around the world. Politicians rate poorly in terms of public respect. How do you see ethics and moral values in a governmental context?

A major theme of my book is that the failures of globalisation are almost universally failures of government. There are some deep questions of political theory about the extent to which a sovereign government is bound by normal moral principles. There is a school of thought about government – broadly defined, the realist 'tradition' – which holds that a government (as distinct from individual politicians within a government, who, being citizens, have the obligations of all other citizens) cannot be or should not be a moral undertaking, as opposed to pursuing amorally what it defines as the national interest. I do not want to go into these questions of political theory except to record my belief that limited-government, constitutional democracies are, and should be, moral actors and therefore be governed by moral principles in their behaviour. By virtue of what they do, however, we have to accept that governments face moral choices that are more difficult and complex in some ways than those that individuals or even corporations face. So, I think we do have to recognise these characteristics of the state.

The second point I would make is that if we are talking about achieving the broad set of objectives that I discussed – namely social, environmental and economic – government is an indispensable actor. Without responsive and efficient governments that provide the basic services on which all market economies depend, above all property protection and the provision of basic infrastructure (where that cannot be provided by the market), no economy will succeed. Where governments of this kind are lacking – and they are lacking in my view in at least three-quarters of the countries of the world – economic development does not proceed satisfactorily. There is no doubt that it is the failures of government, which are very deep-seated and deeply rooted in many societies, that explain why so many countries are unable to engage productively in the globalised economy and why they do not develop. I write about this at length in my book. It is the greatest challenge of our world to fix this, but the truth is that there is not a simple solution.

The third point is one that I made in my talk. I believe it is perfectly legitimate for a society to be concerned about, for example, the environment in which it lives and, indeed, the global environment. Equally, it is perfectly legitimate for a society to be concerned about the social conditions of its people and to intervene to change them. So I am not a radical libertarian. I think political processes exist in order to make decisions of these kinds, and I have no problem in principle with regulation and taxation – we can then discuss the specifics – in order to achieve such objectives. I think that is part of what it means to be a member of a political community. But it is the job of the political process to do this, not of businesses at the behest of activists. As long as groups of activists are not in power they have no more legitimacy in imposing their objectives than any other group in society trying to influence the political process.

Unfortunately, in many countries, for reasons we understand very well, political processes are defective – this is also an issue I discuss at length in my book – and in some countries, indeed, many countries, political processes are entirely and wholly defective. In fact, worse than that, they are monstrous. There are no simple solutions to that problem either. So, where I come out in the end in my book is to say that governments are essential. The state must do things and respond to the demands of people, yet the state will always fail. This is no more than to point out the obvious: as St Augustine would surely agree, we live in a fallen world and have to live with that fact.

This is a standards-related point. For the information of the audience, the ISO – the international organisation involved in standards setting – decided that CSR was an interesting topic and it set up a special advisory group on social responsibility that consisted of such like-minded groups as Greenpeace, the International Chamber of Commerce, Consumers International and Shell, amongst others. The special advisory group reported back to a conference in Stockholm in June of this year, and it was interesting that the developing-country members of the ISO got together the night before and stood up before almost anybody had a chance to say anything and said they were fully in support of an international standard on social responsibility. It was a problem for them that Shell has its own definition of social responsibility, as does Exxon, Mobil and Caltex. Each member has a different definition, which is not helping development in their own countries because they are trying to meet many different standards established by companies wanting to invest in their countries. I wonder if you have any comment on that.

I am sure they are right. As I indicated in my presentation, the notion of what is socially responsible behaviour is inevitably and irretrievably political and controversial, both in theory and even more in practice. People are going to differ vastly in how they approach it, so the result will be that different countries will have a different sense of what their companies should be doing, and different companies will have a different sense of what social responsibility means for them in their particular operations. This is unquestionably a source of confusion. It was partly for that reason and because of the costs associated with it, as I mentioned, that I have believed for some time that once a notion is accepted you will get – and in fact you are already seeing it through the UN Compact – an attempt to agree to a global, and then ultimately a globally legislated, common standard of social responsibility.

There are two ways you can approach such an effort. One would be to hope that when people sit down and try to agree on what socially responsible behaviour actually means among diverse countries they will realise, very swiftly, that there is no common standard whatsoever. The effort is completely hopeless and should be abandoned. That would be my optimistic view, and it may be that the representatives of developing countries, who are not stupid, realise that is exactly what would happen and it would end the problem from their point of view. The other possibility, of course, is that such minimum standards are agreed. There are clearly efforts in a whole range of areas – like labour standards and the environment – to set rules that would be legislated internationally and would affect the behaviour of companies.

The reason I find that problematic is that, in some areas, although not all, what are almost universally accepted to be socially responsible forms of behaviour are not, in fact, socially responsible. That is to say, they are socially irresponsible because they are damaging to some countries likely to be affected by them. While it is certainly not an ideal solution, I believe it is the responsibility of sovereign governments to decide appropriate standards for their own countries through the political process. Views can legitimately differ across countries, radically and substantially. There is no reason why companies should, in general, have a completely different view of appropriate standards from those of the countries in which they operate.

I recognise, however, that there are some very difficult cases for companies, but the attempt to agree on global, common standards of what it is to be socially responsible, and then to impose them on companies, is, in my view, a potentially dangerous path towards excessive regulation of the entire world economy. Personally, I would oppose it.

Could you explain how you reconcile the position of the moral responsibility, as I think you called it, of corporate businesses with what I think you could call the rampantly profit-seeking interests of the shareholders of those businesses, especially in a world where there is competition for the investments of those shareholders.

This is where life gets interesting. It is obviously possible for basic morality to be incompatible with continued survival in business: if all your competitors are offering bribes, you may feel tempted to do the same. But I think, or perhaps hope, that most of what I regard as moral behaviour is compatible with – and supportive of – successful business operation. There are obviously exceptions to this, but I do not believe that companies that aim to survive over a long period benefit from behaving and being known to behave with inordinate ruthlessness towards their employees, customers, and the communities in which they are located. If companies did you would expect their labour costs to be higher, the prices they can get for their goods and services to be lower, and their ability to forge productive relations with their communities to be impaired. So, in all these respects, just as with individuals, a reputation, whether deserved or not, for behaving in a moral and decent way is a valuable one to have. This is no more than, if you like, a form of fairly enlightened self-interest.

Things get really interesting if you consider some of the more intractable cases. Suppose you are in an industry with a by-product that is potentially an environmentally destructive effluent or something of that kind. You know that all your competitors are discharging this effluent and it is genuinely costly to clean it up. You cannot get the cost back in the sale price of the product. What do you do? Go out of business or discharge the effluent? If there is not a social agreement on a common regulation – and this is a standard case in which I think there is likely to be one – it is very difficult to argue that the company should avoid the environmentally harmful practice because if it does it will go out of business.

To take another classic case, I see no reason why a company should not continue to manufacture cigarettes. However, I do not think a company is entitled to lie about the consequences of smoking them. What is moral behaviour is not always easy to define and I accept that, at the borderline, there are some very tricky cases. However, I think that the core areas in which you would expect a company to behave morally – that is to say, in terms of the treatment of its employees, dealings with its clients, and honesty about what it is doing – are ones where ethical practices are likely to be beneficial, rather than harmful, for a company that expects to survive in the long run. But, obviously, we can all think of counter-examples.

You have talked several times about companies existing for the longer term. What is an acceptable timeframe for companies to take a long-term view of the world, both from the social and environmental point of view but also in terms of their own business?

I am merely observing the simple fact that the establishment of the limited liability joint-stock company allowed the creation of entities that were not only much larger than companies had ever been before but also had the capacity for being effectively immortal. And many companies duly became effectively immortal. I once looked at the 30 largest companies by market capitalisation in Europe and found that only one company had been created in the previous 30 years and many of them dated back to before the First World War. Now you might say that tells you a lot about Europe, but even in the United States many companies have been around for generations. In fact, they are among the oldest institutions in our societies. I am not suggesting that in their investment decisions they should do a discounted cash flow for the next 100 years, not least because at a reasonable rate of interest the long-term costs and benefits are not likely to be very relevant. But companies have to take into account the capital, in the broadest sense, that they possess, which obviously includes their stock of know-how and of relationships.

Let me give you just one example that is relevant to my own business, the *Financial Times* (FT). The FT has existed since 1888. It is perfectly clear that the competitive advantage of the FT derives largely from its position in the labour market. It derives from the quality of the journalists we are able to attract and our ability to pay them less than what almost any other competitor would have to pay, because they want to work for us. They want to work for us because they think the paper has values, both in the way it operates and in what it produces. That asset is extraordinarily valuable to the paper. It would be very foolish for the management of the paper to sacrifice that asset for any relatively short-term advantage.

So, while you could imagine setting up a company in the knowledge that it is doomed to self-destruct in three years, you are more likely to be establishing a business that you expect to be around for quite a long time. That might suggest setting up a joint-stock company, and going through the business of having an initial public offering and getting outside shareholders. In that case, you have to be fully aware that in making decisions about business opportunities in the short-to-medium run you are going to affect relationships that influence your competitiveness in the long run, among them the relationships you have with your customers and employees. It is perfectly proper, indeed essential, for businesses to take those relationships into account in deciding how to behave because they will determine how successful that business is likely to be. That will not be true of all businesses at all times but it will be true of many and, in my view, it is certainly true of the largest ones that now exist in the world.

Vote of thanks
Elizabeth Koh

Martin, thank you for a very thorough and knowledgeable analysis of what is a very difficult subject area. Corporate social responsibility is on the hot list of emerging concepts that businesses need to understand and do something about. It is a subject that has a wide variety of interpretations and is often very misunderstood. You have pointed out that defining the public interest is an area of extreme difficulty. Do we employ children in factories so they are safe from prostitution? Do we close down industries in order to protect our resources? There are no easy answers to these questions.

However, the issues are not new ones. There has always been a tension between the need for businesses to make profits and the needs of society, but this issue has perhaps been considered more intensely in recent times. We see consumers' lack of trust in major companies such as Enron. Consumers avoid goods and services from certain companies when they believe those companies have not acted in society's best interests. I think there is increasing pressure from society on companies to take more responsibility.

But do we accept Milton Friedman's view that the business of business is business or do we adopt the CSR thesis that companies will build shareholder value by taking account of the impacts on society? This is the business case for CSR, if you like. I particularly liked your term "enlightened profit maximisation". I do not think we can rely on business to solve all of society's problems, as you rightly point out, but there is definitely a need for enlightenment on some of these issues.

So thank you very much for increasing our knowledge and awareness of some of the dilemmas that we face in our businesses. We all appreciate the fact that you have taken time out to join us today, and hope you enjoy your stay in New Zealand.