Social Responsibility A Matter Of Corporate Strategic Management

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The following article, written by Adrienne von Tunzelmann of MDL, was published in THE INDEPENDENT, 24 January 1997, page 9. It was the third in a three-part series. The earlier two articles were by Roger Kerr, Executive Director of the New Zealand Business Roundtable (issue of 13 December 1996) and Nick Park, lecturer in management systems at Massey University (issue of 17 January 1997).

This article focuses on the strategic management theme in corporate social responsibility.

In debating the social responsibilities of business, both Roger Kerr and Nick Park miss an important area of debate, one that for the managers of companies probably defines the ground of social responsibility more usefully than the moral arguments. This is, in short, its importance in the strategic management of the modern company.

Debate at the moral level is important, not least because the new landscape for business, government and individuals which we have created in New Zealand with economic and social reform requires us to review roles and capabilities. It is unlikely that the question of who performs what functions in society best, given the need to make best use of resources, will be answered now in the same way it was up to the 1980s.

One aspect of this change was highlighted by a major study last year of corporate social responsibility in New Zealand, carried out as a joint project between Victoria University's Institute of Policy Studies and Ernst and Young and published as *Social Responsibility and the Company*. We found that many companies are now giving attention to where corporate social responsibility fits into the strategic management of the company. They are doing this in the more immediate context of the pressures of competition and the search for added value than in moral vein. That makes the debate even more timely.

Based on the study, which involved looking at what companies operating in New Zealand are doing, it is possible to see two pragmatic issues lying behind Kerr's argument and Park's response. These are: the proper scope of management activity; and the actual nature of the constraints on management activity.

There is no more pressing strategic task for company managers than the task of seeking to influence the future environment of the business (or as Michael Porter would urge, influencing the environment for the industry), which will fundamentally determine the company's ability to generate value for its shareholders long term. The scope of this task has long since ceased to be as straightforward as that of Adam Smith's industrial capitalist whom no doubt modern managers would envy. First, the environment for business is unimaginably different. Secondly, we have 'invented' strategic management.

Avishai[1] has cogently portrayed a complex corporate world which neither Adam Smith, nor even in his time Milton Friedman, could have anticipated: the "magical" changes of technology, including interactive telecommunications, computer-integrated systems, shared data-base marketing alliances and supplier and customer networking, and the accompanying customisation, globalisation and disaggregation of business activity. As Peter Drucker has argued, these developments have transformed the nature of competition and the nature of work.

Equally, the nature of the management challenge has been transformed. The focus of strategy needs to be vastly broader than the traditional product/market approach of Adam Smith's day. It now engages managers in considering a complex array of factors of which the social context in which the company operates is an integral part. And it requires the wealth generating function of the company to be thought of as constituting a set of relationships - with employees, customers, suppliers and community interests as well as shareholders - which can add or subtract value and from which the company derives its ability to go on creating wealth.

An additional external element in strategic management for the company is the regulatory environment and the part companies may well want to play in influencing it. There is a moral dimension here, in that collectively-held values will be brought to bear on the 'licence to operate' - if society sees a divergence between corporate activity and these values, there will be pressure to regulate. So if a majority in society held Park's view on the social responsibilities of business, and businesses fell short in their voluntary actions, there is a possibility of regulatory intervention to compel companies to behave in a certain fashion. The foresighted manager will be aware that the company is required to have regard to these influences, and not just passively.

The same issue raises an efficiency question. Recent overseas work on the sources of economic prosperity talks of the role of trust in the creation of social capital. Francis Fukuyama argues that the society of the United States has trusted business enough to permit the corporate (limited liability) form, but not enough to desist now from regulating corporate activity - quite extensively. In his analysis this imposes a substantial additional cost on business and threatens the nation's international competitiveness and hence prosperity. His approach supports the view that the best option inherently for companies, and for society, is for businesses (and other institutions) to be self regulating rather than being regulated by others, but that this requires a level of trust within the wider community.

The implication in all these factors is that the strategic management of the company is being taken to the point where the company is inevitably concerned with the social conditions of the community in which it operates, and the wider social environment. The diagram shows the boundaries of the company as spanning the interests of its four major constituent parts, and as being cognisant of the interface between the company and government, and the company and the community.

Diagram

Shareholders, customers, suppliers and employees have interests which fall within the company's boundaries, and interests which exist independently. Transactions across those points on the boundaries are an inherent element of strategic management. Here one is led to agree with Park that the analysis of a business must not ignore "the strength of all stakeholder interests, and the likely influence of their effects upon outcomes." Shareholders should expect this type of analysis as part of the work management does in developing strategies for the company's long term success. This is not to be confused with the concept of a stakeholder society, as promoted by the Labour Party in the UK.

A strategic management rationale for social responsibility is quite consistent with Kerr's view that companies should only do the things that enhance returns to shareholders. But it also suggests a wider set of purposes for social responsibility activity than Kerr would seem to allow, certainly when considered in terms of social engagement that goes beyond the most basic level of routine contractual activities, i.e. those governed by legal requirements or by the principles of sound management. It is still in the company's interests for managers to seek their own responses to social conditions, but with a wider vision of what the company needs to be doing to ensure its survival as wealth creator. It would be easy for Park's moral perspective to divert attention from the question of what companies and their managers might actually do. Kerr is more practical on this.

An area where Kerr and Park should reach agreement concerns the moral responsibilities of owners acting as members of society, not as part of the company, to improve social conditions. Park would see this exercised through social pressure or regulation. Kerr would see it exercised through the wishes of shareholders to the extent that they freely choose to use their ownership rights for this purpose. To an extent, both omit to say that the typically dispersed ultimate owners of public companies are not in a position to instruct managers on how they want the company run. Under any viewpoint, however, principals/owners will want the company to be well run and, in whatever terms, to be successful. So what practical guide do managers as their agents have?

One powerful guide is the terms on which company performance is judged by financial markets. We have seen a fundamental shift in financial market thinking and methodology, from an accounting approach to assessment of the long term sustainability of company earnings (discounted cash flow), which has to do with how the value of the company is measured over its life. And as Kerr indicates, there is technically no conflict between short and long term profitability in modern financial analysis.

This relatively recent phenomenon, something else not contemplated by Adam Smith, allows markets to factor into their assessment of the value of a company the ability of the company to protect and enhance future profitability by the effective management of risk. Risk may include potential impacts on the value of strategic assets through changes in reputation, operational flexibility or regulatory provisions. As suggested in *Social Responsibility and the Company*, the contribution active social engagement makes is the enhanced capacity for companies to manage the factors in the social and political environment which might impact on company goals.

In emphasising the link between social responsibility and company goals, it is not necessary to see any of the above as implying the cynical manipulation of society for the ends of business. Far from diminishing the importance of the social contribution the company makes while searching for successful strategies, a strategy around social responsibility that is clearly focused on shareholder value creation is more likely to strengthen the value of the activity to the community than one which lacks a management rationale. This is being found by commercial entities themselves (companies, banks and so on), and also increasingly by the community organisations companies support.

[1]Bernard Avishai, What is Business's Social Compact, Harvard Business Review, Jan-Feb 1994

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