Industrial Performance Center
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Note on Corporate Citizenship in a Global Economy

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MIT-IPC-02-008

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In a Global Economy

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The issue of corporate citizenship and the role of corporations in society has been debated for centuries. The debates move through various waves of intensity, often provoked by the revelation of corporate scandals and/or problems provoked by various business practices (i.e., product safety and labor relations during the Industrial Revolution, defense-related corruption scandals in the 1970s, accounting abuses and the impact of globalization today). Notwithstanding this long history, and the fact that each year dozens of articles on this topic are published and numerous prizes for corporate social responsibility are awarded, there exists no agreed-upon definition of corporate citizenship. In fact, both in the literature and in the more general corporate social responsibility movement, there co-exist alternative -- sometimes even competing -- conceptions of what constitutes good corporate citizenship, why it is important, and how it should be implemented.

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Introduction

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2. Alternative Models of Corporate Citizenship

Although the literature on corporate citizenship (sometimes referred to as corporate social responsibility—CSR) is extensive and has many subtle distinctions within it, one can divide this literature into four highly-stylized models: 1) minimalist, 2) philanthropic, 3) encompassing, and 4) social activist conceptions of corporate citizenship. These four models differ in terms of both the supposed beneficiaries of

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[1] This note was prepared for the Sloan School 50th Anniversary Celebration, to be used in conjunction with the case, “”The Promise and Perils of Globalization: The Case of Nike.” This note was prepared with the active involvement and research assistance of the following MBA students: Vanessa Chamah, Brian Curtis, Elizabeth Fosnight, Archana Kalegaonkar, and Adnan Qadir. Many of the thoughts presented in this note were developed collectively with Professor Zairo Cheibub, of the Federal University Fluminense, Niteroi, Brazil, in a joint paper we wrote on the topic.

corporate action (shareholders vs. broader societal stakeholders) and the motivation behind these actions (instrumental vs. moral/ethical). See Table 1.

Table 1 - Alternative Models of Corporate Citizenship

		MOTIVATION	
		Instrumental	**Moral/ Ethical**
BENEFICIARIES	**Shareholders**	Minimalist	Philanthropic
	Stakeholders	Encompassing	Social Activist

The more traditional or **minimalist** conception of corporate citizenship was perhaps best articulated by the Milton Friedman. According to Friedman, “the social responsibility of business is to increase the wealth of its shareholders” (1970). In other words, the sole responsibility of business is to those who have invested capital in the company. By maintaining a singular focus on wealth creation, businesses will promote efficiency and achieve optimal economic performance, which is the ultimate good that a business can do for society. Of course, corporations should not violate laws or engage in any irregular activities that could harm the wealth of shareholders, but any attempt to incorporate social goals into core business activities will, according to this view, lead to inefficiencies. Moreover, given that most managers do not have expertise in the area of social responsibility, engaging in these activities will simply distract them from their primary and fiduciary responsibility, which is to protect and promote shareholder wealth.

The **philanthropic** model is an extension of this traditional view. Although it, too, is concerned primarily with the optimization of efficiency and shareholder wealth, it does recognize that individual managers, shareholders, and sometimes even companies can, at times, engage is various philanthropic activities. However, these activities are seen **not** as important or even related to core business activities, but rather as motivated by various moral or ethical reasons.

A more inclusive stakeholder view of the corporation underlies the third, more **encompassing** model of corporate citizenship. According to this view, management is responsible not solely to shareholders but also to other groups (e.g., employees, consumers, creditors, suppliers, local communities) that may be affected by the company's practices. As a result of this potential impact, managers must take into consideration the interests of these groups when making decisions. Some proponents of this approach contend that corporate responsiveness to a wide constellation of stakeholders supports the resiliency of the firm in the face of external threats (Freeman 1984 in Brummer 1991). This, in turn, promotes the long-term survival of the firm. Others argue that company engagement in broader societal issues directly enhances company profitability and hence shareholder wealth.[2] Thus, according to this third model of corporate citizenship, corporate behavior may be directed toward a wider constellation of actors, but it is nonetheless instrumental, geared toward maximizing benefits to this broader (albeit still limited) group.

The fourth, **social activist** model of corporate citizenship extends the boundaries of supposed beneficiaries beyond those groups directly affected by company decision-

[2] See Elizabeth Murphy, "Best corporate citizens have better financial performance," Strategic Finance, January 2002.

making and toward society at large. According to this view, corporations should act to enhance broader societal goals and not merely to benefit a more restricted number of shareholders and/or stakeholders. Corporations should act not merely out of instrumental concerns but rather out of moral or even ethical considerations. In fact, because corporations are usually powerful and wealthy actors in society, they have a moral obligation to act in such a way that aids their less fortunate fellow citizens.

Of course, there exist many other, more subtle views of corporate citizenship. (See the bibliography for a sampling of other views.) The point of this note is **not** to provide a comprehensive review of the literature on corporate citizenship but rather to highlight that there exists significant divergence of opinion over several key dimensions of this issue, including:

1. The role of management: Should managers behave solely to enhance shareholder wealth or should they act to benefit other groups (both within and outside the firm) as well? Do managerial responsibilities extend beyond what is required either by law or contractual obligation?

2. The relation to profit: Should corporate decision-making be driven solely by economic considerations or are other (social) factors equally important? How does one measure and account for these other considerations? Is there an economic benefit to being a good corporate citizen?

3. The realm of responsibility: Are corporations responsible for only the direct effects of their decisions and strategies or also the indirect effects? What are the boundaries or limits of these responsibilities?

3. Globalization

The debates surrounding competing conceptions of corporate citizenship have become more complex and heated as a result of globalization. During the last two decades of the twentieth century, global trade and global capital mobility increased dramatically. For example, trade among the industrial democracies grew at almost twice the rate of total economic output during the 1970s and 1980s.[3] Whereas global trade amounted to about one-third of total world output in the early 1970s, it approached 45 percent in 1995. Intra-industry trade, an indication of competition within similar product markets, far outstripped inter-industry trade, thus heightening competition among producers for similar markets. At the same time, world trade became progressively less dominated by exchanges within the OECD nations, since various newly-industrialized countries (e.g., Korea, Singapore, Brazil, Mexico, India, and China) increased their exports after the oil crisis of the late 1970s. A recent study by the World Bank shows that 24 developing countries, home to about 3 billion people, increased their integration into the world economy since 1980. Manufacturers rose from less than 25 percent of developing country exports in 1980 to more than 80 percent in 1998.[4] As a result, these countries achieved higher growth in per capita incomes (on average 5 percent growth), longer life expectancies, and better schooling.[5]

Financial integration and movement of capital across borders also increased dramatically in these years. For example, international bank lending grew from around

[3] Geoffrey Garrett, Partisan Politics in the Global Economy, (Cambridge University Press, 1998): p. 51.
[4] World Bank, Globalization, Growth, and Poverty, (The World Bank, 2002): p. 5.

$200 billion in 1973 to almost $4 trillion in 1992.[6] Although the raw numbers on international capital flow are staggering, some economists, including those working at the International Monetary Fund, believe that the best indicator of capital mobility is the existence of government restrictions on international capital movements. In the early 1970s, less than 15 percent of countries had no capital controls. By the mid-1990s, about 30 percent of countries had removed controls on capital mobility.[7] This trend continued throughout the decade.

This increased flow of trade and capital, as well as the dramatic improvements in information, communication, and transportation technologies, has opened up all sorts of opportunities for multinational corporations (MNCs) to invest in or source from lower cost developing countries. Yet these opportunities are not without risk. As corporations increasingly disperse parts of their value chain throughout the developing world, they encounter a number of issues that challenge their original conceptions of corporate citizenship. How should these corporations behave when they are operating in several different countries, each with its own wages, regulations, customs and standards (or lack thereof)? What standards should they abide by and who (i.e., national governments, international organizations like the ILO, or the corporations themselves) should set these standards? To whom are these corporations responsible? Their shareholders and direct employees? Their vendors, suppliers and customers? Or even the employees of their third-party vendors and the local communities in which those factories are located? What

[5] However this same study shows that not all developing countries have benefited from increased globalization. In fact, much of the developing world trades less today than it did 20 years ago. This explains, in part, the growing poverty and income inequality manifest in much of the developing world.
[6] Garrett, op. cit., p. 54
[7] Richard Herring and Robert Litan, Financial Regulation in the Global Economy, (Brookings Institution, 1995): pp. 26-27.

are the boundaries or limits of a corporation’s responsibilities? In short, globalization has exacerbated the tensions and debates already existent within the corporate social responsibility movement.

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