

CHAPTER TWO

CONCEPTUAL CONTEXT

2.1 INTRODUCTION

The field of Corporate Social Responsibility (CSR) is particularly extensive as it involves dealing with a wide range of often divergent issues, such as ethical investment practices; the impacts of an organisation's activities on the environment, society and economy; the engagement of organisations with their different stakeholder groups; as well as issues related to an organisation's internal board structure and executive practices, etc. This means that in order to get to a thorough understanding of the idea *CSR*, it is necessary to also explore the meanings of certain related concepts that are most relevant in terms of shaping and driving the CSR agenda. Therefore, in line with the first objective as indicated in *Chapter One*, the purpose of the current chapter is to provide the reader with an overview of some of these concepts, namely *Corporate Governance (CG)*, *Socially Responsible Investing (SRI)*, *Stakeholder Engagement (SE)*, and *Sustainable Development (SD)*. In doing so, the conceptual context or framework of this study will be revealed. These particular concepts were chosen by this study because they are independently very prominent themes in business and academic literature and because they seem to be the main factors influencing and influenced by the CSR discourse.

The first relevant concept of importance to CSR refers to the overall management of organisations in responsible and sustainable manners, namely *Corporate Governance*.

2.2 CORPORATE GOVERNANCE (CG)

2.2.1 Conceptual Overview of CG

The term *Governance*, refers to the ways whereby individuals and institutions, public and private, manage their collective affairs. It is a continuing process through which conflicting or diverse interests may be accommodated and cooperative action may be taken. It

includes formal institutions and regimes empowered to enforce compliance, as well as informal arrangements that people and institutions either have agreed to or perceive to be in their interest (Commission on Global Governance, 1995:1-2). With regard to governance in the corporate world, it broadly refers to the ways in which corporations are directed, administered, and controlled (Baker & Anderson, 2010).

Corporate Governance (CG) can subsequently be defined: “...as the ways by which boards oversee the running of companies by their managers, and how board members are held accountable to shareholders and the companies. This has implications for company behaviour not only to shareholders but also to employees, customers, those financing the company, and other stakeholders, including the communities in which the business operates.” (UN Global Compact & IFC, 2009:4)

It can further be described as all the activities which make up the internal regulation of the business in compliance with the obligations based on the firm by legislation, ownership and control. It incorporates the trusteeship of assets, their management and their deployment. It means carrying the business as per the stakeholders' desires (Management Study Guide, 2011; Cannon, 1994:165). Accordingly, CG also concerns the relationships among the various internal and external stakeholders involved, as well as the governance processes designed to help a corporation achieve its goals. Within these processes, the mechanisms and controls that are designed to reduce or eliminate the principal-agent problem are particularly important (Baker & Anderson, 2010). The CG structure specifies the distribution of rights and responsibilities among different participants in the organisation, such as the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs (Anon, 2008a). According to Hawkins (2006:114), CG implies a robust system by which companies are directed and controlled across four key areas: The first of these is *financial accounting*; followed by the *configuration and competence* of the executive board; along with *recognition of the stakeholders* in the business; the fourth and last element is *transparency*. By means of this robust system, corporate responsibility and commitment must be **captured by the executive and blended into the business** at every level.

In view of the above, King (2007) believes that an informed explanation of CG would involve a description of all the processes that assist directors to discharge and be seen to be discharging the responsibilities created by their duties. A board has collective authority in making decisions but each director incurs individual liability - which should motivate a director to practise good governance. Therefore, effective CG requires a clear understanding of the respective roles of the board and of senior management and their relationships with others in the corporate structure (BRT, 2002:1). From a narrow point of view, *governance* can be seen as a fancy term for the way in which directors and auditors handle their responsibilities towards shareholders (EIU, 2002:5). However, such a narrow definition, adopting and advocating as it does a top down approach to management, serves to exemplify the inherent weaknesses of a command and control managerial style. Adopting both a bottom up **and** top down approach to management can better facilitate progress in regards to CSR (Jones *et al.*, 2006). Corporate governance needs to be about promoting corporate fairness, transparency and accountability.

In light of the fact that CG permeates every level of the organisation, its activities and actual day-to-day operational workings, it should not be confined to management alone, but aim to reflect the whole organisation and its stakeholders (Jones *et al.*, 2006). The concept can also be expanded to explain a firm's relationship to society, often blurring the distinction between corporate governance and corporate social responsibility (EIU, 2002:5). The aim of CG is to align as closely as possible the interests of individuals, corporations and society (Anon, 2008a). In this view, Cannon (1994:165) explains that the pattern and nature of corporate governance in specific nations or societies derives from the interaction of four broad forces, namely **board structure**, **societal pressure**, **regulation situation** and **ownership pattern**. These forces can be viewed as the elements of corporate governance.

2.2.2 Practical Implications and Strategies of CG

According to King (2007) CG represents good, hardnosed business, because it has been established that those companies that practise good governance are able to raise capital more cheaply and attract a better class of employee - two very important matters in the sustainability of a business. Effective corporate governance requires a proactive, focused state of mind on the part of directors, the CEO and senior management, who all must be

committed to business success through maintenance of the highest standards of responsibility and ethics (BRT, 2002:2). Good governance is far more than a 'check-the-box' list of minimum board and management policies and duties. A good corporate governance structure is a working system for principled goal setting, effective decision-making and appropriate **monitoring of compliance and performance** (BRT, 2002:2). Clearly, the importance of good corporate governance goes far beyond the interests of shareholders in an individual company. Indeed, the central corporate governance principles of transparency and accountability are crucial to the integrity and legal credibility of our market system (Witherell, 2002:8).

Hawkins (2006:117-118) provides a **framework for good corporate governance** in terms of behaviour and performance:

- At the heart of good governance, are the **corporate values** that create the ethos and culture of the operation. Every company is different, but it is generally reflective of the management style and approach cascaded from the CEO down. The values of the organisation should be supported by the stakeholders, including investors, customers, employees and the wider community. This support will provide the framework for strategic development and be reflected in behaviour and performance (see 5.2.2).
- **Strategic foresight** forms a crucial part of the board's role in leading the organisation. This frequently benefits from non-executive directors who are able to bring a wider perspective and knowledge. At the same time, they must also be able to understand the business and bring balance to strategic initiatives.
- In all of this, the role of the **multiple stakeholders** is essential to being able to move forward, without a continuous drain or direction change that is driven by external or internal pressure groups. Successful companies of the future will be value-focused and operate within a disciplined approach, linking financial performance and strategic positioning. By managing risk and measuring shareholder value, they will operate within a framework that includes all stakeholders and brings sustainable development within the corporate strategy. This more enlightened governance model means that executives must consider the wishes of all their stakeholders (see 2.4).

- **Improved transparency** is a fundamental part of building stakeholder confidence. Financial reporting is only part of the equation and sustainable reports provide an opportunity for organisations to openly declare their commitment and approach to the community and the environment.
- PR (Public Relations) communications and rhetoric are of little value unless they are supported by **action and performance**. If business leaders are to promote their organisations to stakeholders, they need to be able to measure the health of their business operations. The challenge is that as each company is a unique entity, which means that outside high level categories, it will be extremely difficult to reach consensus for key monitor indexes. What would be more practical, would be to develop an approach such as the excellence model, to provide a measurable profile.
- The final phase is clearly to be a programme of **continuous improvement** that is embedded in the organisation. Globalisation, or even its impact at a local level, is producing a continuous evolution in the business landscape. As such, it is important that organisations remain adaptable and responsive to market change. The challenges of maintaining market competitiveness demand that organisations are continuously pushing the envelope of performance, design, cost and processes.

It is worth considering that while it is easy to focus on the major multi-national organisations and brand leaders, these issues also apply to all businesses, whatever their size. According to King (2007), the major debate at the moment is whether governance should be on a 'comply or else', or a 'comply or explain' basis (see 4.8). The probability is that a hybrid situation will develop in the sense that some governance practices will become compulsory and others remain as guidelines.

2.2.3 The Importance of CG, Particularly to CSR

By building confidence and trust, good governance allows the corporation to have access to external finance and to make reliable commitments to creditors, employees and shareholders. It is this contract that underpins economic growth in a market economy (Witherell, 2002:8). In support of this argument, Neal and Cochran (2008:6) found compelling empirical evidence that corporate governance is relevant in terms of business

performance. Not only do the markets pay attention to corporate governance, but they reward good governance and punish poor governance, which in turn is integral to Corporate Social Responsibility (CSR). Hawkins (2006:114) maintains that true corporate governance and responsibility grows from an **integrated system** that links executive authority, financial accounting, board accountability and stakeholder aspirations to transparency, which entails a code of principles that is applied in practice. When trust in the organisation is undermined, lenders and investors lose their appetite for risk, and shareholders offload their equity, resulting in lost value and reduced availability of capital. Thomsen (2006) clarifies this argument by indicating that CSR is a way to characterise corporate values and/or corporate behaviour, while CG is concerned with the **institutional conditions** for these values. In other words, CSR and corporate values are usually the result of a given set of corporate governance mechanisms. Thomsen (2006) further believes that corporate values are created when companies **internalise the values** of salient stakeholders, of which owners and managers appear to be the most important. The internalisation of stakeholder preferences takes place in a hypothetical three-stage process: 1) allocation of ownership rights, 2) board composition, and 3) the influence of important stakeholders:

- In **stage 1**, the ownership decision allocates **ownership rights** across the relevant parties, i.e. the company's present and potential stakeholders. This is a matching problem in which owners with specific characteristics are matched with firms, which have their own specific characteristics. Owner characteristics include access to information, capital and knowledge. Strictly speaking all firm characteristics are attributable to the relevant stakeholders, but it simplifies the discussion considerably to talk about firm characteristics (*see Chapter 5*).
- In **stage 2**, the board composition decision allocates **board seats** over the set of potential board members, which include the stakeholder representatives as well as professional managers and board members. Boards are normally elected by the owners, but in some countries other stakeholders (employees, governments) also appoint board members. Owners delegate many decision rights concerning corporate values to the board. In companies that separate ownership and control, this implies that managers play a pivotal role in creating or changing corporate value systems (*see 5.2.2*) and that the composition of the board is a key determinant of this process.

- In **stage 3**, the board enters into **implicit contracts with key stakeholders**. Companies can clearly be influenced by means of formal contracts and market transactions, but these relations may be modelled as constraints subject to which the corporate objective function is maximised (Thomsen, 2006).

Against this background, it is clear that Corporate Governance is a necessary system which companies must have in place before effective CSR can take place. Corporate Governance is therefore not a subset of CSR, as it refers to the source and foundation of the corporate value system. This would further imply that the CG system is also primarily responsible for shaping a company's '**personality**' (see Chapter 5).

The second concept to be explored by this study relates to the practice of ethical investments, namely Socially Responsible Investing (SRI).

2.3 SOCIALLY RESPONSIBLE INVESTING (SRI)

2.3.1 Conceptual Overview of SRI

Socially Responsible Investing (SRI) is an increasingly popular investment strategy that integrates financial objectives with social and environmental objectives (CFA Institute, 2011, Donovan, 2011). As such, SRI refers to a range of investment strategies that seek to align corporate values with personal values around issues such as environmental stewardship, poverty alleviation, and human and animal rights (Savitz & Paschall, 2009:54). SRI can therefore be defined (De Jongh *et al.*, 2007:7) as: *"...investment that incorporates an active consideration of environmental, social and governance (ESG) issues into investment decision-making and ownership."* It has also been referred to as *ethical investment*, *sustainable investment*, *best-of-class investment*, and *triple 'p' bottom line investment* referring to *People*, *Planet* and *Profit* (see 2.5.3). SRI can further be described as an **investment process that integrates social, environmental, and ethical considerations** into investment decision making (Renneboog *et al.*, 2008a:1). SRI is closely related to CSR because social investors seek to identify companies with strong CSR records for their investments and to encourage increased levels of CSR performance (European

Commission, 2008:7; Lydenberg, 2007). Unlike traditional types of investments, SRI applies a set of investment screens to select or exclude assets based on ecological, social, corporate governance or ethical criteria, and often engages in the local communities and in shareholder activism to further corporate strategies towards the above aims (Renneboog *et al.*, 2008a:1). In this regard, SRI might also be viewed as the **strategy** being followed during investment decisions in order to achieve social, environmental as well as financial returns (Bench Marks Foundation, 2003:49).

De Jongh *et al.* (2007:51) identify and dispel certain **myths** regarding SRI:

- Responsible investment is not about philanthropy, although society and the environment in general may benefit from the outcomes.
- SRI is also not about sacrificing financial returns in pursuit of some sort of broader social good.

Very simply, SRI is investment that incorporates an active consideration of environmental, social and governance issues into investment decision making and ownership.

Kurtz (2008:253) indicates that SRI stands at the intersection of two powerful streams of western thought - on the one hand, *religious and moral reasoning*; on the other, *economic and financial theory*. The first tradition insists on the relevance of ethics to all realms of human activity, while the second tradition argues for a narrow focus on risk and return in capital allocation decisions. Socially responsible investment is based on the premise that **both world views matter**. In large part due to these two often opposing thought streams, Bakshi (2007:529) explains that not everyone supports the idea of SRI. Despite impressive data to the contrary, the impression often persists that socially responsible investors sacrifice monetary profits in order to take a moral high ground or pursue socially relevant goals. Advocates of SRI have contested this allegation by renewing arguments in favour of a triple bottom line (people, planet, profits), but also by producing hard data to show how high standards of CSR are undeniably related to better performance all round.

In addition to traditional financial criteria to make investment decisions, Hamner (2008:2) reveals that most SRI is done by mutual funds and institutional investors who buy and sell

shares of publicly traded corporations. In the past, SRI has generally been about negative screening which means the avoiding of certain undesirable sectors such as tobacco, nuclear power, gambling, etc. But recently, SRI has changed into taking a positive approach by searching for the **best practices** among competitors. SRI funds that use positive screening involve criteria for Sustainability or Corporate Social Responsibility (CSR), to evaluate companies. These Sustainability/CSR criteria include a range of themes such as health and safety, corporate governance, pollution prevention, labour relations, indigenous peoples and more. The SRI movement has at its core a fundamental question (Renneboog *et al.*, 2008b:304): should a firm aim at maximising **shareholder value** or **social value** (defined as the sum of the value generated for all stakeholders)? This is an important question that immediately brings the issue of the social responsibility of business into play.

2.3.2 The History of SRI

Ethical investing is not a new concept and has ancient origins in Jewish, Christian and Islamic traditions. Nowadays, and in contrast to its ancient base on religious traditions, modern SRI is more based on the varying personal ethical and social convictions of individual investors. Since the 1960s, a series of social campaigns, e.g. the anti-war and the anti-racist movements, have made investors aware of the social consequences of their investments (SEG, 2011; Donovan, 2011a; Sharlow, 2009; Renneboog *et al.*, 2008a:3). The first modern SRI mutual fund, the Pax World Fund, was founded in 1971 in the US. This fund was created for investors opposed to the Vietnam War (and militarism in general) and it avoided investments in weapon contractors. In the 1980s, protests by social investors turned their focus on the racist system of apartheid in South Africa. SRI investors, particularly from the US and Europe, have applied pressure on companies doing business in South Africa to turn those operations away to other countries, and urged mutual funds not to include South-African nor western firms with South-African subsidiaries into their investment portfolios (SEG, 2011; Donovan, 2011a; Sharlow, 2009; Renneboog *et al.*, 2008a:3).

The history of SRI can be divided into **two general periods**, the first running from 1970 to the mid-1990s, and the second from the mid-1990s to the present. In the **first period**, SRI

was largely a North American phenomenon. Throughout this period and continuing to today, US religious organisations have played a leading role in shareholder activism through the annual filing of hundreds of shareholder resolutions on social and environmental issues (Lydenberg, 2007). Apart from faith-based activism, the demand for change was also driven by traumatic disasters such as the explosion at the Chernobyl nuclear reactor in the Ukraine in 1986 and the Exxon Valdez oil spill, which damaged over 1000 km of coastline off Alaska in 1989 (SEG, 2011). Such disasters served as a motivation for the formation of the Coalition for Environmentally Responsible Economies, CERES, as a partnership between leading environmental groups and institutional investors seeking ways to align investment dollars with social and environmental responsibility. In the UK, the Ethical Investment Research Service (EIRIS) was already in existence since 1983 (Blowfield & Murray, 2008:281; Bakshi, 2007:526). During the **second period**, SRI developed into a worldwide phenomenon, starting in the United Kingdom, where it took root in the 1980s, and extending rapidly to Europe, and then to Asia, Africa, and Latin America. Its growth has paralleled the strong growth of interest in CSR throughout the world over this time (Lydenberg, 2007).

The SRI movement has come a long way from the days when its proponents were accused of neglecting their fiduciary responsibility. This can be observed from the following **trends** (Bakshi, 2007:526-527):

- Since 1995 SRI funds have grown 40% faster than the wider investment market.
- Socially screened investing officially arrived on Wall Street in 1999 with the launch of the Dow Jones Sustainability Index, which takes into account five corporate sustainability principles: innovative technology, corporate governance, shareholder relations, industrial leadership, and social well-being.
- In 2001, the FTSE4Good sustainability index was jointly set up by the Financial Times and the London Stock Exchange.
- In 2004, some of the world's largest corporations, which are part of the UN's Global Compact initiative (see 4.4), declared that "Who Cares Wins". This was also the title of a report these companies jointly issued outlining the business case for sustainability.

The 18 financial institutions among the signatories of “Who Cares Wins” manage assets of over \$6 trillion.

- SRI has moved from concerned individuals to institutional strategies. For example, the Association of British Insurers has found that including social responsibility can reduce portfolio volatility and increase returns. This is partly because SRI investors tend to be ‘picky but sticky’ - more long-term and loyal.
- In many European countries it is now mandatory for pension funds to disclose the extent to which social, environmental and ethical issues were taken into consideration in the investment process.
- Major investment banks have been developing SRI capacity including Citigroup and Goldman Sachs. Morgan Stanley estimated that in the UK alone, SRI has grown from its former position of 5% of the stock market (in 2007) to 15% in 2009.
- The Johannesburg Stock Exchange (JSE) has also recently developed criteria for measuring the triple bottom line performance of companies.

In May 2004, the JSE launched the SRI Index in South Africa. The Index philosophy is founded on the principles of the three pillars of the triple bottom line, namely environmental, social and economic sustainability (see 2.5.3), with good corporate governance underpinning each. These principles are encapsulated in the Index indicators, which are then structured along the categories of Environment, Society and Governance and related sustainability concerns (JSE, 2011). Another key feature of the Index is the alignment with global standards while reflecting the complex nature of social responsibility in South Africa. The purpose (JSE & EIRIS, 2007:2) of the SRI Index is to:

- identify those companies listed on the JSE that integrate the principles of the triple bottom line and good governance into their business activities
- provide a tool for a broad holistic assessment of company policies and practices against globally aligned and locally relevant corporate responsibility standards

- serve as a facilitation vehicle for responsible investment for investors looking for non-financial risk variables to include in investment decisions, as such risks do carry the potential to have significant financial impacts
- contribute to the development of responsible business practice in South Africa and beyond

2.3.3 Scope of Modern SRI

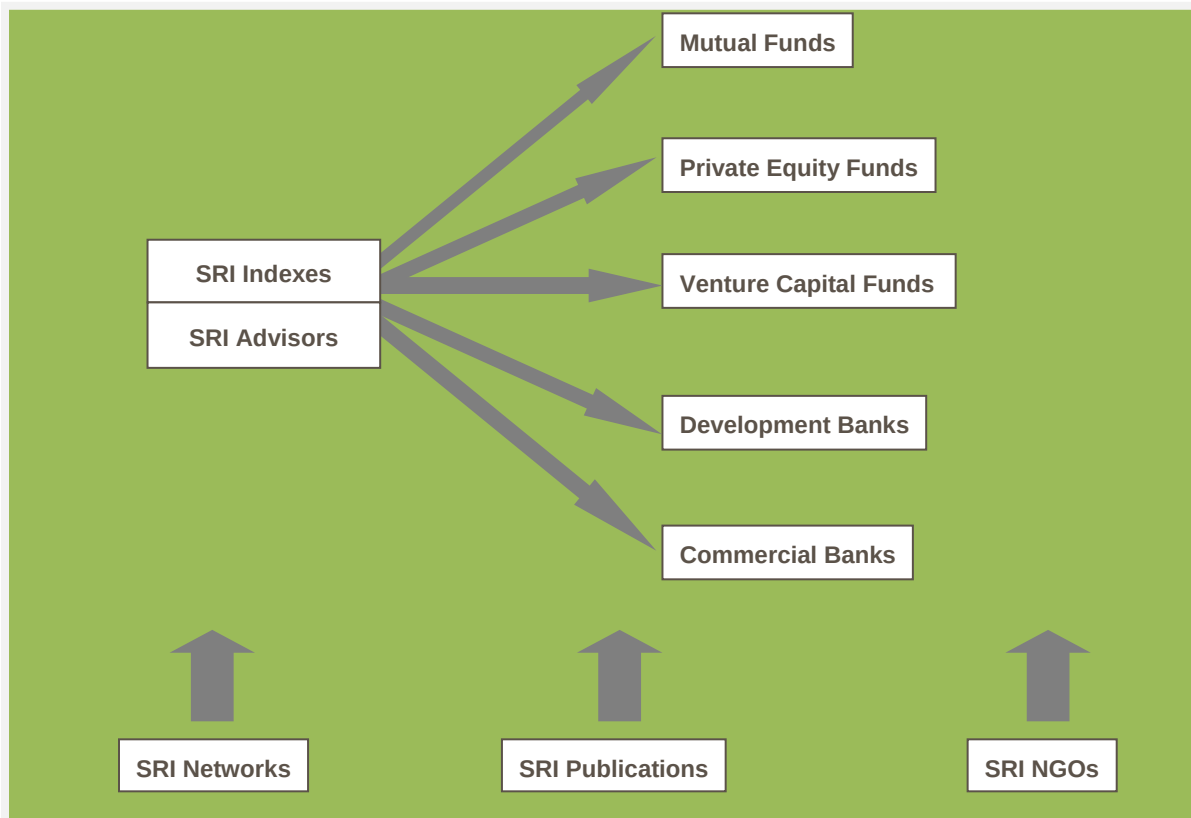
By 1995, there were an estimated \$639 billion under management in the USA which were being guided by some criteria of social investing. The world of SRI expanded even wider in the following decade. In 2005, the first socially screened Exchange Traded Funds (ETFs) were launched. Catholic, Protestant and Islamic faith-based investors all have options, and newer funds have been developed that focus specifically on labour and equal employment issues, as well as on the environment (Blowfield & Murray, 2008:281). Socially Responsible Investing (SRI) today encompasses an estimated **\$2.71 trillion** out of \$25.1 trillion in the U.S. investment marketplace (Social Investment Forum, 2011). This includes over 260 mutual funds and accounts held by individual investors and communities (Sharlow, 2009).

One of the newest themes to emanate from SRI is the idea of '**sustainability investing**'. *Sustainability* refers to the extent to which a company's business practices address today's social and environmental needs without compromising the quality of life for future generations (*compare section 2.5 on Sustainable Development*). Sustainability investors actively seek out companies engaged in good behaviour, rather than passively excluding those engaging in bad. They believe that companies with sound environmental, social and governance (ESG) policies are not only superior ethically, but also financially (Leahy, 2008:48). As of October 2004 there were at least 12 'families' of market indexes of sustainable companies and over 35 individual indexes in at least 7 countries. There are more than 700 SRI mutual funds and about a hundred SRI funds that are specifically focused on sustainable companies and not just negative screening for undesired sectors (see **Figure 1** for a structure of the SRI market). The SRI indexes and funds publish the specific criteria for sustainability that they use to select or recommend companies for

investment. The market is thereby clearly stating how it defines sustainability (Hamner, 2008:3).

Figure 1

Structure of the SRI Market



Source: Hamner (2007)

Kinder (*in* Kurtz, 2008:251) offers the following classification for the **types of social investors** today:

- **Value-based investors:** These social investors act in accordance with deeply held religious or ethical views. Their decision to include non-financial variables in their portfolio policy is driven primarily by their desire to have investments that are consistent with their moral beliefs. Most religious institutions that practice SRI fall into this category, as do many secular organisations focused on causes such as the environment or human rights.

- **Value-seeking investors:** Value-seeking investors use social and environmental data to enhance portfolio performance. There is a growing body of evidence that companies which manage environmental, social, and governance risks most effectively tend to deliver better risk-adjusted financial performance than their industry peers.
- **Value-enhancing investors:** This group uses shareholder activism techniques to enhance investment value, and focuses primarily on corporate governance.

2.3.4 Approaches/Levels of SRI

According to Lydenberg (2007), investors pursue SRI strategies for a number of reasons or objectives:

- To avoid investments inconsistent with their ethical precepts
- To improve corporate behaviour on social and environmental matters
- To identify financial risks often overlooked by traditional analysts
- To participate in public debate on the proper relationship between corporations - and other issuers of investment products - and society

In order to achieve these objectives, investors typically utilise the following three approaches or strategies when practising SRI:

- **Screening** refers to the practice of evaluating investment portfolios or mutual funds based on social, environmental and good corporate governance criteria (Social Investment Forum, 2011). As briefly alluded to earlier (see 2.3.1), screened funds have either negative screens or positive screens. Those with negative screens remove firms that produce objectionable goods and services, or operate in distasteful industries or countries. Such funds often exclude firms that deal in tobacco, alcohol, gambling, defence and nuclear power (Donovan, 2011b; European Commission, 2008:12). In addition, they might screen out firms that operate in countries with human rights abuses or repressive regimes, or those that are categorised as terrorist states. Positive screening is the selection of investments that perform best against corporate governance, social, environmental, or ethical criteria,

and which support sustainability. Positive screening is associated with a 'triple-bottom-line' investment approach, ensuring that a company performs well according to economic, social and environmental criteria (SEG, 2011; Donovan, 2011b; SEEP, 2009a:32; Blowfield & Murray, 2008:284; Cochran, 2007:451).

- **Shareholder advocacy** involves using the position of an owner in a company to actively encourage a company to improve. Many SRI funds use their shareholding to promote superior social and environmental performance. At the most basic level this is manifested in how they vote at the annual general meetings of companies that they invest in. However, some SRI funds go further and carry out **dialogue** with companies to try and influence corporate behaviour and practices (SEG, 2011; Leahy, 2008:47; Bakshi, 2007:528). Shareholder advocacy can take many forms, from something as simple as a phone call or letter-writing to filing a formal shareholder resolution calling for a company to take a particular action (which can ultimately come to a vote in front of all shareholders). These activities can be conducted privately or publically (Donovan, 2011b; SEEP, 2009a:33; Blowfield & Murray, 2008:289; Calvert Group, 2008). Dialogue efforts include talking with companies on issues of social, environmental or governance concerns. Shareholder advocacy also frequently involves filing and co-filing shareholder resolutions on such topics as corporate governance, climate change, political contributions, gender/racial discrimination, pollution, problem labour practices and various other issues. This process generates investor pressure on company management, often gathers media attention, and educates the public on social, environmental and labour issues (Social Investment Forum, 2011; Donovan, 2011b; SEEP, 2009a:33).

- **Community investing** aims at directing capital from investors and lenders to communities that are underserved by traditional financial services institutions. Community investing provides access to credit, equity, capital, and basic banking products that these communities would otherwise lack (SEG, 2011; Donovan, 2011b). Community investing makes it possible for local organisations to provide financial services to low-income individuals and to supply capital for small businesses and vital community services, such as affordable housing, child care, and healthcare (Social Investment Forum, 2011; Donovan, 2011b; SEEP, 2009a:33). The principle behind community investment is to make investments that will strengthen local communities (Cochran, 2007:451). Investors often

accept slightly below-market rates of return to encourage investment that can build or rebuild communities (Calvert Group, 2008).

SRI can thus be viewed as a broad field with many points of connection and disconnection with Corporate Social Responsibility (CSR). It would be natural to assume that socially responsible investment represents an implementation of CSR in financial markets, but many social investors have motivations very different from what might be called the academic view of CSR (Kurtz, 2008:249). While CSR is widely regarded as a voluntary business contribution to the societal guiding model of sustainable development, SRI can be regarded as an application of CSR and SD principles in investment decisions. It merges the concerns of a broad variety of stakeholders with shareholder interests in both CSR and SD. In other words, SRI embeds CSR in the functioning of shareholder capitalism (European Commission, 2008:7).

For investors who are truly motivated to perform their duties within socially responsible parameters, one important issue that will constantly need to be addressed is the regard for the views and opinions, as well as the well-being of the general public and members of more directly affected (by corporate activities) communities. The critical issue of *Stakeholder Engagement* will subsequently be discussed.

2.4 STAKEHOLDER ENGAGEMENT (SE)

2.4.1 Conceptual Overview of SE

In response to the enhanced role of business in society, more and more members or representatives of different social groups impacted by corporate behaviour, claim their right to be informed of, consulted on and involved in corporate decision-making. Consequently, many corporations have come to realise the importance of engagement and dialogue with a variety of individuals and entities on social, environmental and economic issues (Smith *et al.*, 2010:5; Sillanpää, 2007; Branco & Rodrigues, 2007:13). *Stakeholders* can be identified as people or institutions that are affected, or might be affected, by an organisation's activities. Likewise, stakeholders can, in return, affect the activities of that organisation (see

Tables 1 & 2). It should further be acknowledged that there are also other groups (e.g. NGOs, academics or religious organisations) with a burning interest in a company's activities who may not seem to be directly affected by the company's actions but who should also be included in the stakeholder grouping (MMSD, 2002; *also see* Garvare & Johansson, 2010:738; IFC, 2007:10; REVIT, 2005:4; Phillips, 2004:2).

In a CSR context, the focus on stakeholders goes beyond the strict historical focus by corporations on stock- and shareholders. Corporate stakeholders include, at the very least, employees, customers, suppliers, media, non-governmental organisations and the communities and markets in which they operate (Cohen, 2007; Schilling, 2000:225). Stakeholder theorists thereby object to the alleged "special status" of shareholders on the ground that many other groups have a legitimate claim or 'stake' in a corporation (Boatright, 2002:1839). Stakeholder theory incorporates overlooked interests and the interests of the under-represented who do not participate directly in the decision-making processes of the recognised instances of corporate governance (Bonnafeous-Boucher & Porcher, 2010:206). The impetus behind the use of the term '*engagement*' in stakeholder theory and CSR literature, is the need to emphasise that for firms merely to *interact* with stakeholders, is no longer sufficient. In light of this, '*engagement*', is used to recommend a type of interaction that involves, at minimum, recognition and respect of common humanity and the ways in which the actions of each may affect the other (Noland & Phillips, 2010:40).

Against this background, **Stakeholder Engagement (SE)** can be viewed as an umbrella term encompassing a range of activities and interactions of an organisation, which can be divided into **eight components** (IFC, 2007:12):

- *Stakeholder Identification and Analysis*: refers to time invested in identifying and prioritising stakeholders and assessing their interests and concerns.
- *Information Disclosure*: means communicating information to stakeholders early in the decision-making process, in ways that are meaningful and accessible, and to continue this communication throughout the project life.
- *Stakeholder Consultation*: starts with the planning out of each consultation process, inclusive consultation, documenting the process, and the communication of the follow-

up.

- *Negotiation and Partnerships*: implies that for controversial and complex issues, the company will enter into good faith negotiations that satisfy the interests of all parties. By forming strategic partnerships, value is added to impact mitigation or project benefits.
- *Grievance Management*: involves the establishment of accessible and responsive means for stakeholders to raise concerns and grievances about the company's activities.
- *Stakeholder Involvement in Project Monitoring*: means the direct involvement of affected stakeholders in monitoring project impacts, mitigation and benefits, and the involvement of external monitors where they can enhance transparency and credibility.
- *Reporting to Stakeholders*: on environmental, social and economic performance, both those consulted and those with more general interests in the company's activities.
- *Management Functions*: is the building and maintenance of sufficient capacity within the company to manage processes of stakeholder engagement, track commitments, and reporting of progress.

According to Freeman and McVea (*in* Freeman & Velamuri, 2008), the stakeholder approach has **seven distinguishing characteristics**:

- First, it offers a **single strategic framework** that allows a manager to deal with changes in the external environment without the need for new strategic paradigms. In this way, it is particularly suited for the dynamic environments that are so prevalent today.
- Second, the stakeholder approach is a **strategic management process** rather than a strategic planning process. The focus is less on predicting the future and more on proactively plotting the direction of the firm.
- Third, a central concern of the stakeholder approach is the **achievement of the organisation's objectives** through the harnessing of support of all those who are

affected by the firm's actions, as well as all those who can affect the progress of the firm.

- Fourth, the stakeholder approach emphasises the critical role of **values-based management**, by recognising that a diverse collection of stakeholders will cooperate with the firm over the long term only if they share a core set of values.
- Fifth, it is at once a **prescriptive and a descriptive framework**. It advocates a holistic approach to management, integrating economic, social, political and ethical considerations.
- Sixth, rather than take a stylised view of stakeholders based on very general roles based groupings (such as shareholders, suppliers, etc.), the stakeholder approach places great importance in acquiring a fine grained **understanding of the particular stakeholders** of each firm. This deep understanding enables the management to develop tailored solutions for particular stakeholders, as with mass customisation.
- Finally, it starts off with the premise that a firm can exist and sustain itself only if it offers solutions that **balance the interests of multiple stakeholders** over time. Taking a stakeholder approach to CSR means a focus on integration across stakeholders and on practical managerial solutions that create value for customers, employees, suppliers, communities and financiers.

As such, SE can be defined (Sloan, 2009:26), in very general terms, as the **interaction process of involving** individuals and groups that either affect or are affected by the activities of a company.

2.4.2 Background to the SE Concept

As already mentioned in the introduction chapter (see 1.1) as well as the previous section (see 2.4.1), the past few decades have seen a shift in the role of the corporation in society. This was due to factors such as the globalisation of markets, the emergence of global social and environmental challenges like HIV/AIDS and climate change, as well as the decreased ability of individual national governments to address these issues by themselves. Added to

this, is a large increase in the number of international non-governmental organisations (NGOs) from just above 3000 to well beyond 40 000 in less than 10 years which clearly introduced an influential third sector to societal debate and decision-making (Sillanpää, 2007; also see Andriof & Waddock, 2002:20-21). In view of this, there has been a definite increase in the complexity and dynamics of the operating environment of organisations, especially for businesses. In order to understand and address the issues emerging out of this dynamic complexity, individual actors, whether businesses, civil society organisations or governments, are becoming increasingly dependent on mutual learning, shared knowledge and pooled capabilities. In this changing environment, businesses now play a more important role than ever before (Sillanpää, 2007).

Subsequently, Ranganathan (1999) indicates that companies are increasingly recognising social and environmental performance-dimensions as crucial for long-term sustainability, and stakeholder relations are emerging as of equal importance to financial performance in the eyes of many stakeholders. Particularly since the mid-nineties, there has been a discernible shift in the mind-set of the business community. Milton Friedman's famous statement that *"the business of business is business,"* has increasingly given way to a view of business and society as closely and **unavoidably intertwined**. New managerial theories urge management to take into consideration not only shareholders' interests, but also those of other groups, organisations or individuals who have a stake in the company. This is only possible when management fully understands the needs and interests of these stakeholders. It is precisely for this purpose that SE is required (Smith *et al.*, 2010:5; Parmar *et al.*, 2010:404).

Freeman and Parmar (2007b) trace the *Stakeholder* concept back to the Stanford Research Institute, where in the late 1960s it was originally used to organise executives' assumptions about the environment external to their firms (also see Parmar *et al.*, 2010:405). Stakeholder analysis was first used in the corporate planning process by Igor Ansoff and Robert Stewart (cited in Clarke, 1998) who stated that: *"While...responsibilities and objectives are not synonymous, they have been made one in a 'stakeholder theory' of objectives. This theory maintains that the objectives of the company should be derived by balancing the conflicting claims of the various 'stakeholders' in the firm, managers, workers, stockholders, suppliers, vendors."* The idea was then employed and tested by a group of

scholars and consultants at The Wharton School, one of whom eventually refined the concept into a fully-fledged theory of strategic management. R. Edward Freeman's 1984 "*Strategic Management: A Stakeholder Approach*" set forth a new method and set of techniques for executives to use to better understand how to manage key stakeholder relationships (see also Bruce & Shelley, 2010:3; Schilling, 2000:225).

Based on several years of consulting experience and thousands of conversations with managers, Freeman's first book presented a new description regarding the meaning and implications of being an effective executive; particularly through the use of the *stakeholder level of analysis* to frame and categorise strategic engagements (Smith *et al.*, 2010:6; Freeman & Parmar, 2007b). Clement (2005) indicates that during the 20 years since Freeman first proposed his stakeholder approach to strategic management, an extensive body of research has been performed on his theory. Such research has included not only the efforts of the management researchers who have tested, revised, and refined his theory, but also the views of the corporate executives who have used the stakeholder approach in their strategic planning.

Stakeholder theorists have since come to argue for the following: (1) all stakeholders have a right to participate in corporate decisions that affect them, (2) managers have a fiduciary duty to serve the interests of all stakeholder groups, and (3) the objective of the firm ought to be the promotion of all interests and not those of shareholders alone. Each of these propositions can be elaborated in different ways, and not every stakeholder theorist adopts all three (Boatright, 2002:1839). Accordingly, Clement (2005) identifies five important lessons from the stakeholder model for today's business leaders. These lessons may be summarised as follows: (1) Corporations are facing increasing pressures to respond to their stakeholders; (2) Corporations have a legal basis for responding to a wide range of stakeholders; (3) Corporations are being led by executives no longer guided by the principles of their professions; (4) Corporations respond to powerful stakeholders with legitimate, urgent claims; and (5) Corporations can improve the bottom line by responding to stakeholder concerns.

The following two tables (**Table 1** & **Table 2**) identify two different levels of stakeholders, namely primary and secondary stakeholders.

Table 1*Primary Stakeholders – Nature of Interest and Power*

STAKEHOLDER	NATURE OF INTEREST – STAKEHOLDER WISHES TO:	NATURE OF POWER – STAKEHOLDER INFLUENCES COMPANY THROUGH:
EMPLOYEES	- Maintain stable employment in firm - Receive fair pay for work - Work in safe, comfortable environment	- Union bargaining power - Work actions or strikes Publicity
OWNERS/ STOCKHOLDERS	- Receive a satisfactory return on investments (dividends) - Realise appreciation in stock value over time	- Exercising voting rights based on share Ownership - Exercising rights to inspect company books and records
CUSTOMERS	- Receive fair exchange: value and quality for money spent - Receive safe, reliable products	- Purchasing goods from competitors - Boycotting companies whose products are unsatisfactory or whose policies are unacceptable
SUPPLIERS	- Receive regular orders for goods - Be paid promptly for supplies delivered	- Refusing to meet orders if conditions of contract are breached - Supplying to competitors
COMPETITORS	- Be profitable - Gain a larger share of the market - See the entire industry grow	- Technological innovation, forcing competitors to "keep up" - Charging lower prices
RETAILERS/ WHOLESALEERS	- Receive quality goods in a timely fashion at reasonable cost - Offer reliable products that consumers trust and value	- Buying from other suppliers if terms of contract are unsatisfactory - Boycotting companies whose goods or policies are unsatisfactory
CREDITORS	- Receive repayment of loans - Collect debts and interest	- Calling in loans if payments are not made - Utilising legal authorities to repossess or take over property if loan payments are severely delinquent

Source: Frederick et al. (1992)

Table 2*Secondary Stakeholders – Nature of Interest and Power*

STAKEHOLDER	NATURE OF INTEREST – STAKEHOLDER WISHES TO:	NATURE OF POWER - STAKEHOLDER INFLUENCES COMPANY THROUGH:
LOCAL COMMUNITIES	- Employ local residents in the company - Ensure that the local environment is protected - Ensure that the local area is developed	- Refusing to extend additional credit - Issuing or restricting operating licenses and permits - Lobbying government for regulation of the company's policies or methods of land use and waste disposal
SOCIAL ACTIVISTS	- Monitor company actions and policies to ensure that they conform to legal and ethical standards, and that they protect the public's safety	- Gaining broad public support through publicising the issue - Lobbying government for regulation of the company
MEDIA	- Keep the public informed on all issues relevant to their health, well-being and economic status - Monitor company actions	- Publicising events that affect the public, especially those which have negative effects
BUSINESS SUPPORT GROUPS (e.g., trade associations)	- Provide research and information which will help the company or industry perform in a changing environment	- Using its staff and resources to assist company in business endeavours and development efforts - Providing legal or "group" political support beyond that which an individual company can provide for itself
FOREIGN GOVERNMENT	- Promote economic development - Encourage social improvements	- Granting permits to do business - Adopting regulations
FEDERAL, STATE AND LOCAL GOVERNMENTS	- Raise revenues through taxes - Promote economic development	- Issuing regulations, licenses, and permits - Allowing or disallowing industrial activity
THE GENERAL PUBLIC	- Protect social-values - Minimise risks - Achieve prosperity for society	- Supporting activists - Pressing government to act - Condemning or praising individual companies

Source: Frederick et al. (1992)

2.4.3 Challenges for Stakeholder Theory

Despite the clear increase in importance and prominence of the *SE* concept over the past few years, there are still a few theoretical challenges for stakeholder theory that might ultimately affect the usefulness of the concept for academics or business people:

- **The problem of definition:** Many believe that the original definitions of '*stakeholder*' refer to any group or individual who can affect or is affected by an organisation's objectives. Some have then argued that such a wide definition implies that terrorists can also be stakeholders, thus making '*stakeholder*' lose its implicit legitimacy. Others have argued that the term should be restricted to those groups who are definitional of the firm, such as customers, suppliers, communities, financiers, and employees who all have a clear stake in the firm. The result of these differing views in definition is that it is difficult to say what kinds of moral obligations are at work, when the very nature of who has the obligation is obscure. More practically, if who is a stakeholder is imprecise, it is difficult to formulate priority rules about whose interests count and when they come into play (Jones *et al.*, 2002; also see Parmar *et al.*, 2010:406).
- **The background theory problem:** Given its multidisciplinary origins, much of the disagreement about stakeholder theory is diagnosable as differing sets of background theories at work. For instance, it is debated if stakeholder theory should proceed from the legal sciences, philosophy, economic or social sciences, which might all be appropriate background disciplines. There are also scholars concerned with environmental issues who have suggested that the environment be seen as a stakeholder. With such an impressive array of potential background theories, perhaps it is foolhardy to wish for one, univalent stakeholder theory (Jones *et al.*, 2002). There have also been a variety of recent debates about whether stakeholder theory is truly a theory, a framework, or an approach. From a pragmatist perspective, these debates have little value, other than conferring some type of social legitimacy on to a narrative. The true legitimacy of stakeholder theory lies in its managerial point of view, which is profoundly useful to executives and stakeholders in framing and maintaining their relationships (Freeman & Parmar, 2007b). Subsequently, stakeholder theory motivates managers to embrace the pragmatic and pluralistic approach and recommends we avoid the philosophical and single theory approach (Freeman *et al.*, 2004:365).

- **The challenge of no objective function:** Some scholars have questioned the ability of stakeholder theory to offer managers an objective function for decision-making. The fact of the matter is that stakeholder theory questions the very need for an objective function. Managers need to use moral imagination to find ways to jointly satisfy rival stakeholder claims, and in cases where joint solutions cannot be found, they need to make sure that the same stakeholder group does not continue to be neglected (Freeman & Parmar, 2007b). The problem with focusing on a single objective is that there is too much complexity and uncertainty in the world, which means that managers need to use judgement now more than ever (Freeman *et al.*, 2004:365).

- **The problem of value creation and trade, and ethical theory:** Traditionally, theories of business have begun and ended with economic logic. Business has been seen mostly as a way of creating 'economic value', with ethics perhaps serving as a side constraint (Jones *et al.*, 2002). Most notably, stakeholder theory has been upheld as a rival to 'stockholder theory'. It is, however, important to remember (Freeman *et al.*, 2004:365) that **shareholders are also stakeholders**. Dividing the world into 'shareholder concerns' and 'stakeholder concerns', is roughly the logical equivalent of contrasting apples with fruit. Shareholders are stakeholders, and it does not get us anywhere to try to contrast the two. Schilling (2000) points out that the primary emphasis of stakeholder theory is the recognition that the firm is part of a system of interdependencies, and that shareholders are but one constituency group in a plethora of constituency groups to be served. Since the firm exists to serve stakeholders, *financial performance* is only a very small slice of a firm's total performance. It is quite natural to suggest that the very idea of value creation and trade is intimately connected to the idea of creating value for stakeholders. Business is about putting together a deal so that suppliers, customers, employees, communities, managers, and shareholders all win continuously over time (Freeman *et al.*, 2004:365).

Although it is useful to take note of the above-mentioned challenges to the concept, the definite increase of application of SE by companies the past few years, is clear indication that there are **much more benefits and acceptance** of the idea, than there are any significant rejections of it.

2.4.4 Importance and Benefits of SE

According to Noland and Phillips (2010:48), it makes sense for firms to initiate and facilitate respectful, honest and productive multilateral communication with their stakeholders; because stakeholders make up these firms, and the relationship networks to which these stakeholders belong make up the communities and markets within which these firms do business. Furthermore, because of the financial, physical and environmental effects that businesses can have on individuals and communities, it is important that businesses actually identify and communicate with those persons who have some legitimate stake in them. It is further important for the public to recognise that individuals make up these businesses, and that these individuals (or employees) are also important stakeholders (Noland & Phillips, 2010:40). Stakeholder Engagement is also one of the key parameters used to identify socially responsible companies (Sloan, 2009:27), whether it is agencies that rate companies in terms of sustainability and social responsibility, ethical investors that take ownership positions in different firms, or organisations that set standards for the disclosure of sustainability performance (*also see Garvare & Johansson, 2010:737*).

Without engaging stakeholders, there can be no common enduring agreement, ownership or support for a particular project (Sloan, 2009:27). Therefore, a venture is more likely to succeed, especially in the long-term, if it takes into consideration the environment in which it operates and endeavours to meet the needs of the stakeholders affected by it. As such, stakeholder engagement could be viewed as a form of risk management (REVIT, 2007:1). SE initiatives further lead to sustainability because they build on local capacity and knowledge, and they are more likely to be compatible with long-term development plans. Working closely with local communities can help decision-makers gain greater insight into the communities they serve, enabling them to work more effectively and produce better results. In turn, the communities can learn how the decision-making process works and how they can influence it effectively (NCCSAP, 2005:3). Consequently, SE is a vital component of the sustainable development of communities.

Apart from all these social benefits, Smith *et al.* (2010:6-8) outlines five major ways by which stakeholder engagement can also contribute to a company's economic performance:

- **Stakeholder engagement can solve problems:** Addressing company social or environmental impacts effectively often cannot be achieved without the collaboration, knowledge and expertise of stakeholders. On some issues, stakeholder participation will be essential to the implementation of solutions, on others they can provide 'out of the box' thinking that can lead to innovative win-win solutions for all parties. They also often bring a wider perspective on issues and solutions that companies might not have access to on their own, including knowledge of the local context as well as better understanding of anger expressed against the company because of its social or environmental impacts.
- **Stakeholder engagement helps management see the future:** Stakeholder familiarity with operations on the ground might well highlight where supply chains or company actions are not consistent with company policies, where there is potential risk or where there are yet to be explored opportunities. More generally, stakeholder attention to an issue can be an early warning of evolving public expectations and regulatory or political concern, which might well escalate with alarming rapidity.
- **Stakeholder engagement is a facilitator of trust:** By providing stakeholders with the company's perspective on issues and being responsive in addressing their concerns, stakeholders would be more likely to be cooperative rather than confrontational. As a relationship is built, confrontation may extend to trusting cooperation on common issues of concern, as well as enabling stakeholders, in some cases, to understand the limitations of corporate action.
- **Stakeholders are potentially influential partners:** Companies can work with stakeholders to shape industry standards and, given their access to like-minded politicians and regulators, possibly have their concerns taken into consideration in the formulation of legislation.
- **Stakeholder engagement can improve the company's public image:** Successful stakeholder engagement is likely to reduce public criticism, thus contributing to a positive view of the company in the eyes of all of its stakeholders, as well as saving

time and resources spent on fighting negative campaigning. Apart from consumers' growing awareness of issues of ethical conduct; there is also evidence that a responsible public image is beneficial for the recruitment and retention of employees.

2.4.5 Stakeholder Engagement as Part of CSR

Carroll (1991:43) refers to a natural fit between the idea of corporate social responsibility and an organisation's stakeholders. The word '*social*' in CSR has always been vague and lacking in specific direction as to whom the corporation is responsible. The concept *stakeholder* personalises social or societal responsibilities by defining the specific groups or persons business should consider in its CSR orientation. Management's challenge is to decide which stakeholders merit and receive consideration in the decision-making process. In most instances, there are numerous stakeholder groups crying for management's attention. Two vital **criteria** for sorting out the urgency or importance of the various stakeholder claims are the following (Carroll, 1991:43):

- **Stakeholder Legitimacy:** This refers to the extent to which a group has a justifiable right to be making its claim. For example, a group of 300 employees about to be laid off by a plant-closing decision has a more legitimate claim on management's attention than the local chamber of commerce, which is worried about losing the firm as one of its dues-paying members.
- **Stakeholder's Power:** This refers to the capacity to be able to exert influence over management's decisions and is a factor that may include significant differences. Thousands of small, individual investors, for example, wield very little power unless they can find a way to become organised. By contrast, institutional investors and large mutual fund groups have significant power over management because of the sheer magnitude of their investments and the fact that they are organised.

From a CSR perspective their legitimacy may be most important. From a management efficiency perspective, their power might be of central influence. The management of stakeholders in a socially responsible manner involves a **practical four-level framework** (Freeman & Parmar, 2007a) which executives use to create value for customers,

employees, suppliers, communities, and financiers and to connect values and ethics to the execution of their business strategy:

- The first level is about **purpose and core** - values, requiring executives to have clear answers to questions like: what do we stand for, and for whom do we want to create value?
- After articulating the specific ends a firm wants to serve, the second level addresses the means of **achieving those goals with stakeholders**. Key questions are: how are we going to manage and govern our relationships with stakeholders so that participation will continue to be fruitful for both parties, and what principles are we committed to so that stakeholders can count on our support and our actions?
- The third level addresses the **wider societal context** in which the firm operates. In order to take account of whether or not society appreciates and approves of the direction the firm is going, executives must ask questions like: what are our most vocal critics saying about us, and is there a way of opening a dialogue with our critics, so that we can learn from them how to realise our purpose and principles in a better way?
- The final level encourages executives to **see leadership as inextricable from ethics**. On this view, the very idea of leadership cannot be stated without implied ethical judgement. Presumably, leaders are legitimate and social legitimacy begins with the idea that one is acting from an ethical point of view.

Cohen (2007) claims that effective SE by corporations strengthens accountability and performance, serves as an early warning mechanism by managing risk as well as new product and service development, and improves decision-making; it involves an on-going dialogue which is crucial to the success and **sustainability** of corporations.

In fact, all three the above-mentioned concepts, *CG*, *SRI* and *SE*, are ideas and practices which are framed by striving towards one overarching theme, namely *Sustainable Development (SD)*. The meaning of this broad concept will subsequently be explored.

2.5 SUSTAINABLE DEVELOPMENT (SD)

2.5.1 Conceptual Overview of SD

The term *Sustainable Development (SD)* started its evolution in the early 1970s and over the years became a buzz-word for environmental and social scientists who rarely agree on its definition. The term became so popular because it offers an alternative to the traditional concept of *development*, which focused on growth as the ultimate end and regarded the means to achieve this end as irrelevant (Brilius, 2010:422; Khator & Fairchild, 2006:13). The most popular or widely accepted definition of sustainable development came from the report of the World Commission on Environment and Development (WCED) in 1987 when describing it as **"...development that meets the needs of the present without compromising the ability of future generations to meet their own needs"** (IISD, 2011; Marais, 2010:2; Brilius, 2010:422; UN, 2008:18; Clugston & Calder, 1999:1). The ultimate goal of SD is the advancement of life within the carrying capacity of the environment and at no expense to future generations. It is based on the logic that as a society works toward progress, its initiatives are more likely to be sustainable if they are based on integrated decision making that acknowledges the interdependent linkages between economic growth, social development and environmental protection (FAITC, 2011). Explicit in this definition is a contrast, and indeed a potential conflict, between two interests: those of present and future generations. This is a conflict arising out of recognition that growth in material well-being has implications for the environment. Consequently, it implies the need for a 'trade-off' – which is a choice that has to be made from the fact that two goals are at least partly in conflict. The nature of the trade-off one favours is strongly influenced by one's perspective (McNeill, 2000).

In 2001, the OECD's (Organisation for Economic Co-operation and Development) policy brief gave the following more technical definition for the concept *SD* by describing it as:

...a development path along which the maximisation of human well-being for today's generations does not lead to declines in future well-being. Attaining this path requires eliminating those negative externalities that are responsible for natural resource depletion and environmental degradation. It also requires securing those public goods that are essential for economic development to last, such as those provided by well-functioning

ecosystems, a healthy environment and a cohesive society. Sustainable development also stresses the importance of retaining the flexibility to respond to future shocks, even when their probability, and the size and location of their effects, cannot be assessed with certainty (OECD, 2001:2).

For organisations, the following more **practical definition** (IISD, 1992) of SD can be suggested:

For the business enterprise, sustainable development means adopting business strategies and activities that meet the needs of the enterprise and its stakeholders today while protecting, sustaining and enhancing the human and natural resources that will be needed in the future.

Corporate Sustainability can subsequently be described (Elkington, 2007) as the field of thinking and practice by means of which companies and other business organisations work to extend the life expectancy of: ecosystems (and the natural resources they provide); societies (and the cultures and communities that underpin commercial activity); and economies (that provide the governance, financial and other market context for corporate competition and survival). By paying attention to such wider issues, companies are better placed to ensure that their own business models remain valid and adaptable.

Bossel (1999:17) explains that SD involves the “*co-evolution of human and natural systems*” and in order to define an indicator set for societal development, the different relevant sectors or subsystems of the societal system must first be identified. In a systems view of SD, **six essential subsystems** can be distinguished. Each of these subsystems can further be viewed as representing a certain type of **potential** that is vital to the development of the total system. In this relationship, the term ‘*potential*’ denotes a stock or vital asset, which can grow or depreciate, and must be maintained in good state in order to contribute its share to the development of the total system. These subsystems together with their corresponding potentials are the following (Bossel, 1999:18-19):

- **Individual development:** refers to issues such as civil liberties and human rights, equity, individual autonomy and self-determination, health, right to work, social integration and participation, gender and class-specific role, material standard of living,

qualification, specialisation, education, family and life planning horizon, leisure and recreation and arts. *Individual potential* describes the potential for competent individual action as produced by - and producing - the possibilities for individual development. It is the accumulated result of tradition and culture as well as socio-political and economic conditions.

- **Social system:** includes population development, ethnic composition, income distribution and class structure, social groups and organisations, social security, medical care, and old age provisions. *Social potential* denotes something less tangible: the ability to deal constructively with social processes, and to employ them for the benefit of the total system. This has a strong cultural component determining social coherence and relationships. It includes such aspects as honesty, trust, competence and efficiency.
- **Government:** refers to government and administration, public finances and taxes, political participation and democracy, conflict resolution (national, international), human rights policy, population and immigration policy, legal system, crime control, international assistance policy, and technology policy. *Organisational potential*, as manifested in the know-how and performance standards of government, administration, business and management, is vital for effective resource use (natural and human) for the benefit of the total system.
- **Infrastructure:** involves settlements and cities, transportation and distribution, supply system (energy, water, food, goods, and services), waste disposal, health services, communication and media, facilities for education and training, science, research and development. *Infrastructure potential* denotes the stock of built structures like cities, roads, water supply systems, schools and universities. It is the essential backbone of all economic and social activity.
- **Economic system:** comprises of production and consumption, money, commerce and trade, labour and employment, income, market, and interregional trade. *Production potential* of the economic system includes the stock of production, distribution and marketing facilities. It provides the means for all economic activity.

- **Resources and environment:** consists of the natural environment, atmosphere and hydrosphere, natural resources, ecosystems, species, depletion of non-renewable resources, regeneration of renewable resources, waste absorption, material recycling, pollution, degradation, and carrying capacity. *Natural potential* represents the stock of renewable and non-renewable resources of materials, energy and bio-systems, including the capacity for waste absorption and regeneration.

Subsequently, in order for sustainable development to materialise, it is essential that all of these subsystems are operating efficiently and in adequate balance with each other.

2.5.2 Background to the SD Concept

According to Findlay-Brooks (2007), the WCED was set up by the United Nations (UN) in 1983, in response to growing concerns about the deterioration of the global environment. It became known as the Brundtland Commission after its chair, Dr Gro Harlem Brundtland, Former Prime Minister of Norway. In contrast to earlier environmental thinking, which focused on protecting the environment from economic development, the WCED report brought environment and development together in the concept *SD*. Responding to the report, the UN called on governments to make SD a central guiding principle and to develop policies which aim to preserve peace, encourage sustainable growth, alleviate poverty, address population growth and conserve and enhance the resource base. The importance of involving both NGOs and business in working towards these goals was strongly emphasised. The WCED definition embraces the notion that sustainable development is not simply about environmental protection, conservation of finite resources or maintenance of biodiversity. It recognises a wider set of challenges for attaining sustainable development: for instance, the questions of poverty alleviation, population stabilisation, female empowerment, employment creation, human rights observance and opportunity redistribution. Need, futurity and equity are socioeconomic and political issues; that are only relevant to the extent that they can be delivered to present and future generations through human endeavour (Sillanpää, 1999:529)

The 2002 United Nations World Summit on Sustainable Development, in Johannesburg, South Africa, adopted a declaration on sustainable development that committed

governments to building a humane, equitable, and caring global society, cognisant of the need for human dignity for all (Moosa, 2007). The world's countries thereby assumed a collective responsibility to advance and strengthen the interdependent and mutually reinforcing pillars of sustainable development at the local, national, regional, and global levels. They also issued a “*Plan of Implementation*” that contained detailed recommendations on various aspects of sustainable development, after which many governments prepared strategies for sustainable development. This includes new and improved approaches to managing environmental resources and ecosystems (Moosa, 2007).

From the above, it is evident that the idea of SD is considered a very important issue on an international level. Pearce and Atkinson (1998:7-8) provide the following two reasons as motivations why sustainable development remains a **valid policy concern**:

- **Time horizons:** First, sustainable development urges people to consider a *longer term time horizon* than overlapping generations may consider appropriate, and it invites people to seek out *guarantees* that development will be sustainable. The fact is that current generations cannot provide any guarantee that the next generation will in fact utilise its inheritance in such a way that it leaves the right bequest to the following generation. No-one can bind the next generation. All that can be done is to ensure that they **could** behave that way **if they chose**, and this is achieved by leaving them a per capita asset stock at least equal to the one we have today.
- **The composition of capital:** The second reason for thinking that sustainable development is not a redundant concept is that it focuses attention on what exactly it is that should constitute the inheritance between generations. Believers in *social sustainability (SS)*, for example, might argue that the stock of social capital should not decline further because the symptoms of its decline are ‘intolerable levels’ of social unrest, crime, drug abuse and so on.

Kates *et al.* (2005:19) make the claim that one of the successes of SD has been its ability to serve as a grand compromise between: those who are mainly concerned with nature and environment, those who value economic development and those who are dedicated to improving the human condition.

2.5.3 The Dimensions of SD

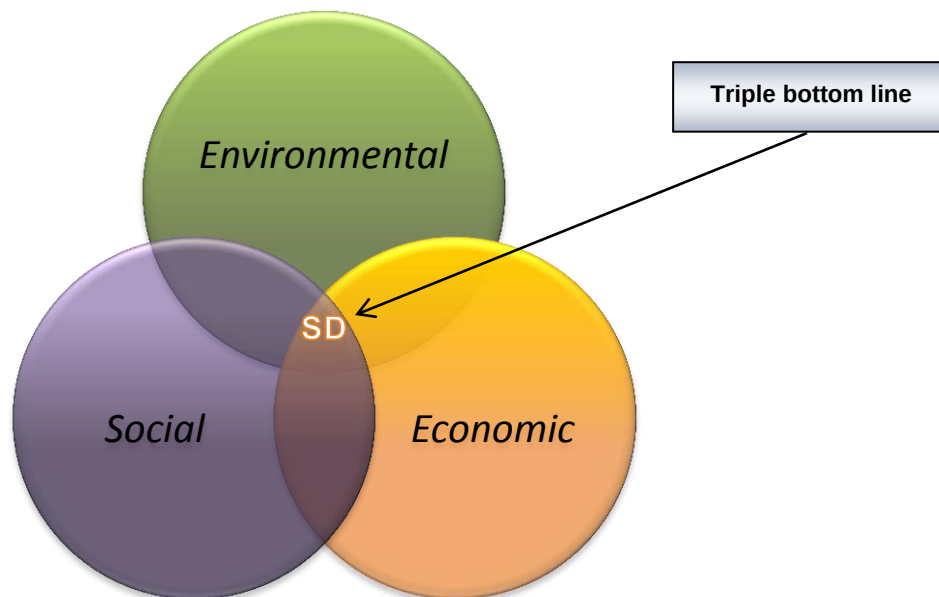
The concept *SD* comprises many different elements that are usually categorised into three dimensions: **environmental**, **economic** and **social**. These dimensions each appear to have a specific function (EEA Grants, 2006:3):

- the environment is the necessary **basis** for sustainable development
- the economy is the **tool** to achieve sustainable development
- the good life for all (the social dimension) is the **target** of sustainable development

Subsequently, the most common way of illustrating sustainable development, is the ‘three spheres / pillars / dimensions diagram’ (see **Figure 2**). True sustainable development is seen as development that meets the ‘triple bottom line’ where all three systems interact on an equal basis (Anon, 2007).

Figure 2

The Dimensions of Sustainable Development (SD)



Source: Anon (2007)

The concept of SD has been applied at micro level to operating companies and business. In this regard, the **Triple Bottom Line (TBL)** concept underscores the fact that companies and other organisations create value in multiple dimensions. Given the nature and focus of modern accounting, the financial bottom line is generally an inadequate expression of the total value equation (Elkington, 2007). The term *TBL* was introduced in 1994 by John Elkington, countering the narrower focus on the then fashionable term eco-efficiency, which focused on the financial and environmental dimensions of performance. TBL thinking, by contrast, extended to social impacts - and to the wider economic impact issues that are rarely captured in the traditional financial bottom line. A linked phrase, **People, Planet, Profit**, alternatively People, Planet, Prosperity, is based on the same concept (Elkington, 2007). The **primary goals of TBL** can be outlined (Mahoney & Potter, 2004:154) as the following:

- **Transparency and effectiveness:** allowing people to assess or ensure that organisations are doing the right thing in terms of their core business
- **Accountability:** allowing organisations to take responsibility for their actions and to report this honestly to their stakeholders
- **Consultation and responsiveness:** enabling organisations to ensure positive relationships both internally and externally and responding to the feedback from stakeholders through informed and appropriate decision-making
- **Impact assessment:** allowing organisations to identify the nature and scope of impact of the actions they take particularly across and between the three dimensions
- **Information and communication** (including PR function): enabling organisations to use the results of their processes for future decision making and to convey, as and when appropriate, these results to the public

O'Connor (2006) considers the three dimensions of SD (or the Triple Bottom Line) to be **interdependent** on each other. Achieving sustainability would mean a process of co-evolution with regard to the 'triple bottom line', which means the simultaneous respect for (or satisfaction of) quality / performance goals pertaining to each of the three spheres. It affirms that economic activity, while having its specific imperatives (innovation, competitive

search for profits, etc.) and a certain organisational autonomy, must be nonetheless 'in the service of' the wider social sphere; it presumes that society's purposes or values include environmental sustainability; finally it presumes that the biophysical environment does hold the potentialities for some meaningful sort of long run sustaining of economy and society (O'Connor, 2006).

To achieve a harmonious relationship between the three dimensions (economic, social and environmental) of development, certain **principles** need to be followed within each sphere:

– ***Environmental dimension***

Pearce (1999:7) believes that environmental concerns are very important for sustainability because the natural environment is the physical context within which we live and that sustainability requires that we recognise the limits of this environment. In other words, due to the fact that human welfare ultimately depends on ecological services, it is important to manage scarce natural resources in a prudent manner. Ignoring safe ecological limits will increase the risk of undermining long-term prospects for development. The environmental interpretation of sustainability focuses on the overall **viability and health** of living systems – defined in terms of *resilience*, *vigour* and *organisation* (MIND, 2007). These ideas apply to natural (or wild) and managed (or agricultural) systems, and cover wilderness, rural and urban areas. *Resilience* is the potential of a system state to **maintain** its structure/function in the face of disturbance. *Vigour* is associated with the primary **productivity** of an ecosystem. *Organisation* depends on both **complexity and structure** of an ecological or biological system. In this context, natural resource degradation, pollution and loss of biodiversity are detrimental because they increase vulnerability, undermine system health, and reduce resilience (MIND, 2007). The environmental aspects of sustainable development requires a balance (Pearce, 1999:7) between protecting the physical environment and its resources, and using these resources in a way that will allow the earth to continue supporting an acceptable quality of life for human beings (*some would say "all beings"*). To achieve this, the following are some overlapping **principles** (Anon, 2007; Blowfield & Murray, 2008:315) that need to be followed: Protecting the earth's life support systems (air, water, soil); using renewable resources no faster than nature can replenish them; minimising the use of non-renewable resources through the three R's (Reduce, Reuse, and Recycle); marketing of green products; effective natural resource and waste

management; respecting the load capacity of ecosystems and minimising pollution and damage to the environment and health of all living creatures; and instilling environmental awareness in all sectors of society.

– **Social dimension**

Social development usually refers to improvements in both individual well-being and the overall social welfare, that result from increases in *social capital* – typically, the accumulation of capacity for individuals and groups of people to work together to achieve shared objectives. Social capital is the resource which people draw upon in pursuit of their aspirations and is developed through networks and connectedness, membership of more formalised groups and relationships of trust, reciprocity, and exchanges. It includes human capital such as education and skills, as well as cultural capital such as social relationships and customs. The quantity and quality of social interactions, including the level of mutual trust and extent of shared social norms, help to determine the stock of social capital. Trust, power and security are also important elements of cognitive social capital (MIND, 2007). For any development to be sustainable, Welford (*in* Callens & Tyteca, 1999:42) emphasises the need to deal with the issue of **equity**. Equity applies not only to relationships between the First and Third Worlds, but also within countries between people, which, e.g. implies the reduction of unemployment. The social aspects of sustainable development require that we enable the development of fair and just societies that foster positive human development and provide people with opportunities for self-actualisation and an acceptable quality of life. To achieve the above, the following are some **principles** that can be followed: promoting social equality amongst people by discouraging all forms of discrimination (e.g. race, gender, religion, ability and economic status); implement protective strategies that reduce vulnerability and ensure that basic needs are met; allowing for social and cultural integrity by encouraging and enabling cultural continuity within a global society; minimising impacts on local and/or indigenous communities; enhancing human and labour rights; improve working conditions; fostering self-reliance and self-determination; encouraging community participation (especially for vulnerable groups in decisions that affect them), cooperation and ownership in decision-making, governance and development management; improving human health through food security, access to health services and the creation of healthy human settlements; preserving cultural capital and diversity across the globe; poverty alleviation, maintaining societal health and its ability to withstand shocks; encouraging

individual responsibility for the communal good and communal responsibility for the individual good (Blowfield & Murray, 2008:317; Anon, 2007; MIND, 2007).

– ***Economic dimension***

Economic progress is evaluated in terms of welfare (or utility) – measured as ability and willingness to pay for goods and services consumed. Thus, economic policies typically seek to increase conventional gross national product (GNP), and induce more efficient production and consumption of (mainly marketed) goods and services. The stability of prices and employment are among other important objectives. The main idea underlying economic sustainability is to maximise the flow of income that could be generated while at least maintaining the stock of assets (or capital) which yield this income (MIND, 2007). The economic dimension is important because it addresses issues of the depletion of non-renewable resources, global constraints on economic growth, and correct procedures for assigning costs to environmental pollution and other negative impacts currently borne by society as a whole (Pearce, 1999:7). The economic aspects of sustainable development requires the development of an economic system that facilitates equitable access to resources and opportunities and the fair sharing of finite ecologically productive space; enables sustainable livelihoods; and establishes viable businesses and industries based on sound ethical principles. The focus is on creating prosperity for all, not just profits for a few, and to do this within the bounds of the ecologically possible and without infringing on basic human rights. Upholding the following **principles** (Anon, 2007) will help accomplish the above: promoting equity within countries, between nations, and between generations; encouraging ethical business practices such as fair trade; promoting an equitable distribution of true costs and benefits so that one group is not impoverished or otherwise harmed to enrich another; supporting local economies and local job creation through practices such as local economic development and SMEs (small and medium enterprises) development; and measuring business success by the triple bottom line (TBL) of profit.

For a company, success is attained through the achievement of overall organisational objectives without compromising the balance of the relationship between these three dimensions. Businesses are subsequently motivated to adopt a Triple Bottom Line (TBL) approach for different reasons (Mahoney & Potter, 2004:154), such as: defending and improving their reputation against stakeholders; making immediate and tangible financial

gains from sustainable business actions (the traditional business case); better long-term business performance due to broader acceptance and support from society.

2.6 CONCLUSION

The ever expanding CSR universe is filled with a broad variety of overlapping and interrelated concepts. Most of these concepts serve either as the driving forces behind, or as manifestations of the CSR agenda. The concept descriptions and clarifications provided in this chapter, have shown that the main ideas promulgated by each of these concepts (CG, SRI, SE, and SD), are often much the same and at times indivisible. Although they are self-determining and powerful ideas in their own right, these CSR related concepts are usually reciprocally interdependent on one another within business and academic arenas. As a result, concepts such as Corporate Governance (CG), Socially Responsible Investing (SRI), Stakeholder Engagement (SE), and Sustainable Development (SD) all have important roles to play in shaping the contractual relationship between business and society and improving the quality of all human life on the planet. These ideas will continue to help form an understanding of the directions that society will compel business to head into, in order to ensure a balance between the needs of: (1) corporations and their stakeholder groups; as well as between (2) current and future generations.

In terms of this chapter's contribution to the overall objective of this research, the explorations of these concepts (in particular the theoretical dimensions of SD) have been specifically valuable for the development of the different 'profiles' - that can be identified with the use of the Corporate Personality measuring instrument, developed by this study.

Now that some of the most important concepts related to corporate social responsibility have been discussed, the following chapter will be focused on providing an explanation of the CSR concept itself. This will be accomplished by firstly looking at the developments of different definitional constructs of CSR in literature over the years; and secondly by exploring the current theoretical and practical implications of the CSR concept for business and society today.