Measuring the business benefits of corporate responsibility

Whilst many, including McKinsey now argue that responsible behaviour is a strategic issue for firms, many still see being responsible as a discretionary activity which needs to have a business case made for it.

Corporate responsibility is a key issue for modern businesses, whether it is questions about ethical sourcing, pollution and greenhouse gases, responsible hiring practices, responsible marketing or any other issue which may seem to appear as if from nowhere.

Some argue that being responsible is just something businesses should do: it's about being ethical and how business should behave. Generically many arguments have been made for the business benefits from being responsible. Some of these are enhanced reputation with customers, better employee relations and thus more retention and easier hiring of top talent, reduced operating costs and lower business risk. But that argument won't wash with most finance directors.

However, if managers think about corporate responsibility as being like any other business activity then it comes down to a case of prioritising resources, and routine decision-making. There are established ways of making these decisions – so why aren't they used?

How businesses make these decisions is being researched by a team at Cranfield in a study of major companies, supported by the European Academy of Business in Society (and EABiS's founding business partners, IBM, Johnson & Johnson, Microsoft, Shell and Unilever). Cranfield is looking to develop a standard approach that can be used by businesses.

To date much of the research in this field has focused on whether 'good' firms make better returns in the stock markets – but the stock markets are not actually efficient ways of measuring value. Remember the dot-com crash?

A far better way of establishing companies' value is to look at the impacts on future cash flow – this is, after all, how finance directors evaluate capital projects and how stock market analysts assess the value of firms.

Therefore what managers need to do systematically is assess the impact of stakeholders on their firms.

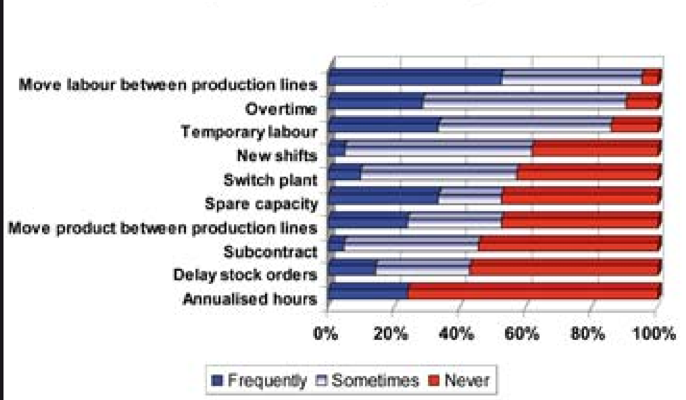
Two-way relationships

When managers think about stakeholders it is often about what stakeholders want from the business – often for the business to stop doing something or to give them money.

Managers do not always evaluate what the business wants from stakeholders – this might be a licence to operate or more loyalty from employees or from customers.

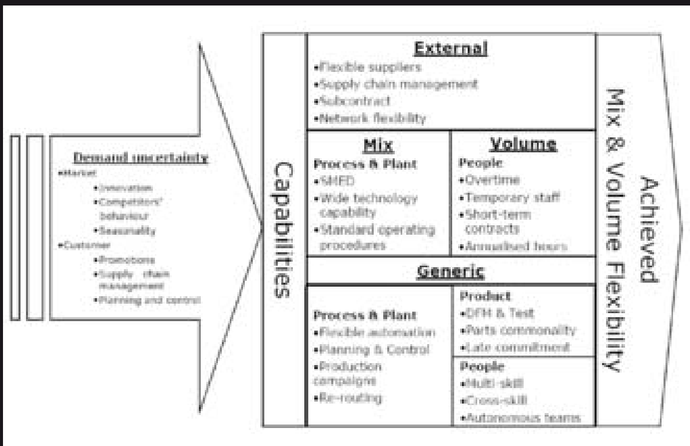
So, for example, in our work with EDF we were looking at the impact of engaging the local community in building a hydro-electric dam and we were able to show that a priority for EDF was for the dam to open on time.

Figure 1. Flexibility Techniques



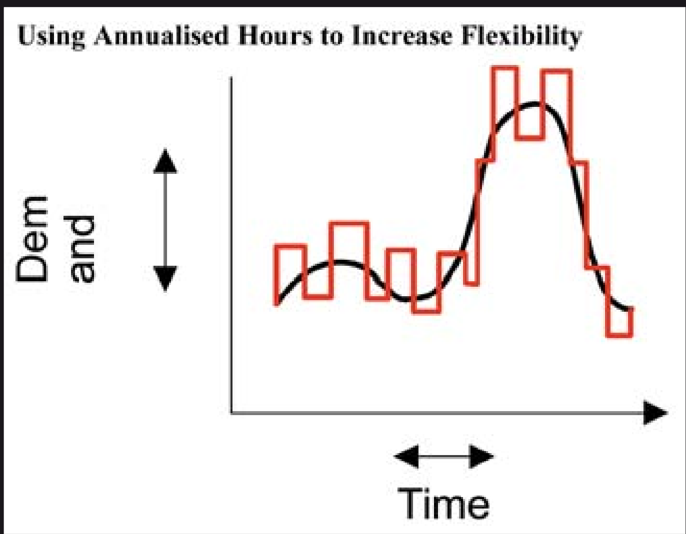
We could then model the risk of delays from protests and put a cost against them. In that context, paying relocation costs and providing other benefits to the local community make sense, and an appropriate budget can be established.

Cranfield will also be working closely with Lloyds TSB and Holcim to develop internal processes.



Box 1 shows the basic idea of mapping how stakeholder issues affect company value by focusing on the seven drivers of shareholder value – most often sales, costs, time and volatility.

But if it's all so simple – what are the problems? We have looked further at the processes involved in making the trade offs, and Box 2 sets out the steps.



Two key steps seem to cause problems. First, the sheer number of stakeholders and their competing issues – we found that this degree of complexity can be reduced by looking at the stakes, rather than the stakeholders. In our dam case, for example, several groups had a common concern – the threat to fish.

The other key problem is prioritising stakes and stakeholders. Different firms go about this in different ways, often mixing issues such as ability to work with the stakeholder, degree of impact and the urgency of the issue. But this, in the end, becomes the key step. Managers need a systematic way to assess priorities and to rank these among competing interests. For example, one firm ranks stakeholders by rating the impact on the stakeholder on a scale of 1-5, the impact of the stakeholder on the firm on a similar scale and then ranking the organisation's capacity to deal with an issue on a similar scale and multiplying the results to give a score out of 125.

An alternative approach is shown in Figure 3 where stakeholders are assessed in two dimensions – stakeholder interest in the firm or issue and then impact of the stakeholder on the firm. What is different in looking at corporate responsibility is that the managers need to look at the long-term impacts of their behaviours towards stakeholders and thus how those stakeholders might or might not be involved with the business in the future.

So, although stakeholders can be prioritised by more or less subjective measures, in the end the financial case has to be made using traditional financial tools. Many firms and managers might think there is little new in this approach and on many levels they would be correct. However this doesn't explain why businesses often fail to take corporate responsibility into account and why so many heads of corporate responsibility in business are looking for metrics to assess the business corporate social performance. The answer, we believe, is simply that senior managers have too limited a perspective on the strategic implications of corporate responsibility and so they fail to see the many benefits that arise from engaged corporate responsibility.

In general, like all managers, those working in the field of corporate responsibility are short of time and money, so putting some discipline into decision-making will help them and help make a robust business case. We believe that what is now needed is the will at senior levels to implement such an approach.

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