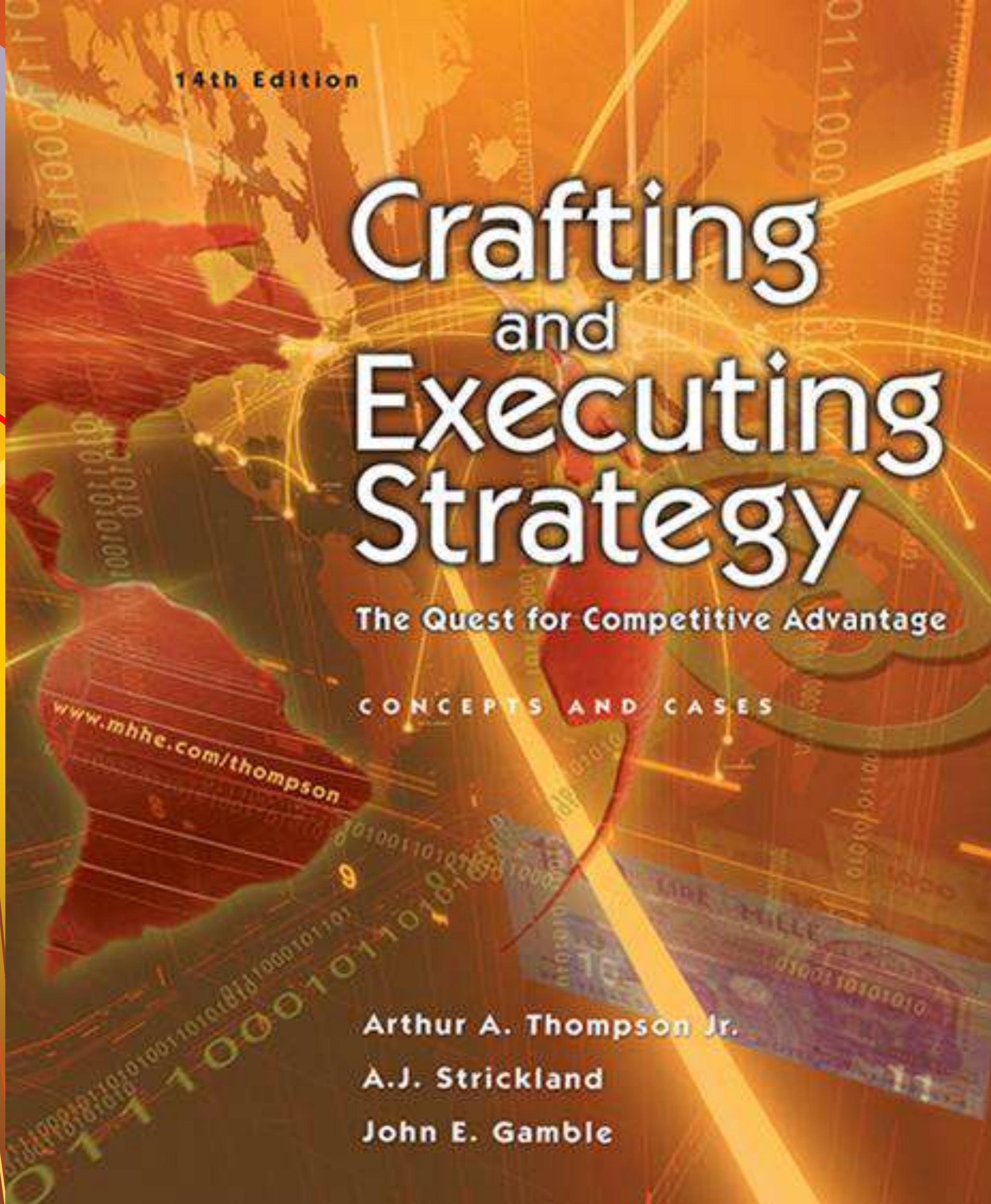
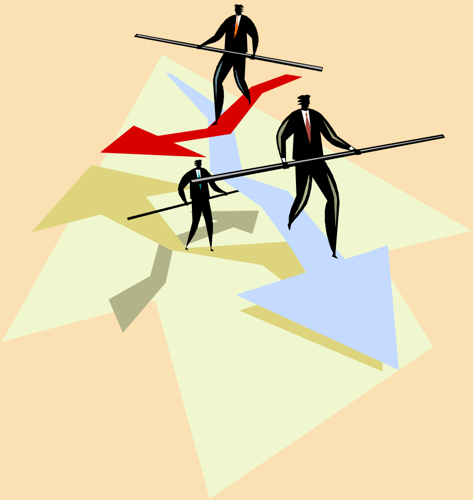

14th Edition
Crafting and Executing Strategy
The Quest for Competitive Advantage
CONCEPTS AND CASES
www.mhhe.com/thompson
Arthur A. Thompson Jr.
A.J. Strickland
John E. Gamble

Chapter

10

Strategy, Ethics, and Social Responsibility

Screen graphics created by:
Jana F. Kuzmicki, Ph.D.
Troy State University-Florida and Western Region



"There is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say engages in free and open competition, without deception or fraud."

Milton Friedman
Nobel Prize-winning economist

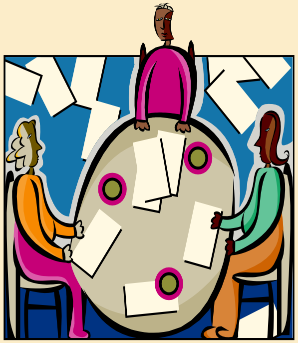
Chapter Roadmap

- **Strategy and Ethics**
- **What Do We Mean by Business Ethics?**
  - **Three Categories of Management Morality**
  - **What Are the Drivers of Unethical Strategies and Business Behavior?**
  - **Business Ethics in the Global Community**
  - **Approaches to Managing a Company's Ethical Conduct**
  - **Why Should Company Strategies Be Ethical?**
  - **Linking a Company's Strategy to its Ethical Principles and Core Values**
- **Strategy and Social Responsibility**
  - **What Do We Mean by Social Responsibility?**
  - **Linking Strategy and Social Responsibility**
  - **The Moral Case for Corporate Social Responsibility**
  - **The Business Case for Socially Responsible Behavior**
  - **The Controversy over Do-Good Executives**
  - **How Much Attention to Social Responsibility Is Enough?**
  - **Linking Social Performance Targets to Executive Compensation**

Linkage of Strategy to Ethics and Social Responsibility

Key Issues

- Should there be a ***link between*** a company's ***efforts*** to ***craft*** and ***execute*** a winning ***strategy*** and its ***duties*** to
  - Conduct activities in an ethical manner?
  - Demonstrate socially responsible behavior by
    - **Being a committed corporate citizen *and***
    - **Attending to needs of non-owner stakeholders?**



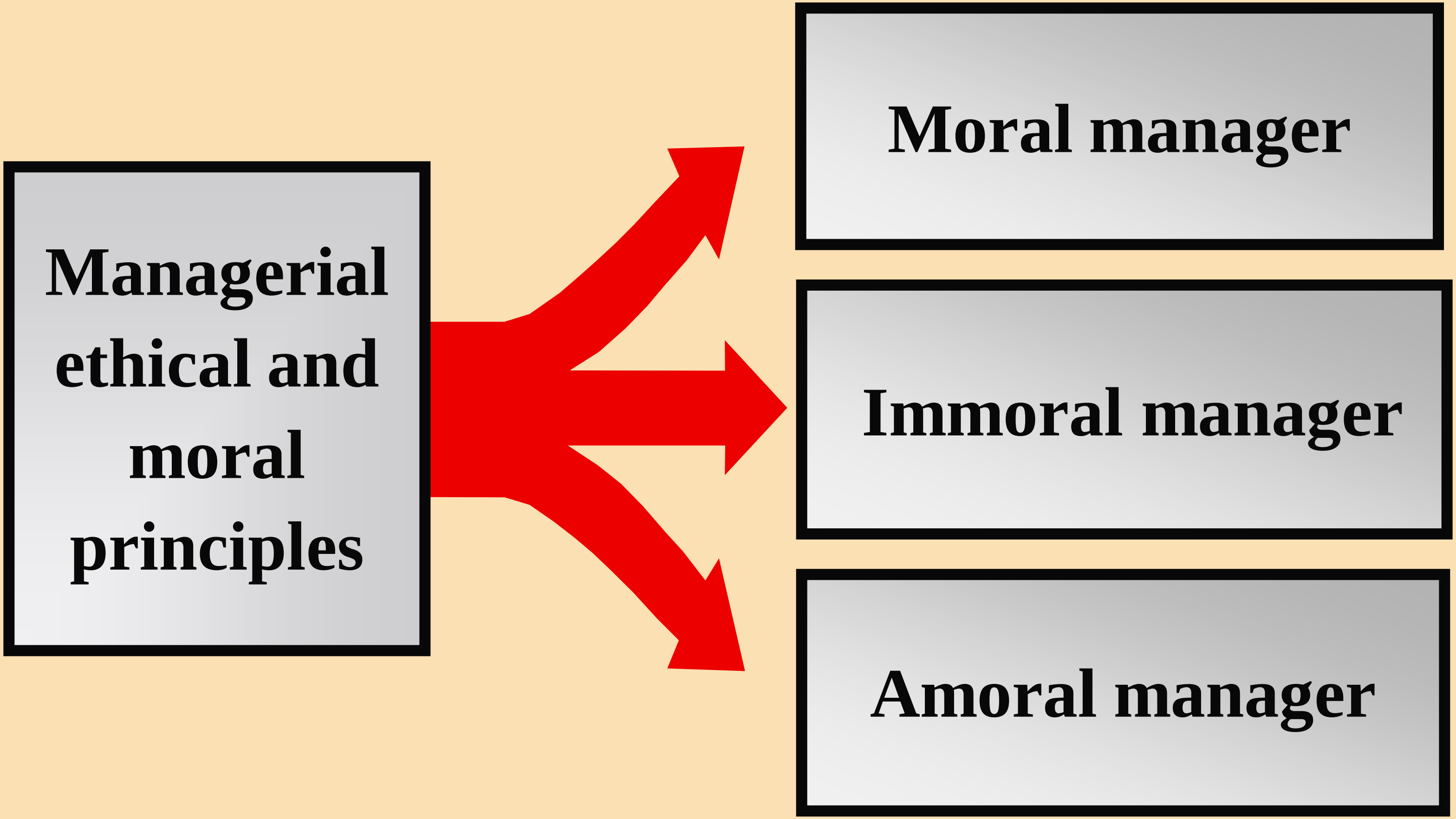
What Are Ethical Principles?

- Involves ***concepts*** of
  - ➔ Right and wrong behaviors
  - ➔ Fair and unfair actions
  - ➔ Moral and immoral behaviors
- ***Examples*** of ***ethical behaviors***
  - ➔ Honesty
  - ➔ Integrity
  - ➔ Keeping one's word
  - ➔ Respecting rights of others
  - ➔ Practicing the Golden Rule
- ***Beliefs*** about what is ***ethical*** serve as a ***moral compass*** to ***guide behaviors*** of individuals and companies

Concept of Business Ethics

- ***Business ethics*** involves applying general ethical principles and standards to business behavior
- ***Ethical principles*** in business are not different from ethical principles in general
- ***Business actions*** are judged by
  - General ethical standards of society
  - Not by more permissive standards

Three Categories of Management Morality



Characteristics of a Moral Manager

- Dedicated to high standards of ethical behavior in
  - Own actions
  - How the company's business is to be conducted
- Considers it important to
  - Be a steward of ethical behavior
  - Demonstrate ethical leadership
- Pursues business success
  - Within confines of both letter and spirit of laws
  - With a habit of operating well above what laws require

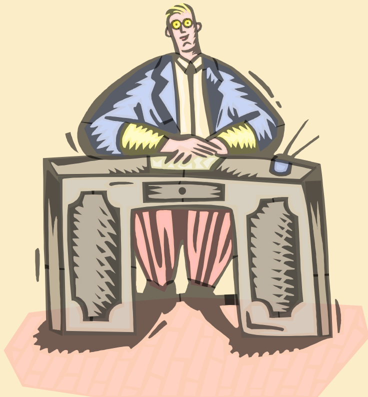
Characteristics of an Immoral Manager

- Actively opposes ethical behavior in business
- Willfully ignores ethical principles in making decisions
- Views legal standards as barriers to overcome
- Pursues own self-interests
- Is an example of capitalistic greed
- Ignores interests of others
- Focuses only on bottom line – making one's numbers
- Will trample on others to avoid being trampled upon

Characteristics of an Intentionally Amoral Manager

- Believes business and ethics should not be mixed since different rules apply to
  - Business activities
  - Other realms of life
- Does not factor ethical considerations into own actions since business activity lies outside sphere of moral judgment
- Views ethics as inappropriate for tough, competitive business world
- Concept of right and wrong is lawyer-driven (what can we get by with without running afoul of the law)

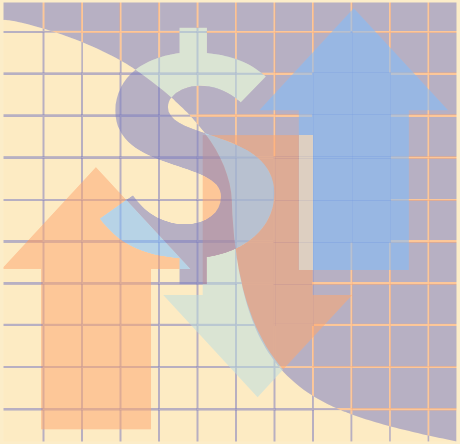
Characteristics of an Unintentionally Amoral Manager



- Is blind to or casual about ethics of decision-making and business actions
- Displays lack of concern regarding whether ethics applies to company actions
- Sees self as well-intentioned or personally ethical
- Typical beliefs
  - ➔ Do what is necessary to comply with laws and regulations
  - ➔ Government provides legal framework stating what society will put up with—if it is not illegal, it is allowed

What Are the Drivers of Unethical Strategies and Business Behavior?

- The large numbers of immoral and amoral business people
- Overzealous pursuit of personal gain, wealth, and other selfish interests
- Heavy pressures on company managers to meet or beat earnings targets
- A company culture that places profits and good performance ahead of ethical behavior



 McGraw-Hill/Irwin

Overzealous Pursuit of Personal Gain, Wealth, and Selfish Interests

- People obsessed with wealth accumulation, greed, power, and status often
  - Push ethical principles aside in their quest for self gain
  - Exhibit few qualms in doing whatever is necessary to achieve their goals
  - Look out for their own best interests
  - Have few scruples and ignore welfare of others
  - Engage in all kinds of unethical strategic maneuvers and behaviors

Heavy Pressures on Company Managers to Meet or Beat Earnings Targets

- Managers often feel enormous *pressure to do whatever it takes* to deliver good financial performance
- Actions often taken by managers
  - Cut costs wherever savings show up immediately
  - Squeeze extra sales out of early deliveries
  - Engage in short-term maneuvers to make the numbers
  - Stretch the rules further and further, until limits of ethical conduct are overlooked
- Executives feel pressure to hit performance targets since their compensation depends heavily on company performance
- Fundamental problem with a "make the numbers" syndrome – Company does not serve its customers or shareholders well by placing top priority on the bottom line

Company Culture Places Profits and Good Performance Ahead of Ethical Behavior

- In an ethically corrupt or amoral work climate, people have a company-approved license to
  - Ignore "what's right"
  - Engage in most any behavior or employ most any strategy they think they can get away with
  - Play down the relevance of ethical strategic actions and business conduct

- Pressures to conform to the norms of the corporate culture can prompt otherwise honorable people to
  - Make ethical mistakes
  - Succumb to the many opportunities around them to engage in unethical practices

Business Ethics in the Global Community

- Notions of right and wrong, fair and unfair, moral and immoral, ethical and unethical exist in all societies
- Two schools of thought
  - ➔ ***Ethical universalism***
    - **Holds that human nature is the same everywhere and ethical rules are cross-cultural**
  - ➔ ***Ethical relativism***
    - **Holds that different societal cultures and customs give rise to divergent values and ethical principles of right and wrong**

Cross-Culture Variability in Ethical Standards

- Apart from *certain universal basics* –
  - Honesty
  - Trustworthiness
  - Fairness
  - Avoiding unnecessary harm
  - Respecting the environment –

  variations exist in what societies generally agree to be *right and wrong* in the *conduct of business activities*

- *Factors affecting cross-cultural variability*
  - Religious beliefs
  - Historic traditions
  - Social customs
  - Prevailing political and economic doctrines
- *Cross-country variations* also exist in the *degree* to which certain *behaviors* are *considered unethical*

Ethical vs. Unethical Conduct

- What constitutes ethical or unethical conduct can vary according to
  - Time
  - Circumstance
  - Local cultural norms
  - Religion

- Thus, no objective way exists to prove that some cultures are correct and others wrong about proper business ethics
- ***Therefore, there is merit in the ethical relativism view that proper business ethics has to be viewed in the context of each country's societal norms***

Payment of Bribes and Kickbacks

- A thorny ethical problems is faced by multinational companies
  - Degree of cross-country variability in paying bribes as part of business transactions
- Companies forbidding payment of bribes in their codes of ethics face a formidable challenge in countries where payments are entrenched as a local custom

- Foreign Corrupt Practices Act prohibits U.S. companies from paying bribes in all countries where they do business

 McGraw-Hill/Irwin

table 10.1 **Perceived Degree of Governmental Corruption in Selected Countries, as Measured by a Composite Corruption Perceptions Index (CPI), 2002** (A CPI Score of 10 is "highly clean" and a score of 0 is "highly corrupt.")

Country	2002 CPI Score*	90% Confidence Range	Number of Surveys Used
Finland	9.7	9.5–9.9	8
Denmark	9.5	9.3–9.7	8
New Zealand	9.5	9.3–9.6	8
Sweden	9.3	9.2–9.4	10
Canada	9.0	8.9–9.2	10
Netherlands	9.0	8.8–9.1	9
Great Britain	8.7	8.4–8.9	11
Australia	8.6	8.0–9.0	11
Norway	8.5	8.0–8.9	8
Switzerland	8.5	7.9–8.9	9
Hong Kong	8.2	7.8–8.6	11
United States	7.7	7.2–8.0	12
Chile	7.5	7.0–7.9	10
Germany	7.3	6.7–7.7	10
Israel	7.3	6.7–7.7	9
Japan	7.1	6.6–7.4	12
Spain	7.1	6.5–7.6	10
France	6.3	5.9–6.8	10
Italy	5.2	4.6–5.7	11
Uruguay	5.1	4.6–5.6	5
Malaysia	4.9	4.6–5.2	11
South Africa	4.8	4.5–5.0	11
South Korea	4.5	3.9–5.1	12
Brazil	4.0	3.8–4.2	10
Peru	4.0	3.7–4.4	7
Czech Republic	3.7	3.3–4.2	10
Mexico	3.6	3.3–3.9	10
China	3.5	3.1–4.1	11
Argentina	2.7	2.5–3.1	10
India	2.7	2.5–2.9	12
Russia	2.7	2.3–3.3	12
Pakistan	2.6	1.7–3.3	3
Philippines	2.6	2.4–2.9	11
Vietnam	2.4	2.0–2.9	7
Indonesia	1.9	1.7–2.2	12
Kenya	1.9	1.7–2.2	5
Paraguay	1.7	1.5–1.8	3
Bangladesh	1.2	0.7–1.6	5

**Note:* The CPI score ranges between 10 (highly clean) and 0 (highly corrupt); the data were collected between 2000 and 2002 and represent a composite of multiple sources, as indicated in the number of surveys used. The CPI represents the perceptions of well-informed people regarding the frequency of corrupt payments, the value of bribes paid, and the resulting obstacles to businesses.

Source: Transparency International, *2003 Global Corruption Report*, www.globalcorruptionreport.org, accessed October 1, 2003, pp. 265–66.

table 10.2 **The Degree to Which Companies in Major Exporting Countries Are Perceived to Be Paying Bribes in Doing Business Abroad**

Rank/ Country	Bribe Payer Index (10 = low; 0 = high)	Rank/ Country	Bribe Payer Index (10 = low; 0 = high)
1. Australia	8.5	12. France	5.5
2. Sweden	8.4	13. United States	5.3
3. Switzerland	8.4	14. Japan	5.3
4. Austria	8.2	15. Malaysia	4.3
5. Canada	8.1	16. Hong Kong	4.3
6. Netherlands	7.8	17. Italy	4.1
7. Belgium	7.8	18. South Korea	3.9
8. Britain	6.9	19. Taiwan	3.8
9. Singapore	6.3	20. China (excluding Hong Kong)	3.5
10. Germany	6.3	21. Russia	3.2
11. Spain	5.8		

Note: The Bribe Payers Index is based on a questionnaire developed by Transparency International and a survey of some 835 private sector leaders in 15 emerging countries accounting for 60 percent of all imports into non–Organization for Economic Cooperation and Development countries—actual polling was conducted by Gallup International.

Source: Transparency International, *2003 Global Corruption Report*, www.globalcorruptionreport.org, accessed October 1, 2003, p. 267.

table 10.3 Bribery in Different Industries

Business Sector	Bribery Score (10 = low bribery; 0 = high bribery)
Agriculture	5.9
Light manufacturing	5.9
Fisheries	5.9
Information technology	5.1
Forestry	5.1
Civilian aerospace	4.9
Banking and finance	4.7
Heavy manufacturing	4.5
Pharmaceuticals/medical care	4.3
Transportation/storage	4.3
Mining	4.0
Power generation/transmission	3.7
Telecommunications	3.7
Real estate/property	3.5
Oil and gas	2.7
Arms and defense	1.9
Public works/construction	1.3

Note: The bribery scores for each industry are based on a questionnaire developed by Transparency International and a survey of some 835 private sector leaders in 15 emerging countries accounting for 60 percent of all imports into non–Organization for Economic Cooperation and Development countries—actual polling was conducted by Gallup International.

Source: Transparency International, *2003 Global Corruption Report*, www.globalcorruption-report.org, accessed October 1, 2003, p. 268.

Approaches to Managing a Company's Ethical Conduct

Unconcerned or non-issue approach

Damage control approach

Compliance approach

Ethical culture approach

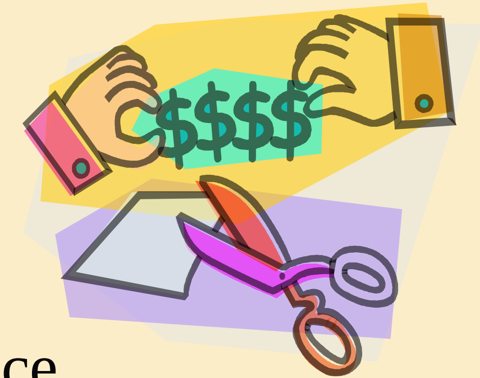
table 10.4 **Four Approaches to Managing Business Ethics**

	Unconcerned Approach	Damage Control Approach	Compliance Approach	Ethical Culture Approach
Underlying beliefs	• The business of business is business, not ethics. • Ethics has no place in the conduct of business. • Companies should not be morally accountable for their actions.	• Need to make a token gesture in the direction of ethical standards (a code of ethics).	• Company must be committed to ethical standards and monitoring ethics performance. • Unethical behavior must be prevented and punished if discovered. • A reputation for high ethical standards is important.	• Ethics is basic to the culture. • Behaving ethically must be a deeply held corporate value and become a way of life. • Everyone is expected to walk the talk.
Means of dealing with ethics issues	• There's no need to make decisions concerning business ethics—if it's legal, it is okay. • No intervention regarding the ethical component of decisions is needed.	• Act to protect the company against the dangers of unethical strategies and behavior. • Ignore unethical behavior or allow it to go unpunished unless the situation is extreme and requires action.	• Establish a clear, comprehensive code of ethics. • Prevent unethical behavior. • Provide ethics training for all personnel. • The company has an ethics compliance office, a chief ethics officer, and formal ethics compliance procedures.	• Ethical behavior is ingrained and reinforced as part of the culture. • Rely on coworker peer pressure—"That's not how we do things here." • Everyone is an ethics watchdog—whistle-blowing is required. • Ethics heroes are celebrated; ethics stories are told.
Challenges in trying to make the approach work	• Financial consequences can become unaffordable. • Some stakeholders are alienated.	• Credibility problems with stakeholders can arise. • The company is susceptible to ethical scandal. • The company has a subpar ethical reputation—executives don't walk the talk.	• Organization members come to rely on the existing rules for moral guidance—fosters a mentality of what is not forbidden is allowed. • Rules and guidelines proliferate. • The locus of moral control resides in the code and in the ethics compliance system rather than in an individual's own moral responsibility for ethical behavior.	• New employees must receive an ethics induction. • Formal ethics management systems receive less emphasis. • Relying on peer pressures and cultural norms to enforce ethical standards can result in eliminating some or many of the compliance trappings and, over time, induce moral laxness.

Source: Adapted from Gedeon J. Rossouw and Leon J. van Vuuren, "Modes of Managing Morality: A Descriptive Model of Strategies for Managing Ethics," *Journal of Business Ethics* 46, no. 4 (September 2003), pp. 392–93. Reprinted with kind permission of Kluwer Academic Publishers.

Characteristics of Unconcerned Approach

- Prevalent at companies whose executives are immoral and unintentionally amoral
- Business ethics is an oxymoron in a survival-of-the-fittest world
- The business of business is business, not ethics
- If the law permits "unethical behavior," why stand on ethical principles
- Companies are usually out to make greatest possible profit at most any cost
- Strategies used, while legal, may embrace elements that are ethically shady



Characteristics of Damage Control Approach

- Favored at companies whose managers are intentionally amoral but who fear scandal
- Managers are desirous of containing any adverse fallout from claims the company's strategy has unethical components
- Companies often make some concession to window-dressing ethics and may adopt a code of ethics
- Managers may opt to incorporate unethical elements in the company's strategy as long as the elements can be explained away
- Executives may look the other way when shady behavior occurs

Characteristics of Compliance Approach

- From light to forceful compliance is favored at companies whose managers
  - Lean toward being somewhat amoral but are highly concerned about having ethically upstanding reputations *or*
  - Are moral and see strong compliance methods as best way to impose and enforce high ethical standards
- Emphasis is on securing broad compliance and measuring degree to which ethical standards are upheld

- Driving force behind commitment to eradicate unethical behavior stems from a desire to
  - Avoid cost and damage associated with unethical conduct *or*
  - Gain favor from stakeholders from having a highly regarded reputation for ethical behavior

Actions Taken With a Compliance Approach

- Make code of ethics a visible and regular part of communications with employees
- Implement ethics training programs
- Appoint a chief ethics officer
- Have ethics committees to give guidance on ethics matters
- Institute formal procedures for investigating alleged ethics violations
- Conduct ethics audits to measure and document compliance
- Give ethics awards to employees for outstanding efforts to create an ethical climate
- Install ethics hotlines to help detect and deter violations

Characteristics of Ethical Culture Approach

- **Top executives believe high ethical principles must**
  - Be deeply ingrained in the corporate culture
  - Function as guides for "how we do things around here"
- **Company seeks to gain employee buy-in to**
  - Company's ethical standards
  - Business principles
  - Corporate values

- **Ethical principles in company's code of ethics are**
  - Integral to day-to-day operations
  - Promoted as "business as usual"
- **Strategy must be ethical**
- **Employees must display ethical behaviors in executing the strategy**

Why Should Company Strategies Be Ethical?

- An ***unethical strategy***
  - Is morally wrong
  - Reflects badly on the character of company personnel
- An ***ethical strategy*** is
  - Good business
  - In the self-interest of shareholders

Linking Strategy With Ethics

- If ethical standards are to have more than a cosmetic role, boards of directors and top executives must work diligently to see they are scrupulously observed in
  - Crafting the company's strategy and
  - Conducting every facet of the company's business
- Two sets of questions must be considered by senior executives when a new strategic initiative is under review
  - Is what we are proposing to do fully compliant with our code of ethical conduct? Is there anything here that could be considered ethically objectionable?
  - Is it apparent this proposed action is in harmony with our core values? Are any conflicts or concerns evident?

What Is Corporate Social Responsibility?

- Notion that corporate executives should ***balance interests*** of ***all stakeholders*** began to blossom in the 1960s
- ***Social responsibility*** as it applies to businesses concerns a company's ***duty*** to
  - Operate by means that avoid harm to
    - **Stakeholders**
    - **Environment**
  - Consider the overall betterment of society in its
    - **Decisions**
    - **Actions**

What Is Socially Responsible Business Behavior?

- A company should strive to ***balance benefits*** of ***strategic actions*** to
  - **Benefit shareholders against any possible adverse impacts on other stakeholders**
  - **Proactively mitigate any harmful effects on the environment that its actions and business may have**
- ***Socially responsible behaviors*** include
  - **Corporate philanthropy**
  - **Actions to earn the trust and respect of stakeholders for a firm's efforts to improve the general well-being of**
    - **Customers**
    - **Employees**
    - **Local communities**
    - **Society**
    - **Environment**

Fig. 10.1: Categories of Socially Responsible Business Behavior

Linking Strategy and Social Responsibility

- Management should ***match*** a company's ***social responsibility strategy*** to its
  - **Core values**
  - **Business mission**
  - **Overall strategy**

- The ***combination*** of ***socially responsible endeavors*** a company elects to pursue ***defines*** its ***social responsibility strategy***
- Some companies are ***integrating social responsibility objectives*** into their
  - **Missions**
  - **Performance targets**
  - **Strategies**

The Moral Case for Corporate Social Responsibility

- Businesses should promote the betterment of society, acting in ways to benefit all their stakeholders because
  - ➔ ***It's the right thing to do!***

- Based on an implied ***social contract,*** society
  - ➔ Grants a business the right to conduct its business affairs
  - ➔ Agrees not to unreasonably restrain a business' pursuit of a fair profit
- In return for a ***"license to operate,"*** a business should
  - ➔ Act as a responsible citizen
  - ➔ Do its fair share to promote the general welfare

Reasons to Behave in a Socially Responsible Manner

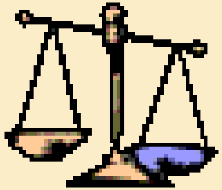
- Generates internal benefits
  - ➔ Enhances recruitment of quality employees
  - ➔ Increases retention of employees
  - ➔ Improves employee productivity
  - ➔ Lowers costs of recruitment and trainings

- Reduces risk of reputation-damaging incidents, leading to increased buyer patronage
- Works in best interest of shareholders
  - ➔ Minimizes costly legal and regulatory actions
  - ➔ Provides for increased investments by socially conscious mutual funds and pension benefit managers
  - ➔ Focusing on environment issues may enhance earnings

Do We Really Want Do-Good Executives?

- At least 4 different views exist regarding use of company resources in pursuit of a better world and the efforts of "do-good" executives
  1. Any money authorized for social responsibility initiatives is theft from a company's shareholders
  2. Caution should be exercised in pursuing various societal obligations since this
     - Diverts valuable resources
     - Weakens a company's competitiveness
  3. Social responsibilities are best satisfied through conventional business activities (doing what businesses are supposed to do, which does not include social engineering)
  4. Spending money for social causes
     - Muddies decision making by diluting focus on a company's business mission
     - Thrusts executives into role of social engineers

How Much Attention to Social Responsibility Is Enough?



- What is the ***appropriate balance*** between
  - ***Creating value*** for shareholders?
  - ***Obligation to contribute*** to the larger social good?
- What ***fraction*** of a firm's ***resources*** ought to be aimed at
  - Addressing ***social concerns?***
  - Bettering the ***well-being*** of ***society*** and the ***environment?***
- ***Approaches*** to ***fund*** a ***social responsibility strategy can***
  - Allocate a specified percentage of profits
  - Avoid committing a specified percentage of profits

No widely *accepted standard* for *judging* if a company has *fulfilled* its *citizenship responsibilities* exits!