

# Creating a Virtue Matrix Strategy

## The Challenge

The world's large corporations face a particularly challenging time as they deal with unrelenting pressure to show more corporate social responsibility (CSR). The media often attack corporations for slips in their behaviour, consumers are showing an increased willingness to punish corporations they think are not being socially responsible, and employees are less inclined to work for corporations they believe are not socially responsible.

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**There is no widely accepted standard for corporate social responsibility performance.**

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The tricky and frustrating challenge for corporations on the receiving end of these escalating expectations is that CSR covers an incredibly wide sphere of activity. To be socially responsible, corporations are asked to:

- Adhere to strict standards of governance and business morality;
- Protect and steward the environment in which they operate;
- Ensure the emotional, physical and financial health of their employees; and
- Contribute to the health, education, well-being and prosperity of the communities in which they operate.

On top of this challenge, the standard required for being considered socially responsible in each of these diverse areas is ambiguous, at best. There is no widely accepted standard for CSR performance. Some standards, such as the United Nations-sponsored Global Compact or the Global Reporting Initiative, are emerging. However, no single performance standard has gained anything close to broad acceptance, and there is certainly no widespread understanding of what CSR really means.

Finally, the commentators, customers and employees calling for corporate social responsibility have little or no advice for the corporations as to how they should trade off earning returns for their shareholders against performing acceptably well across this wide spectrum of social areas. They just want social responsibility from their corporations—whatever that may mean—and less than acceptable performance will be punished. Whether we are talking about the case of Royal Dutch Shell after the Brent Spar incident, or Nike in the wake of Asian sweatshop allegations or Arthur Andersen after the Enron scandal, the punishment can be harsh indeed.

Because the CSR universe is broad, the standards high (yet ambiguously defined), and the economics mysterious, it is extremely difficult for a corporation to rebut an allegation that it is being socially irresponsible. When Wal-Mart is assailed for allegedly engaging in sexually discriminatory employee practices, it is difficult for the company to defend itself as being socially responsible throughout its activities. Commentators, customers and employees tend to ascribe overall irresponsibility to Wal-Mart, whether rightly or wrongly, based on this one issue.

Corporations need a way of anticipating and being prepared for CSR issues, or they risk either falling irretrievably behind or failing to earn the appropriate rewards for their investment in CSR—or both. Corporations need a tool for thinking about CSR and a process for developing a comprehensive CSR strategy that can be carried out throughout the corporation and communicated to the outside world.

Defensively, such a tool and process would enable a corporation that is being attacked for apparent under-performance in some aspect of CSR (e.g., contributing

to local educational institutions) to argue, compellingly, that its low commitment to school funding is by design. It could explain that it is investing heavily in several other CSR categories because those alternative areas are where the corporation has the capacity to create proportionately more social value. Offensively, the tool and process would enable a corporation to promote itself legitimately to customers, employees and other stakeholders, as a corporation that is committed to high standards of CSR.

## The Virtue Matrix Tool

A corporation can use the Virtue Matrix as a tool to assess its own performance and to develop a CSR strategy. The Virtue Matrix consists of four quadrants (Exhibit 1) and provides a framework for evaluating civil, governmental and stakeholder claims, while encouraging business leaders to be as innovative in enriching society as they are in increasing wealth for their shareholders.

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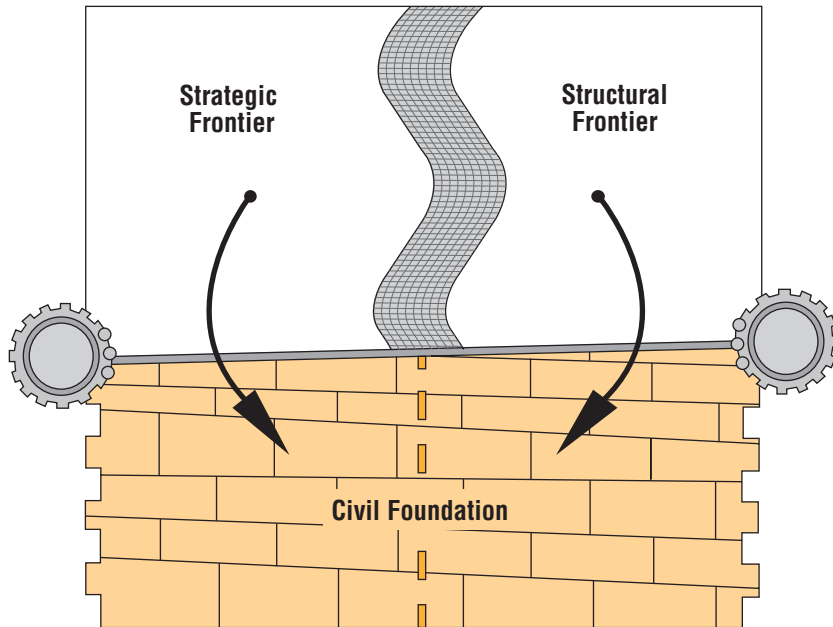
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The bottom pair of quadrants makes up the *Civil Foundation*, which is a depiction of the historical development of the laws, regulations, norms and behaviours that underpin our civil society.

The right quadrant, *Civil Foundation—Compliance*, is the accumulation of laws and regulations with which corporations must comply. For example, a corporation that chooses to discriminate on the basis of age, gender, religion or sexual preference risks being fined or prevented from continuing to operate. These laws and regulations

## Exhibit 1—The Virtue Matrix



tend to build up over time, as the economy advances. In developed economies, the legal and regulatory environment tends to be deep and robust, while it is often fragile in less developed nations.

In the lower left quadrant, *Civil Foundation—Choice*, are the customs and norms to which corporations tend to adhere by choice, rather than by fiat. Lack of adherence to the customs and norms in an industry or economy can result in a corporation being ostracized from others in the industry, experiencing lower customer loyalty, or having greater difficulty in attracting and retaining employees. For example, in some cities and industries, it is a norm for corporations to give 1–5 per cent of pre-tax profits to charity and, in doing so, become a member of “The One Per Cent Club.”

The top left quadrant, the *Strategic Frontier*, encompasses activities for which motivation is intrinsic (i.e., it feels like the right thing to do) and whose impact on shareholder value at the time the activity is launched is ambiguous. In this case, however, the activity, once established,

produces sufficiently positive reactions from customers, employees or other stakeholders to make it a positive contributor to shareholder value creation. The introduction of environmentally friendly beauty-care products by The Body Shop is an example of an intrinsically motivated action that achieved economic success far beyond what might have been anticipated.

**The Virtue Matrix is a dynamic model, in that actions in the *Frontiers* tend to migrate into the *Civil Foundation* over time.**

The upper right quadrant, the *Structural Frontier*, houses activities that are both intrinsically motivated and contrary to the interests of shareholders. The benefits of corporate conduct in this quadrant accrue principally to society (i.e., there are substantial externalities) rather than to corporations, creating a fundamental barrier to corporate action. The most effective weapon against inertia in the *Structural Frontier* is collective action among corporations, governments and non-governmental

organizations. One example is the voluntary coalition of the world’s five dominant cement manufacturers, led by Holcim Limited, to reduce the industry’s disproportionately high carbon dioxide emissions.

The Virtue Matrix is a dynamic model, in that actions in the *Frontiers* tend to migrate into the *Civil Foundation* over time. Successful actions in the *Strategic Frontier* tend to be copied by the innovator’s competitors and become a norm in the industry in question and hence part of the *Civil Foundation—Choice*. The Body Shop achieved effectiveness far beyond its own walls when competitors realized that they needed to copy the company’s environmentally conscious actions or risk losing a painfully large share of their beauty business. Collective actions in the *Structural Frontier* tend to be enshrined in laws and regulations, becoming part of the *Civil Foundation—Compliance*. For example, the Kyoto Accord is in the process of migrating from an initiative by numerous parties in the *Structural Frontier* to a legally binding agreement in the *Civil Foundation*.

A corporation with a great commitment to social responsibility will have a Virtue Matrix strategy that has the following four features:

1. It puts mechanisms in place to ensure that it is in strict compliance with the letter and spirit of all laws and regulations in the *Civil Foundation—Compliance*;
2. It takes the lead in adopting the norms and conventions of its industry, rather than being a laggard in the *Civil Foundation—Choice*;
3. It has several chosen *Strategic Frontier* projects underway that are of particular relevance to its own stakeholders across the spectrum of CSR areas; and
4. It is leading several chosen *Structural Frontier* projects, for which it actively builds coalitions for change and overcomes the externalities associated with these new initiatives.

A corporation with a great commitment to social responsibility has internal processes for choosing its focus areas, invests prudently in projects to overcome deficits in the *Civil Foundation* and breaks new ground in the *Strategic* and *Structural Frontiers*. When asked why it doesn't do *x* or *y*, it can explain authoritatively that *x* and *y* are not its CSR focus areas, but *a*, *b* and *c* are its three chosen activities, and why these are more critical to pursue than *x* or *y*.

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**To develop a Virtue Matrix strategy, a corporation first needs to perform a CSR assessment by working through the quadrants.**

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### The Virtue Matrix Assessment

To develop a Virtue Matrix strategy, a corporation first needs to perform a CSR assessment by working through the Virtue Matrix quadrants clockwise, from the lower right.

#### CIVIL FOUNDATION—COMPLIANCE

The key issue for this quadrant is: Is the corporation now, or does it wish to be, in full compliance with all the laws and regulations pertaining to its jurisdiction and its industry? In order to assess its performance in the *Compliance* quadrant, the corporation should ask itself the following questions:

- What are all the laws and regulations pertaining to important CSR areas such as business standards, environmental protection, employee relations and community support that apply to the corporation?
- To what extent does the corporation seek to be in full compliance with each of the above laws and regulations?
- How does the corporation ensure that it meets all laws and regulations?
- How does/can the corporation demonstrate and communicate compliance?

The goal of the assessment in this quadrant is to come to a conclusion as to:

- The two to three priorities for overcoming compliance issues that prevent the corporation from being in 100 per cent compliance; and
- Any new processes required for ensuring 100 per cent compliance on an ongoing basis.

#### CIVIL FOUNDATION—CHOICE

The key issue for this quadrant is: To what extent does the corporation wish to be a leader or a laggard, in adhering to the norms and customs in its jurisdiction and its industry? In order to assess its performance in this quadrant, the corporation should ask itself the following questions:

- What are the industry's norms and customs in all the important CSR areas?
- Who is the leader in setting norms in the industry, as demonstrated by above-average commitment and a comprehensive action plan?
- To what extent is the corporation a leader or a laggard in adopting norms?
- How does the corporation choose to adopt norms that emerge in the industry? Does it look to a leader inside the industry? Does it look outside the industry?

The goal of the assessment in this quadrant is to come to a conclusion as to:

- The corporation's goal with respect to the *Civil Foundation—Choice*:
  - industry leader in adopting new norms and conventions;
  - “fast follower”; or
  - some other goal;
- The two to three initiatives that would be most important (to stakeholders) to upgrade performance in adopting norms and conventions; and
- The new processes required to ensure adherence on an ongoing basis at the level of the stated goals.

#### STRATEGIC FRONTIER

The key issue for this quadrant is: What are the greatest opportunities in all the primary CSR areas in which the corporation could create great value for customers or employees by taking bold action of a sort that has never been taken before? In order to assess opportunities in this quadrant, the corporation should ask itself the following questions:

- How does the organization pursue and develop proposals for innovative activity in the *Strategic Frontier*?
- What activities that the corporation's customers, employers, shareholders or suppliers want could the corporation provide, if it chose to do so?
- What are the impediments to putting such practices into action?
- What could be the business case for undertaking such practices?

The goal of the assessment in this quadrant is to come to a conclusion as to:

- The corporation's goal, with respect to the *Strategic Frontier*:
  - to be known inside and beyond the industry for making periodic breakthroughs that lead to the establishment of new conventions;
  - being seen as a “fast follower”; or
  - some other goal;
- The two to three innovative initiatives in the *Strategic Frontier* that would be most important to stakeholders; and
- A plausible action plan for each initiative.

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**A key issue is: To what extent does the corporation wish to be a leader or a laggard, in adhering to the norms and customs in its jurisdiction and its industry?**

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#### STRUCTURAL FRONTIER

The key issue for this quadrant is: How can we determine the areas in which there is a compelling need for customers, employees or society that cannot be tackled alone because of the great externalities, but

in which the corporation could play an initiating role in creating a coalition for action? In order to assess opportunities in this quadrant, the corporation should ask itself the following questions:

- What practices desired by customers/ employees/shareholders/stakeholders would require collective action among corporations in the industry in order to make them happen?
- How could a coalition of interested corporations be pulled together for each potential practice?
- What governmental/non-governmental organizations might the corporation include in a coalition?

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**The corporation will be well-positioned to fend off attacks from single-issue CSR critics.**

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The goal of the assessment in this quadrant is to come to a conclusion as to:

- The corporation's goal, with respect to the *Structural Frontier*:
  - to be known inside and beyond the industry as an instigator in creating coalitions for breakthroughs in CSR areas fraught with externalities in cases where individual action by one firm is insufficient;
  - being seen as a “fast follower”; or
  - some other goal;
- The two to three new initiatives in the *Structural Frontier* that would be most important to stakeholders; and
- A plausible action plan for each of the priority initiatives, including the structure and composition of the coalitions that would need to be built.

## Virtue Matrix Strategy

The corporation's Virtue Matrix Strategy pulls together the assessment from each of the four quadrants to produce a comprehensive strategy as follows:

- The corporation's goal, with respect to the overall Virtue Matrix:
    - to be known for being 100 per cent compliant, leading adherence to norms and conventions, being an innovator in the *Strategic Frontier* and an instigator of coalitions in the *Structural Frontier*; or
    - to be as compliant as necessary without getting into trouble, a “fast follower” on new norms and conventions, and able to avoid the risks associated with the *Frontiers*; or
    - some combination of these two categories;
  - The top five initiatives that warrant the most urgent action, drawn from the 8 to 12 highest priority initiatives across the four quadrants;
  - A comprehensive action plan for each of the five priority initiatives; and
  - A plan for communicating the corporation's overall Virtue Matrix Strategy and its individual initiatives.
- With such a Virtue Matrix Strategy in place and well-communicated, the corporation will be well-positioned to fend off attacks from single-issue CSR critics who say: “Why aren't you doing the following for society? You would, if you were a responsible corporation.”

Rather than responding defensively, as many corporations do today, the company would be able to answer thoroughly and confidently any questions about what it is doing and why. The company could outline the reasons why that strategy makes the most sense for both the corporation and society. And it would be more likely not to be asked the question in the first place, because its commitment to CSR as well as to shareholders would be evident from the execution and communication of its Virtue Matrix Strategy.



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*Roger Martin is Dean of the Rotman School of Management at the University of Toronto and Academic Director of the AIC Institute for Corporate Citizenship. The Institute was created in late 2004 with the generous support of AIC Limited's Chairman and CEO, Michael Lee-Chin; its purpose is to help current and future business leaders integrate corporate citizenship into their business strategies and practices by creating and disseminating a robust, actionable decision-making model.*

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