OVERCOMING THE CEO's DILEMMA

Doing 'good' versus doing 'well'

By Alison Kemper & Roger Martin

Forty years ago, the American economist and thinker, Milton Friedman, took the position that corporations cannot be socially responsible, only people can. The corporate executive's primary responsibility is to create the most profit while following the 'basic rules of society'. He/she can be socially responsible at home.

In this article, **Roger Martin** *and* **Alison Kemper** *disagree, arguing that it is impossible to isolate CEOs from their values. But how can they do 'good' and 'well' at the same time?*

Since 1970, when the *New York Times Magazine* published Milton Friedman's *The Social Responsibility of Business is to Increase Profits*, the top executives of firms have had diminishing licence to steer companies towards their personal ethical goals. While, in earlier and simpler years, the reputations of CEOs and their firms were inextricably linked, Friedman sought to untie the connections between the management of public companies and the moral preferences of their managers.

His argument, that executives are to increase profits and that the shareholders could distribute their dividends and capital gains to any charity or cause they pleased, was ultimately persuasive in North America and had considerable influence in the UK and beyond. While corporate leaders are obliged to commit fully their minds and attention to their firm and to remain firmly tethered to their BlackBerrys, they heed their consciences in their own time.

Isolating CEOs from their values is simply not possible: our values drive our decision-making, and CEO values drive executive decisions. For example, Finkelstein, Cannella and Hambrick, three eminent scholars in the field of organisational behaviour, use a model that puts the CEO's values in the forefront of all decision-making and strategic leadership. Friedman may have had a valid economic argument, but his view of leadership was extremely limited. Further, the value of an executive's capacity to make good decisions about complex problems has been overtaken by the value of his or her ability to create and use financial models. While this is a great way to make many business decisions, it leaves CEOs wondering how to estimate the net present value of cleaner rivers or literate overseas factory workers. While CEOs are human beings who often care deeply about environmental and social issues, there's no easy way to bring them into firm decision-making.

Over the last 20 years, business academics have attempted to reintroduce social issues into managerial decision-making in two ways. First, they characterise inaction as a risk. If firms continue to externalise their costs by dumping pollution into the air or water, they incur concomitant reputational and legal risks. Second, they seek to establish that financial rewards follow good deeds. These arguments convince those who are willing to be convinced. For others, environmental insurance, reputation management and green marketing strategies appear to be

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suitable substitutes. For savvy managers, the relationship between doing good and doing well is not obvious. Without using this commonplace algorithm of virtue, how can CEOs legitimately address CSR issues?

THE VIRTUE MATRIX

Roger Martin's 2002 article, *The Virtue Matrix*, delineates four types of corporate social responsibility dilemmas and the kinds of strategic responses each demands. None of the approaches require that the CEO becomes a moral giant to effect positive solutions. Instead, they entail a new level of perception and analysis. By recognising opportunities to address local and global problems at a company or industry level, firms can gain recognition, reputation and, occasionally, profits.

CEOs who wish to make a difference in the world can cultivate this perception. When a firm recognises local or global problems as its own opportunities, it can generate significant positive impacts while increasing its own strengths. Responding to the legal, regulatory and civil society demands on firms requires significant levels of expensive resources and the attention of academics, but it doesn't allow CEOs to harness their firms' unique resources to resolve critical issues.

THE CASE OF WAL-MART'S SUSTAINABILITY INDEX

Over the last 20 years, retailers, customers, manufacturers and governments have struggled to meet the fluctuating demand for sustainably produced and low impact goods. The global nature of supply chains, the threat of WTO action against regulation in local markets, the omnipresence of unreliable marketing schemes and product claims, have all created a market failure of vast proportions. There is simply not enough reliable information for consumers willingly to pay the additional costs of sustainable production.
Under the leadership of its CEO, Mike Duke, Wal-Mart identified this as an opportunity to redefine retail once more.

Instead of waiting for the US government to bring forward CO_2 labelling similar to the UK's PAS 2050, they announced their own product sustainability index. They gathered university academics from a broad range of fields, many of their largest suppliers, US government officials, and some of their competitors to begin the process of creating a global, multi-dimensional set of standards, reporting process, and ratings scheme. The index is being rolled out in three stages:

1. A survey asking their largest suppliers about their corporate practices (not about specific products).
2. The design of open source IT architecture that will allow the compilation, storage, analysis and retrieval of information on hundreds of thousands of companies and millions of products.
3. The publication of information about each product they sell.

This move will allow them to use their enormous market power to specify standards, demand and publish compliance reports, and ensure that consumers are able to purchase the goods they want at prices they are willing to pay.

No government demanded Wal-Mart's compliance. No non-profit insisted that Mike Duke ensure his company conformed to its standard. Regardless, Duke and his team determined that a transparent, widely used measure of sustainability would be good for their business.

At the centre of this initiative there is no CEO with a guilty conscience donating to a portfolio of environmental groups he/ she hopes will become tame. Wal-Mart's new index is the result of managerial creativity, ambition and acuity. Only Wal-Mart could unify nearly 100,000 vendors and manufacturers to shift incrementally $400 billion in annual consumer spending toward greener products. They saw an opportunity and claimed it. In doing so, they positioned Wal-Mart for growth in a resource-constrained future, they increased the switching costs of customers, and they gained further power over their supply chain.

DOING GOOD VS DOING WELL: WHY NOT DO IT BETTER?

Corporate leaders have, for far too long, seen sustainability and corporate social responsibility concerns as a brake on their firm's performance rather than an accelerator of innovation, product development, or sales. Since Friedman, they have had to estimate the tradeoffs between doing good and doing well. Wal-Mart shows another way forward. In creating an index that can help customers make informed decisions about their purchases, Wal-Mart is taking enormous strides toward a greener future.

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In doing so, they have ceased to worry about doing good vs doing well: they are doing better.

They are doing better purchasing. They are creating better customer relations. They are gathering better data on consumption and sustainability. They are likely to keep happier, more informed employees. They are improving the buying experience.

And they might be making a better, more sustainable world.

Admittedly, Wal-Mart is an outlier in almost every respect. They work on a scale that can have profound impact throughout the globe. But small and medium sized companies can do better, too.

When Robin Chase and Antje Danielson founded Zipcar in Cambridge, Massachusetts in 1999, they were able to perceive an environmental problem - long-term ownership of low efficiency cars - as a new market. They did not succeed in getting whole populations to stop driving, nor did they try. Instead, Zipcar has changed not only the ownership, but also the driving patterns of their 275,000 members in the US, Canada and the UK. They can't solve all the problems of our dependency on the internal combustion engine, but they can have a real impact and make a real profit. They chose to do better.

Doing good to do well	Doing better
Identifying the most powerful and salient critics	Recognising new applications of firm expertise and resources
Assessing costs and benefits of responding	Create and evaluate business plan
Compliance (or not)	Roll out (or not)
Public relations and/or marketing campaign	Assess results

SEEING THE OPPORTUNITY: DOING BETTER

According to Orlitzky and Swanson, top executives cannot always see the negative consequences of their firm's activity due to 'normative myopia'. We believe this myopia can also prevent them from seeing the possibilities for their firms to make gains and to create and develop viable and profitable solutions. Because their mandated focus is on the company and its shareholders, CEOs can shy away from the innovative solutions that will also benefit the rest of the world.

Our tendency to define doing good as a distraction from business makes it harder to see the openings for new products and services, harder to commit employees and other resources, harder to risk new ventures. But, by recognising which of the world's critical needs present market opportunities – a product that needs new features or a process that needs to be redesigned for example - we can reposition the issues humans care about as problems CEOs can help solve.

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While doing good demands skilful reaction to criticism, doing better demands the skills of sound management. Perceiving, defining and acting on new opportunities are normal business practices.

When seen this way, CSR becomes a driver of new products, new technologies, and new strategies. Wal-Mart has been able to get its suppliers, competitors and critics to collaborate on an initiative that will improve its own data gathering, purchasing power and bottom line. Zipcar has grown to be a US$100 million company in little more than 10 years because it has offered a membership based driving option no one thought North Americans would choose.

CEOs who view their firms as players on a larger stage can find these opportunities more readily than those who are only concerned with beating their competitors' numbers. Gleaning information from outside the boundaries of the firm, or even the industry, provides CEOs with new realms of possibility.

CLOSING THE LOOP

The CEO whose basic human concerns are not reflected in the scope of his or her work cannot maintain peak performance indefinitely. Jensen and Meckling, whose theories were written to direct a CEO's attention to shareholders, did not imagine that executives could or would become machines devoted to a sole purpose. Instead, they posited a world in which all good deeds would be reflected in rising equity valuation, in which legitimate corporate well-doing was marked by increased share price.

CEOs who do not work in such a world can instead avoid the tension between doing good and doing by perceiving the world more clearly, by responding to those critical needs and issues it has the resources to address, and by capturing the fair value of their initiative. Such realism can spark new strategies. Such recognition of human capacity can generate returns. Unless and until the stark contrasts between business and society are reduced, the world's most capable business leaders will be without a role in resolving our toughest problems.

COMMUNITY COMMENT

Paul Polman
CEO, Unilever

"Too many investors have become short-term gamblers: the more fluctuations in share price they can engineer, the better it is for them. It is not good for the companies or for society, but it is influencing the way firms are being run, all the same.
To drag the world back to sanity, we need to know why we are here. The answer is: for consumers, not shareholders. If we are in sync with consumer needs and the environment in which we operate, and take responsibility for society as well as for our employees, then the shareholder will also be rewarded.
Too many people think in terms of trade-offs... that, if you do something which is good for you, then it must be bad for someone else. That's not right and it comes from old thinking about the way the world works and what business is for: Milton Friedman's optimisation of short-term profits. We have to snap out of that old thinking and move to a new model. Our new business model will decouple growth from environmental impact. We will double in size, but reduce our overall effect on the environment. Consumers are asking for it, but governments are incapable of delivering it. It is needed for society and it energises our people - it reduces costs and increases innovation. Businesses like Unilever have a major responsibility to society and thus a major role to play. This role is, frankly, very appealing to me as CEO as it is something I am personally very passionate about. I admit selfishly that what attracted me to the role was the ability to use a company of this size not only to do what is right for the company but also what is right for society. There was a chance to turn Unilever into a really great company and to have the kind of personal influence you can only really have as CEO."

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Roger is a leading business strategist, author and Dean of the Rotman School of Management at the University of Toronto. He is an advisor to Procter & Gamble, Steelcase and several other companies on design and strategy, has written twelve Harvard Business Review articles and published six books including his latest, **Fixing the Game: Bubbles, Crashes, and What Capitalism Can Learn from the NFL.**

Roger is a Criticaleye Thought Leader, was included in the 2009 **Thinkers 50** *and, in 2010, was named by BusinessWeek as one of the world's 28 most influential designers.*

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Alison is completing her Ph.D. at the Rotman School of Management in Strategic Management, where she researches the impact of social ratings on companies. After a successful career as a leader and manager in a variety of community-based and activist non-profit organisations, Alison began to work with Roger on the ways large organisations interact with their social environment, and specifically, on the intrinsic problems of CSR theory.

Contact the authors through www.criticaleye.net