Corporate Social Responsibility for SMEs

Overview of the Present Situation

Background

The recent financial crisis has caused most of the world to question the stability of the economy

As such, the motives and actions that actually drive the business world were also (and constantly still being) questioned

The idea that seemed fundamental for centuries that the sole objective of firms should be to maximize profit also became questionable

Background

Profit being the main goal of course still remains to be the case but the approach is constantly challenged

Solely profit is no longer enough, the firms and companies need to create and increase VALUES

As a result, the new fundamental idea was firms to be run in order to maximize shareholder value

Background

The definition of "values" however is not clear and differs widely depending on numerous factors including:

- the economical situation of the nation in general;

- the economical situation of the region/ sector where the company or firm operates,

- the economical situation of the company itself (as opposed to competitors),

- the legal regulations in force;

- corporate strategies and culture;

- etc.

Change

The public and general opinion is starting to put emphasis on viewing employees, suppliers, and other corporate stakeholders and their situation primarily

As such, the occurrence of excessive CEO compensations result in a public outrage especially when the employees are "suffering" in the same economic situation

People seem to care more but in most cases only when they are personally involved

UNIVERSITY OF SZEGED

Main Drawbacks

While it is difficult to ascertain the exact reasons for the present situation, several factors seem to be at work in the same time

The new value-based approach was widely welcome at first but it seems that it did not meet the expectations

The tremendous level of excitement surrounding their initiation seems to have turned to disappointment and mistrust towards future changes

Possible Reasons

The most plausible reasons for the value-based perspectives, strategies and approaches in general to not meet the previous expectations include the following:

- **they were introduced prematurely, before the firm or the community was ready to implement them, or**

- **the expectations were unreasonable due to exaggerated marketing in order to sell the new method**

What is CSR in relation o SME-s

Defining CSR

Corporate Social Responsibility (or CSR for short) has most often been presented as the company's responsibility to either truly do good or to give something back to society

This could indeed refer to a wide variety of things starting from strategically buying local products, through organizing community events all to involvement in the fight against climate change

The level of involvement and more importantly the level of true determination towards the cause may vary

Different Kinds of CSR

CSR means different things to different people

Most experts (Friedman, Baron) share the view that there are indeed different kinds of CSR

1) “True CSR” - which is unprofitable

2) “Hypocritical CSR” - which might seem to be socially beneficial (may even really be) but is profitable for the company

UNIVERSITY OF SZEGED

What CSR Really Is

CSR should not primarily be about an obligation felt towards society but more importantly a tool or process for structuring mutually beneficial agreements between the different constituencies sharing the value in question

In this approach CSR attempts to create a new cultural mindset (or replace a previously existing one) that considers how to operate in a way that creates value

UNIVERSITY OF SZEGED

How CSR Works

The main idea behind CSR is that it is important for a company to operate in a socially responsible manner

By doing so it considers the importance of all of its stakeholders

And in the same time it focuses on how they contribute to the company's goals

Through which long-term, sustainable creation of value can be ensured

CSR Achievements

The correct use of CSR can help a company to operate smoothly and also can support the following areas of operation (among others):

- **recruiting and retaining employees,**
- **providing risk management (with special regard to reputational risks),**
- **being used as a “marketing tool” and assisting in differentiating firm branding,**
- **helping to avoid unwanted governmental investigations and “interference”**

Veritas Virtus Libertas

SZTE UNIVERSITY OF SZEGED

CSR Achievements

CSR has the potential to be much more than a "feel-good concept" for companies and their management

It indeed can make good business sense IF (and only if) it is practiced in a strategic manner

Embracing a program of CSR, a company can provide a win-win situation for the mutual benefit of both the shareholders and other stakeholders

The Value-Based Approach

In the Beginning

The most commonly used management tool regarding the value-based approach is Value-Based Management (VBM for short) also known as Value-Driven Management (VDM for short)

In the beginning of the spread of the VBM “movement”, the most important question was, who possesses the best metric (or unit) for measuring value creation

As a result the market focused on the selling and purchase of the newest methods and software for measuring value creation

UNIVERSITY OF SZEGED

Development of VBM

It soon became apparent that having a metric for measurement was not sufficient

Need arose for a system to be designed that would build and support a sustainable cycle of value creation

Also the company's business strategies and the development of its value should also be harmonized or at least connected

The system should include a process (or processes) in order to meet the new requirements

UNIVERSITY OF SZEGED

The VBM System

At a minimum, a company's VBM system is required to command the following areas (non-exclusively) :

- full support of the management (especially that of the top executives);

- a link between behaviour and compensation;

- employees' understanding of the system (both "Why? "-s and "How?"-s);

- a capital market focus

Most importantly the company must realize that a VBM metric is only a measure of success and NOT success itself

UNIVERSITY OF SZEGED

VBM

VBM sets the transformation of the cultural mindset within a company in order to maximize the company's value creation as its goal

VBM is NOT a "quick fix" nor a "panacea" that can be purchased entirely from an outside source

Its implementation requires serious effort which in order to be successful needs to include a cultural change

Setting Up a VBM System

Management should be committed to strategies that create value

In other words a company's management should only commit to strategies in which the present value of the growth opportunities is positive (exceeds zero)

A fundamental component of every company's internal control system should be its compensation program

The Compensation Program

It is important to consider the fairness criteria when designing a compensation program

The basic paradigm espoused by the proponents of VBM is that what a company measures and (more importantly) rewards will get done

Consequently, the compensation program MUST measure employees' activities that contribute toward value creation and reward those efforts

The compensation plan (regarding both the level of compensation and its form and composition) should pay employees to think and act like owners themselves

The Basics of VBM – Compensation and Cash Flow

The Basics

The Basics regarding VBM and its successful implementation start with the company's compensation system and strategies

Public opinion plays an important role in this regard

Companies must be aware of the fact that the public's perception is that executive compensation has become unacceptably excessive even during the state of an economic crisis

The key word should be: FAIRNESS

The Basics

Apart from public opinion the political implications of the company's behaviour shall also be considered during the development and implementation of a complete VBM program

The reason for this is that it can and (most likely) WILL effect a company's reputation

And reputation means (virtually) "everything" for a company as on the long run it WILL ultimately affect its value- and wealth-creating ability

UNIVERSITY OF SZEGED

The Main Concept

The concept of "free cash flow" should be the foundation of value-based management at all times

No matter what a company chooses to do, free cash flow should always be at the heart of any effort in order to understand how management can contribute to a company's value

what makes it so important in this respect is that it makes it possible for companies to represent the amount distributed to its investors and, as such to represent the core determinant of the company's value

Value Determinants

Virtually anything can be considered as a "value" for a company, although there are some that are more commonly observed as such, than others

These are also known as "Value Drivers" and include the following (non-exclusively):

- **sales,**
- **sales growth,**
- **operating profit margins,**
- **asset-to-sales relationships, and**
- **cash taxes**

Free Cash Flow

Free Cash Flow (or FCF for short) is basically a measure of financial performance

The simple method to calculate it is as follows:

FCF = Operating Cash Flow – Capital Expenditures

FCF is a tool used to represent the cash that a company is able to generate after the money required to maintain (or expand) its asset base has been laid out

This way FCF allows a company to pursue opportunities that enhance shareholder value

Free Cash Flow

A company need cash in order to (among other activities) be able to:

- **develop new products,**
- **make acquisitions,**
- **pay dividends, and**
- **reduce previously acquired debts**

FCF can also be calculated in complex way taking every factor into account in the following manner:

FCF = EBIT(1 – Tax Rate) + Depreciation & Amortization – Change in Net Working Capital – Capital Expenditure

* **EBIT: Earnings Before Interest & Tax**

7 Steps for Implementing VBM

Commitment

Setting up or switching to Value-Based Management requires a sustained commitment on an organizational level

It depends on the company and its circumstances but in most cases it also requires a lengthy period of organizational development

According to past experiences, integrating VDM into an organization's culture will take approximately three years on average

The Process of Implementation

The exact implementation is up to the company's management but there are 7 factors (or steps) that should be observed during the process:

1: Lifelong Education

2: Emphasis on Value Creation

3: Employee Selection

4: Restructuring

5: Compensation

6: Employee Empowerment

7: Management Commitment

Factors to Consider (the "Steps")

1: Lifelong Education

New technologies and methods of successful operation appear constantly

To be able to access the know-how on time benefits both the employees and the managers

Companies have to give their employees comprehensive training as that way their workers will systematically create value (consciously or unconsciously)

Factors to Consider (the “Steps”)

2: Emphasis on Value Creation

Companies must keep the corporate culture alive

A value-driven organization is required to:

- make spontaneous celebrations for their organizational achievements,

- give spontaneous gifts to their employees, and

- have every worker involved in the value creation

Such events will revitalize a value-driven organizational culture

Factors to Consider (the “Steps”)

3: Employee Selection

The goal of employee selection should be to find the appropriate person who has similar or even the same values as the company, thus contributing to the business

For this to work optimally principles and values must be clearly and specifically identified within and FOR the company

Factors to Consider (the "Steps")

4: Restructuring

The company might need restructuring in order to facilitate the creation of value

Companies should not be very hierarchical and vertical

There shall only be a few layers of authority

The work shall be divided in work teams and the manager should appear as the coach

These kinds of companies have more facility to create value

UNIVERSITY OF SZEGED

Factors to Consider (the "Steps")

5: Compensation

There is a trend to reward competent employers with some incentives
There are also other methods to compensate workers, which include:

- **Profit sharing,**
- **Employee stock ownership plans (ESOP),**
- **Executive and managerial plans, and**
- **Gain sharing**

These systems reward the competence, creativity and creation of value of its employees and will most likely bring out a value-creating behaviour

UNIVERSITY OF SZEGED

Factors to Consider (the "Steps")

6: Employee Empowerment

Organizations must be sure that each of their employees have all the information they need and when they need it in order to be effective

Information is most vital in order to be able to

- make good decisions and
- solve problems they can find carrying out their responsibilities

If companies can be open and participative, employees will become more empowered and companies will be more proactive

Factors to Consider (the "Steps")

7: Management Commitment

Companies need managers to implement long-term commitment throughout the organization

Besides the compromise and the responsibility, communication has a lot of strength

Managers must write the mission, philosophy and the business principles of the company in order to help every person who integrates the company to understand the target

The Five Topics of VBM

The Value-Based Perspective

A successful implementation requires more than analyzing and interpreting different situations

It means that the company must apply a value based system and that there must be major changes in the organizational culture

It is not enough for the management to understand and correctly apply the VDM concept if there is no awareness of the values, starting from the top management to all decision makers and to company employees as well

The Value-Based Perspective

This new concept is based on how people's values drive their actions and by considering them in the decision-making process the company can come much closer to maximizing values over time

Value Driven Management is related to 5 major topics:

- **Company (values);**
- **Workplace;**
- **Marketplace;**
- **Community; and**
- **Environment**

Veritas Virtus Libertas

UNIVERSITY OF SZEGED

The Major Topics

Company (values)

An organization is built of employers and employees, policies, traditions and customs, rules and regulations, products and visions, partnerships and competition, strategies and management styles

In order to reach success, managers must take into consideration values that are key elements for the company, such as:

- **Client-orientation,**
- **Integrity,**
- **Professionalism,**
- **Respect, and**
- **Teamwork**

UNIVERSITY OF SZEGED

The Major Topics

Workplace

Workplace actually refers to the employees and the employers working together to ensure the success of the company

Managers have the responsibility to guide their subordinates so they can improve the entire activity

It focuses on employee involvement, reciprocity, quality, team work, regulations and different development techniques

Veritas Virtus Libertas

UNIVERSITY OF SZEGED

The Major Topics

Marketplace

Marketplace refers to supply and demand, customers and consumers, partners and suppliers, competition, new trends, and it functions based on certain values and rules

It basically represents the central field of action, the setting in which the company can check its performances and its power

UNIVERSITY OF SZEGED

The Major Topics

Community

The community is composed from the public sector and the non-governmental sector, which collaborate for creating conditions for economic growth and for creating new jobs

It has a major role in developing companies' activities as there is a mutual relationship between companies and the community and they affect each other constantly and mutually

The Major Topics

Environment

Environment relates to surroundings and living organisms, but also to the external and internal factors that influence the company's activity, such as:

- **partners,**
- **suppliers,**
- **competition,**
- **third parties,**
- **local and national authorities,**
- **laws and regulations**

The Major Topics

Environment

Environment can be defined using multiple approaches but in every case it is vital for the company as without it the company cannot operate

For this reason every company must learn to operate in harmony with its environment, know its role and place within it and furthermore protect and sustain it

Different Approaches to Environment

Defining the Key Term(s)

WHAT IS “ENVIRONMENT”?

Multiple definitions are possible and acceptable

It always depends on the aspect of approach

The most important ones to be reviewed for VBM are the following:

1.) General Environment

2.) Economic Environment

3.) Business Environment

UNIVERSITY OF SZEGED

Defining the Key Term(s)

1.) General Environment (or Environment in general)

The sum (total) of ALL SURROUNDINGS of a living organism, including natural forces and other living things, which provide conditions for development and growth but may also hold danger and cause possible damage

|+| The broadest approach, includes everything

|-| Too general, yet not suitable to be used in every aspect

Defining the Key Term(s)

2.) Economic Environment

The totality of economic factors that influence the buying behaviour of consumers and institutions. Factors include:

- **Employment**
- **Income**
- **Inflation**
- **Interest rates**
- **Productivity**
- **Wealth**

UNIVERSITY OF SZEGED

1. Defining the Key Term(s)

3.) Business Environment

The combination of internal and external factors that influence a company's operating situation The business environment can include factors such as:

- **Clients and Suppliers**
- **Owners, Stakeholders and Shareholders**
- **Competitors and "Competition" itself**
- **Technologies (old ones and improvements)**
- **Government activities (such as support schemes)**
- **Laws**
- **The Market (itself and its trends)**
- **Social issues and trends**
- **National and regional economy and trends**

How CSR Interprets Environment

Apart from the obvious moral issues, environment is linked very much to business

Someone who is utilising his/her environment in the best way possible, not only has the best way to use raw materials but also sees through and is capable of monitoring the best practices throughout the entire system and process of supply or production

How CSR Interprets Environment

The basic question that needs to be answered regarding environment is no other then the use of energy

About 60% of people are willing to pay as much as 10% more for (socially/ environmentally) responsible products

Furthermore, the type and amount of energy used both contribute to operational costs

How CSR Interprets Environment

Possible Benefits

ACHIEVING CUSTOMER SATISFACTION – Adjusting to needs

Since environmental awareness is a key concern these days, customers are globally looking for suppliers and companies who can offer quality for a reasonable price without having to worry about compromising their own, or their children's future

How CSR Interprets Environment

Possible Benefits

CUT DOWN ON OPERATIONAL COSTS – Being clever and observant

Switching the production methods or updating them to be energy efficient always pays off on the long run, even if investment seems costly in the beginning

Even if the energy, water or raw materials go to waste, they had to be paid for, and in this sense the company gets nothing in return for their money

Environmental CSR

Opening Thoughts

Companies increasingly desire to appear "green"

Toyota and Bank of America have new buildings that are Gold-certified by the US Green Building Council

Dell Computer allows customers to buy carbon offsets when they purchase a new computer

Nike and Microsoft planned to be 100% carbon neutral by as early as 2013

UNIVERSITY OF SZEGED

Opening Thoughts

But why the sudden interest?

The answer of course is mostly

PROFIT

But how does Environmental CSR bring profit for the companies?

When is environmental CSR profitable?

The needs of consumers have changed

A new generation of “green” consumers seems to have emerged,

willing to pay higher prices for clean products

Could this be enough for firms to follow? Are they merely responding to this shift?

Or are they reacting proactively to political measures?

The answer is somewhere in between

When is environmental CSR profitable?

The level of competition in a market affects the amount of environmental CSR firms undertake

if the market for “brown” (less environmentally friendly) products is highly competitive, then its prices will be low →

→ fewer consumers will wish to buy “green” products

should the “brown” market exhibit market power, then prices will be high →

→ consumers will switch to the green goods

What to consider?

The answers to most questions regarding costs will simply come to the AMOUNT OF ENERGY used

and HOW that energy is used and the raw materials are (re)sourced

Get these wrong → the costs can be high

Maintain dependence on these resources too long, and be prepare to be left behind by competitors

Study THE WHOLE PROCESS to identify where the most “waste” occurs

Get it wrong → the costs can be high

UNIVERSITY OF SZEGED

“Are you doing it right”?

If so, one may benefit from the following factors:

I. A Sustainable Risk Management System

II. Overall Cost Reduction

III. Pleased (most probably more loyal) Customers

UNIVERSITY OF SZEGED

Sustainability

Veritas
Virtus
Libertas

Being Sustainable is the “Key”

Preserving the planet for the future generation(s) is a moving mission, but companies need to be more precise, more business oriented and most of all more practical

Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs

This should be achieved by making the economy more competitive

UNIVERSITY OF SZEGED

Being Sustainable is the "Key"

A more competitive economy can be achieved by providing access to resources in an easier and preferably a more environmental friendly way

Sustainability is originally designed to be profitable on the long run, but this does not mean that a company could not profit from it right away or even during the process of switching to being sustainable for that matter

The EU 20-20 Strategy (Programme)

Three principles were formed to help the fulfilment of the Strategy

1) Intelligent growth

which means to create an economy based on knowledge and innovation

2) Sustainable growth (or development)

make the economy more competitive

3) Inclusive growth

including the expansion of the ratio of employed people as well as inspiring regional and social cohesion and strengthening and stabilizing economy trough these instruments

Corporate Interest Regarding Sustainability

Things to consider for a company include:

- Energy Use
- Water Use
- Waste Management
- Green Meetings
- Green Building Practices
- Conservation
- Purchasing (What & When)
- Social Responsibility
- Employee Engagement
- Customer Education
- Promoting the Local Economy

Achieving Sustainability

There are 10 principles that a company should observe in order to achieve sustainability:

1: Share the Responsibility
2: Use Resources Efficiently
3: Prevention VS Remedy
4: Conserve
5: Minimise Waste Production
6: Make Information Accessible
7: Make Public Participation Possible
8: Respect and Make Effort to Understand
9: Never Stop to Improve
10: Think Global

10 Principles to Achieve Sustainability

The 10 Principles

1: Share the Responsibility

All employees, contractors, and agents should be aware of sustainable development policies and guiding principles and should be encouraged to act accordingly

Encourage them to share their knowledge of the concepts and practical application of sustainable development

2: Use Resources Efficiently

Develop and apply programs and pricing mechanisms for efficient and economic use of energy and materials throughout operational process

UNIVERSITY OF SZEGED

The 10 Principles

3: Prevention VS Remedy

Focus on preventing adverse environmental and economic effects that may be caused by Corporate policies, programs, projects and decisions rather than reacting to them (and possibly remedying such effects) after they have occurred

Be prepared to address adverse environmental effects of Corporate activities that cannot be prevented

UNIVERSITY OF SZEGED

The 10 Principles

4: Conserve

Always plan ahead! Design, build, operate, maintain and decommission Corporate facilities in a manner that protects essential ecological processes

5: Minimise Waste Production

Develop and follow through the following 3 steps:

1) Eliminate total waste production if possible, if not: reduce amount

2) Fully utilise every reusing and/or recycling possibility

3) Dispose of remaining waste in an environmentally friendly way

UNIVERSITY OF SZEGED

The 10 Principles

6: Make Information Accessible

Share relevant information on a timely basis with employees, people interested and governments to promote a greater understanding of current and planned business activities and to identify impacts associated with the Corporation's plans and operations

UNIVERSITY OF SZEGED

The 10 Principles

7: Make Public Participation Possible

Transparency is very important, why not gain more? Provide opportunities for potentially affected and/or interested parties to share their opinions when evaluating development before deciding on a final program

8: Respect and Make Effort to Understand

Take different social and economic views, values, traditions, etc. into account when developing or carrying out new programs

Make diversity into a strength instead of letting it become your weakness

UNIVERSITY OF SZEGED

The 10 Principles

9: Never Stop to Improve

The only possible answer to innovation is YES! Always research, develop, test and implement newer and newer technologies, practices and institutions in the areas most important for the company

10: Think Global

There are no political and jurisdictional boundaries to our environment, BUT there IS ecological interdependence among provinces and nations

Connection Between CSR and the Value-Based Approach

Need for a Connection

Traditional VBM was often short sighted and thus needs to evolve if it is to continue to flourish

The idea VBM represents seems to be a correct one but correct and successful implementation seems to be difficult for many companies

Implementing the new approach might be effective if it were to be done through a method the companies are more familiar with already

CSR fits in well within a VBM framework because CSR appears to make good business sense

Fusion?

A “marriage” of traditional VBM with the growing trend toward corporate social responsibility (CSR) is most likely to have favourable effects on the company

The combination is termed Value(s)-Based Management (or VsBM for short)

Value(s)-based management, as defined here, represents a marriage between the shareholder-centric orientation of traditional VBM and the society-centric orientation of the CSR movement

UNIVERSITY OF SZEGED

Common Characteristics

The objective of VBM is a cultural change that involves modifying behaviour to align the interests of a company's management with those of its shareholders

Companies that successfully integrate VBM throughout their organization experience a dramatic alteration in their culture

CSR also has as its objective to achieve a transformation in cultural mindsets

Common Characteristics

CSR promotes the idea that companies must operate in a socially responsible manner, such that they consider how their operations impact the company's numerous stakeholders

Evidence is strong that such stakeholders are critical for a company's long-term, sustainable value creation

VBM also focuses mainly on value creation and pays attention to various value factors, areas and sources

Conclusion

The major conclusion is that VsBM approach, can lead to a win-win situation for both the company's shareholders and its numerous other stakeholders by leading to a virtuous cycle of doing good and doing well

Doing good for employees, the environment, and/or the community and in the same time achieve profit

VsBM seems to be a method to convert "Hypocritical CSR" into "True CSR" without losing values on either side

Good and Best Practices

Measuring Corporate Interest (Regarding Sustainability)

The best, most accepted and easiest way of planning ahead is to calculate the expected Return On Investment (ROI for short)

By calculating the ROI value whenever possible some bad investments can be avoided

The same methods and objectives do not apply for every single company, but all of them have costs and expected gains from which the probable level of benefit can be calculated using the following method:

$$ROI = (Gains - Cost)/Cost$$

UNIVERSITY OF SZEGED

Examples for the Most ROI and Created Values

ADOBE SYSTEMS INCORPORATED (San José, CA, USA)

Achievement:

Savings on employee energy, packaging, shipping and travel expenses, reducing need for office space, leasing office buildings

Method or idea:

Achieving Platinum level LEED (Leadership in Energy & Environmental Design) Certificate on four main buildings,
Encourage employees to work form home, enable telecommuting + offer alternative transportation mode programs to employees ;
Enable download of products instead of shipping them

Amount of savings:

$ 680,000,000 in annual energy costs;
50% of travel expenses

UNIVERSITY OF SZEGED

Examples for the Most ROI and Created Values

CISCO SYSTEMS (San José, CA, USA)

Achievement:
Savings on employee travel expenses, reducing need for office space and highly increasing flexibility

Method or idea:
Creating and widely enabling "Virtual Workforce" and telecommuting

Amount of savings:
$ 100,000,000 in three years (not counting business trip expenses)

Examples for the Most ROI and Created Values

STARBUCKS

Achievement:
Reducing energy use, cutting CO_2 emission and improving reputation

Method or idea:
Replacing nearly all of its incandescent and halogen lighting with latest LED technology bulbs (over 7,000 company-owned stores)

Amount of savings:
\$ 30.00 annually per light bulb (and cuts CO_2 by half an oil barrel)
\$ 600.00 annually per 1,000 ft^2 (and cuts CO_2 by 10 oil barrels)

UNIVERSITY OF SZEGED

Examples for the Most ROI and Created Values

TESCO

Achievement:

Reducing energy use, cutting CO_2 emission and improving reputation

Method or idea:

Changing to Natural Refrigeration units, which use fewer hydro fluorocarbons (HFCs)

Amount of savings:

£ 200,000,000 annually

UNIVERSITY OF SZEGED

Corporate Interest

Not every benefit can be determined financially, but this does not mean that a company should not be interested in gaining them

Projects may produce monetary returns such as
- **reduced fuel use,**
- **lower waste disposal fees, and**
- **fewer governmental fines BUT**

Many of the returns from sustainable behaviour don’t translate well into money, e. g.:
- **employee happiness,**
- **reduced turnover,**
- **improved health for the communities,**
- **enhanced brand appeal to consumers**

THANK YOU FOR YOUR KIND ATTENTION!