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Corporate Social Responsibility and Socially Responsible  
Investment:

New Paradigm, Latest Fad, or Ingenious Plot?

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## I. THE DIFFUSION OF A NEW CONCEPT

According to a widely held view, the production, investment and lending decisions of managers and bankers should not be based exclusively on narrowly defined economic considerations. Public opinion increasingly requests the private business sector to help achieve social, environmental and ethical objectives. The notion of corporate social responsibility (CSR) may “encompass an array of meanings” (UNCTAD 1999: 346). Yet it is hardly disputed by now that strategic management has to take into account how corporate activities affect various groups of *stakeholders* (Freeman 1984). A generally accepted list of a company’s stakeholders may not exist, but workers, customers, suppliers, local communities as well as future generations are typically included. This contrasts with the concept of *shareholder value*, according to which the overriding objective of companies should be to serve the (profit) interests of their owners.<sup>1</sup>

Within the realm of CSR, the notion of socially responsible investment (SRI) encompasses “a wide number of extra-financial criteria” (EUROSIF 2003: 6). The Association for Sustainable & Responsible Investment in Asia (ASrIA 2003: 4) defines SRI as an approach that “integrates social and environmental considerations into investment decisions” and as “a means by which the financial community can direct investment towards sustainable development.”

A simple Google search illustrates the popularity of CSR and SRI. The latter is also known as sustainable and responsible investment. Using these terms results in almost as many entries as searching for “profitable investment” (Figure 1). Entries for “profitable investment”

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<sup>1</sup> Milton Friedman’s message is clear from the title of one of his papers: “The social responsibility of business is to increase its profits” (Friedman 1984)

are even outnumbered when adding up the entries for both meanings of SRI.<sup>2</sup> It becomes still more obvious that new concepts are all the rage when comparing the search results for CSR and the alternative concept of shareholder value. Measured by the number of internet entries, it appears that CSR with its orientation towards a company's various stakeholders commands considerably stronger support than the one-dimensional orientation towards a company's shareholders. It fits into this picture that a comparison of the results reported in Figure 1 with a similar search three months earlier reveals a slightly declining number of entries for "shareholder value", whereas CSR entries increased from 2.7 to 2.9 million.

**Figure 1 somewhere here**

The diffusion of the notions of CSR and SRI owes much to public opinion. EUROSIF (2003: 6), a European non-profit organization promoting SRI, stresses "the public's broader consciousness of sustainable development issues". In a worldwide survey undertaken in 2001, more than two thirds of respondents wanted companies to focus on more than profits; this share is likely to have risen further in recent years.

More strikingly perhaps, companies have reacted fairly quickly to public pressure. The way in which major companies advertise provides a first indication. For example, Altana, an internationally active chemical company, posited in a recent campaign that thinking about profits "is not thinking far enough." Most managers share, or at least say they share, the conviction that it is not enough for firms to earn money for their owners. In a survey of the 1500 delegates, most of them business leaders, attending the World Economic Forum's Davos meeting in January 2004, fewer than one in five respondents considered profitability to

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<sup>2</sup> It has to be kept in mind, however, that there may be substantial overlapping as both meanings of SRI are often used in the same source.

be the most important measure of corporate success (*The Economist* 2004b). While just 5 percent of respondents named CSR in its own right as the single most important criterion, almost a quarter regarded as most important the reputation and integrity of the brand, to which CSR is supposed to contribute.

Before turning to more controversial issues in the subsequent sections, a few additional observations may indicate how companies, governments, international organisations and markets reacted to public pressure for looking beyond profitability. At the company level, codes of conduct have proliferated. The Center for the Study of Ethics in the Professions at the Illinois Institute of Technology has collected over 850 codes of business ethics.<sup>3</sup> Much more impressive numbers are reported in a recent study by CSR Europe (2003: 10), a non-profit organisation for the promotion of CSR, according to which some 20.000 codes exist in the textile sector alone. Furthermore, various companies present CSR-related achievements in their Annual Reports, or even publish separate reports devoted to CSR. In this respect, Starbucks Coffee Company claims to have made “the cutting-edge step of having its second Corporate Social Responsibility Annual Report verified by an outside auditor, so readers can be assured the facts and figures it presents are accurate” (Asmus 2002).

At the public level, national governments have established CSR departments in Ministries of Trade and Industry. The United Kingdom even appointed a Minister for Corporate Social Responsibility in March 2000 (Commission of the European Communities 2001: 5). The Global Compact, launched by UN Secretary General, Kofi Annan, at the World Economic Forum’s Davos meeting in 1999, figures prominently among multilateral initiatives. The Global Compact seeks to advance responsible corporate citizenship by bringing companies

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<sup>3</sup> Available online from: <http://www.iit.edu/departments/csep/PublicWWW/codes/index.html> (accessed in April 2004).

together with UN agencies, labour and civil society to support ten principles in the areas of human rights, labour standards, the environment and the fight against corruption.<sup>4</sup> Other international organisations climbed on the bandwagon. For instance, UNCTAD argued that, in addition to the principles of the Global Compact, “there is a need to bring the economic development dimension more into focus and we feel there is a role for UNCTAD to do this” (Odenthal 2003: 92). By organising meetings, UNCTAD would like to ultimately come to a consensus about what it is that companies can contribute to economic development.

Finally, markets offer various CSR and SRI-related products and services. Leading index companies launched indices of socially responsible companies, e.g., the Dow Jones Sustainability Indexes and the FTSE4Good Index Series (see also Section IV). Specialised rating agencies provide non-financial analysis to the markets. There are CSR newswire services available as well as magazines on business ethics, which offer *Social Investing Awards*<sup>5</sup> and list the *100 Best Corporate Citizens*.<sup>6</sup> In summary, CSR and SRI have become an industry in their own right which, at any rate, is thriving (*The Economist* 2004b).

## II. HOW EFFECTIVE IS THE CSR CONCEPT?

Some advocates of CSR claim that the concept helps both society and business at the same time. For example, organisations such as the aforementioned CSR Europe state as their mission to “help companies achieve profitability, sustainable growth and human progress by

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<sup>4</sup> The tenth principle against corruption was added only in July 2004 at the first Global Compact Leaders Summit. For details, see the Global Compact’s homepage: <http://www.unglobalcompact.org/Portal/> (accessed in July 2004).

<sup>5</sup> See, for example, <http://www.business-ethics.com/SRI-01-02.htm> (accessed in April 2004).

<sup>6</sup> See, for example, <http://www.business-ethics.com/100best.htm> (accessed in April 2004).

placing CSR in the mainstream of business practice” (<http://www.csreurope.org/aboutus/default.aspx>; accessed in August 2004). Likewise, the EU’s Green Paper *Promoting a European Framework for Corporate Social Responsibility* argues (Commission of the European Communities 2001: 3): “Companies ... expect that the voluntary commitment they adopt will help to increase their profitability.” However, CSR is unlikely to silence critical non-government organisations (NGOs) if it results in higher profits. Moreover, it is open to question whether CSR is an effective means to achieve social progress.

Effectiveness depends on the actual reach and the behavioural impact of the CSR concept. First of all, one may have doubts whether the public pressure on the corporate sector is as pervasive as the activities of NGOs tend to suggest. The New Economics Foundation, an NGO in the United Kingdom, comes to a fairly sceptical conclusion (Doane 2003: 28): “Our expectations that the market will deliver progress on CSR simply does not hold up to scrutiny. For the market to succeed, it relies on consumers to reward good business. Yet research on ethical consumerism consistently shows that consumers are relatively passive.” Two observations are offered in support of this sceptical assessment:

- In the United States, the interest of consumers in environmental concerns has declined in recent years.
- In the United Kingdom, 83 percent of consumers *intend* to act ethically, but fewer than 18 percent do so in practice *occasionally* and only 5 percent are considered to be *fairly active*.

A similar qualification applies to the argument of Tapscott and Ticoll (2003) that citizens and communities routinely put firms under the microscope in a world of whistleblowers and inquisitive media. The much publicised pressure by NGOs tends to have limited effects as

long as their activities are targeted at a fairly small number of large and visible companies. The UN Research Institute for Social Development reckoned recently that most firms remain fairly immune to the pressure driving the CSR agenda (UNRISD 2004: 2). As a result, the practical relevance of CSR and SRI appears to be restricted to a minor segment of the corporate sector. Utting (2003: 6-7) points out that there are over 60.000 TNCs: “Probably no more than several hundred have codes of conduct or produce environmental and social reports.”

Furthermore, the CSR concept rests on *voluntary* commitments by companies which tends to come at the cost of effectiveness. Vague commitments, and the lack of sanctions to enforce them, invite the “credibility question” (Utting 2003: 6): Are companies really practising what they preach, i.e., does CSR amount to more than public relations and window-dressing? While Utting (2003) acknowledges that a considerable number of large corporations have become more proactive about CSR issues, the charity Christian Aid dismisses CSR as a “tool in promoting and improving the public image of some of the world’s largest companies” (quoted as in *The Economist* 2004b). Apart from the disputed credibility of voluntary commitments, the effectiveness of CSR also depends on the counterfactual, i.e., the regulatory system that would exist if companies had not committed themselves voluntarily. From the business point of view, CSR may be a clever move to adjust to public pressure and, thereby, prevent stricter and binding government regulations. The latter might well be more effective in changing actual corporate behaviour (see also Section V).

Recent episodes from development banking in Germany as well as the Global Compact reveal the plausibility of these arguments. A critical account of export and project financing of the Kreditanstalt für Wiederaufbau (KfW; since recently: KfW Group), the German development bank, does not only take issue with the vague character of environment-related lending guidelines (Urgewald 2004). At the same time, other aspects of CSR seem to have



had little behavioural consequences: The KfW's management is quoted to have admitted that greater transparency and a more open dialogue with NGOs have not significantly affected corporate strategy. In 2003, the Green Party, as part of the ruling coalition in Germany, suggested to amend the KfW's by-laws and include the principle of sustainable development as a statutory lending requirement. The initiative failed: By agreeing to a less binding self-commitment to environmental protection and sustainable development, political decision-makers and KfW executives took the wind out of the Greens' sails.

Companies joining the Global Compact are expected to make a "sincere effort" to aspire to its ten principles. But the Global Compact is not a regulatory instrument; it does not enforce, not even measure, good behaviour of participating companies.<sup>7</sup> Nevertheless, few US companies participated until mid-2004 for fear of lawsuits based on claims that they violated the Compact's principles. US participation may increase after substantial efforts by the UN and the American Bar Association to ensure effective protection against lawsuits (*The Economist* 2004a). According to critics, however, this protection clearly bears out the public-relations character of the Compact.

### **III. SRI: FINANCIAL MAINSTREAM OR NICHE MARKET?**

Similar to the CSR concept, there seems to be a certain degree of wishful thinking among the proponents of SRI. The EU's *Green Paper* notes that social criteria are increasingly influencing the investment decisions of individuals and institutions; the demand for SRI funds in Europe is said to increase rapidly (Commission of the European Communities 2001). More

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<sup>7</sup> See "What is the Global Compact" on its homepage <http://www.unglobalcompact.org> (accessed in July 2004).

pretentiously, the Executive Director of the European Sustainable and Responsible Investment Forum (EUROSIF), claimed that SRI is entering the financial mainstream in Europe.<sup>8</sup>

However, a careful reading of the study on which the latter claim was based suggests several qualifications (EUROSIF 2003). There is no single definition of SRI, and empirical results differ widely depending on the definition. The *core* of institutional European demand for SRI, i.e., the demand by institutional investors applying elaborate screening practices, amounts to just 34 billion Euro. The market volume increases by a factor of ten (to 336 billion Euro) when institutional investors applying simple exclusions and weaker engagement practices are included. Simple exclusions, so-called negative screening, are of the sort “no tobacco companies” or “no activity in Myanmar”. It is debatable whether simple exclusions should be regarded as SRI by institutional investors; as noted by EUROSIF (2003: 11), they are often part of conventional risk management.

According to the core definition, the institutional SRI market in Europe may be growing, but it remains a small niche market. As concerns pension funds, which are said to play a leading role in developing this market, “core SRI” amounts to just about 2 percent of their total equity holdings (EUROSIF 2003: 14). This share is very close to the 2.3 percent of total mutual fund assets in the United States that, reportedly, had been invested in 230 SRI funds by the end of 2000 (Schröder 2003: 2). In addition, the core institutional SRI market in

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<sup>8</sup> See the press release on the publication of EUROSIF (2003); <http://www.eurosif.org/pub/lib/2003/10/srirept/press.shtml> (accessed in July 2004).

Europe is largely restricted to the United Kingdom (Figure 2). In Germany and France, the sums involved are less than 3 and 2 billion Euro, respectively.<sup>9</sup>

**Figure 2 somewhere here**

All this is not to ignore that, in another respect, the SRI idea has clearly made it into the financial mainstream: As noted in Section I, major index companies have designed and publish indices such as the Dow Jones Sustainability Index (DJSI) and the FTSE4Good, which at least these companies perceive to be built on the SRI concept. NGOs are not so sure! The DJSI World as of December 2003, for example, included companies such as Royal Dutch/ Shell, Nestlé and Hewlett-Packard which, for different reasons, have attracted harsh criticism by NGOs.<sup>10</sup> Hence, it is not surprising that NGOs such as the New Economics Foundation complain that, by letting in the “best of the baddies”, many SRI funds and indices “make a mockery of sustainable development and ethical investment” (Doane 2003: 28).

This critique may have implications for the proposition of “dual returns” to SRI. According to this hypothesis, SRI does not only offer social and environmental rewards but also financial returns often exceeding the returns to conventional investments. Similarly, Tapscott and Ticoll (2003) argue that companies that optimise the needs of all stakeholders are more likely to deliver high returns to investors. The notion of dual returns appears to be in conflict with financial market theory which predicts a deterioration in the risk-return trade-off,

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<sup>9</sup> In Germany, Austria and Switzerland, about 80 mutual funds exist which take into account ethical, social, ecological and other SRI-related criteria. However, the total volume of SRI funds offered in these countries represented only 0.4 percent of total investment fund volume in 2000 (EUROSIF 2003: 41).

<sup>10</sup> For instance, the Hong Kong Christian Industrial Committee mentions Hewlett-Packard (HP) as an example of “façade CSR”; the conditions of the sub-contracting workers of HP in China are said to be in striking contrast with the picture HP paints in its CSR report (Wong 2003: 19).

i.e., a downward shift of the I-curve in Figure 3, if the SRI concept results in a substantially reduced number of available investment instruments.

**Figure 3 somewhere here**

The empirical evidence is mixed. Doane (2003: 28) finds that the so-called SINDEXT, comprising those FTSE100 companies which did not make it onto the FTSE4Good, outperformed their SRI counterparts in the recent bear market, and concludes: “It pays to misbehave.” Other studies provide fairly strong support to the hypothesis of dual returns. For instance, researchers of WestLB, a German bank, show that companies included in the DJSI outperformed other companies and conclude: “More gain than pain - Sustainability pays off” (Garz 2003: 3). Based on a broader review of the empirical literature and an analysis of investment funds and indices in Germany, Switzerland and the United States, it seems fair to say that “socially screened assets have no clear disadvantage concerning their performance compared to conventional assets” (Schröder 2003: 25). From the theoretical perspective of Figure 3, this result is clearly better than expected.

The finding that the empirical picture compares favourably with theoretical predictions may be because the latter are based on problematic assumptions, notably that financial markets are informationally efficient. However, the empirics may be flawed as well. As mentioned before, it is dubious to equate indices such as the DJSI with an effective concept of SRI. Furthermore, empirical studies may be biased: The performance of SRI funds is lifted systematically if companies are excluded which underperform because of public pressure, class actions and government intervention; tobacco companies represent a case in point. Finally, better corporate performance, by allowing for better social behaviour, may improve the chances to be included in SRI funds, rather than the other way round. In other words, SRI

is not exogenous, but may depend on financial returns.<sup>11</sup> Taken together, the verdict is still open when it comes to the question of dual returns to SRI.

#### IV. TRADE-OFFS AND CONFLICTS: A NORTH-SOUTH PERSPECTIVE

The question of whether or not CSR and SRI come at the cost of profitability represents just one of the possible trade-offs to be considered. Conflicts of interest may not only arise between the shareholders of a company and its stakeholders, but also between different groups of stakeholders.<sup>12</sup> The CSR/SRI concept is likely to result in standards and codes of conduct that serve only some stakeholders well. This is because the implications of standards and codes typically go beyond stakeholders who take part in defining them.

This problem has a North-South dimension. As Utting (2003: 7) notes, the mainstream CSR agenda is defined largely in the North. At the same time, firms setting themselves up as “good global citizens” tend to apply *uniform* standards in a profoundly *non-uniform* world (*The Economist* 2001). The risk for developing countries, particularly the poorest among them, is that a level regulatory playing-field based on the ethical insights of NGOs and/or companies in developed countries limits competition, effectively discriminates against developing countries, or is even misused in a protectionist way by developed countries.

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<sup>11</sup> This sequence of cause and effect is quite obvious if philanthropy is considered instead of SRI or CSR. It is difficult to imagine that Bill Gates would have become a most generous philanthropist if Microsoft had not been as profitable as it was.

<sup>12</sup> A curious example was reported in the German press in spring 2004: Milk-producing farmers, suffering from overproduction and producer prices too low to cover costs, protested against supermarket chains and demanded from them to comply with their CSR by paying more to milk producers, rather than supplying consumers with cheap milk.

For example, the French supermarket chain Carrefour may have good intentions when imposing northern standards on all its suppliers around the world (CSR Europe 2003: 11). The aim of the code of conduct, which Carrefour developed in cooperation with the Fédération Internationale des Droits de l'Homme, is to get all suppliers to respect international standards on working conditions, child labour, freedom of association, non-discrimination, etc. The problem with this approach is that local suppliers in developing countries come under additional pressure. What Utting (2003: 8) observes for Chinese suppliers in the apparel and footwear industries probably applies to other countries and industries, too: Local suppliers “often find themselves in a sort of straitjacket with CSR departments of [foreign] corporations demanding more in terms of CSR standards and expenditures, while purchasing departments of the same corporation insist on tighter margins and delivery schedules.”

The decision of Reebok, a sports-goods company, to withdraw business from a subcontracted Thai factory in 2002 points to an even more serious trade-off. Workers at this factory worked for more than 70 hours per week, and Reebok presented the withdrawal as proof of its CSR. And indeed there may be one sweatshop less in Thailand. The downside is that about 400 workers may now be “ethically unemployed” (*The Economist* 2002). Not only neoliberal economists, but also globalisation critics such as Professor Ajit Singh (2003 : 50) consider it necessary to ask whether promoting higher labour standards in the formal sector is the best way to achieve poverty reduction in developing countries. The anti-sweatshop

movement and the resulting corporate commitments to enforce labour standards in the small formal sector may lead to deteriorating working conditions in the large informal sector.<sup>13</sup>

Sometimes it is even questionable that northern parties involved in the definition of international standards have good intentions. This is the case, for instance, when labour unions in the United States call for stricter oversight and enforcement of working and environmental standards in the neighbouring export-oriented Mexican *maquiladores* as a prerequisite for access to US markets (Barkin 2003: 15).

Similar conflicts apply to the SRI concept which, as the CSR agenda in general, reflects mainly the concerns of the North, whereas the consequences tend to be felt largely in the South. This shall be exemplified in the remainder of this section by (i) referring to the debate on foreign direct investment (FDI) in developing countries and (ii) discussing the so-called Equator Principles.

As concerns FDI, developing countries are falling over themselves to lure transnational corporations (TNCs) into their countries (Singh 2003). The reasoning of NGOs, including trade unions in the North, suggests, however, that developing countries are very much mistaken when they seek to attract FDI. The critics blame TNCs for paying sub-standard wages to workers in developing countries, forcing them to work under sweatshop conditions, and transferring environmentally harmful production processes, i.e., misusing developing countries as “pollution havens”.<sup>14</sup> Consequently, many NGOs and globalisation critics want

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<sup>13</sup> According to CSR Europe (2003: 10), codes of conduct “provide protection for full-time employees, but leave the majority of workers - casual or seasonal labourers, the majority of whom are women - unprotected”.

<sup>14</sup> In China, for example, at least one third of FDI is concentrated in pollution-intensive industries (Taube 2003: 20).

TNCs to be strictly regulated, whereas most developing countries have liberalised FDI regulations considerably since the 1980s (UNCTAD 2002: 7).

This suggests that, from a developing country perspective, it may have undesirable effects if NGOs set the agenda with regard to international FDI-related standards. Less FDI of a cost-saving type, so-called efficiency-seeking FDI, is likely to flow to developing countries if social and environmental standards become more binding.<sup>15</sup> And the labour and environmental conditions may even deteriorate if local companies replace foreign companies:

- TNCs typically pay higher wages in developing countries than prevail locally (Graham 2000; ODI 2002).
- Wang and Jin (2002) show for the case of China that TNCs have the best environmental performance of all ownership forms.

In other words, the crux is not only that the North tends to impose FDI-related standards on the South, but also that these standards may prove counterproductive once the counterfactual is taken into account.

The Equator Principles, a voluntary set of guidelines for managing social and environmental issues related to the financing of development projects, were adopted by some international banks in June 2003. It is important to recall how these principles emerged and what were the driving forces that led to the agreement. The euphoric reading is that “10 international banks stepped forward to take a leadership role on global environmental and social issues” (Lazarus 2004). But further down in her account, the same author, a senior

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<sup>15</sup> Some studies suggest that this type of FDI is superior to purely market-seeking FDI, e.g., in terms of economic growth effects in developing host countries (Nunnenkamp and Spatz 2004).



adviser at the International Finance Corporation (IFC), reveals the more selfish motivation of banks: A senior banker responsible for risk management approached the IFC, a member of the World Bank Group, and asked this institution to guide the banks towards a common approach of managing risks in project lending. The coordination failure to be overcome was that “the staff [of this banker] always noted that if they did not finance the project, it would be done by the competition next door, and the bank would unnecessarily lose the business” (Lazarus 2004).

The private banks got the requested support from the IFC and agreed on a common approach. It is open to question, however, whether this is good news for anybody but the banks which succeeded to limit competition and to reduce the risk of litigation over environmental damage ensuing from project financing (Bonzom and Kamp 2003). Meanwhile further banks have adopted the Equator Principles; participating banks account for about 80 percent of project finance lending (Lazarus 2004). Proponents of the “greening” of project financing maintain that the lenders increasingly recognise their responsibility for promoting sustainable investment and enforcing environmental guidelines. The unpleasant implication for borrowers is that they are confronting an effective cartel; environmental and social standards can no longer be negotiated. Borrowers with different preferences have less choices in financing projects — which can hardly be regarded as an undisputed success.

## **V. CSR AND THE NEED FOR GOVERNMENT REGULATION**

The discussion in the previous sections invites the question whether it is appropriate to rely on – more or less - voluntary corporate commitments when it comes to environmental and social standards which the business sector shall observe. It is mainly in this regulatory dimension that the CSR/SRI concept may represent a new paradigm, though not necessarily a better one. Public regulation of the business sector by national governments or multilateral

institutions represents the obvious alternative to voluntary corporate commitments. Mandatory regulations, of course, have their own problems. In Germany, for example, the “regulatory overkill” is widely perceived to act as a serious disincentive to private investment. Yet it is for good reasons that the EU’s *Green Paper* warns: “Corporate social responsibility should ... not be seen as a substitute to regulation or legislation concerning social rights or environmental standards” (Commission of the European Communities 2001: 7).

As it seems, companies often embraced the CSR/SRI concept not least because this move pre-empted more binding public regulation. According to Wong (2003: 18), there is a simple reason for companies to consider CSR to be “the smart thing to do”: The business strategy is that “before losing control with state regulation and civil society regulation, companies better act first and act voluntarily.” The reaction of TNCs to the Global Compact fits into this line of reasoning.<sup>16</sup> The President of the International Chamber of Commerce added an important proviso after praising the UN initiative in May 2000 ([http://www.iccwbo.org/home/news\\_archives/2000/buda\\_global.asp](http://www.iccwbo.org/home/news_archives/2000/buda_global.asp); accessed in July 2004): “There must be no suggestion of hedging the Global Compact with formal prescriptive rules. We would resist any tendency for this to happen.” In the business community, the Global Compact has been promoted as an initiative of “enlightened self-interest” (Richter 2003: 79); this author suspects that the Compact allowed TNCs to undermine efforts to build up more efficient public regulation.

The regulatory imbalance that characterizes existing international investment agreements (IIAs) supports the view that the business community has been largely successful in preventing binding corporate obligations. IIAs have been concluded bilaterally,

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<sup>16</sup> See also the reaction to the proposal of a UN Code of Conduct on Transnational Corporations in the early 1990s (Richter 2003).

plurilaterally in the context of regional integration agreements, and multilaterally (notably the WTO agreement on Trade-Related Investment Measures). Most of them have in common that they comprise little on corporate obligations, whereas governments have increasingly tied their own hands by agreeing to stricter discipline with regard to FDI policies (e.g., the prohibition of local-content requirements and similar performance requirements). Even though some developing countries, notably India, have harshly criticised this regulatory imbalance and would like to maintain flexible and selective FDI policies, there is a clear trend: The prevailing euphoria about FDI and fierce competition for it increasingly relieve TNCs from government regulation. At the same time, FDI subsidies and voluntary codes of conduct proliferate.

This combination of deregulation, subsidisation and CSR is unlikely to enhance the benefits developing host countries may derive from FDI inflows. Empirical analyses indicate that deregulation *per se* does little to stimulate FDI flows.<sup>17</sup> Furthermore, the preoccupation with deregulation must not blind policymakers in developing countries as to the regulatory void in important respects:

- It seems somewhat naive to demand TNCs to refrain from restrictive business practices as part of their CSR, unless an effective competition law is in place and enforced by the government.
- Likewise, TNCs cannot reasonably be expected to transfer modern technology to host countries only because such transfers figure prominently in voluntary codes of conduct. Again the critical question is whether the government plays

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<sup>17</sup> For details, see Nunnenkamp and Pant (2003) and the literature given there.

its role, for example, by setting up and enforcing appropriate rules on intellectual property rights.

- NGOs sometimes complain that the mainstream CSR agenda is silent on tax evasion by TNCs and the ensuing erosion of the tax base in developing countries. However, the more serious problem seems to be that host-country governments offer generous subsidies and tax privileges when competing for FDI. Incentives-based competition explains, for example, why foreign mining companies avoided paying taxes and royalties in Chile (Utting 2003: 7). It will make little difference to call upon TNCs to meet their tax obligations and contribute to public revenues (UNCTAD 2003: 164-5), unless governments take responsibility for stopping the race to the top in subsidising FDI.

All this suggests that developing countries should not expect too much from the CSR/SRI concept when drawing on TNCs in order to stimulate development at home. As noted by UNCTAD (2003: 165), the discussion of good corporate citizenship focuses on the environment, human rights and working conditions, whereas “there is ... little debate about issues pertaining directly to the economic development interests of developing countries.” However, even an extended CSR/SRI agenda that included development issues such as poverty alleviation, skill upgrading, linkage creation and technology transfers would not do the trick, unless host-country governments do a proper job in all these areas.

## **VI. SUMMARY**

In various respects, the behavioural consequences of the CSR/SRI concept tend to be more apparent than real even in developed countries where this concept is most popular. From this perspective, CSR and SRI seem to be a fad, rather than a new paradigm. Yet developing countries may experience some unpleasant consequences. This is because the costs of the

CSR/SRI agenda are partly externalised, i.e., shifted towards stakeholders not taking part in defining the agenda. From this perspective, the CSR/SRI concept appears to be a plot laid by its proponents in developed countries. It is mainly with regard to the regulatory dimension that CSR and SRI may represent a new paradigm, though not necessarily a better one. The risk is that voluntary corporate commitments replace government regulations even in areas where the latter are indispensable.

Public policy tasks that should not be “privatised” include: competition policy, social policy priorities, as well as the weighting of competing economic, social and environmental goals. Of course, one can argue about how far government regulation should go in these areas. At the same time, the limitations of the CSR/SRI concept clearly suggest that governments should stick to their guns. If an appropriate regulatory framework is in place and effectively enforced, company executives striving for profitability, rather than being pressed to perform public tasks, represent the complementary part of an efficient division of labour between the private and the public sector.

This is not to ignore that governments, particularly those in many developing countries, may lack the capacity to regulate effectively, or the willingness to do so. But it is no promising alternative to call upon TNCs not to take advantage of weak legal and administrative systems in developing host countries (e.g., UNCTAD 2003: 165). Rather, this request points to the basic defect of the CSR/SRI concept, namely that private entities are assumed to perform functions that belong to governments.

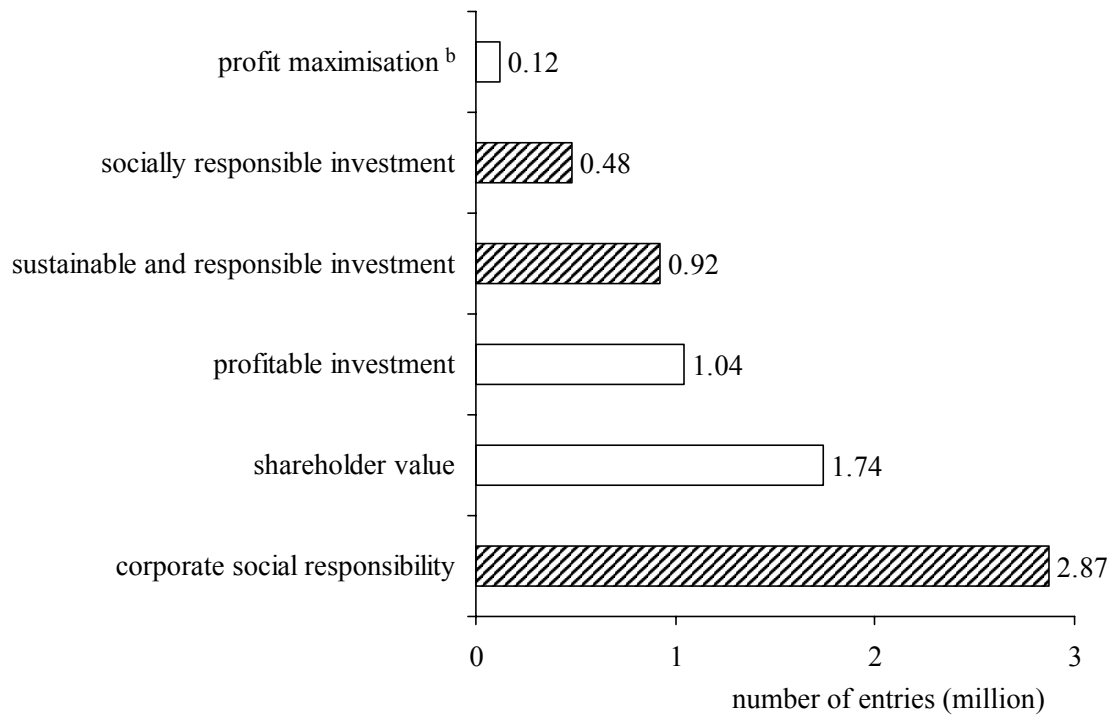
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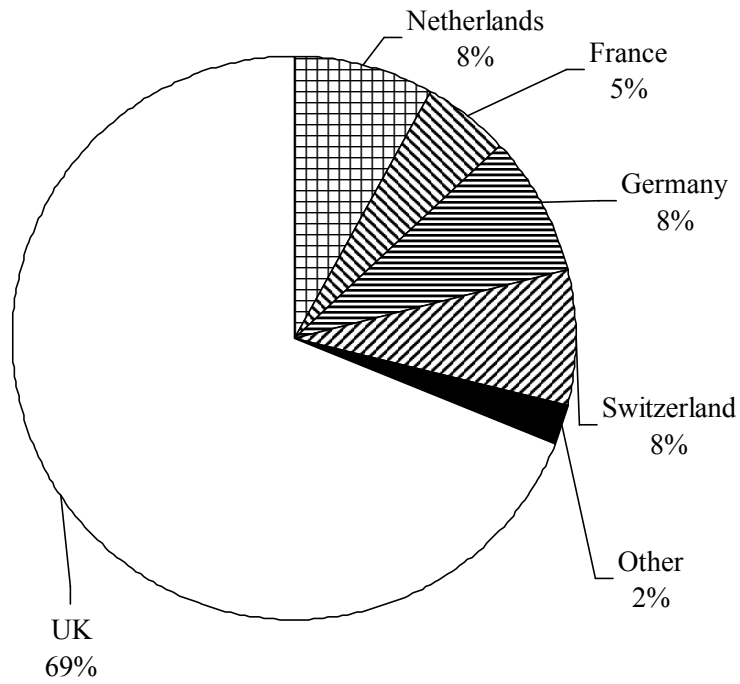
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Figure 1 — Results of a Google Search<sup>a</sup>

<sup>a</sup> July 2004.— <sup>b</sup> Entries with British spelling of maximisation plus entries with American spelling.

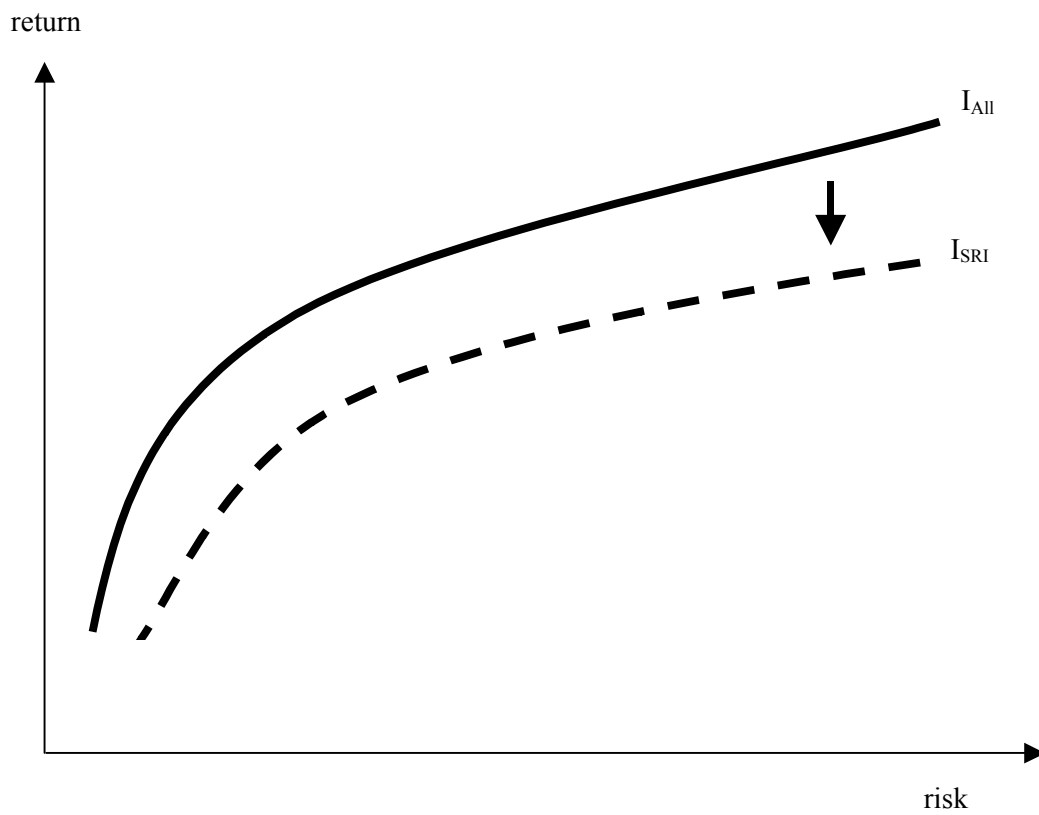
Figure 2 — Core Institutional SRI Market in Europe<sup>a</sup>: Shares of Major Countries



<sup>a</sup>Total market volume: 34 billion Euro.

Source: EUROSIF (2003).

Figure 3 — Screening for SRI: Theoretically Expected Impact on the Risk-Return Trade-off<sup>a</sup>



<sup>a</sup>Lines of efficient portfolios with an unrestricted investment universe ( $I_{All}$ ) and the subset of SRI ( $I_{SRI}$ ).