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## Corporate Social Responsibility

### CSR Doesn't Pay

**Corporate managers should try and act responsibly. But they shouldn't expect the market to reward them for doing so.**

We increasingly hear that corporate social responsibility has become a business imperative. Newspapers, magazines and books glowingly describe the business benefits of behaving responsibly--and caution managers about the business risks of a poor CSR performance.

Executives are repeatedly informed that by demonstrating concern for the environment, human rights, community development and the welfare of their employees both in the U.S. and abroad, they will make their firms more profitable. Their firms will gain a competitive advantage by appealing to the growing numbers of socially and environmentally oriented consumers, investors and employees.

The belief that corporate responsibility "pays" is a seductive one: Who would not want to live in a world in which corporate virtue is rewarded and corporate irresponsibility punished? Unfortunately, the evidence for these rewards and punishment is rather weak. There is a "market for virtue," but it is a very limited one. Nor is it growing.

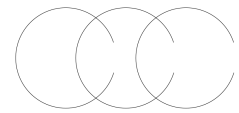
One can certainly find examples of firms with superior CSR performance that have done well, as well as firms with poor CSR reputations that have performed poorly. But there are at least as many examples of firms with good CSR records that have not done well and firms with poor CSR reputations that rewarded their shareholders.

The good news is that firms with superior CSR performance have not performed any worse than their less virtuous competitors. But the disappointing news is that neither have they done any better. For most firms, most of the time, CSR is largely irrelevant to their financial performance.

Revealingly, the long-term performance of socially responsible investment funds has been no better, or worse, than those of funds that use other criteria to predict future shareholder value.

Part of the reason why CSR does not necessarily pay is that only a handful of consumers know or care about the environmental or social records of more than a handful of firms. "Ethical" products are a niche market: Virtually all goods and services continue to be purchased on the basis of price, convenience and quality.

Although ethical mutual funds have grown in size, they have had no measurable impact on share prices. Mainstream investors still rarely consider a firm's CSR record in deciding which shares to buy, sell or hold. While many business students now profess an interest in working for more responsible firms, their less responsible competitors appear to have no difficulty in attracting top talent.



**Starbucks** (nasdaq: SBUX) provides a good example of the limited importance of CSR to financial performance. The firm enjoys a strong CSR reputation due to its generous labor policies and its commitment to improve the earnings and environmental practices of coffee growers in developing countries.

Yet since the beginning of 2008, its shares have recently declined nearly 50% (at last glance the S&P 500 is down "only" 36%). The stock's disappointing performance has absolutely nothing to do with CSR: It is entirely due to the firm's overexpansion and, most recently, the increasing unwillingness of consumers to pay as much for a cup of coffee as for a gallon of gasoline.

Other CSR icons, such as Levi Strauss, **Gap** (nyse: GPS) **Whole Foods** (nasdaq: WFMI) and **Timberland** (nyse: TBL) have also fared poorly in the marketplace.

**General Electric** (nyse: GE) has been widely applauded by environmentalists for its "Ecomagination" line of more energy efficient and environmentally responsible products. These products have sold well, prompting many observers to conclude that for corporate America, "green" has become the new "green."

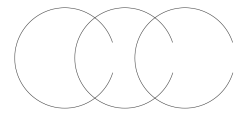
Before the recent market chaos, GE's share price had been stagnant for nearly six years. Whatever GE's current or projected earnings from Ecomagination, as well as from the firm's substantial investments in alternative energy, they have been overshadowed by Wall Street's disappointment with GE's overall earnings. In fact, GE performed much better under Jack Welch, who was not known for his interest in environmental responsibility. Moreover, GE also continues to make substantial, and highly profitable, investments in the financing and construction of coal-fired power plants, indicating that there is still money to be made by less environmentally responsible behavior. The firm with possibly the world's poorest environmental reputation is **Exxon Mobil** (nyse: XOM) largely due to its reputed indifference to the problem of global climate change and its continued focus on fossil fuels. Yet Exxon-Mobil is one of the world's most profitable corporations. Over an extended period of time, it has performed far better financially than **BP** (nyse: BP) which changed its brand to Beyond Petroleum to emphasize its responsibility to help reduce the world's dependence on fossil fuels, and which, unlike Exxon-Mobil, has supported mandatory greenhouse gas reductions.

The contrast between Exxon-Mobil and BP reveals another limitation of the business case for corporate responsibility. It is often difficult to distinguish responsible and irresponsible firms. While BP may have a more responsible record than Exxon-Mobil when it comes to the issue of global climate change, Exxon-Mobil has recently been far more successful in preventing accidents and avoiding oil spills. It is thus not obvious which firm is more 'responsible.'

To take another well-known example: **Merck** (nyse: MRK) has been widely applauded for its development and free distribution of a drug to cure river-blindness, a dreadful disease which affects tens of millions of the world's poorest people. Yet this same company withheld important information regarding the safety of its highly profitable drug Vioxx.

These examples are not unusual: Few firms are consistently responsible--or irresponsible--across all their business operations.

One can find examples of successful firms for whom CSR has been a core element of their business strategy. Patagonia and Seventh Generation come readily to mind. Other firms such as **Dupont** (nyse: DD) **Alcoa** (nyse: AA) and **IBM** (nyse: IBM) have reaped substantial savings from reducing their energy use while **Toyota** (nyse: TM) has successfully marketed hybrid cars.



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But it is important not to generalize from these examples. To assume that the business environment has fundamentally changed and that we are entering a new world in which CSR has become critical to the success of *all* or even *most* firms is misinformed. The market has many virtues, but reconciling corporate goals and public purposes is unfortunately not among them. Managers *should* try to act more responsibly. But they should not expect the market to necessarily reward them--or punish their less responsible competitors.

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