THE UNIVERSITY OF NEWCASTLE
AUSTRALIA

Faculty of Business and Law

GSBS6481 International Business Strategy

Week 11: Corporate Social Responsibility of MNEs and Governing Global Corporations and

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Reference & Readings

- Peng, Mike W (2021), *Global Strategy*, 5th ed. USA: Cengage Learning.
  - Chapter 11 & 12.

Key concepts

- Stakeholder
- A stakeholder's view of the firm
- Corporate social responsibility (CSR) practices
- Corporate governance
- Ownership types
- Principle-agent conflict
- Principle-principle conflict
- Governance mechanisms

Outline

- Corporate Social Responsibility of MNEs
  - ➢ The stakeholder view of the firm
  - ➢ Main areas of CSR for MNEs
    - ▪ Student presentations / discussions on MNEs' CSR reports
  - ➢ Three perspectives on CSR
  - ➢ CSR and corporate performance
- Governing global corporations
  - ➢ Owners
  - ➢ Managers
  - ➢ Board of directors
  - ➢ Governance mechanisms

A Fundamental debate on the nature of the firm

- The CSR debate centers on the nature of the firm in society. Why does the firm exist?

- One side of the debate argues the "the social responsibility of business is to increase its profits, which leads to efficient capital and product markets"

- Advocates of shareholder capitalism argue that if firms attempt to attain social goals, managers will lose their focus on profit maximization

A Stakeholder View of the Firm

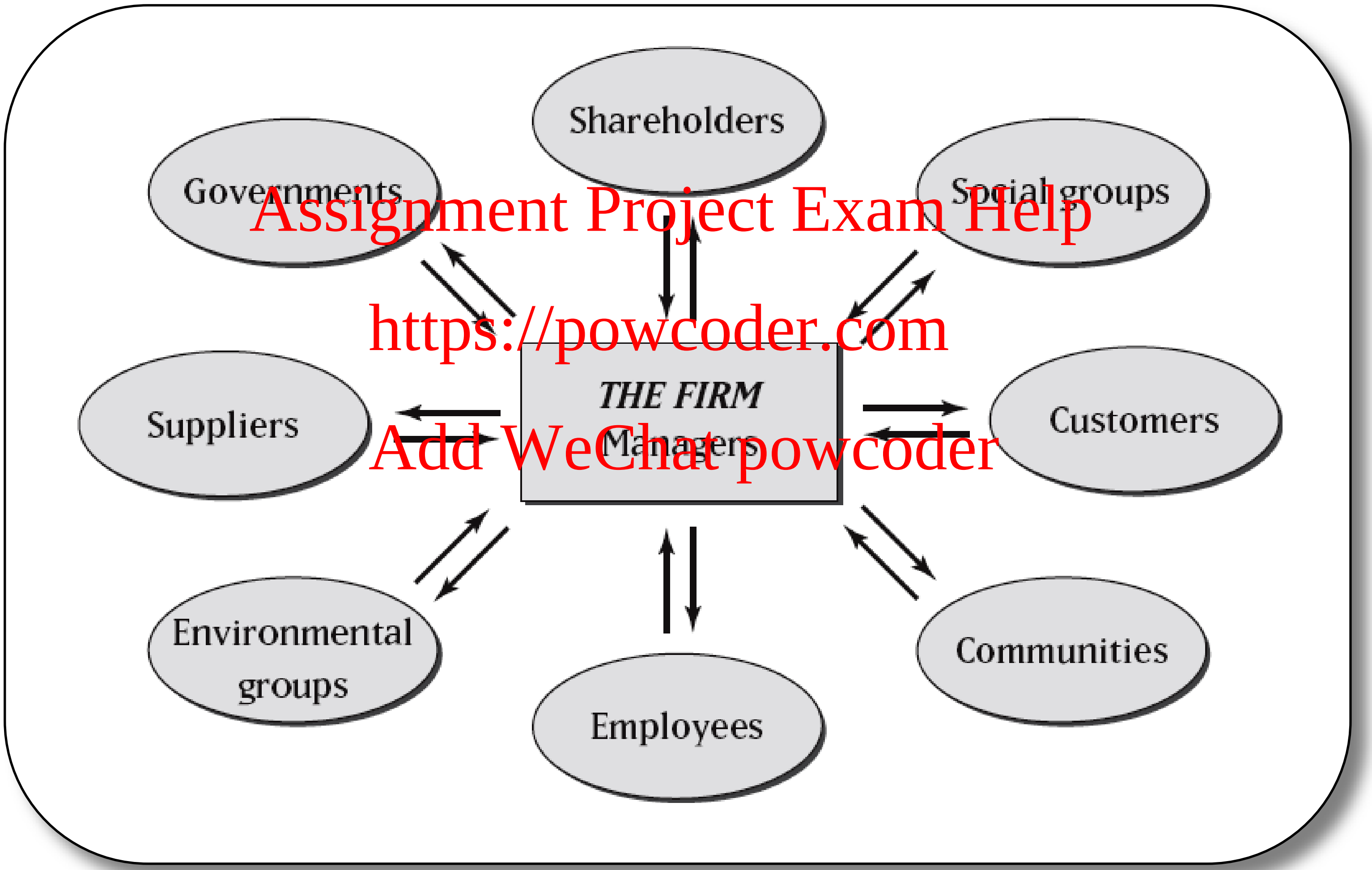
- A stakeholder is “any group or individual who can affect or is affected by the achievement of the organization’s objectives”

- Primary and secondary stakeholder groups

  - Primary stakeholder groups are those on whom the firm relies for survival and prosperity

  - Secondary stakeholder groups are defined as “those who influence or affect, or are influenced or affected by, the corporation, but they are not engaged in transactions with the corporation and are not essential for its survival”

A Stakeholder View of the Firm (cont.)



Source: Adapted from T. Donaldson & L. Preston, 1995, The stakeholder theory of the corporation: Concepts, evidence, and implications (p. 69), Academy of Management Review, *20: 65–91. Copyright © 1995. Reprinted by permission of Academy of Management Review via Copyright Clearance Center.*

A big picture perspective

- Goal for CSR is global sustainability, defined as the ability "to meet the needs of the present without compromising the ability of future generations to meet their needs"
- Drivers of global sustainability efforts:
  - Rising levels of population and inequity, high levels of poverty in some countries,
  - Increasing important roles of NGOs and other civil society
  - Effects of industrialization on the environment crisis e.g. global warming

Moral Obligations of Multinational Enterprises?

Multinational corporations have power that comes from their control over resources and their ability to move production from country to country.

Moral philosophers argue that with power comes the social responsibility for corporations to give something back to the societies that enable them to prosper and grow.

What do you think?

Learning from CSR/Sustainability reports

- Corporate Social Responsibility reports (or sustainability report) can be found from many multinational companies' websites. E.g.
  - ➢ Woolworths Group (woolworths.com.au -> "sustainability")
  - ➢ Peabody (peabodyenergy.com -> "sustainability")
- CSR reports can also be found in websites of the following organizations and be downloaded for free
  - ➢ The Sustainability Disclosure Database
  - ➢ https://www.globalreporting.org/reportregistration/verifiedreports
  - ➢ The UN Global Compact www.unglobalcompact.org/ ("Who We are" -> "Our Participants")
- These reports provide information about the CSR activities of the companies in different areas. However, be aware some companies also use these reports for "greenwashing"

Student presentations

- Every student please download and discuss a recent Corporate Social Responsibility report (or sustainability report) of a multinational company
- Each student please have a brief presentation introducing the report you have examined
- Please consider the following in your presentation:
  - What are the main businesses of the company;
  - What are the main areas covered in the report;
  - What are the main highlights in the report

CSR for MNEs recommended by international organizations

- MNEs and Environment
  - Should respect the host country laws and regulations concerning environmental protection (OECD, UN)
  - Should supply to host governments information concerning the environmental impact of MNE activities (ICC, UN)
- MNEs and Human Rights
  - Should respect human rights and fundamental freedoms in host countries (UN)

Note: OECD= Organisation for Economic Co-operation and Development (OECD); UN= United Nation; ICC = International Chamber of Commerce; ILO = International Labor Office

CSR for MNEs recommended by international organizations (cont.)

- MNEs and Employment Practices
  - Should cooperate with host governments to create jobs in certain locations (ICC)
  - Should respect the rights for employees to engage in collective bargaining (ILO, OECD)
- MNEs and Host Governments
  - Should not interfere in the internal political affairs of the host countries (OECD, UN)
  - Should consult governments and national employers' and workers' organizations to ensure that their investments conform to the economic and social development policies of the host countries (ICC, ILO, OECD, UN)
  - Should reinvest some profits in the host countries (ICC)

CSR for MNEs recommended by international organizations (cont.)

- MNEs and Laws, Regulations, and Politics
  - Should respect the right of every country to exercise control over its natural resources (UN)
  - Should refrain from improper or illegal involvement in local politics (OECD)
  - Should not pay bribes or render improper benefits to public servants (OECD, UN)
- MNEs and Technology Transfer
  - Should develop and adapt technologies to the needs of host countries (ICC, ILO, OECD)
  - Should provide reasonable terms and conditions when granting licenses for industrial property rights (ICC, OECD)

The three perspectives on CSR

- Industry-based view
  - Rivalry among competitors
  - Threat of potential entry
  - Bargain power of suppliers
  - Bargain power of buyers
  - Threat of substitute

The three perspectives on CSR (cont.)

- Resource-based view
- CSR-related resources can include *tangible* technologies and processes as well as *intangible* skills and attitudes

  - Do CSR-related resources and capabilities add *value*?
  - CSR-related resources are not always *rare*.
  - The advantage based on CSR-resources will only be temporary if competitors can *imitate* it.
  - Does the firm have *organizational* capabilities to do a good job on CSR?

The three perspectives on CSR (cont.)

- Institution-based view
  - Formal institutions
  - Informal institutions

Four responses of MNEs

- Reactive strategy: little or no support by top manageme
  - ➢ "not my problem"
- Defensive strategy: focuses on regulatory compliance
  - ➢ "what's the point"
- Accommodative strategy: CSR as a worthwhile endeavo
  - ➢ "if it is easy"
- Proactive strategy: Actively participate in policy discussions, build alliances with stakeholders and voluntarily go beyond what the regulations require
  - ➢ "green crusaders"

CSR and corporate performance

The CSR-economic performance puzzle: Does CSR improve economic performance?

From CSR to global CSR: Critical Debates

Domestic versus overseas social responsibility

- Potentially increases profits, provides employment to host countries and increases standards of living there
- However, often domestic employees and communities pay the price for this expansion

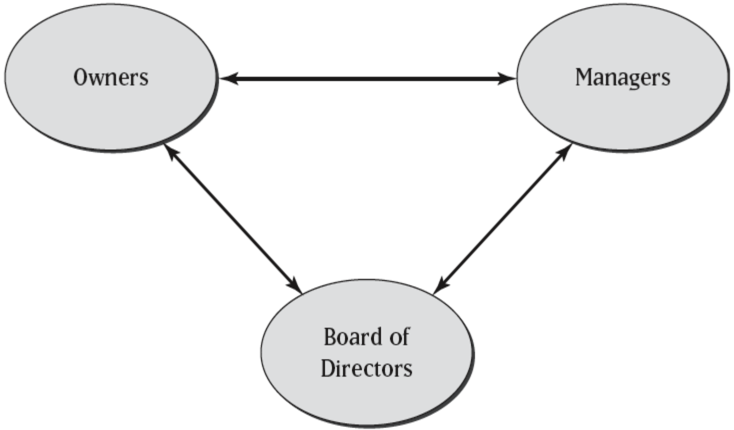
Active versus inactive engagement overseas: To what extent should an MNE use threats or its power to impose its values in a country?

Race to the bottom ("pollution haven") versus race to the top: Some companies may move to a country to escape environmental regulations

Corporate Governance

- Definition
  - "the system by which companies are directed and controlled“ -European Corporate Governance Institute

- Key elements
  - involves regulatory and market mechanisms, and the roles and relationships between a company’s management, its board, its shareholders and other stakeholders, and the goals for which the corporation is governed.



Owners

- Concentrated versus Diffused ownership
  - concentrated ownership and control – founders usually start up firms and completely own and control them on an individual or family basis
  - diffused ownership – publicly traded corporations owned by numerous small shareholders but none with a dominant level of control
  - separation of ownership and control – the dispersal of ownership among many small shareholders, in which control is largely concentrated in the hands of salaried, professional managers who own little (or

Ownership types

- Family ownership
  - The majority of large corporations throughout continental Europe, Asia, Latin America, and Africa feature concentrated family ownership and control
- State ownership
  - State-owned enterprises (SOEs) are de facto owned and controlled by government agencies; thus, SOE managers and employees have little motivation to improve performance
- And many other ownership types, e.g.
  - “institutional ownership” which refers to the ownership stake in a company that is held by large financial organizations, pension funds etc.

Private ownership versus state ownership

Table 2.6 Private Ownership versus State Ownership

	Private ownership	State ownership
Objective of the firm	Maximize profits for private owners who are capitalists (and maximize shareholder value for public shareholders if the firm is publicly listed).	Optimal balance for a "fair" deal for all stakeholders. Maximizing profits is not the sole objective of the firm. Protecting jobs and minimizing social unrest are legitimate goals.
Establishment of the firm	Entry is determined by entrepreneurs, owners, and investors.	Entry is determined by government officials and bureaucrats.
Financing of the firm	Financing is from private sources (and public shareholders if the firm is publicly traded).	Financing is from state sources (such as direct subsidiaries or banks owned or controlled by governments).
Liquidation of the firm	Exit is forced by competition. A firm has to declare bankruptcy or be acquired if it becomes financially insolvent.	Exit is determined by government officials and bureaucrats. Firms deemed "too big to fail" may be supported by taxpayer dollars indefinitely.
Appointment and dismissal of management	Management appointments are made by owners and investors, largely based on merit.	Management appointments are made by government officials and bureaucrats who may also use non-economic criteria.
Compensation of management	Managers' compensation is determined by competitive market forces. Managers tend to be paid more under private ownership.	Managers' compensation is determined politically with some consideration given to a sense of fairness and legitimacy in the eyes of the public. Managers tend to be paid less under state ownership.

Sources: Extracted from text in (1) M. W. Peng, 2000, *Business Strategies in Transition Economies* (p. 19), Thousand Oaks, CA: Sage; (2) M. W. Peng, G. Bruton, & C. Stan, 2014, Theories of the (state-owned) firm, Working paper, Jindal School of Management, University of Texas at Dallas.

Trends in Ownership Changes

- In the Anglo-American world
  - Large institutional investors have both the incentive and the resources to closely monitor and control managerial actions.
  - Ownership of US firms has gradually become more concentrated in the hands of institutional investors in recent decades.
  - UK corporations have also experienced a similar transformation in their ownership patterns
- Since the 1980s, SOEs have failed to deliver satisfactory performance due to an incentive problem.
- Privatization has reduced the SOE share of the global GDP from over 10% in 1979 to under 5% today.

Managers

- Principal-Agent conflicts

  - Arising from the relationship between shareholders and professional managers

- Principal-Principal conflicts

  - Such conflicts are between two classes of principals: controlling shareholders and minority shareholders

Principal-Agent Conflicts

- Agency Theory
  - Because the interests of principals and agents do not completely overlap, there will *inherently* be principal-agent conflicts, which result in agency costs
  - Conflicts persist because of *information asymmetries* between principals and agents (agents always know more about their tasks than principals)

Principal-Agent Conflicts(cont'd)

- Agency Problems
  - Excessive on-the-job consumption
  - Low-risk, short-term investments
  - Empire-building (excessive diversification)
  - In SOEs, agency problems are also extensive
- Reducing Agency Problems
  - While it is possible to reduce information asymmetries and minimize agency problems, it probably is not realistic to expect to completely eliminate such problems

Principal-Principal Conflicts

- Principal-Principal Conflicts
  - Instead of between principals (shareholders) and agents (professional managers), the primary conflicts are between two classes of principals: controlling shareholders and minority shareholders
  - Tunneling and related transactions

Board of Directors

- Key features
  - Board size
  - Board Composition: Otherwise known as the insider/outsider mix
  - Leadership Structure: involves whether the board is led by a separate chairman or by the CEO who doubles as a chairman—a situation known as CEO duality
  - Board Interlocks: When one person affiliated with one firm sits on the board of another firm
- The role of Boards of Directors
  - (1) control, (2) service, and (3) resource acquisition functions
- Directing strategically: Directors must strategically

Internal Governance Mechanisms

- Voice-based mechanisms
- Shareholders' willingness to work with managers, usually through the board, by "voicing" their concerns.
- "Carrots" and "sticks"
  - Carrots: Very high pay for performance?
  - Sticks: Dismissal
    - Global 2500 MNEs: Involving 40% of all CEO changes in 2002

External Governance Mechanisms

- Exit-based Mechanisms: The Market for Corporate Control
- The takeover or mergers and acquisitions (M&A) market.
- The stock of a firm will be undervalued by investors when managers engage in self-interested actions and internal governance mechanisms fail.
- In the 1980s, nearly half of all major US corporations received a hostile takeover offer.

Internal and External Governance Mechanisms: A Global Perspective

Internal governance mechanisms	*External governance mechanisms*: Weak	*External governance mechanisms*: Strong
Strong	(Cell 1) Germany Japan	(Cell 2) Canada
Weak	(Cell 3) State-owned enterprises	(Cell 4) United States United Kingdom

Source: Cells 1, 2, and 4 adapted from E. R. Gedajlovic & D. M. Shapiro, 1998, Management and ownership effects: Evidence from five countries (p. 539), Strategic Management Journal, *19: 533–553.*