COMPETING RESPONSIBLY

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Abstract: In this paper we examine the effects of different competitive conditions on the determination and evaluation of strategies of corporate social responsibility (CSR). Although the mainstream of current thinking in business ethics recognizes that a firm should invest in social responsibility, the normative theory on how specific competitive conditions affect a firm's social responsibility remains underdeveloped. Intensity of competition, risks to reputation and the regulatory environment determine the competitive conditions of a firm. Our central thesis is that differential strength of competition produces differential moral legitimacy of firm behavior. When competition is fierce or weak, different acts or strategies become morally acceptable, as well as economically rational. A firm has to develop its own strategy of social responsibility, in light of its competitive position, as well as ethical considerations.

1. Introduction

It is widely accepted in business ethics that a moral evaluation of firm behavior should focus on the impact of the firm on the rights and legitimate interests of its stakeholders. CSR is often defined in stakeholder terms as well. The European Commission, for example, defines CSR as "a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis, as they are increasingly aware that responsible behavior leads to sustainable business success."

When we define the responsibilities of a firm in stakeholder terms, we should realize that the firm itself is a nexus of stakeholders. A firm is a co-operative venture for mutual benefit, a coalition of participants (clients, employees, share owners, suppliers), who are all economic stakeholders of each other, and who all depend on the continuity of the firm for their wealth and well-being. Hence, the ability of a firm to survive is an important instrumental moral goal, in view of the legitimate interests and rights of many stakeholders. This means that policies and strategies of companies directed at the continuity of the firm (operationalized in terms of profitability, market share, growth, future cash flows, etc.) must be considered as morally justified activities, prima facie. The continuity of the firm is an important moral value, albeit of an instrumental nature.

This has a bearing on CSR. Contrary to what the European Commission suggests, in the above quotation, there is not always a positive relationship between responsible
behavior and sustainable business success. The relationship depends on many factors, important ones of which are the competitive conditions of a firm. Depending on the competitive conditions, some CSR initiatives can be beneficial to a firm, others not. Therefore, not all forms of CSR are feasible for a firm given the actual market in which the firm has to be successful. Competitive conditions are an intervening variable, influencing the relationship between CSR and business success, and even deciding over whether this relationship is positive or negative.

In our view, competitive conditions affect a firm’s social responsibility with respect to specific dilemmas, as well as with respect to the CSR strategy a firm can or should adopt. This is so, because competitive conditions are determinants of a firm’s survivability, which is an instrumental moral value. In light of the moral value of survivability, managers have a duty to take the competitive conditions of their firm into account in all the strategic decisions that they make, including decisions about CSR. From this, it does not follow, however, that the survivability of the firm should always override other considerations. Sometimes the stakeholders would be better off if a certain business activity were terminated immediately. Take, for instance, the production of CFCs that erode the ozone layer. All living creatures on planet Earth have a high stake in stopping the production of CFCs. So a law that forbids the production of CFCs, as it was actually adopted in, among others, the United States, is morally desirable, even if it means that certain CFC-producing firms would not survive as a result. Furthermore, sometimes the timely liquidation of a firm is legitimate in order to secure the financial interests of stakeholders. Finally, if a certain business violates human rights to stay in business, this could not be legitimized by referring to the instrumental moral value of the firm’s survivability. In other words, if the evil of putting the continuance of a firm in jeopardy is the lesser evil, survival of the firm will be overruled by other moral considerations.

Following John Kay, we define business strategy as a firm’s scheme for handling the relationships with its environment. Such a scheme includes market entry decisions, product positioning decisions and an approach to relationship building with stakeholders. A scheme may be articulated or implicit, pre-programmed or emergent. The level of conscious design by management of a scheme may vary, since all strategies are based on a mixture of calculation and opportunism, of vision and experiment. CSR as a strategy aims particularly at social and environmental aspects of doing business. Assessing CSR from a strategic perspective, may seem to imply that ethical responsibilities are subordinated to economic imperatives. It may seem as if CSR is not intrinsically valued, but only instrumentally. The suspicion arises that the motivation of firms behind CSR is not truly ethical, since it is in their self-interest. We cannot treat this problem fully within the scope of this paper, because we would then have to deal with the philosophical question what exactly constitutes the moral worth of an action. Is it the respect for the moral law, as Kant suggested? Or are moral sentiments like empathy and sympathy necessary conditions for a truly ethical motivation? For the purpose of this paper, it suffices to assume that for a strategy of CSR to be qualified as ethical or moral it is not required that self-interested reasons be completely absent. Beyond this, we stress the instrumental moral value of the continuation of a
firm with respect to the fulfillment of the legitimate expectations of stakeholders. From the perspective of the social responsibility of a firm, it can only be considered a good thing when ethics contribute to the continuation of the firm, since this way a firm will be able to contribute more to the well-being of stakeholders and of non stakeholders such as the environment. Furthermore, the fact that CSR can serve strategic purposes does not say anything about the motivations behind it. Maybe the members of the board of directors are truly motivated by a sense of moral duty, maybe they are only backing the CSR efforts because it is good for business or for themselves. They will probably have mixed motives to integrate CSR in their corporate strategy. We suggest that the qualification of a strategy as a strategy of CSR should not depend on the motivation of managers, but only on goals and outcomes, just like this is the case for any other business strategy.

CSR should make sense from the perspective of the overall competitive strategy of a firm (and the other way around), and should be treated as an integral part of it; not only because this furthers the long-term survival of a firm, but also because this way the moral claims of stakeholders have the best chance of becoming an accepted part of the firm's decision-making structure and its organizational culture. This way, the relationship between ethics and economics becomes in large measure a matter of strategic choice rather than discovery, as Lynn Sharp Paine has argued.

Many business ethicists agree that, regardless of what a firm does to improve its social performance and to take on its moral responsibilities, it should also be profitable in the long run. Mostly, however, this relationship is discussed only in general terms. Little attention is paid to the relationship between specific competitive conditions and the possibilities of a firm to adopt a specific CSR strategy. Sethi and Sama developed a descriptive model of the effect of marketplace competition, industry structure and firm resources on ethical business conduct. It is important to describe how competitive conditions influence ethical business behavior, but this does not tell us to what extent and in what sense it is morally acceptable that market conditions influence the outcomes of the decision-making process. To answer this question, we will have to look more specifically into the relationship between competitive conditions and CSR. This brings us to the following research question:

How can firms compete in a morally acceptable way, given the fact that they have to survive in an environment where competition is (a) more or less intense, (b) more or less regulated, and (c) more or less susceptible to the scrutiny of influential stakeholders?

By specifying the relationships between specific competitive conditions and CSR strategies, greater justice can be done to the special circumstances that confront a firm that tries to balance its social responsibility with the need to be profitable.

To develop a specifying model of the relationship between CSR and competition, we will first discuss the assumption of perfect competition in economic theory. This assumption totally paralyses the debate on CSR from an economic perspective, so we will first have to show why, from an ethical perspective, this assumption must be rejected. Next, in section three, we will introduce a conceptualization of competitive forces and competitive strategies, based on the work of Porter. In sections four to six,
we will examine what CSR strategies are feasible for firms, under different competitive conditions. In chapter seven we will draw a number of conclusions.

2. Intensity of Competition and CSR Strategies

Why should firms pursue profitability? Profits are not the purpose of a business activity, but a means of building the business and rewarding employees, executives, and investors, says Solomon. According to Peter Drucker, profits are not the explanation, cause, or rationale of a firm's behavior and management decisions, but the test of their validity. Steinmann and Löhrl express a similar view when they call profitability the formal criterion of success of business activities. This criterion does not say anything as to how a firm can or should become profitable. Although the market system functions in such a way that only profitable firms will eventually survive, this does not tell management which roads will lead to corporate success. As part of the social world, the world of business is socially constructed, rather than economically determined. Corporate strategies are formed in sensemaking processes, which involve a degree of freedom. This implies that a firm can choose to integrate social responsibility into its corporate strategy. If a firm does so, management will probably be convinced that it is good for business. Whether a certain CSR strategy is indeed good for business depends on how the market and other stakeholders will respond.

Ex ante, no one can point to competitive pressures as a condition that completely eliminates the firm's social responsibility. Only the hypothetical case of perfect competition would possibly qualify as an excuse for not engaging in CSR. Standard economic theory says that, under the condition of perfect competition, firms do not have the financial means to bear costs that are unilateral, or that cannot be recovered by means of setting a premium price. Therefore, CSR efforts leading to marginal cost increases are simply not a viable option under the condition of perfect competition. When CSR efforts lead to cost savings, or to profitable new business opportunities as they often do, perfect competition not only allows for these kinds of efforts, but they are necessary, since they will lead to the maximization of profits. The tension between profits and morality is therefore limited to those CSR efforts that do not lead to a win-win situation.

But even when CSR efforts do not result in a win-win situation under perfect competition, we would argue that corporate responsibility is not completely eliminated. A firm has the moral duty to prevent posing a serious threat to health, safety or the environment, even when this means that the firm will go bankrupt. Harsh market conditions are no excuse here. Short of unilateral measures, a firm could in this case encourage government regulations or self-regulation of the industry to ensure that every competitor in the business faces the same costs. Firms always have a moral responsibility to (help) counteract a market situation in which immorality leads to a competitive advantage by seeking a solution on a higher institutional level. This is an instance of what De George has called 'the principle of ethical displacement.' We suggest that this is one of the key ethical principles of CSR, since in this way a firm helps to counter the negative side effects (or the external costs, as economists would
say) of the free market system. As one of the players on the market, each firm bears a part of the collective responsibility of all players to promote the ethical functioning of their market.

In a situation of perfect competition, a firm has no room to take on moral responsibilities that involve more costs than benefits relative to the costs and benefits of the competitors. However, since perfect competition is a theoretical ideal type which does not have much in common with most real markets, it is not justified to simply assume that firms have to deal with the extreme conditions of perfect markets. That is why we reject the view of Milton Friedman, who bases part of his criticism of CSR on this ideal description of the market, as is shown by the next quotation: "The participant in a competitive market has no appreciable power to alter terms of exchange; he is hardly visible as a separate entity; hence it is hard to argue that he has any 'social responsibility' except that which is shared by all citizens to obey the law of this land and to live according to his lights." This view of the firm as an entity that is barely visible and has no power to change things for the better or for the worse is clearly flawed as a general theory of the firm. It does not acknowledge that multinational firms in particular are becoming more and more visible to a global public and that in many markets firms have the power to influence the terms of the exchange. Friedman's assumption that most markets could be treated as if they were perfectly competitive is therefore not a methodologically proper one to make for present purposes. Nor is his conclusion acceptable which is based on this assumption, that a firm cannot have any responsibilities other than increasing its profits within the limits of the law and moral custom. Since competition in most real markets is less than perfect, we can conclude that firms in general do have at least some market power and therefore some financial room to enhance CSR.

Although we do not agree with Friedman that in general there is no room for individual firms to engage in CSR efforts that involve more costs than benefits relative to the competitors, we do want to acknowledge that the functioning of markets does put limitations on what a firm can afford with respect to CSR. This leads to a number of ethical questions. Is it morally relevant that some firms have to deal with fierce competition whereas other firms enjoy the comfort of less intense competition, when it comes to determining the moral responsibilities of a firm? Does it make a difference from a moral perspective when a firm bears considerable costs in order to comply with the law, while most of its competitors do not, because the law is not enforced consistently? Finally, what is the relevance of corporate reputation for CSR? Does reputation as a coordination mechanism always stimulate socially responsible behavior? In the next sections, we set out to answer these questions.

3. Competitive Forces and Competitive Strategies

We will base our analysis of the relationship between competition and CSR on Porter's seminal research into the competitive strategies of firms. Porter has introduced a distinction between competitive forces and competitive strategies. Competitive forces determine the degree of competitiveness within an industry. They are: the
entry of new competitors, the threat of substitutes, the bargaining power of buyers, the bargaining power of suppliers, and the rivalry among the existing competitors. These five forces influence a firm's prices, costs, and required investments, which are the constituents of return on investment. The entry of new competitors depends on economies of scale, brand identity, and capital requirements. The threat of substitutes is dependent on the relative price performance of substitutes and the buyer's propensity to substitute. The bargaining power of buyers is dependent on buyer concentration versus firm concentration, buyer volume, and the buyer's ability to integrate backward, as well as on the price sensitivity of buyers, among other things. The bargaining power of the supplier is dependent, among other things, on supplier concentration versus firm concentration, the importance of volume to the supplier, and the presence of substitute inputs. Finally, the rivalry among the existing competitors is dependent on things like the growth of the industry, intermittent overcapacity, product differences, brand identity, and switching costs.

For our purpose, it is important to note that, according to Porter, a firm is usually not a prisoner of its industry's structure. "Firms, through their strategies, can influence the five forces. If a firm can shape structure, it can fundamentally change an industry's attractiveness for better or worse. Many successful strategies have shifted the rules of competition in this way." Competitive strategies are ways for a firm to increase its competitiveness within an industry. Porter distinguishes three such strategies, namely cost leadership, differentiation and focus.

In cost leadership, a firm sets out to become the low-cost producer in its industry. To achieve the status of low-cost producer, a firm must find and exploit all sources of cost advantage. Typically, low-cost producers sell a standard product and place emphasis on reaping scale or absolute cost advantages. Having a low-cost position yields a firm above average returns in its industry, despite the presence of strong competitive forces. Its cost position gives the firm a defense against rivalry from competitors, because its lower costs mean that it can still earn returns after its competitors have lost their profits through rivalry.

A firm differentiates itself from its competitors if it is unique in something that is widely valued by buyers. It selects one or more attributes that many buyers in an industry perceive as important, and uniquely positions itself to meet these. If a firm pursues forms of uniqueness that buyers do not value, it may be different from its competitors but not differentiated. The best way to learn whether a product is truly differentiated is to see if it is rewarded for its uniqueness with a premium price.

The focus strategy rests on the choice of a narrow competitive scope within an industry. The focuser selects a segment or group of segments in the industry and tailors its strategy to serving them to the exclusion of others. This can be a particular buyer group, a segment of the product line, or a specific market region. The strategy rests on the premise that the firm is thus able to serve its narrow strategic target more effectively or efficiently than competitors who are competing more broadly.

If strategies of CSR do qualify as (part of) a competitive strategy, then we have a sound argument to back up the claim that CSR can contribute to a sustainable competitive advantage and hence to profitability. To investigate this, we will examine a
number of markets with varying degrees of competition and briefly explore some ways in which strategies of CSR can lead to a competitive advantage, or are affected by the competitive characteristics of these types of markets. To determine which CSR strategies could succeed, we will also take into account some features of the legal environment and the effect of the strategy on reputation. The combination of these three competitive conditions—intensity of competition, legal environment, and the effect on reputation—determines which strategy of CSR is commercially appropriate.

We will assume that a certain industry structure will result in more or less intense competition, depending on the five competitive forces. It takes an extensive and laborious analysis to present a complete picture of the competitive forces for an industry. For the theoretical purpose of this study, we do not need such a level of detail. For practical reasons, therefore, we will distinguish between three ideal types, or ‘frozen moments,’ of markets, that capture the intensity of the competition for an imaginary firm, at a certain point in time. We will refer to the three levels of competitiveness as ‘fierce,’ ‘strong’ and ‘weak.’ This distinction is based on stipulations, which are, of course, artificial. Empirically, the intensity of competition varies gradually along the five competitive forces.

For each level of competitiveness, we will investigate the strategic opportunities and limitations for firms to engage in CSR efforts and to deal with moral problems and dilemmas. In general, we can say that a strategy of low costs is the dominant competitive strategy under fierce competition. Only forms of CSR that are reconcilable with a low-cost strategy are competitively feasible under fierce competition. Differentiation is the dominant strategy under strong competition. CSR strategies that help a firm to differentiate itself from its competitors are appropriate under strong competition. Under weak competition, there is no dominant strategy. This market lacks competitive pressure altogether, so that very different strategies can lead to business success. Table 1 outlines the specific CSR strategies that are available to firms under different levels of competitiveness. In sections four to six, we will explain these strategies in greater detail.

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<th>Intensity of competition</th>
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<td>Dominant generic competitive strategy</td>
<td>Low-cost strategy</td>
<td>Product-differentiation strategy</td>
<td>Low-cost or product-differentiation</td>
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<td>Specific CSR strategy</td>
<td>Ethical displacement strategy: Self-regulation</td>
<td>Compliance with the spirit of the law</td>
<td>All CSR strategies are possible</td>
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<td>Legal compliance</td>
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4. CSR Strategies Under Conditions of Fierce Competition

We define fierce competition as a market in which a firm has little or no power to influence prices, because several or all of the following features of the industry structure make the five forces of competition very strong: (i) the entry barriers are low, for instance, because of low capital requirements and because brand identity is not important; (ii) the product can easily be substituted, because there is a high buyer propensity to substitute; (iii) the buyers have a strong bargaining power, because their concentration is relatively high; (iv) the bargaining power of suppliers is relatively high, due to a lack of substitute inputs; and (v) the concentration within the industry is low whereas the product is (almost) homogeneous (no product differentiation), causing the rivalry between competitors to be high. In general, one can say that fierce competition leads to low profitability and forces companies to follow a low cost strategy.

Under fierce competition, firms cannot afford to invest in CSR, if this will lead to higher costs than the competitors have to bear, because the buyers will almost immediately switch to a cheaper competitor. Under conditions of fierce competition, a firm has no financial room to bear costs that are structurally higher than those of competitors. Even under these conditions, there are some CSR strategies that are recommendable for firms. These are strategies which, although costly in the short term, are sufficiently beneficial to make them the rational option under fierce competition.

We will consider three of them, namely ethical displacement, legal compliance, and reputation protection.

**Ethical Displacement**

Ethical displacement means that if an ethical conflict cannot be solved at a certain level of social aggregation (the individual, the organization, the industry, or the national international political level), then one should look for a solution at a level other than that at which the dilemma occurs. Ethical displacement is not only relevant for a market with perfect competition, but also for a market with fierce competition, since individual firms cannot afford high unilateral investments in CSR. Firms in this situation have a duty to look for competitively neutral means to promote CSR at the industry level. A system of self-regulation of the industry should impose the same costs on all the competitors. This way no individual firm runs the risk of a competitive disadvantage. In a market with fierce competition it is, therefore, a viable form of CSR to take the initiative for industry self-regulation.

**Legal Compliance**

Under conditions of fierce competition, a firm usually has to set modest goals with respect to its strategy of CSR. It can start by trying to comply with the law. Carroll identifies legal responsibilities as one of the dimensions of CSR. Lynn Sharp Paine considers legal compliance to be an important strategy for ethics management. Both authors agree that obedience to the law is not the highest possible achievement in business ethics, but that it is an important beginning. We would like to stress here
that even this beginning can be difficult for firms, and sometimes presents a serious ethical and competitive challenge.

From an ethical perspective (assuming the instrumental moral value of the firm), a firm has to ensure itself that even the legalistic minimum level of CSR will not lead to a competitive disadvantage. To be sure, not all cost disadvantages are a competitive disadvantage. To become a competitive disadvantage the additional costs would have to be so high, or so persistent, that the firm risks losing its business to its competitors. Whether legal compliance will lead to a competitive disadvantage depends for an important part on certain features of the legal environment. Compliance with the law will probably lead to a competitive disadvantage when competitors structurally bear less costs by using loopholes in the law; or when the law is not enforced effectively. In a situation of fierce competition, an acceptable degree of enforcement would have to be determined by the probabilities of detection and conviction, and the size of the fine, compared to the cost advantage resulting from transgression.

Under fierce competition, a firm can be pressured strongly to take advantage of loopholes in the law, when not doing so would lead to a considerable relative cost disadvantage. Likewise, a firm is pressured to break the law when the law is not enforced effectively enough to create a satisfactorily level playing field among the competition. In both cases, compliance with the law could lead to bankruptcy. Hence, if a firm wants to secure its own survival, the competitive condition of fierce competition could force it to choose between its own survival and the duty to comply with the law. Under such extreme circumstances, a firm faces a moral dilemma. As we argued in section one, the continuation of the firm presents an instrumental moral value to all the stakeholders. Securing the survival of the firm is therefore morally desirable, provided that the business itself is not of an immoral nature. On the other hand, securing the continuation of the firm would imply that one breaches the moral and legal duty to comply with the law. How should a firm deal with this dilemma? The fairness of competitive conditions provides an important clue to answering this question.

Legal institutions can create circumstances that entail unfair competitive disadvantages for some firms. An example would be legislation which forbids companies to pay bribes to government officials in other countries. The USA has such legislation, under the Foreign Corrupt Practices Act of 1977. Similar legislation has recently been introduced in The Netherlands as well. Until now, the Prosecution Council has only started a few bribery cases. This is not because Dutch managers are so law abiding when it comes to bribery. On the contrary, paying money or giving gifts to government officials in order to get them to do their work (which would be a form of extortion) is widely understood as being an unfortunate but unavoidable part of doing business in some parts of the world. The rather weak enforcement of anti-bribery laws in the Netherlands creates a cost disadvantage for the compliant firms. The obedient firms are worse off as a result of their legally correct behavior, whereas the firms that violate the law benefit. A lack of law enforcement that creates a competitive disadvantage for compliant firms is an example of unfair competition. If this occurs in a fiercely competitive environment, then we believe the responsibility of firms not to pay bribes might be mitigated to some extent. Here we take recourse to the rule, introduced by
Velasquez, that the moral responsibility for an act is mitigated (but not annihilated) by the difficulty to avoid the act, among other things. It is primarily the responsibility of the government to ensure that the legal environment does not create unfair competition. According to the principle of ethical displacement, however, employer organizations and industrial organizations have a responsibility to lobby for legal improvements in this context.

A situation of unfair and fierce competition does not generally justify bribery. Paying bribes, whether one takes the initiative or not, poses a serious moral problem, because it contributes to corruption and makes markets less efficient. Therefore, it is morally better if a firm tries to stay in business without paying bribes. The only point we want to make here is that following the moral duty to comply with the law can take its toll for a firm, when competition is fierce. Managers can be confronted with tough moral choices, when compliance with the law has to be pitted against company survival. Since legal compliance in a fiercely competitive market involves a moral commitment and moral choices from a firm’s management, we believe that this strategy can rightly be called a form of CSR.

**Reputation Protection**

Another possible strategy of CSR in a market with fierce competition is the protection of a good reputation among customers. We call this a form of CSR because reputation protection involves taking care of social aspects of the relationship that cannot be completely captured in a contractual form. Although a firm’s reputation is not restricted to the assessment of past performance by customers (both individual and/or industrial), but comprises the assessment by all stakeholders, we will limit ourselves to the reputation of the firm among its customers. This focus on the customer is motivated by the fact that in a fiercely competitive market the relation between corporate reputation and actual buying behavior is very important for the continuation of the firm. We define effect on reputation as the cumulative effect of a certain issue on the customers’ beliefs with respect to those features of an organization and its product that influence their buying behavior. The opportunities of firms to use reputation protection as a CSR strategy depend on the interests of the customers. These interests can involve characteristics of the core product, but they can also involve company policies.

The condition of fierce competition involves that brand identity is not so important and the product is almost homogeneous. The customers’ interests, as far as the product itself is concerned, are closely related to features of the core product, such as product quality, price, and availability. The product has to be reliable and the price has to be on a level comparable to the prices competitors ask, otherwise the customers will buy a competitor’s product next time. In general, we can say that under the condition of fierce competition, reputation will be negatively affected if a certain breach of morality has repercussions for the features of the core product, such as its reliability and safety, and if the customers know about these repercussions. The magnitude of the negative effect will, of course, depend on the perceived importance of the impacts on health or safety. If, for instance, beef is suspected to contain growth hormones, some
consumers will look for alternative meat products. Even under fierce competition, such reputational risks can be well worth avoiding.

Company policies, even when they do not affect the quality of products, can cause negative reputational effects among customers, when they perceive the policy as immoral or indecent. This might be a reason for customers to boycott a product or a firm, even if no customer’s interest is being hurt directly. Companies like Heineken, Ikea, Nike, and Shell have, each in their own way, experienced what risks a public perception of social irresponsibility can mean to the business, especially when non governmental organizations (NGOs) target a firm with their campaign.

Public perceptions of a company’s social and environmental performance sometimes strongly influence the buying behavior of consumers, but the pressure of public perception is felt less strongly on the business-to-business market. Here, other consumers come into play, who are often less concerned about social and environmental issues. Business-to-business markets can also be fiercely competitive. Under such conditions, a firm cannot always afford to worry much about a declining reputation in the eyes of the wider public, when their business clients are insensitive to moral issues, or even benefit from them. In business-to-business markets, this parting of public anxiety and consumer interests can be observed frequently. An example of this is the case of the Dutch based-firm IHC Caland in Burma (Myanmar). IHC Caland had agreed to produce an offshore storage and offloading system for oil and gas for Premier Oil, off the coast of Burma. The deal was not illegal under European Union legislation at the time. Like so many other firms, IHC Caland was criticized by pressure groups for its presence in Burma. According to these groups, IHC Caland was supporting the military regime in Burma, by contributing to the economy and hence to the means of existence of the regime. IHC Caland, however, could expect only a few orders of this size each year. Failing one of them could seriously harm their results. Moreover, IHC Caland had already signed a contract with Premier Oil. Leaving Burma would imply a breach of contract which would be detrimental to IHC Caland’s reputation within the industry. This would be a threat to the continued existence of IHC Caland, in a market where buyers have great bargaining power. IHC Caland’s conclusion on the Burma deal was that they would only pull out, if it was forbidden by the government. By taking the matter to a higher (political) level of social organization, IHC Caland in fact invoked the principle of ethical displacement.

We conclude that even under fierce competition, several strategies of CSR are available to firms. Legal compliance is required also under fierce competition, although there should be greater understanding for the costs that legal compliance sometimes poses to companies under fierce competition. Ethical displacement is a CSR strategy that involves relatively low costs, as it aims at equalizing costs between competitors. Inquiring about the problem solving potential of ethical displacement should always be considered morally imperative for firms, when fierce competition makes unilateral CSR initiatives unattractive. Reputation protection, finally, is a means to prevent great costs for companies, which is not only economically feasible but even economically imperative under fierce competition. On the business-to-business market, however, the reputation mechanism may not always make a firm align with the CSR expecta-
tions of the larger public. Inevitably, firms under fierce competition will sometimes disappoint the public at large from a CSR perspective. We believe that a competitive analysis helps to understand why these disappointments are not always justified.

5. CSR Strategies under Conditions of Strong Competition

The term ‘strong competition’ refers to markets in which competitors have more financial room to bear costs due to choices made as a result of their moral and social responsibilities. Competition is strong, rather than fierce, if one or two of the five forces of competition are weak, while the other forces remain strong. For instance, the entry barriers are high because of the importance of brand identity and the high costs involved in developing it. Competition is still strong because of the other forces of competition. In these kinds of markets, profit margins need not be as razor-thin as they are in markets with fierce competition. When it comes to exploring the possibilities of the strategies of CSR, strongly competitive markets will be less restrictive.

The dominant generic strategy in a market with strong competition is product differentiation. Firms will try to differentiate their products or services in the eyes of the customers to justify a premium price. The distinctive capabilities of architecture of relational contract, reputation, innovation, as well as the strategic assets of a firm (such as exclusive dealing contracts) are the basis for product differentiation. John Kay defines architecture as a network of relational contracts within, or around, the firm. Architectures depend on the ability of the firm to build and sustain long-term relationships and to establish an environment that penalizes opportunistic behavior.

If a strategy of product differentiation succeeds, the competition in the market becomes less intense than in a market with fierce competition, because product differentiation results in a higher entry barrier. This way a firm can avoid the low-cost strategy which is dominant in a market with fierce competition. CSR initiatives can contribute to a strategy of product differentiation and are therefore appropriate for a market with strong competition. Sometimes, they even lie at the core of the differentiation strategy itself. The chosen strategy of CSR may build on an already developed distinctive capability of the firm, such as reputation or the high-quality of the architecture of relational contracts. A good reputation and high quality architecture can, however, also be the result of a long-term engagement with moral issues and stakeholders’ interests in business. Below, we will discuss four ways in which CSR can become an integral part of business strategy, under conditions of strong competition: compliance with the spirit of the law, stakeholder management, brand reputation management and ethical reporting, and ethical product differentiation.

Compliance with the Spirit of the Law

Under conditions of strong competition, a firm has financial room to comply not only with the letter, but also with the spirit of the law. This requires paying attention to the rationale of the law, in order to interpret it correctly and arrive at a proper understanding of how the law should be interpreted in new situations. An example of this is how firms respond to loopholes in tax legislation. If the intention of the legislator
is known, but imperfectly expressed in the letter of the law, a firm can consider it its social responsibility to comply with the spirit of the law. Also, a firm has more to gain from this strategy, since distinctive capabilities like a sustainable network of long-term relationships (architecture) and reputation presuppose at least that a firm is able and willing to comply with its contracts in a non-opportunistic way, aimed at establishing long term relationships. Furthermore, the adaptations of the decision-making structure and the organizational culture necessary to enable compliance with the spirit of the law, are first steps in the direction of a full-fledged approach to integrating moral considerations in the decision-making of the firm. Stakeholder management is such an approach, and this will be discussed next.

Stakeholder Management

The management and guarding of the interests of stakeholders is essential if a firm wants to strengthen its architecture. According to Kay, architecture is one of the distinctive capabilities on which a competitive advantage can be built. One of the ways in which architecture adds value to individual contributions is through the establishment of a co-operative ethic. In our view, stakeholder management can contribute to building an environment that penalizes opportunistic behavior by monitoring the relationship of the firm with each stakeholder, so that appropriate action can be taken if anything goes wrong. Measures that could be taken to achieve this goal are social and ethical auditing, introducing an ethical committee or ethics officer, and a procedure for dealing with complaints, among other things.

It may seem that presently powerless stakeholders are irrelevant from a strategic perspective. Mitchell, Agle, and Wood have argued, however, that powerless stakeholders who are affected in their interests, will aspire for power vis-à-vis the company, in order to promote their interests. One can never tell in advance whether a stakeholder who has no power at all to act against a certain firm, will not one day find the means to do so. Often, such powerless stakeholders are helped by NGOs to promote their cases. This possibility will always be of some importance to the sustainability of a firm in the long run. Take for example the victims of the Nazi regime’s robbery of gold and other possessions during the Second World War. Banks that co-operated with the Nazis during the war had to deal with the claims of Holocaust survivors at a much later date. More recently one can think of the protest of the Ogoni against Shell’s activities in Nigeria. The environmentalist movement of the Ogoni did not seem powerful enough to influence Shell’s policy. It was only after the killing of Ken Saro-Wiwa by the Nigerian regime that Shell was forced to address the problem of the Ogoni in a new way.

Brand Reputation Management and Ethical Reporting

Another important distinctive capability that can be used widely in strongly competitive markets is brand reputation management. The importance of brand reputation as a distinctive capability can be seen in markets where product quality is important, but it can only be identified through long-term experience. The market for accountancy
services provides a good example. A certified public accountant adds value only if he represents a firm that has an established reputation of independence and trustworthiness. When a public accountancy firm loses its reputation among the users of financial reports, the added value of the audit for the client disappears. Only accountancy firms that succeed in upholding a reputation of independence and trustworthiness will stay in business in the long run. This example shows how the social responsibility of a firm can be addressed at the strategic level of decision-making.

Brands can serve several strategic functions. They are a means by which a producer can establish the reputation of a product. They can provide continuity. And the consumption of branded products may be a means by which consumers can express their identity. CSR becomes important from a branding perspective, when many consumers appreciate a corporate image of CSR. Global brands like Motorola, Nike, and Heineken run great financial risks if their brand names become associated with child labor, human rights violations, or discrimination. Consumers seem to be extra critical of the CSR performance of a company when it represents a famous brand. Nevertheless, one should not overestimate the impact of consumer sovereignty on the assessment of the qualities of a product or of ethical issues. Consumers face cognitive and motivational limitations, and limited opportunities to gather information about products or firms.

Some global brands have responded to the greater public scrutiny by setting up a system of ethical and social reporting. For instance, Shell and British Telecom publish independently audited reports, covering issues like environmental impact, health, child labor, and corruption. Reporting can be an important tool of brand management and stakeholder management alike, by gathering information about the needs of stakeholders and about the firm’s own performance. By reporting about its ethical and social performance, a firm can at least appear to be making an effort to inform its stakeholders. No matter how imperfect the quality of ethical auditing and reporting may be, the firm will be perceived as being more open and trustworthy. The assurance that the firm is trustworthy already comes from the mere fact that it publishes ethical and social reports. The signal to the stakeholders is clear: a firm that invests in ethical and social reporting not only commits itself to the market, but acknowledges that it has to earn the approval of the public at large by showing that it tries to take on its responsibilities. Whether a firm actually does take its responsibilities seriously is of course not guaranteed by ethical and social reporting as such. To answer this question, independent monitoring of a firm’s behavior remains necessary. Social and ethical reporting however, does give stakeholders information about the policies and measures of a firm with respect to CSR. This is at least a good starting point for further dialogue between stakeholders and the firm.

From a strategic point of view, an investment in ethical and social reporting makes sense for global brands in particular. Firstly, they are most likely to become the target of public scrutiny. Secondly, these brands build on their reputation and, therefore, not only have a lot to lose, but also a lot to gain from a reputation of good corporate citizenship.
Ethical Product Differentiation

It is possible to differentiate a product based on some ethical quality or aspect, if the consumer is ready to pay a premium price because he or she values the particular strategy of CSR that a firm intends to follow. There are many examples of such strategies. Take, for instance, the firms that use fair-trade labels to sell coffee or bananas at a premium price, claiming that part of the premium will benefit small farmers who are dependent on such a premium for a 'reasonable and fair income.' By convincing customers of the social value offered at the premium price, the firms succeed in differentiating their 'fair' product form normal, 'unfair' trade.

Although the strategy of ethical product differentiation might be appropriate in the case of strong competition, it is also risky. If the customer fails to attach value to the ethical product claim, the firm loses business to competitors. The premium price will be perceived as unjustified. Furthermore, it is risky to claim that a product has some ethical quality to it that is lacking in the products of competitors. As The Body Shop has experienced, a firm that claims to safeguard ethical values in the production process will receive extra critical attention from journalists and consumers. The company was accused of misleading the public, since among other things only a fraction of the product ingredients were actually bought from fair trade supply channels, while the bulk of the ingredients were bought from normal (purportedly unfair) supply channels. To counter this kind of criticism, The Body Shop has invested in social and ethical auditing and reporting.

6. CSR Strategies under Conditions of Weak Competition

A market with weak competition has several characteristics that change the strategic importance of CSR. Competition in a market is weak when all five forces of competition are weak or tend to be weak: (i) the threat of entry of new competitors is low, because of economies of scale and well-established brand identity; (ii) the product cannot easily be substituted, because of high switching costs; (iii) the buyers have little bargaining power, because their concentration is relatively low; (iv) the bargaining power of suppliers is relatively low due to the threat of backward integration; and (v) the concentration within the industry is high, causing the rivalry between competitors to be low. Taken together, these five forces of competition lead to weak competition.

Markets with weak competition can be either oligopolistic or monopolistic. Because of the lack of competition in such markets, firms have market power, which means that they can ask higher prices or reduce their quality, without losing too much business. Because of the lack of efficiency and quality in many markets with weak competition, intervention of the government through antitrust legislation and supervisory organs is often undertaken to safeguard the interests of consumers and the public. Market power, however, can have some positive effects as well. It enables a firm to invest in CSR. A firm in a weakly competitive market has the financial and managerial room to choose any of the CSR strategies described in the previous chapters. It is another issue whether all these strategies would be equally wise choices.
Compliance with the spirit of the law makes sense in a market with weak competition, because in this way a firm can prevent or reduce the chance of (further) government intervention. Most firms will consider it in their interests to prevent government intervention, because this way they have more control of the situation. If a firm in a market with weak competition refrains from misusing its market power, it indeed takes away the necessity of government intervention. However, when important interests of consumers or the public at large are at stake, for instance in public transport or energy supply, compliance with the law may not suffice. If important interests are at stake, dissatisfaction of consumers or the public can easily become a political issue. That is why, in these kinds of markets, it is in the interests of a firm to at least keep their key stakeholders satisfied, by using the strategy of stakeholder management or some form of ethical reporting. After all, these tools of ethical management not only benefit the stakeholders but also improve the overall quality of management, by keeping in touch with changing social expectations.

7. Conclusions

In this paper, we addressed the question of how specific competitive conditions affect CSR, and which CSR strategies are feasible for a firm under different competitive conditions. The competitive condition can be defined by three characteristics: the intensity of competition, the legal environment, and the risks to reputation.

The central moral argument underlying our analysis is that, in general, the continuation of a firm has an instrumental moral value because normally all stakeholders have a legitimate stake in this continuation. If, however, a person or group is better off if a business activity is terminated, management has to balance rights and obligations in such a way that the lesser evil is chosen. If this means that a firm will not be able to survive then this is the lesser evil in such a case. If however, most stakeholders with legitimate claims on a firm have an interest in the continuance of the firm in order to secure their stakes and if this continuance means that the interests of a certain stakeholder or non-stakeholder cannot be secured fully, this could be the lesser evil that should be chosen. It all depends on the nature of what is at stake. From a deontological perspective, for example, the stakes of all stakeholders do not override fundamental rights to liberty, life and property. Starting from these premises, we conclude that fierce competition can be a morally mitigating factor for making use of loopholes in the law or to violate the law. The latter, of course, depends on the moral issues surrounding a certain law. We conclude that legal compliance can already be an ambitious strategy of CSR, for firms that have to deal with fierce competition.

In the case of strong competition, there is more room for other strategies of CSR that can contribute to product differentiation. We briefly explored the strategies of compliance with the spirit of the law, stakeholder management, brand reputation management and ethical reporting, and ethical product differentiation. To a great extent, these strategies are a necessary response to the demands of different stakeholders who have the option of taking their business to a competitor.
It is a defining characteristic of a market with weak competition that it lacks this kind of competitive pressure altogether. The legal environment, however, does provide a reason for firms in such a market to adopt some form of CSR, because of the risk of government intervention. Other reasons for firms in a market with weak competition to adopt a more ambitious strategy of CSR are of a more intrinsic nature, like the desire of management to be part of a ‘good’ or ‘well-managed’ company.

We analyzed the correspondences between the chosen strategy of CSR and the competitive conditions that confront a firm. From a strategic perspective, this may seem self-evident. From a moral perspective, however, it is anything but self-evident to stress the moral value of a firm’s survival. Are we not prioritizing the self-interest of the firm above all other stakeholder interests, and hence, above moral duties that override self-interest? In a way we are, but only in so far as we want to acknowledge that every functioning system has to reproduce itself in order to be able to comply with whatever duty is imposed on it (‘ought implies be’). Only if morality is best served by the immediate termination of business activities does this prioritization lose its validity. After all, the reasons for prioritizing a firm’s survival are moral reasons.

We have outlined the main features of a normative framework that specifies how firms can compete in a morally acceptable way, given the characteristics of their competitive environment. Further empirical research could provide more detailed insight into the mechanisms through which competitive conditions actually influence the CSR strategies that firms implement. A hypothesis derived from our framework is that the more firms integrate CSR into their corporate strategy, the better they will be able to cater for the legitimate demands of their stakeholders. Also, more in-depth research is needed, from both a moral and strategic perspective, into the strategic potentials of different CSR strategies under different competitive conditions. In this way business ethics could develop a contingency approach to CSR, instead of looking for the one best ethics for all firms.

Notes


5. Compare C. W. Hill and T. M. Jones, “Stakeholder-Agency Theory,” *Journal of Management Studies* 29 (1992): 145: “[O]bviously, the claims of different groups may conflict. . . . However, on a more general level, each group can be seen as having a stake in the continued existence of the firm.” This passage is also quoted with approval in a recent article by R. Phillips, R. E. Freeman, and A. C. Wicks, “What Stakeholder Theory is Not,” *Business Ethics Quarterly* 13(4) (2003): 484.


18. Ibid., 7.


22. One could object that bankruptcy might also mean that the interests of some stakeholders are protected. Although bankruptcy can be the best solution in the case of insolvency, it also means that the interests of the stakeholders are terminated. One could argue that this is not a moral problem, since after the bankruptcy, the assets will be put to more efficient use. Hence, total utility would benefit from bankruptcy. This argument, however, is built on the assumption that the market is efficient. This means, among other things, that the rules governing the market place affect all the competitors in the same way. However, as we argued above, a lack of law enforcement punishes
legal compliance and rewards non-compliance. In these circumstances, it may happen that an efficient and obedient firm goes bankrupt, while an inefficient disobedient firm survives. As a result, the social optimum will not be achieved.


24. Fombrun and Rindova define corporate reputation as follows: “A corporate reputation is a collective representation of a firm’s past actions and results that describes the firm’s ability to deliver valued outcomes to multiple stakeholders. It gauges a firm’s relative standing both internally with employees and externally with its stakeholders, in both its competitive and institutional environments.” C. Fombrun and C. van Riel, “The Reputational Landscape,” in Revealing the Corporation. Perspectives on Identity, Image, Reputation, Corporate Branding, and Corporate-Level Marketing, ed. J. Balmer and S. Greyser (London/New York: Routledge, 2003), 230.


26. Ibid., 66–86.


29. “We suggest that a theory of stakeholder identification and salience must somehow account for latent stakeholders if it is to be both comprehensive and useful, because such identification can, at a minimum, help organizations avoid problems and perhaps even enhance effectiveness.” Mitchell, Agle, and Wood, “Toward a Theory of Stakeholder Identification and Salience,” 859.

30. Ibid., 263.

31. Ibid., 263.


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