

ETHICAL BUSINESS: *Some Unsettled Issues*

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*Parts of this presentation have been extracted
from my book **Strategy in the New Age of
Capitalism** (forthcoming, U.P. Press)*

The title of this webinar - “Ethical Business” - implicitly poses the question: Are business organizations morally bound to serve the needs of society?

- It is widely held that business has a moral obligation to serve the needs of society. This view is consistent with current thinking on Corporate Social Responsibility.*
- This popular concept of CSR stands in stark contrast with the notion made popular by economist Milton Friedman that business has no responsibility other than to make profit.*

Where we stand on the issue

- We take the unconventional view that business corporations are institutions created by society to perform specific functions for the community.
- Institutions, business firms included, have no moral responsibility to serve the interest of others. They are ***ethically neutral***.
- However, the individuals that comprise institutions are morally committed to serve the interests of others.
- What corporate owners, their appointed managers and other personnel do have is the ***strategic*** responsibility to serve the interest of the corporation, which is to maximize profit.

We draw on insights from the social sciences to support our contention. We refer in particular to two social science theories – Social Darwinism and Social Functionism.

The social science perspective on profit-seeking behavior: Insights from Social Darwinism

- *From the evolutionary viewpoint, all individuals and social institutions, just like their counterparts in the biological world, are driven by self-interest.*
- *Consistent with this doctrine is the long-standing economic notion that business firms are motivated solely by profits, and the most profitable ones have the best chances of survival.*

The social science perspective: Insights from Social Functionalism

- *In line with American Sociologist Talcott Parsons' theory of social functionalism, we define the role of the firm in modern society as one of creating economic value.*
- *In keeping with the teachings of Classical and Neoclassical Economics, we hold that the lure of profit serves as the most effective motivation for business organizations to serve the interests of society.*

Revisiting the profit motive

- *The goal of profit-maximization is a defining tenet of neoclassical economics and has been one of the fundamental ideas behind the emergence of Western Capitalism as the dominant form of economic organization.*
- *The near obsessive preoccupation with shareholder value has also lead to unwanted zero-or negative-sum economic consequences for society and for all other stakeholders in the firm.*

Unhampered profit-seeking behavior leads to a number of undesirable consequences:

- *To consumers: higher prices, poor quality products and services*
- *To workers: unfairly low wages, poor working conditions*
- *To business partners: unfavorable terms and conditions*
- *To society: environmental degradation, low incomes and unequal opportunities to large segments of society*

The ultimate effect of profit-seeking behavior as currently practiced is the destruction, rather than the creation of potential value.

Non-inclusive growth and the case for inclusive business strategies

- *One of the worst anomalies of our time is the ever-widening gap in income and wealth between the very rich and privileged few in most societies, and the masses at bottom of the social pyramid that are mired in abject poverty.*
- *Corruption and ineptitude in government have been primarily responsible for non-inclusive growth, especially in the emerging market economies.*
- *Business, too, has been responsible for this unwanted outcome of capitalism.*
- *A growing number of progressive business leaders around the world now believe that business itself must take up the challenge to make capitalism more inclusive*

Shareholder wealth maximization reconsidered

- *If business is to implement socially beneficial initiatives for the purpose of achieving its long-run strategic goals, it has to radically change the manner in which it does business. In particular, it needs to rethink the way it pursues its profit objective.*
- *As an alternative to profit or shareholder wealth maximization as the raison d'être for the business enterprise, we propose to state the function of the business firm in modern society as one of producing economic value, and appropriating the economic wealth created among all the groups that contribute to the production process – including the owners.*
- *By implementing appropriate strategies and putting in place governance mechanisms for creating value for its other stakeholders, we contend that the residual value that accrues to the owners of the firm (aka profits) will consequently be maximized.*

Stakeholder strategies create value for the various stakeholders in various ways

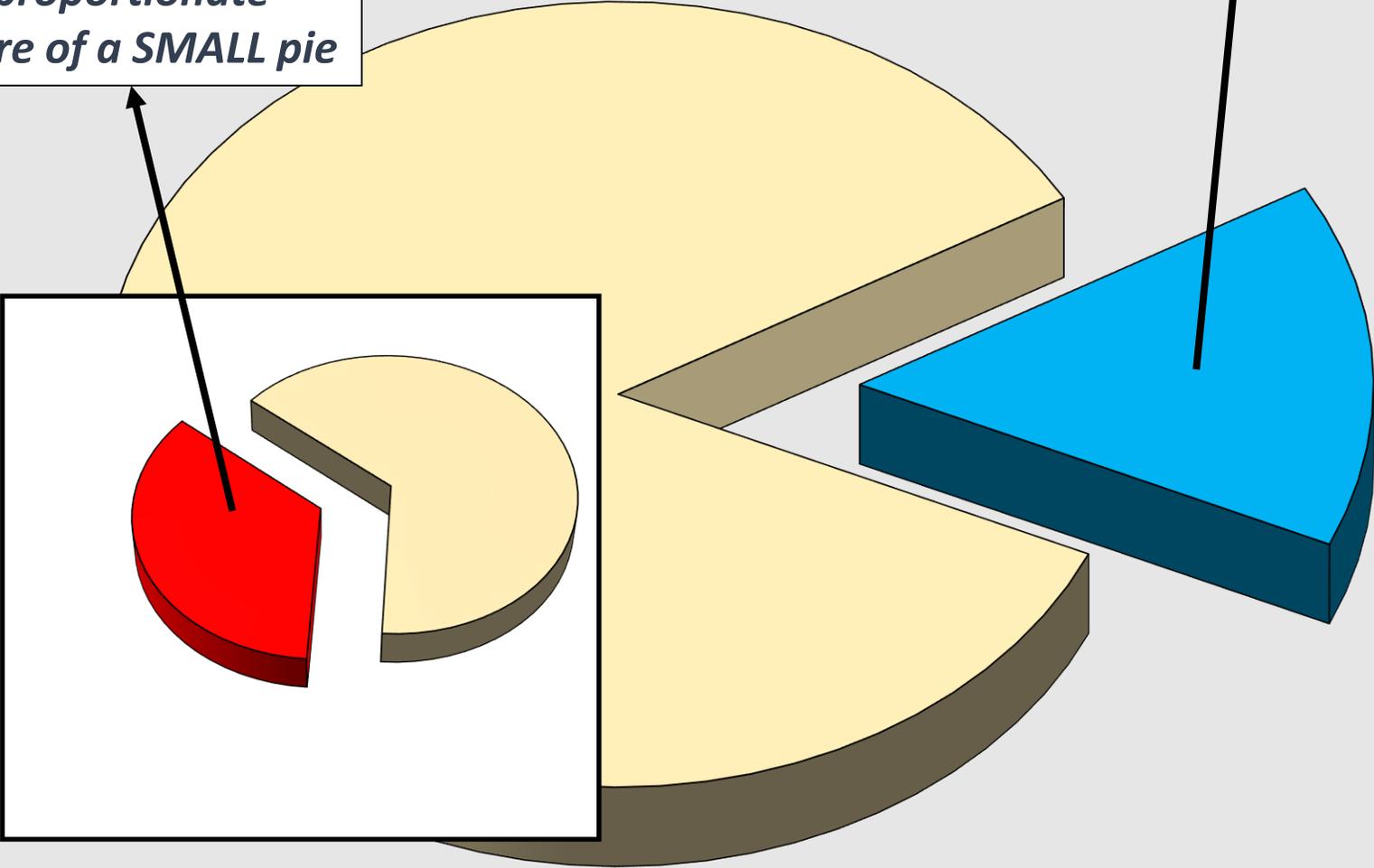
- *Creating value for customers through product development, generous prices and customer care*
- *Creating value for workers by offering comfortable wages, good working conditions, skills development*
- *Creating value for business partners by establishing a mutually beneficial, trusting relationship with them*
- *Creating value for the community by addressing the needs of the least privileged members of society and by helping create a sustainable ecosystem.*

The resources used by the firm to serve the material needs of stakeholders are *investments* intended to maximize *long-run* output, not *costs* to be minimized in order to maximize *short-run* gains

THE TWO STRATEGIES COMPARED

Aiming for a LARGER proportionate share of a SMALL pie

Settling for a SMALLER proportionate share of a BIG pie



PUTTING IT ALL TOGETHER

Seeing the big picture

