Conversations with DISBELIEVERS

Persuading Companies to Address Social Challenges

John Weiser • Simon Zadek • November 2000

Conversations with Disbelievers

How and when can businesses "do well by doing good"?

This report for the first time brings together much of the available quantitative evidence that addressing social challenges can help businesses improve their financial bottom lines. Designed to be used by business managers, nonprofit leaders, brokers and intermediaries, as well as students and the research community, it provides practical guidance on how best to use available evidence in encouraging businesses to address social objectives. Organized to provide a ready reference to the key data and case studies, it notes the potential weaknesses of the currently available evidence, what types of evidence are the most convincing, and how this evidence can best be marshaled and communicated effectively.

The report is essential for anyone wanting to persuade skeptics - and of course for the skeptics themselves - of the financial benefits to companies of effectively addressing social challenges as a core element of their business strategy.

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I. Executive Summary

The purpose of this paper is to encourage business to deepen its Corporate Engagement with communities. By Corporate Engagement (CE), we mean activities that:

- Offer the potential of having a positive impact on low-income communities.
- Form part of an ongoing corporate strategy for community involvement and enhanced business performance.
- Offer potential direct or indirect benefit to the corporation.
- Include both philanthropic activities and/or activities that tap into the corporation's core competencies and operations - its power to purchase, develop products, invest, market, hire and train, and innovate.

This definition covers all businesses, all employees, and all types of communities, including those close to business operations, distant communities down supply chains, and "non-geographic communities", i.e., communities of interest.

To encourage business to deepen its CE, the paper reviews the quantitative evidence showing when and how CE creates business as well as societal benefits. The primary audience for this paper consists of people who seek to persuade skeptics of the business benefits of CE. This can include fellow managers, government officials, and nonprofit leaders. The motivation for this paper has been the question: why is it that there are relatively few corporations that have committed significant resources to CE, when there seem to be so many studies that purport to show a clear business benefit?

Answering this question requires entering into conversations with disbelievers - business people who are at best skeptical that CE can provide a significant financial benefit to corporations. These conversations help illuminate why the currently available evidence is not persuasive, what types of evidence are most convincing, and how this evidence can best be marshaled and communicated effectively.

In conversations with disbelievers, we found that what some might consider convincing evidence is often dismissed by business people for one or more of the following perceived reasons:

- Information type (for example, survey data) is not deemed reliable
- Evidence is not considered relevant to key goals
- Sources of evidence are suspect
- Evidence does not address the business person's underlying attitudes

Convincing business people is not a matter of evading their skepticism. Rather, it is a matter of understanding the corporate imperatives and cultures that make such skepticism a core survival technique, and working to ensure that CE can demonstrably be consistent with, and relevant to, these operating realities. The key is not simply to show business people that CE can be financially rewarding. This is an important but insufficient piece of the puzzle. When a business person is already over-stretched in meeting the challenges of the complex and highly competitive corporate environment, it is critical to demonstrate that CE improves their ability to meet *existing* objectives. The key is to show not only that it can generate black on the bottom line, but that it does so in strategically important areas of business performance.

It is in this context that we looked at why some businesses do in fact increase CE activities. We identified three broad sets of drivers that moved managers to increase CE:

- Pressure: a short-term need to respond to external pressures such as regulation or advocacy groups
- Values: an expression of core values in the company
- Strategy: CE supports or enhances a key long-term business strategy

These three drivers are not mutually exclusive. The rationale for CE typically evolves over time. Companies that increase CE activities initially because of high-profile public pressure, for example, often find over time that there is a deeper strategic rationale for responding to societal concerns in a systematic manner. Values may form a bedrock of why some businesses engage in CE, but may not provide an adequate driver unless these values are made consistent with market realities through their integration into the business process.

With these drivers in mind, we turned to the quantitative evidence purporting to show a relationship between business benefit and CE.

Our review highlighted the following key results:

1) Disbelievers can be right. Many of the studies that purport to show benefits do not, in fact, prove their point. Some are poorly designed; others use unreliable indicators; some show that there is a financial benefit, but don't show the cost required to attain that benefit, or the relevance of the benefit to the underlying business strategy.
2) Disbelievers are often wrong. There are many well-crafted, reliable studies from reputable sources that do show business benefits to increasing CE. The most compelling evidence shows that CE can create significant business benefit when it is clearly linked to a core business goal or strategy. Dismissing this evidence is often rooted in misunderstanding, fear and ignorance rather than calculated assessment.
3) Disbelievers are increasingly mistaken to dismiss the potential benefits from CE. This is because of the potential impact of CE on the ability

of companies to build and manage their knowledge base in a way that enables financially attractive innovation in products and processes.

Conversations with disbelievers can be both frustrating and a source of considerable learning. Perhaps the most important single lesson is that people disbelieve for a reason, and often what in context is a very good reason. For those who have been persuaded of CE's business benefits, the disbelief in CE can seem improbable at best, and immoral in its more stubborn forms. But both the passivity and evangelical aggression that arise in equal measure in an attempt to address disbelief are certainly counter-productive. Far more effective is to enter into conversations with disbelievers in a spirit of engagement, learning, and even adventure. The reasons for disbelieving can be overcome, but only by those who are sufficiently trusted in understanding what arguments count, and how best to make them count. This paper reflects what we have learnt from the disbelievers, and offers some concrete advice for others who will have similar conversations.

Guide to Reading the Paper

We have organized this paper in an unconventional way. Rather than starting out by carefully reviewing our methodology and definitions, we instead provide a quick immersion for readers into our approach and main findings. This quick immersion occurs in the next two chapters: The Disbelievers Scorecard and Quick Tour. We then slow down the pace significantly, and provide a more methodical review of our scope, approach, and definitions in the following chapter, entitled What Are We Talking About? Finally, we suggest the reader find a comfortable place to sit while he or she digs into the final chapter, entitled The Numbers Warehouse. This is a thorough review of many of the most important quantitative measurements showing how and when Corporate Involvement creates business benefits.

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This chapter and the following provide a quick immersion for readers into our approach and main findings. Since the key task of the paper is to understand how to persuade skeptics, in this chapter we present the disbeliever's scorecard - a tool we designed to help people understand why skeptics disbelieve evidence, and how to present the evidence so that it is most persuasive.

We start by looking at why some managers do choose to increase their CE activities, to understand what drives their decisions. If we can understand the drivers that compelled some managers to increase CE activities, we can better understand how and why other managers might be persuaded. We also note the dynamics of the change process, and the impact of increasing CE on the company's ability to innovate.

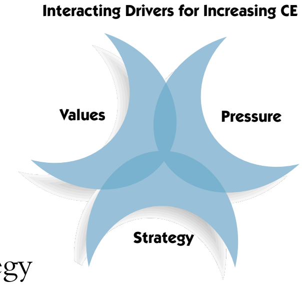
We then look at the rationales that managers have put forward for disbelieving or ignoring the evidence. We present a scorecard based on these rationales that you can use to understand the likely objections to the data presented, and to present the evidence in a more favorable light.

Why Managers Increase CE Activities

In order to understand what would be persuasive to skeptical managers, we surveyed over 100 case examples of businesses that did increase their CE activities. There were a wide range of reasons and rationales for increased CE. While some are specific to a particular company, we were able to identify three general drivers:

1. Pressure: a short-term need to respond to external pressures such as regulation or advocacy groups
2. Values: an expression of core values in the company
3. Strategy: CE supports or enhances a key long-term business strategy

Interacting Drivers for Increasing CE



These three drivers are not mutually exclusive. Rather, they interact with one another, causing shifts over time. Companies that increase CE activities initially because of pressure, for example, often find there is a business strategy rationale that develops over time. Values may also shift, depending on the depth to which CE causes changes in the organization's activities and culture. (Zadek, Pruzan, and Evans, 1997)

In reviewing the case studies, we also noted that innovation plays an important role. Companies under pressure from one or more of these drivers feel a strong need to act and respond. But often when a company experiences a need to respond to drivers pushing it to increase its CE, it does not have the skills and competencies it needs to succeed. In most of the cases we examined in which companies dramatically and successfully expanded their CE activities in response to drivers, they experimented and innovated as they figured out how to compete effectively and profitably under these new circumstances.

Why Managers Disbelieve

While there are many companies that have increased their CE activities, there are many more that have not done so. In order to understand why, we talked with "disbelievers" - managers who are skeptical about the benefits of CE. At the heart of most conversations with disbelievers is a debate over the quality of the evidence. Most disbelievers dismiss the data showing significant business benefits. Often, we heard comments like, "yes, but they would say that, wouldn't they" and "no one in their right mind would believe those numbers". In order to respond effectively to the dismissal of data, it is important to understand why the data is dismissed, and how to react to the different reasons for dismissal.

In our conversations with disbelievers, we teased out four principal reasons why disbelievers dismiss data. These reasons are described below. In each case we describe the general reason, and highlight the main types of data to which it applies. For each category, we note which types of evidence are more persuasive or less persuasive.

1. Information Type

This paper provides many types of evidence in support of the case that CE delivers business benefits, ranging from people's opinions to data on the impact of CE on business functions and finances. Generally, the disbeliever argues that only evidence about the impact on business functions and finances is really credible.

The least credible data, for most disbelievers, is data about *opinion*. The disbeliever, for example, dismisses the many public opinion surveys confirming that a high proportion of consumers say that they would switch their purchasing to buy products made in ethical ways by ethical companies. "They would hardly say anything else", the disbeliever retorts, "since one is asking them if they are ethical. The facts are that consumers buy the products they want at the cheapest price and rarely look at the ethical credentials". The one exception to note here regarding the importance of opinion data is that disbelievers can be quite persuaded by the candid opinion of their peers.

Disbelievers are usually more convinced by data about *action* than about opinion. For example, it is more persuasive to show examples where people actually did purchase products because the producing company is deemed ethical, than it is to show a survey where people said they would. Disbeliever's confidence in such data is, however, limited by the fact that cause and effect can be hard to demonstrate. Did Nike footwear sales fall, for example, because of allegations of use of child labour, or because Nike did not keep pace with fashion?

Data about effects on *business processes and finances* are the most convincing. When CE can be shown to have an impact on a business process that a disbeliever thinks is critically important to success, he or she is most likely to be persuaded. Disbelievers are likely to be engaged by the evidence, for example, that volunteering increases employee morale, when they are already convinced that employee morale is directly linked to financial performance. It is particularly helpful if CE can be shown to have an effect on the finances of the company. Where cause and effect is straightforward, this is the best way to catch the attention of even the most ingrained skeptic. For example, there are numerous studies that demonstrate that cause-related marketing can increase sales and some studies actually set out the net financial gains through such marketing. [For examples of these studies, please see "Marketing and Sales", page 81.]

It can be quite difficult to show a direct link between CE and increases in financial results. For example, Shell International's financial performance is currently excellent, but no one has been able to demonstrate statistically that this has anything to do with its considerable investment in corporate citizenship. But that doesn't mean that skeptics can't be persuaded. Businesses spends billions of dollars each year on important activities, such as advertising and training, even though there is very little evidence showing a direct link between those expenditures and specific increases in the bottom line. The critical issue is to show the link between those activities and improvements in business processes and functions that the skeptic views as key to attaining future profitability.

2. Relevance

Relevance is perhaps the most important foundation on which the disbeliever can challenge the data. This combines several possible elements, including accuracy, materiality, and applicability.

(a) *Accuracy* is about whether the data are correctly describing what they purport to. This can be an arithmetical issue (were the numbers added up correctly), or a statistical issue (was the equation that draws conclusions about cause and effect correctly specified). It also can be a representative issue when it comes to qualitative data (do the quotes really reflect what the body of people felt).

Disbelievers have good reason for their skepticism. Wood and Jones, in a careful review of the data and cases brought forward by advocates, show that many of them, unfortunately, are seriously flawed. They noted that the studies as a group presented inconsistent measures of corporate social responsibility, and that many of the studies were lacking in methodological rigor and were therefore of uncertain validity, reliability, and generalizability. (Wood and Jones, 1995)

Because it is nearly impossible for disbelievers to review the evidence in detail, they tend to rely on the reputation of the organization as a proxy for whether the data is accurate. For example, a statement such as "CE practices of the following type have been shown to reduce turnover by 9.3% in entry-level positions in customer service organizations" would be much more likely to be accepted as accurate if it came from a highly reputable human resources consulting firm than if it came from a small non-profit advocacy group.

(b) *Materiality* is about whether the business effects being described were material in the case or cases in point. This may be a statistical issue of whether the size of the positive effect being recorded is significant. Alternatively it may be a judgement call as to whether the effects are worthwhile. Volunteerism may increase morale, but is it the type of morale booster that does in practice feed through to real financial benefits? A further variant of this concerns value-for-money, or what has elsewhere been described as 'efficiency'. Cause related marketing may indeed increase sales, but is it more or less than if the funds had been spent on other marketing approaches?

The disbeliever is least likely to be persuaded if the evidence presented leads him or her to think that increased CE will not create a large enough effect to matter, or that it will create a large enough effect, but at far too large a cost. The greater the benefit, and the lower the cost, the more interested the disbeliever is likely to become. However, there is a "Catch-22": if the evidence presented claims too great a benefit at too low a cost, the disbeliever may scoff - "if it were that good, why isn't everyone already doing it?"

(c) *Applicability* is about whether the experience being described is applicable to the company or situation in which the disbeliever lives and work. "Just because it worked someplace else, how do I know it will work for me?"

There is often good reason for being skeptical about applicability. For example, there is little doubt that BP enhanced its image in the eyes of opinion leaders concerned with the environment by leaving the Global Climate Coalition. But managers at General Motors would be right if they were skeptical that this then proved that General Motors would make the same gains if it did the same thing. It's not directly applicable, partly because it would not be the 'first out' (as was BP), partly because it is in a different industry, and partly because it is a US rather than a UK-based company. Similarly, it is unclear as to whether Ben & Jerry's positive social image will be retained under the new Unilever ownership even if they have exactly the same programs in operation. Most significant perhaps is that the benefits gained through CE by high-profile consumer brands do not necessarily translate to similar gains for lesser-known companies, particularly if they are essentially business-to-business operations.

Clearly, the least credible evidence comes from situations which are enormously different from those faced by the disbeliever, and the most credible evidence comes from peers facing the same situations as the believer.

3. Source

People believe people, not data.

This should be an 'old adage', at least for this area, because it is just so true. Disbelievers who dismiss data from opinion surveys find themselves lapping it up when a respected colleague or competitor finds it to be of value. Financial data collected by business networks take on a mystical relevance even where similar data produced by academics has been rejected as 'pie in the sky'.

Most managers have a "hierarchy of belief". They are most likely to believe information coming from their peers; after their peers, they are most likely to believe well-respected consultants or vendors; after that, they listen to their trade associations. Information from most academics, foundations, advocacy groups, and much of the media is generally ignored. (Of course, there are exceptions, in that some academics have attained the status of "business gurus", and some business media such as the Wall Street Journal and the Financial Times are generally held in high regard.)

Managers also are deeply suspicious of information that comes from companies like Ben & Jerry's, which they regard as being "outside the mainstream". Since much of the information that proponents bring forward comes from these sources, it is often dismissed without careful review. (Eisen, 2000)

The best way to convince a corporate disbeliever is to bring them face-to-face with a business person who can claim to have tried CE and found that it 'really does work'. Often the stories will be anecdotal, and the business advocate and disbeliever will cheerfully agree that most quantitative data are nonsense and that 'real hands-on experience' is the only way to distinguish fact from fiction.

Of course, there is not always a compliant business person at hand during a conversation with disbelievers. In these situations, the best one can do is to seek credibility by knowing what other business people have said, and by bonding with the disbelievers by acknowledging the problems with data sources and methodology. Evangelists make bad advocates when faced with skeptics. Gain the disbeliever's trust by being more skeptical than them.

4. Underlying Attitudes

Evidence that is brought forward to support increased CE may be accepted or rejected because of underlying attitudes. Weak evidence may be embraced because it supports an underlying attitude. Even the strongest evidence may be rejected because it runs afoul of deeply held beliefs or political agendas. For example, managers often want to increase CE, but don't yet have a rationale that is acceptable in the company. In this case, the business argument enables rather than motivates them to act. The managers need to be able to rationalize their actions using business rather than, say, moral or ethical arguments. But what often energizes them to do something is precisely that undercurrent of caring and ambition to make a wider societal contribution, and maybe being acknowledged for just that.

There is, unfortunately, a dark side to this tale. Just as people will use the business argument to provide support for their caring, they will use it to avoid engaging with difficult challenges. A recent report on how to get more disabled people into the workplace described surveys of managers who revealed a strong distaste for, and indeed anger against, disabled people masquerading under the guise of 'it's just too expensive to help'. Rational arguments and convincing data may be insufficient alone to shift deep-rooted bigotry based on ignorance and fear. In such situations, it is often only direct experience that opens the possibility of a change in attitudes and in turn behavior, whether it be of disabled people or unemployed youths. (Zadek and Scott-Parker, 2000)

Rules of Engagement

People disbelieve for a host of reasons. We have outlined here some of the key ones. Convincing business people is not a matter of evading their skepticism. What is critical is to demonstrate that CE improves their ability to meet their *existing* objectives. The key is to show not only that it can generate black on the bottom line, but that it does so in strategically important areas of business performance.

There is no single way to handle the extraordinary diversity of conversations with disbelievers. However, a few rules of engagement do come to mind that might help the CE advocate to better navigate their way through such conversations making the best use of data and patterns of argument.

(a) Know who you are talking with. Spend as much time as possible listening to what they do in the business, who they have to persuade, and what are likely to be the key objections facing them.

(b) Be an insider. Even if you know little about the business, be sure that you come armed with insider examples of other companies. Don't let the disbeliever think or say "this person understands nothing about business".
(c) Be skeptical first. Following from this, be skeptical about the data, and so build trust in the disbeliever that you know your subject, and do not take her or him for a fool.
(d) Help solve their problems, not yours. Be clear about whether they really are skeptical, or whether they are rehearsing an argument to be had with others. In either case, consider yourself a resource, helping the person to marshal the arguments. Everyone likes a free consultant (if they are good).
(e) Never evangelize. It seems so obvious to say, but we do forget that most people are put off by evangelical arguments, particularly when it is linked to a sense that it will be followed by a request that involves resource and some risk.

Disbeliever's Scorecard

To convince a disbeliever, you have to be able to think, feel, and communicate like one (or indeed like many different ones). This section aims to help you in this task. We have used the key findings in this chapter to create "The Disbelievers Scorecard", which is essentially a list of the main reasons why 'data failure' occurs when in conversation with disbelievers. Its use allows you to predict and effectively handle the complex twists and turns that can and do happen in conversations with disbelievers.

In this scorecard, "1" is the lowest score – the least persuasive evidence. "5" is the highest score – the most persuasive evidence. We will use the Disbelievers Scorecard at the end of sections within the various chapters to present some thoughts about how persuasive the data discussed in that section are.

Try out the Disbelievers Scorecard for yourself. As you go through this paper, note in the margin what are the main challenges that would be

Scorecard: Effect on Business Function

SCORE	1	2	3	4	5	NOTES
INFO TYPE						
RELEVANCE						
SOURCE						
ATTITUDES						

lobbed against each piece of data that we offer in support of CE. You will quickly see the patterns and internalise the lessons. Hopefully you will also discover new elements that can usefully be added to the Scorecard, and so improve your ability over time to navigate critical conversations to an effective conclusion.

III. Quick Tour

This section of the report is a quick tour in two ways. First, it is a quick tour of the most important data - the highlights of our findings. Secondly, because we know that persuading managers is the key goal of marshaling this evidence, we organize the data around a virtual tour of a large multinational company, stopping in the offices of several key managers. We are assuming that each of these managers is a "disbeliever" - they are skeptical of the notion that increasing CE will help them to achieve their goals and objectives. They all agree with the skeptical business manager who told Steve Rochlin at the Boston College Center for Corporate Community Relations: "You can't tell me we're going to community-relate our way to success". (Rochlin, 2000)

As you prepare to join us on this tour, you may find it helpful to imagine that you are a peer or subordinate of these managers, or perhaps the leader of a business intermediary organization, and that you would like to persuade them to give serious consideration to increasing the level of CE in their company. What sorts of arguments would you raise? What do you think would be persuasive? Clearly, when talking with a disbelieving manager, you would not say that CE is the most important factor in achieving business success. If you did, you would probably be politely ignored. Rather, you would bring forward evidence to show that CE can be helpful in attaining specific goals that the manager is trying to achieve. This section will follow a similar pattern. It will describe several key managers, and for each manager, it will note several key goals that he or she has, and how increased CE can help him or her achieve those goals.

Head of Marketing and Sales

The top managers for marketing and sales are focused on issues such as increased sales, product differentiation and customer loyalty. A disbelieving manager is likely to feel that CE is something that will not make much difference in sales, and should be funded solely from the corporate foundation. For example, Saatchi and Saatchi Cause Connection conducted a survey of 169 marketing directors at top UK companies, in which the survey respondents were asked their opinion of a 1998 Mintel study that found that 61% of UK consumers said they would be more likely to buy products or services associated with good causes. Only a third of the marketing directors believed that consumers would actually behave that way in practice. (Pringle and Thompson, 1999)

This highlights the skepticism that surveys about intention and opinion can evoke. Fortunately, there is also evidence about action and bottom-line impact as well. This is particularly true when CE is combined with marketing tools and techniques in cause-related marketing.

Increased Sales

Many companies report that cause-related marketing (CRM) can significantly boost sales. For example:

- London-based Diageo plc reported that between 1994 and 1998, 22 CRM projects helped it raise $600,000 for causes while increasing sales of tracked brands by 37 percent. (BSR, 2000)
- Sears, Roebuck, created a partnership with Gilda's Club (a nonprofit organization that provides a network of local meeting places where people living with cancer can come together for emotional support, social events, and laughter) to promote special ties, scarves, and Levi's 550 jeans. Sears sold 100,000 ties and 30,000 scarves in several months, and sales of 550 jeans increased in-store by 56 percent in Gilda's Club cities, compared to 16 percent in non-Gilda's cities. (Adkins, 1999)

Customer Loyalty

Companies that have engaged in cause-related marketing report that their efforts help attract and build long-term relationships with customers. For example, affinity credit cards, in which a nonprofit organization benefits each time a consumer uses the card to make a purchase, help credit card companies develop long-term relationships with consumers.

Partnering with nonprofit organizations can help a company better target specific demographic or geographic markets. For example, Avon Products, Inc. helped position itself among women as a caring company through its Breast Cancer Awareness Crusade. The program — a partnership between Avon, the Centers for Disease Control and Prevention, the National Alliance of Breast Cancer Organizations, the National Cancer Institute, and the YWCA of the U.S.A. — raises money for community-based breast cancer programs through sales of Avon's pink-ribbon crusade products. (BSR, 2000)

Several studies over the past few years have shown that consumers are drawn to companies that are associated with a social cause or issue. For example:

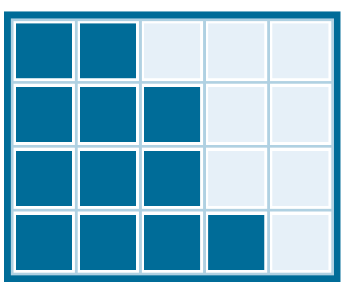
- In the United Kingdom, the 1997 Access Omnibus Survey by Business in the Community, a British business membership organization that supports communities by raising business involvement, found that 86 percent of consumers say they have a more positive image of a company if they see it is "doing something to make the world a better place". Sixty-four percent said that cause-related marketing "should be a standard part of a company's business practices". (BSR, 2000)

- In 1999, the U.S.-based Cone/Roper Cause-Related Trends Report found nearly two-thirds of Americans, approximately 130 million consumers, report they would be likely to switch brands (66% in 1993, 65% in 1998) or retailers (62% 1993, 61% 1998) to one associated with a good cause. Eight in ten Americans have a more positive image of companies who support a cause they care about. (84% 1993, 83% 1998) (Cone Inc., 1999)

[For additional information on how CE can affect marketing and sales, please see "Marketing and Sales", page 81.]

The following table is the first in a series of Disbelievers Scorecards that we present in sections of the text. In preparing this Scorecard, we reviewed the evidence presented in the section with a skeptical eye. We then rated the data on a 1-to-5 scale as to its persuasiveness on four criteria: the type of information, its relevance, its source, and whether or not it is likely to be affected by underlying attitudes. We hope that this approach will be helpful in coming to understand what concerns skeptics might raise about the evidence, and therefore, what issues persuaders should be prepared to address.

Scorecard: Marketing and Sales



SCORE	1 2 3 4 5	NOTES
INFO TYPE		Actual sales figures linked to specific marketing campaigns are high quality, with attitudinal surveys about purchasing intentions being a far less convincing type of data.
RELEVANCE		Strong cause-related marketing data clearly applicable to high profile retail brands, but applicability would be questioned elsewhere. Predictive power of data would also be suspect.
SOURCE		Data coming from business results very credible, whilst the academic studies less so. Survey data from very credible sources.
ATTITUDES		No obvious reason for attitudinal blocks.

Head of Human Resources

Turning to the head manager for Human Resources, we will need to focus on issues of workforce development, recruitment and retention. The skeptical manager is likely to see CE as "window dressing", something to make the employees feel a little better, but not of much real importance to the HR function. Clearly, getting CE right is not as important as making sure that the company's compensation package is both competitive and cost-effective. The skeptical manager may be surprised, however, to learn how much CE can help to increase employee satisfaction and loyalty, improve recruitment and retention, and build the long-term pipeline of employees.

Employee Satisfaction and Loyalty

In a research study sponsored by the Council on Foundations, Walker Information interviewed a representative sample of employees from a cross section of US employers. It found that a company's CE activities have a positive effect on the average employees' satisfaction and loyalty. In particular:

- A company's support of employee volunteerism is a key driver directly influencing employees' feelings about their jobs. For example, employees involved in employer-sponsored community events were 30% more likely to want to continue working for that company and help it be a success.
- Employees who perceive their companies as having good corporate social performance view them more positively and are therefore more committed to them. Corporate social performance is a key determinant of overall reputation, which also influences overall feelings about a job and employee commitment and morale. The level of CE activities (including cause-related marketing, volunteer programs, and product and service innovations) is a primary determinant of corporate social performance. (The Council on Foundations, 1996)

The results are similar in Europe as well. For example, Fleishman Hillard found that 87% of European employees feel greater loyalty to socially-engaged employers. (Fleishman Hillard, 1999)

A skeptic might say, "Well, it's nice that CE activities can help employees feel better about a company. But what business benefits does that create?" The key link between employee attitudes and the bottom line is demonstrated by research conducted by Sears and published in the Harvard Business Review in 1997. Sears developed a rigorous quantitative model that analyzed and predicted the relationships between management quality, employee behavior and financial performance at Sears. Its research found the following:

- Improving employee attitudes by 5 points drives a 1.3 point improvement in customer satisfaction (as measured by Sears' surveys)
- Improving customer satisfaction by 1.3 points drives a 0.5% improvement in revenue. At Sears, 0.5% improvement in revenue means additional sales of $65 million per year. At its current after-tax margin and price-earnings ratio, those extra revenues increase its market capitalization by nearly $80 million.

This shows the potentially powerful bottom-line impact of improvements in employee attitude at Sears. These findings, combined with those noted above, present a portrait of how corporate social performance can create increases in employee satisfaction and loyalty, which can create increases in customer satisfaction, which can in turn create increases in revenue, profits and market capitalization. While Sears is a singular example, we believe that the results should be equally true at other companies in which line employees are the key point of contact with customers. (Rucci, Kirn, and Quinn, 1997)

Recruitment

Increased CE improves a company's overall image, which, not surprisingly, makes it easier to recruit new employees. For example, Turban and Greening found that ratings of a firm's corporate social responsibility were related to ratings of the firm's reputation and attractiveness as an employer, suggesting that such performance may provide a competitive advantage by attracting potential applicants. In addition, attractiveness as an employer correlates significantly with ratings of a firm's community relations, employee relations, and product quality. (Turban and Greening, 1997)

CE activities, when well-designed, can help meet recruiting targets in direct as well as indirect ways. Consider the example of Whitbread, a major leisure company in the UK that runs pubs, restaurants, hotels and fitness clubs. It operates an extensive program of education partnerships with schools, colleges, and universities. To date, the program has involved over 10,000 young people, 1,500 teachers, and 3,000 employee volunteers. While the program was started primarily to create benefits for the communities in which Whitbread operates, it also has helped Whitbread in its efforts to recruit over 30,000 new employees per year. Through its links with schools and colleges, Whitbread has heightened interest in the company, and facilitated career presentations and work-based placements for students. Its activities have also raised the awareness of the company's strategy, and have helped students to better understand how the company is developing as it moves from its historic "Beer and Pubs" origin towards a fully integrated leisure company.

In addition to the recruiting benefits, Whitbread management has noted that volunteers in the program have increased skills in project management and team working. By forging contacts with young people, Whitbread managers also have been able to identify and understand the needs and interests of potential new markets. (Sabapathy, 2000)

Building the Long-Term Pipeline of Employees

With record-low levels of unemployment in the US, managers are thinking much more carefully about how to ensure a long-term pipeline of employees. Participation in School-to-Work programs has become a more important way of ensuring competent and work-ready entry-level employees. A recent study by The National Employer Leadership Council (NELC) recently analyzed 8 companies' school-to-work programs, and found solid evidence of a positive return on investment for the school-to-work programs in most of the companies studied, quantified in terms of:

- reduced recruitment costs;
- reduced training and supervision costs;

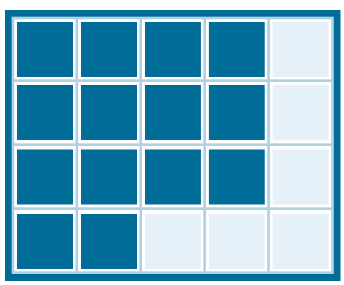
• reduced turnover;
• increased retention rates;
• higher productivity of students; and
• higher productivity and promotion rates of school-to-work program graduates who eventually are hired compared with those of other newly hired workers.

The NELC report concluded, "The benefits of school-to-work programs exceed the costs in nearly three out of four companies studied. All of the companies showed some financial benefit. Moreover, these results include all costs incurred by employers – even if some of the costs were shouldered by private foundations or public agencies, which often is the case. Had the study taken into account outside funding assistance, some of the returns would have been even higher. Finally, these results reflect start-up costs spread over a short period and a small number of students. As the programs continue and serve more students, the startup costs will be spread over more years and more students, which will lead to more favorable results." (National Employer Leadership Council, 1999)

[For additional information on how CE can affect human resources, please see "Human Resources", page 63.]

Scorecard: Human Resources

SCORE 1 2 3 4 5



SCORE	NOTES
INFO TYPE	Largely high quality data, although the data on recruitment would be downgraded by most managers.
RELEVANCE	High level of relevance to many companies, particularly those faced with labour and skill shortages and high training costs of relatively mobile staff.
SOURCE	Survey and case study from high quality sources.
ATTITUDES	One of the areas where prejudice might reduce persuasiveness of data, particularly where diversity and class issues challenge HR approaches.

Head of Operations

The top operating managers are responsible for ensuring that their corporations can produce products and services in a timely, cost-effective way, and can beat their competitors on price, innovation and quality. To persuade a disbelieving operating manager of the value of increased CE, we will need to point to evidence about how CE can help improve the company's ability to innovate, and can help make its products and services more attractive through the use of a diverse set of suppliers.

Innovation and Learning

Kanter, in "From Spare Change to Real Change: The Social Sector as a

Beta Site for Business Innovation", notes that leading companies have discovered that working together with nonprofit and government organizations to solve social problems can give them new insights and approaches to creating business opportunities as well. Solving community needs creates opportunities "to develop ideas and demonstrate business technologies, to find and serve new markets, and to solve long-standing business problems". (Kanter, 1999)

Zadek and Scott-Parker, in "Unlocking Potential: the New Business Case for Employing Disabled People", note similar findings. Companies that redesign their work so that they can increase the number of people with disabilities who can be employed often thereby discover new and better ways to organize work, increase employee productivity, improve their image in the community, and discover new products and services to sell. (Zadek and Scott-Parker, 1999)

The failure to engage in CE, especially the failure to engage in a vigorous and sustained dialogue with multiple stakeholder groups, has been implicated as a key factor in several recent major business difficulties, including those confronted by Shell in Nigeria and with Brent Spar, by Nike in Vietnam, and by BP in South America. Shell management regards its difficulties in Nigeria and with Brent Spar as being caused by a lack of ability to sense and learn about key risks coming from unfamiliar directions. Shell management has indicated that it believes that greater diversity in its management team, and more willingness to engage with stakeholder groups, would have enabled it to understand the problems it was confronting and respond to them in more appropriate ways. This understanding has led to its recent decisions to dramatically shift its approach to interacting with stakeholders, taking a much more open, inclusive and transparent approach. (Raynard, forthcoming)

[For additional information on how CE can affect innovation and learning, please see "Innovation and Learning", page 85.]

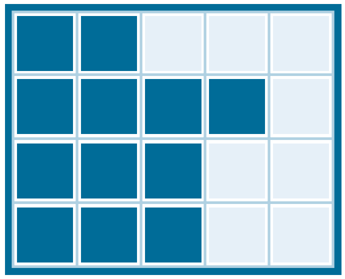
Diversity in Purchasing

Purchasing from diverse suppliers, which is a form of CE, can provide important benefits to businesses. Ford Motor Company currently purchases more goods and services from minority-owned and operated companies than any other US corporation. In calendar year 2000, Ford anticipates purchasing $2.7 billion, roughly 5% of its total goods and services, from minority suppliers. Steve Larson, Manager, Minority Supplier Development at Ford, explains, "It's good business. Minority suppliers provide Ford with some of the highest quality, competitively priced goods and services . . . With the US minority population nearing 30 percent, it is in our best long-term interest to invest in minority businesses and communities. These are our customers." (DiversityInc.com, 2000)

[For additional information on how CE can affect diversity in purchasing, please see "Purchasing/Supplier Development" page 92.]

Scorecard: Innovation and Learning

SCORE	1	2	3	4	5	NOTES
INFO TYPE						Focus on anecdotal, largely qualitative evidence is limiting.
RELEVANCE						Rapidly increasing interest in innovation and knowledge management makes this area feel highly material and applicable, particularly in HR and senior management.
SOURCE						Case material from business executives generally convincing. Statements from managers responsible for purchasing may be regarded with some skepticism because they come from advocates of diversity purchasing.
ATTITUDES						Potential attitudinal blocks regarding diversity issues.



CEO/Top Management Team

The CEO and the top management team has the singular responsibility for managing issues that pertain to the whole corporation, such as strategy, financial performance, mergers and acquisitions, and governance. In addition, they oversee all the functional areas. Accordingly, the CEO and the top management team will be concerned both with the issues presented above, and also with specific ways that increased CE can be helpful in improving stock price, financial performance, corporate reputation, and risk management. We will focus on these issues in this section, noting the most important evidence, and indicating where else in the report additional data may be found.

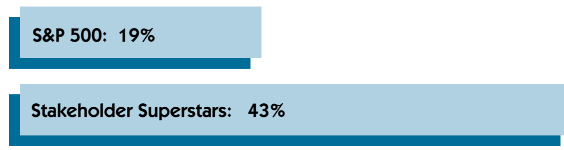
Stock Price and Financial Performance

For most Boards, the key indicator of a CEO's success is the increase in shareholder value, usually as measured by stock price. Showing that CE can affect stock price, either directly by affecting the views of stock analysts, or indirectly by affecting financial performance, is sure to get the attention of CEOs. A current study showing the impact of CE on stock price was recently completed by Towers Perrin. They identified 25 companies that excelled in managing relationships with 5 types of stakeholders: investors, customers, employees, suppliers, and the communities in which the companies operate. The 25 companies include such well-regarded companies as Applied Materials, Cisco Systems, Coca-Cola, General Electric, Johnson & Johnson, Procter and Gamble, and Southwest Airlines.

To determine whether companies excelled in managing stakeholder relationships, Towers Perrin used both publicly available sources, such as the Fortune 100 Best Companies to Work for in America and America's Most

Admired Companies, as well as proprietary data about company activities. They analyzed the performance of these companies over time in comparison to the stock market. The analysis shows that these companies, which they refer to as "stakeholder superstars", outperformed the S&P 500 by more than double over the past 15 year. The total shareholder return was 43% over the past 15 years, while the total shareholder return from the S&P 500 only was 19%. (Schmidt, 2000)

Growth in Shareholder Return, 1984-1999



Source: Compustat; Towers Perrin analysis.

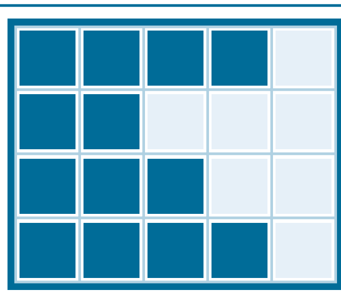
Collins and Porras showed that "Built to Last" companies - visionary companies with goals that extended beyond just maximizing profit - actually were more profitable than their peers. Graves and Waddock extended this analysis by looking in detail at the social performance of "Built to Last" companies. They assessed the corporate social performance and corporate financial performance of 11 "Built to Last" (BTL) companies versus 11 non-"Built to Last" (non-BTL) companies. They found that the BTL companies significantly exceeded the non-BTL companies in both financial measures and CE measures.

- BTL companies had an Return on Equity (ROE) that was 9.8% higher over a 10 year period than non-BTL companies. They had an Return on Assets (ROA) that was 3.55% higher, and a Return on Sales (ROS) that was 2.79% higher. The ten year relative total return to shareholders averaged 63.5% higher for BTL companies than for non-BTL companies.
- BTL companies also out-performed their non-BTL compatriots on CE measures. Using Kinder, Lydenberg, Domini (KLD) data for five CE variables, Graves and Waddock found that BTL companies outperformed non-BTL companies by an average of .578 points on a 5-point scale - roughly 11.6%. (Graves and Waddock, forthcoming)

[For additional information on how CE can affect stock price and financial performance, please see "Stock Price and Financial Performance", page 39.]

Scorecard: Stock Price and Financial Performance

SCORE 1 2 3 4 5 NOTES



INFO TYPE	Principally financial data and in particular stock prices linked to qualitative interpretation of the 'good company'.
RELEVANCE	Although probably accurate, questions about causality undermine confidence in interpretation.
SOURCE	Data provided by reputable business and academic sources, but some are seen as searching for evidence of a positive linkage.
ATTITUDES	No real reason why attitudinal issues should constrain belief of the data.

Reputation

Corporate reputation has become an increasingly important issue for CEOs and the top management team. In a recent study by *Chief Executive Magazine,* conducted by H&K/Yankelovich, 96% of CEOs indicated that they believe that reputation is very important, and 65% dedicate more time to this subject than they did five years ago. (Bovet, 1999) Recent research has shown that a large and growing percentage of most company's total market value is comprised of intangible assets, such as reputation, brand equity, strategic positioning, alliances, knowledge, and the like. A recent study by Interbrand concluded that a full one-quarter of the world's total financial wealth is tied up in intangible assets. (Clifton, 1999)

A corporation's reputation affects its competitiveness in many domains, including a consumer's decision to purchase a product or service, a government's decision to grant a license to operate and other regulatory permissions, and an individual's decision to seek employment with the firm. Corporate reputation research shows that corporate reputation typically is driven by the price, features, and quality of the goods and services that the corporation produces. But more and more, it is also driven by the corporation's commitment to CE. For example, a press analysis determined that 25% of all IBM news coverage in the US was related to its citizenship activities in the community, in education and in the public interest. Many of the articles and electronic media covered IBM's technology leadership as well as its citizenship activities, thereby supporting reputation in both the product and citizenship domains. (Litow, 2000)

In the realm of consumer purchasing, evidence suggests that consumers have come to regard a company's CE activities as being a core part of the business. The Conference Board surveyed 1000 Americans in 1999, and found that almost 89% agree large companies should do more than focus only on achieving profitability within the law. 42% said that they held companies completely or partially responsible for helping to solve social problems like crime, poverty, and lack of education. Lastly, 33% said that companies should focus on setting higher ethical standards, going beyond what is required by law, and actively helping build a better society for all.

The Conference Board found that consumers are willing to back up their expectations with action as well. 46% percent of respondents said that they had carried out a purchase decision in favor of a company, or decided to speak out in favor of a company because of a positive perception of its social responsibility. 49% of respondents said that they had decided not to purchase a product or service from a company, or had spoken critically of a company, because it did not meet their standard for being a socially responsible company. (The Conference Board, 1999)

CE activities can be important in establishing a positive reputation with governments. For example, Cisco Systems' Networking Academies have now expanded to 3,700 sites in 64 countries. John Morgridge, Cisco's Chairman, noted that Cisco began the Networking Academies in part as a way to help address some of the potential needs for network administrators. But it found, as the Networking Academies have grown in scale and impact, that this activity has opened important doors to governments across the world. Its Academy activities have helped create the perception that Cisco is helping to solve problems that matter to governments and citizens, rather than being just as another foreign multinational that is looking to grab a piece of the local market.

Suez Lyonnaise des Eaux, one of the world's largest managers of water systems, has also had very positive experience in using CE as a way to address social issues and improve its reputation with governments. The company has entered into partnerships with governments and NGOs focused on a wide range of issues, from developing cost-efficient ways to provide water and waste treatment in Third-World shantytowns to helping solve the problems of youth unemployment in France. Since governments are a major customer group, improving relationships with governments is a major marketing goal for the company. Please see the case write-up on page 59 below for additional details.

CE activities are also important in shaping reputation with existing or prospective employees. The results noted above on how CE affects recruiting, and the experiences of Texaco and Denny's, noted below on page 80, show how CE activities can help shape reputation in the labour market and thereby change a company's ability to attract talent.

[For additional information on how CE can affect corporate reputation, please see "Reputation", page 45.]

Scorecard: Reputation

SCORE	1	2	3	4	5	NOTES
INFO TYPE	■	■	■			Good blend of financial, case study and opinion poll data. Financial and case study data are convincing, but this type of opinion poll data is considered of limited value in handling complex ethical issues.
RELEVANCE	■	■	■			Relevant maily to high-value, retail brands. Claim of links between ethical behaviour and reputation element of intangible asset intuitively correct but not convincingly demonstrated, and many counter-examples exist.
SOURCE	■	■	■			Reputable sources, particularly the opinion polls, although their credibility might suffer from perceptions that some are seeking to advocate these approaches.
ATTITUDES	■	■	■	■		Focus on asset valuation and consumer polls would raise few attitudinal problems.

Risk Management

The management of risks to operations, quality, customer relations, financial stability and reputation ultimately rests with the top management team. The management of risk has become more difficult for several reasons:

- Globalization of risks: companies are competing in a global environment, with risks coming at them from multiple sources and multiple geographies. It is more difficult to keep abreast of potential risks, and to know how to respond if they occur.
- Heightened surveillance: Companies are being watched by more groups, with more diverse agendas, than ever before. These groups are linked across the globe by the Internet, allowing instant transmission of fact (and falsehood) to millions of consumers.
- Increased demands for transparency: Consumers, labour, and communities have moved from a "trust me" to a "show me" stance, demanding to know more about what a company is doing, and how it affects them.

A commitment to CE can help to ensure that when a company's actions are monitored closely, the picture that emerges is flattering rather than detrimental. In addition, a long-term commitment to CE can help to build trust and faith in the company's good intentions. Consider the experience of Sainsbury's. The British food retail gained reputationally when Oxfam added a carefully worded positive statement at the beginning of the company's annual report congratulating it for moving forward in the area of labour standards in its global supply chains. The company gained similarly when it joined and in many ways helped create the Ethical Trading Initiative, also in close collaboration with Oxfam.

This history of proactive engagement on the issue of labour standards helped deflect public criticism when the issue of labour standards in the global supply chain became a hot issue at the end of the 1990's. Marks & Spencer, a major competitor, was in court at that point, litigating over whether it had been libeled by stories attacking it for unfair labour practices in its supply chain. Tesco's, another major competitor, was under significant pressure to address concerns over unfair labour practices among its suppliers in Africa. Sainsbury's, in contrast, continued to enjoy favorable public relations throughout this period. (Zadek, forthcoming)

Failing to manage CE risks properly can be fatal as well. Consider the case of Monsanto. It failed to engage in a serious way with its critics, and severely misjudged the level of public concern over genetically modified foods in Europe. The ensuing public relations firestorm so badly damaged the reputation of the company that the valuation of the biotechnology portion of the company entirely collapsed. Please see the case study in the section on Innovation and Learning, page 89. (Stipp, 2000)

Finally, a company's a commitment to CE can help to ensure that its management and employees remain committed to socially responsible behaviour, including respecting and complying with the law in all jurisdictions in which the company operates. This can add significant value to the company, because there is strong evidence that behaving in ways that are egregiously socially irresponsible and illegal is detrimental to shareholder value. In 1997, Jeff Frooman of the University of Pittsburgh analyzed 27 event studies that measured the stock market's reaction to incidences of socially irresponsible and illegal behaviour. These event studies used product recalls, environmental lawsuits, anti-trust lawsuits, and regulatory fines as indicators of socially irresponsible or illegal behaviour. The analysis showed that companies that engaged in irresponsible or illegal behaviours in ways that were egregious enough to invoke regulatory and legal sanctions suffered very significant losses in shareholder wealth, which were not ever recovered. (Frooman, 1997)

[For additional information on how CE can affect risk management, please see "Risk Management", page 52.]

Scorecard: Risk Management

SCORE	1	2	3	4	5	NOTES
INFO TYPE	■					Data are largely qualitative and/or anecdotal, although there are a few high-profile examples of the financial costs of 'getting it wrong.' Link to legal dimension is important, particularly in the USA.
RELEVANCE	■	■	■			Risk management is seen as highly relevant, but evidence only covers high profile cases for visible companies. Data not so relevant for companies engaging in low profile community actions.
SOURCE	■	■	■			Advocacy sources are only partly convincing, and arguably less so over time. Company sources of significance of risk dimension are very convincing, as are major consultancies specialising in area.
ATTITUDES	■	■	■			Increasing acceptance of risk element marks an overcoming of resistance often based on degree of corporate arrogance.

Chapter Conclusion

In this section, we took a quick virtual tour of a corporation, noting the specific objectives of particular managers, and bringing forward some of the evidence that CE could help achieve those objectives. We hope that this section has given the reader a taste of the quantitative evidence available showing how CE can help achieve business success, and how to mobilize this evidence in ways that will be persuasive. For more details on the evidence, please see the chapter entitled "The Numbers Warehouse". For more information on the scope and limitations of this paper, as well as the definition of CE and other important terms, please see following chapter, entitled "What Are We Talking About?"

IV. What Are We Talking About?

The previous two chapters provided a quick immersion into our approach and key findings. In this chapter, we provide a more thorough review of the purpose, scope and limitations of the paper. We discuss the definition of Corporate Engagement, explain why we chose the definition, and compare it to other important terms describing the field, including Corporate Social Responsibility, Corporate Community Involvement, and Corporate Citizenship. We close the chapter by defining the various components of the measurement process.

Background

Purpose

The purpose of this paper is to encourage business to deepen its involvement with communities. To attain this end, the paper reviews the quantitative evidence showing when and how CE creates business as well as societal benefits.

This paper was commissioned by the Ford Foundation. The initial scope of the paper was to explore the quantitative measurements of the benefits to corporations of Corporate Involvement in Community and Economic Development, as defined on page 30. We expanded the paper's scope significantly, because the quantitative evidence available regarding Corporate Involvement in Community and Economic Development is quite limited.

Audience

This paper is directed toward people who seek to persuade skeptical managers and executives of the business benefits of CE. They may be managers or executives themselves. They may also be government officials or nonprofit leaders. They have in common an interest in learning more about the evidence showing when and how CE can create benefits for business, and how to mobilize this evidence in ways that skeptical managers will find persuasive. This paper is not directed at skeptical managers. We hope, however, that if they should read the paper, they will find their views represented, and conclude that some of our arguments are just a bit more persuasive than they initially had expected.

Limitations

This study has a number of important limitations. When we started, we set out to concentrate on quantitative evidence. During the course of the study, we recognized the importance of qualitative data in persuading the skeptical manager. Qualitative data helps to provide rationale, context and texture for the discussion, and to amplify important points that quantitative data can't address adequately. Accordingly, we have drawn on qualitative evidence in an illustrative way in this paper. Time and space, however, prevented us from providing a thorough inventory of all the qualitative evidence available. We have only covered thoroughly the quantitative evidence.

Secondly, we also have chosen to focus only on the social aspects of how corporations engage in positive ways with their communities. By social, we mean the economic, organizational, and cultural aspects of corporate engagement with communities. We have chosen not to address any of the environmental aspects of corporate engagement with communities. We have done this for two reasons:

- Our primary focus has been on persuading corporations to address social challenges, especially those confronting low-income individuals and communities, and the social aspects of how corporations interact with society are most relevant here.
- Other organizations (such as the World Business Council for Sustainable Development) have already done an excellent job in analyzing the environmental aspects of how corporations can engage in positive ways with their communities.

Finally, our work is primarily focused on US and UK examples. We are aware that other countries in the world have different traditions and approaches to the role of business in society. We also understand that the very definitions of CE and corporate social responsibility vary from country to country. We are therefore clear that in countries other than the UK and the US, there are different standards for what constitutes persuasive (and unpersuasive) evidence that CE has business benefits, and differences concerning the level of business benefits needed to persuade managers to increase their level of commitment to CE.

Defining Corporate Engagement

There are many views on how businesses ought to interact with society, and almost as many terms describing these different interactions. In this section, we note the definitions for Corporate Engagement and a number of related terms that describe how businesses interact with society. These definitions are not an exhaustive list, nor are they intended to be the final word on the subject. Rather, they are intended to help the reader understand what we are, and are not, covering in this paper.

Corporate Involvement in Community and Economic Development (CI in CED), as defined by the Ford Foundation, is the set of activities that:

- Engage core business operating resources and competencies (including such diverse functions as human resources, product development, marketing, procurement, real estate, investments) in addition to community relations and philanthropy
- Are part of a company's ongoing business strategy and are seen as contributing economic benefit to a company (by unleashing workforce potential, expanding into new markets, improving community relationships, protecting the license to operate, enhancing reputation, and developing new products and services)
- Have a positive impact on community and economic development, particularly for low-income individuals and communities (for example, by improving the skills and earnings of low-income workers; by creating jobs in areas of high unemployment or underemployment; by increasing the access of low-income people to affordable, quality goods and services that improve their economic circumstances; and by increasing private sector investment in small businesses located in low-income communities or owned by minority entrepreneurs)

In our initial exploration, we focused quite closely on measurements of benefits of CI in CED, as this was our mandate from the Ford Foundation. But as we explored, it became clear that there were almost no publicly available quantitative measurements that showed a benefit to corporations and that looked solely at CI in CED. We therefore expanded our research to include the entire universe bounded by **Corporate Community Involvement**, **Corporate Social Responsibility**, and **Corporate Citizenship,** which are related but broader terms.

Corporate Community Involvement, as defined Ed Burke and the Boston College Center for Corporate Community Relations, is:

> "[T]he state of relations between the company and the community in which it has a presence or an impact. It encompasses programs that advance the interests of both the company and its communities, such as donations, employee volunteerism and community partnerships. It involves the impact of the operational activities of the company on its communities as well as programs established to develop relationships with groups and organizations in communities." (Rochlin, 2000)

The term "community" here includes the company's employees, geographic communities in which business has a presence, communities of interest such as environmentalists and mental health reformers, and communities of identity such as students, people with a disability, and women.

Corporate Social Responsibility (CSR), as defined by Business for Social Responsibility (BSR), consists of:

> "Operating in a manner that meets or exceeds the ethical, legal, commercial and public expectations that society has of business."(BSR, 2000)

Corporate Citizenship is a closely related concept. As defined by David Logan of the Corporate Citizenship Company, Corporate Citizenship is

> "The total impact of business on society." (Logan, 2000)

Corporate Community Involvement (CCI), Corporate Social Responsibility (CSR) and Corporate Citizenship (CC) are complex concepts, and much has been written about what particular sorts of practices do, and do not, constitute CCI and CSR. For an insightful analysis of the components of these terms, please see "Corporate Social Performance Revisited" (Wood, 1991), and "Stakeholder Mismatching: A Theoretical Problem in Empirical Research on Corporate Social Performance" (Wood and Jones, 1995). We will not attempt to replicate that discussion here. Instead we will simply note that CI in CED as defined by the Ford Foundation is a subset of each of CCI, CSR, and CC. CI in CED is specifically focused on low-income communities, while CCI and CSR include all the communities in which a company has a presence or an impact, whether low-income or not. In addition, CI in CED focuses somewhat more on a company's core competencies and operations than does either CCI or CSR.

For the purposes of our discussion, we will refer to all of CSR, CCI, CC and CI in CED as "Corporate Engagement" (CE). We have chosen to use a new term because we want be clear that we are including the entire terrain. The alternative would be to use the term "CCI/CC/CSR/CI in CED", but this seemed a little less graceful. We are not intending, however, to signal that the term "Corporate Engagement" should be adopted widely.

In this paper, we are focusing on Corporate Engagement activities that:

- Offer the potential of having a positive impact on low-income communities.
- Form part of an ongoing corporate strategy for community engagement and enhanced business performance.
- Offer potential direct or indirect benefit to the corporation.
- Includes both philanthropic activities and/or activities that tap into the corporation's core competencies and operations - its power to purchase, develop products, invest, market, hire and train, and innovate.

In the paper, we look at all the evidence that CE can create business benefits. We do not sort out the particulars of whether the evidence brought forward is about CI in CED, CCI, CC, or CSR. We believe that the measurements that we look at in this paper will be useful to individuals interested in persuading companies to pursue CI in CED.

Defining the Components of "Measurement"

Since one of the key tasks of this paper is to provide an overview of the state of the art of measuring the benefit to the corporation of CE, we need to unpack the term "measurement" and define its various components.

By way of example, consider the task of measuring changes in the temperature. What we'd like to know is how hot or cold it is at a particular place in the world, and how this changes over time. In order to talk about how hot or cold it is, and how we go about measuring this, we will define some terms that are useful in describing the process and results of measuring changes in the temperature. Temperature is an example of what we will define to be an indicator. An indicator describes some aspect of the world that we would like to discuss or measure. In this case, "temperature" is an indicator that tells us how cold or warm it is at a particular place in the world. We will next define measurement system to be the theory, process and tools that are used to assign a numerical value to the indicator. In the case of temperature, there are several measurement systems, including the Fahrenheit and Celsius systems for assigning a numerical value to the indicator. An example of a measurement tool might be a mercury thermometer, or perhaps a digital thermocouple. We will define measurement data to be the data or information gathered by the measurement tools, and used to assign a numerical value to the indicator. So, for example, measurement data would be collected when someone uses the thermometer or thermocouple to determine the precise temperature at particular place at a particular time. Finally, we will define an outcome measurement to be the use of measurement data to determine how a particular set of activities affects an indicator. So, for example, an outcome measurement on the use of natural gas for heating a home would involve collecting measurements of temperature in the house over time to determine exactly how much the temperature goes up or down as the result of burning a particular amount of gas fuel.

Now let's turn back to the measurement of the corporate benefits of CE. In this case, we will need an indicator that will tell us whether or not the corporation is gaining a benefit from CE. The most important indicator is profitability. If we can show that profitability increases over time as a result of engaging in CE, we will have shown to everyone's satisfaction that the corporation is benefiting from engaging in CE. There are other important indicators that are determined by the business success model for the company or industry. These might include strategic positioning, reputation, brand equity, employee satisfaction, customer loyalty, and the like. The measurement system is the theory, process and tools that we use to assign a numerical value to the indicator. The measurement is the use of those tools and techniques to assign a specific value to the indicator at a specific time or under a specific set of circumstances. The outcome measurement is the use of measurements over time to determine exactly how the indicator (such as profitability) goes up or down as a result of particular CE activities.

We are most interested in three types of outcome measurements, which we will term process measurements, efficiency measurements and return-on-investment measurements. We will define return-on-investment (ROI) measurements to be measurements of the economic benefits and costs to the company of a particular CE activity. These are the most useful types of measurements. They let managers know whether the company's bottom line will be improved if it engages in particular types of CE activities. Unfortunately, as the paper will show, ROI measurements are also the rarest types of measurements.

We will define efficiency measurements to be measurements that compare the cost of a specific CE activity per unit of outcome to the costs of other activities per unit of outcome. So, for example, an indicator that is of interest in human resources is the turnover of staff. An efficiency measurement would be a study that showed whether or not CE activities that reduced the amount of turnover cost more or less than non-CE approaches that reduced turnover by the same amount. Efficiency measurements are not as useful as ROI measurements, but they still can be quite helpful in persuading companies to engage in particular activities, particularly if linked to key elements in the business success model.

Finally, we will define process measurements to be measurements that just show whether CE activities have an effect on outcome indicators. So, for example, a process measurement would show whether using a CE approach enabled a company to reduce turnover. It would not show whether the CE approach cost more or less per unit of reduction in turnover than other approaches, nor would it show whether the company's profitability was enhanced.

Process measurements are the most commonly available measurements, and unfortunately, the least useful. Why? Because there are almost always non-CE approaches to achieving the same goals that CE approaches can achieve. Simply showing, for example, that locating a store in the inner city can help boost the average sales per square foot, doesn't tell us whether it's a more or less efficient way to boost average sales per square foot than other strategies. Nor does it tell us whether the stores in the inner city are more profitable, once all the different costs of operating in an inner city location are factored in. Thus, while process measurements can be useful in starting conversations with disbelievers, they are rarely sufficient to persuade disbelievers to take action.

Chapter Conclusion

In this chapter, we have discussed the scope and limitations of this paper. We have also provided definitions for some of the key terms describing relationships between corporations and society, including Corporate Social Responsibility, Corporate Community Involvement, and Corporate Citizenship. Finally, we noted the components of measurement, and defined various parts of the measurement process.

The following chapter is The Numbers Warehouse. In this chapter, we examine much of the most important publicly available quantitative evidence showing when and how CE creates business benefits. We hope that the Disbelievers Scorecards along the way will help also to show the potential problems that skeptics are likely to note about the data, and thereby prepare persuaders to better respond to these challenges.

V. The Numbers Warehouse

This chapter is an inventory of many of the most important publicly available quantitative measurements that show the benefits to increased CE. We will also note case examples where relevant, although we will not present an exhaustive listing of all case studies. The authors highly recommend finding a comfortable armchair with good lighting before continuing.

It is not necessary to read this chapter from front to back. The chapter is organized into three major areas, and it is possible to skip to the particular areas in which you are most interested, and come back to other areas later as needed. The three major areas, and the topics within each area, are as follows:

1) Measurement of benefits that accrue across the entire corporation
   a) Stock Price and Financial Performance
   b) Reputation
   c) Risk Management
   d) Government Relations/Regulatory Oversight
2) Measurements of benefits that are specific to particular business functions
   a) Human Resources
   b) Workforce Diversity
   c) Marketing and Sales
   d) Innovation and Learning
   e) Diversity in Purchasing
3) Innovations that expand the market
   a) Financial Services Industry
   b) Retail Site Selection
   c) Homeowners Insurance

For each of the topics, we note the benefits that are claimed by advocates, and indicate the managers that are most likely to be interested. We then note the major quantitative measurements of whether and how CE creates those benefits. Please note that we repeat all the quantitative data presented in the Quick Tour, to ensure that all the data are available in one spot. For each section, we provide the Disbelievers Scorecard, indicating what sorts of challenges a skeptic is likely to raise to the data. Please note also that there are some differences between the Disbelievers Scorecards presented in this chapter, and those presented in the Quick Tour chapter. The Scorecards in the Quick Tour referred only to the data presented in the Quick Tour, while the Scorecards in this chapter refer to the complete set of data presented in this chapter.

We also note for each issue or function what key findings are "missing", i.e., what data is still needed to make a compelling case for increased CE to benefit these issues or functions. We will also note potential approaches for developing these missing findings.

A. Measurements of Overall Business Effect

Stock Price and Financial Performance

What Are The Potential Benefits?

Advocates for CE claim that companies that excel at managing their stakeholder relationships produce above-average financial returns and stock price performance. In their view, "developing and maintaining good relationships with stakeholders through positive internal and external relationship building... is a key to long-term success." (Graves and Waddock, forthcoming). Arguing to the contrary, financial analysts claim that any attention given to social issues distracts management from its primary purpose of maximizing shareholder value. Therefore, companies that are clearly committed to CE are predicted to suffer a penalty in the stock market. As we will see below, the weight of the evidence is in favor of the advocates and against the financial analysts.

Which Managers Are Interested?

The top management team is the set of managers that is directly charged with managing the overall financial performance of the firm, and maximizing shareholder wealth. These are the managers who are most interested in understanding whether and how investments in CE can improve the firm's financial performance and stock price.

What Indicators Are Used?

For publicly traded companies, the key indicators are the stock price and earnings, and measures of financial performance, including Return on Equity (ROE), Return on Assets (ROA), Return on Sales (ROS), and Economic Value Added (EVA).

Key Outcome Measurements

The most compelling evidence comes from the comparison of the financial performance of companies that have excelled at CE with a matched set of companies of a similar size in similar industries, or with broad market indicators such as the S&P 500.

Graves and Waddock: "Beyond Built to Last"

As noted above, Graves and Waddock have extended the critical analysis started by Collins and Porras in their 1994 book, "Built to Last". Collins and Porras identified 18 companies as "Built to Last", and compared the performance of these companies to 18 companies of a similar size in the same industry. Graves and Waddock maintained that relationship in their study, but due to mergers, bankruptcies, and unavailable data, were only able to gather full data for 11 of the 18 original pairs. They assessed the corporate social performance and corporate financial performance of these

11 "Built to Last" (BTL) companies versus the 11 non-"Built to Last" (non-BTL) companies. They found that the BTL companies significantly exceeded the non-BTL companies in both financial measures and CE measures.

- BTL companies had an ROE that was 9.8% higher over a 10 year period than non-BTL companies. They had an ROA that was 3.55% higher, and an ROS that was 2.79% higher. The ten year relative total return to shareholders averaged 63.5% higher for BTL companies than for non-BTL companies.
- BTL companies also out-performed their non-BTL compatriots on CE measures. Using Kinder, Lydenberg, Domini (KLD) data for five CE variables, Graves and Waddock found that BTL companies outperformed non-BTL companies by an average of .578 points on a 5-point scale - roughly 11.6%. (Graves and Waddock, forthcoming)

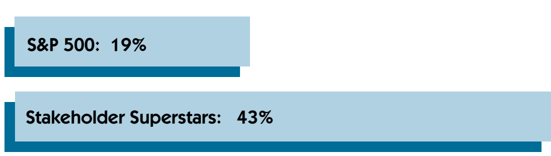
Towers Perrin: "Stakeholders' Perspectives"

As noted above, Towers Perrin completed an analysis similar to Graves and Waddock, and found a similar result. They identified 25 companies that excelled in managing relationships with 5 types of stakeholders: investors, customers, employee, suppliers, and the communities in which the companies operate. The 25 companies include such well-regarded companies as Applied Materials, Cisco Systems, Coca-Cola, General Electric, Johnson & Johnson, Procter and Gamble, and Southwest Airlines.

To determine whether companies excelled in managing stakeholder relationships, Towers Perrin used both publicly available sources, such as the Fortune 100 Best Companies to Work for in America and America's Most Admired Companies, as well as proprietary data about company activities. They analyzed the performance of these companies over time in comparison to the stock market. The analysis shows that these companies, which they refer to as "stakeholder superstars", outperformed the S&P 500 by more than double over the past 15 year. The total shareholder return was 43% over the past 15 years, while the total shareholder return from the S&P 500 only was 19%. (Schmidt, 2000)

While both of these studies are very compelling, it is still worth noting that it is quite difficult to distinguish the causality. Do these companies perform better financially because they engage in more CE? Or do these companies perform better because they have excellent management, and one of the things that excellent managers do is to manage all the stakeholders better? It is also hard to know whether excellent financial performance enables better stakeholder management - i.e., companies that are doing well financially have more resources that

Growth in Shareholder Return, 1984-1999



Source: Compustat; Towers Perrin analysis.

they can use to improve stakeholder relations - or whether better stakeholder relations actually do improve financial performance.

Waddock and Graves: "The Corporate Social Performance - Financial Performance Link"

A 1997 study by Waddock and Graves does shed some light on at least one aspect of the causality. They studied the relationships between corporate social performance (using ratings developed by KLD) and financial performance (as defined by ROE, ROA, ROS) of 469 companies in a broad range of industries. Waddock and Graves found that there was a very significant positive correlation between high ROA and high levels of social performance in their sample; there was a significant positive correlation between high ROS and high levels of social performance, and there was a positive, but not significant, correlation between high ROE and high levels of social performance.

In addition, they found evidence both that above-average social performance causes above-average financial performance, and also the converse: that above-average financial performance causes above-average social performance. In particular, their analysis showed that above-average social performance in one year was a good predictor of better financial performance in the following year, and also that above-average financial performance in one year was a good predictor of better social performance in the following year. One might consider this to be a "virtuous circle". Doing well socially helps improve financial results, which helps then support social results, and so on. (Waddock and Graves, 1997)

One critique that can be made of some of these studies is that they focus on a fairly limited number of businesses. "Surely," the skeptics may say, "if you let me choose precisely which set of companies to analyze, I can show you any result that I want. The real test will be to look at the entire market." A second critique, raised by financial analysts, is that when management is paying attention to stakeholder relations, it is not paying attention to making money. In their view, pursuing CE is squandering limited resources on something that is not core to the business. Accordingly, they would predict, if you look across the entire market, you should see that companies that spend more time and effort on CE should do worse, not better, than companies that do not.

A more balanced view, advanced in our interviews, might be summarized as, "Virtue is its own reward, but unfocused virtue is bad business." In this view, a company's investment in CE will pay off financially only when the investment is focused and connected to its core business strategy. A company that spends time and effort on CE, in ways that is not linked to its core business and strategy, will generally be worse off than a company that does not spend time and effort on CE. This view predicts that in a market in which some firms are pursuing CE in a way that is linked to its core business and strategy, and in which others are pursuing CE in a way that is not, there should be no correlation between level of CE and financial performance. The times where it helps will be offset by the times where it hurts.

This view is supported by the research that has focused on "socially screened" equity funds. These are equity portfolios of stocks from companies that have achieved an acceptable level of performance on specific corporate social responsibility measures, including labour standards, environmental performance, community engagement, diversity in the workforce, and others. A series of studies performed over the past decade have compared portfolios of socially screened stocks to portfolios of non-screened stocks. Some of the studies have shown that the socially screened funds performed better, and others worse, than market indicators. The most recent, and most definitive studies, show that the difference between socially screened portfolios and market portfolios arises because of the difference in volatility and industry exposure between the portfolios. Once the portfolios are matched in terms of volatility and industry exposure, the returns are essentially identical.

DiBartolomeo: Analysis of Domini Index Performance

For example, a thorough study completed in 1996 by Dan DiBartolomeo of the Northfield Information Services, a Boston-based investment consulting firm, showed the following:

- The Domini Social 400 Index (a leading socially screened index of 400 companies) outperformed the S&P 500 index from 1990 to 1995, but the difference in performance could be shown to be primarily due to different industry "bets" implicit in the social screening process. If the Domini Social 400 Index were reweighted, so that it matched the S&P 500's macro-economic and industry exposures, it would have performed essentially the same as the S&P 500 during the study period.

In other words, if an investor were to hold a socially screened portfolio that had the same overall exposure to macroeconomic and industry variables as the market does, he or she could expect to earn the same return as the market. There is neither a financial bonus nor a financial penalty that flows from holding stock in "socially positive" companies. (DiBartolomeo, 1996)

This evidence supports the view that investing in CE, without necessarily linking the investment to the core strategy of the company, on average does just as little harm as good. Needless to say, this would not be overwhelmingly evidence to bring to a skeptic in hopes of persuading him or her to increase CE.

Proponents of the view that CE will benefit companies only when tied into a core business strategy have developed a new index fund, the Dow

Jones Sustainability Group Index. This index was launched in September 1999 and since then has been tracking the financial performance of the corporations whose corporate sustainability ratings are in the top 10% of the market. Corporate sustainability is measured by five indicators:

- Innovative and efficient technology
- High standards for governance
- High returns to shareholders
- Industry leadership
- Commitment to societal well-being

Currently, there is not enough data to show whether this view is supportable, and whether this fund will be more profitable than other socially screened funds.

Social Investment Forum: Socially-Conscious Investors

Positive corporate social performance can be helpful in improving the ability of the corporation to manage relationships with, and attract capital from, "socially conscious" individuals and organizations. But do these individuals and organizations control enough capital to merit the attention of top management? Until recently, the answer clearly was "No." However, the rapid growth of shareholder activism and socially screened investment funds may be changing that answer. Socially screened funds are growing in size at more than twice the rate of the rest of the market. Consider the following facts:

- There were $1,497 billion in screened portfolios in 1999, up from $529 billion in 1997 - approximately 9% of the $16.3 trillion in investment assets under professional management in the U.S. in 1999.
- The assets managed in screened portfolios grew at a rate of 183% between 1997 and 1999, while assets managed by all professional managers grew by only 42%.
- $657 billion of non-screened assets were held in 1999 by institutions that actively submitted or promoted shareholder proxies on social issues.
- Taking social screening and shareholder activism together, approximately $2.2 trillion, or 13% of the total investment assets under management in the U.S., engaged in some type of socially responsible investing in 1999. (Social Investment Forum, 1999)

This data indicates that socially responsible investing has begun to reach a scale where it can start to make a difference in the shareholder relations of publicly traded companies. While this should not be overstated, publicly traded companies may be able to gain some advantage in securing investments from socially conscious consumers if they have a clear commitment to, and strategy for attaining, positive corporate social performance as part of their plan for increasing shareholder value. Leading companies are beginning to report this effect. For example, Stan Litow, Vice President for Corporate Community Relations at IBM, reports that IBM's top ranking in a number of studies of CE have helped him to persuade colleagues of the value of CE, since it helps demonstrate the connection between CE and stock purchases by investment funds. (Litow, 2000)

What's Missing?

One of the major weaknesses of most of the current studies is that they are retrospective - they identify companies that are doing an excellent job now, and show that they performed better than their peers in the past. But this isn't as good as picking companies that are doing an excellent job now, and showing that they will outperform their competitors in the future. It is much easier to pick a winner in hindsight than to do so with foresight. For example, of the 36 companies profiled in In Search of Excellence, three are no longer listed on a stock exchange, and only twelve outperformed the S&P 500 Index over the past five years.

In order to develop prospective studies, researchers need to overcome a number of important technical difficulties. Most important of these is working to develop a consensus among practitioners and academics on how to define and measure CE. Currently, practitioners and academics are employing many methods of measuring CE, which differ dramatically. Without some agreement on what it is that we are seeking to measure, we are unlikely to come up with a study that proves anything to anyone's satisfaction.

Another weakness is that most of the currently available studies do not develop hypotheses about precisely how increasing CE is supposed to create improvements in financial performance and stock price. This is needed to enable us to refine the measurement and data-gathering process, so that we can get a sharp look at all the parts of the system that are involved in the causal chain between investments in CE and improvements in financial performance and stock price. Particularly if one takes the view that CE is only effective when it is tied into business strategy, it becomes very important to measure both the level of CE and also the extent to which it is, or is not, tied into the business strategy.

Potential Approaches for Improving Measurements

The next step in making the case that pursuing CE helps to improve financial and stock price performance is to develop more segmented data that tracks specific CE and business strategies over time. For example, a longitudinal study might assemble a set of companies that are excelling at pursuing CE in a way that is linked closely to their core business strategy, and develop a set of matched companies that are not pursuing CE in such a way. The study would track their financial and stock performance over a five year period. The study would also track "intervening variables" that enable us to get a better picture of precisely how investments in CE are helping to improve financial results.

To understand more about how tracking "intervening variables" would help, consider a situation where we hypothesize a relationship between investments in CE, improvements in employee morale, and improvements in profitability. The implicit model here is that investments in CE will help particular types of companies to improve their employee morale, thereby improving customer service and retaining customers, and thereby improving profitability. To evaluate this model, we will need to track not only investments in CE and profitability, but also changes in employee morale, customer service, and customer retention. This would help to build our ability to predict how and when pursuing CE adds bottom-line benefit to the corporation.

Scorecard: Stock Price and Financial Performance

SCORE	1	2	3	4	5	NOTES
INFO TYPE	■	■	■	■	□	Principally financial data and in particular stock prices linked to qualitative interpretation of the 'good company'.
RELEVANCE	■	■	□	□	□	Although probably accurate, questions about causality undermine confidence in interpretation.
SOURCE	■	■	■	□	□	Data provided by reputable business and academic sources, but some are seen as searching for evidence of a positive linkage.
ATTITUDES	■	■	■	■	□	No real reason why attitudinal issues should constrain belief of the data.

Reputation

What Are the Potential Benefits?

Advocates claim that increases in CE create benefits for a company's reputation. There are many managers who agree. Particularly in highly regulated industries (such as health care, utilities, insurance, and financial services), it is not unusual to find managers who believe that improvements in company image are the most important benefit from engaging in CE activities. So, for example, 8 of the 11 winners of the 1999 Social Compact Award for innovative corporate-community partnerships cited "improved reputation" as one of the key benefits of their CE activity. (Social Compact, 1999)

Which Managers Are Interested?

In general, the managers most concerned with corporate reputation are the managers at the top of the organization. Managing the reputation of the company is ultimately the responsibility of the CEO and the senior executives. In a recent study by *Chief Executive Magazine*, conducted by H&K/Yankelovich, 96% of CEOs believe that reputation is very important, and 65% dedicate more time to this subject than they did five years ago. In addition, managers in the public relations, communications, community relations, and government relations areas are also very concerned with managing corporate reputation. The management of corporate reputation also overlaps with the management of the company's brands, particularly in consumer goods companies. In this case, brand managers also become interested in how the corporate reputation is managed.

Recent research has shown that a large and growing percentage of most company's total market value is comprised of intangible assets, such as reputation, brand equity, strategic positioning, alliances, knowledge, and the like. A recent study by Interbrand concluded that a full one-quarter of the world's total financial wealth is tied up in intangible assets. (Clifton, 1999) Fombrun analyzed the reputational capital of major companies, and developed estimates of $52 billion for the reputational capital of Coca-Cola, $12 billion for Gillette, $11 billion for Eastman Kodak, and $9 billion for Campbell. (Fombrun, 1996) Fombrun also suggests that high levels of reputation grant companies distinctive advantages:

- Their products and stock offerings command higher prices
- Their jobs lure more applicants
- Their clout with suppliers is greater
- Their risks of crisis are fewer

Yet, even though reputation would appear to be very important to top managers, it is important to note that they don't always gather data about it. As reported by Susan Fry Bovet in *PR Week*, only 25% of companies with revenues above $500 million have formal systems for measuring reputation. This number shrinks as the size of the company shrinks as well. Thus, although reputation appears to be important, it isn't something that is measured regularly by most companies. (Bovet, 1999)

What Indicators Are Used?

There are a number of closely related indicators that are used to describe corporate reputation. The measurement of corporate reputation is an area in which practice is rapidly evolving, and in which there is not a consensus on the correct approach. Indicators that are used include the following:

- Corporate reputation, as defined by peers. This is the simplest indicator of reputation. This indicator looks at how highly a company's peers regard that company's management and strategy. Essentially, peers rate peers. Peer review is a fairly common approach to rating expert performance, and is used widely in professions such as medicine, law, and academia.
- Corporate reputation, as defined by stakeholders. This is a more complex indicator of reputation. It looks at how the corporate reputation is regarded by a range of stakeholders, including peers, investors, customers, regulators, suppliers, and the community.
- Corporate brand. Corporate brand is a narrower indicator than corporate reputation. It looks at the implicit "promise" and characteristics that the

corporate brand conjures up in the minds of consumers and investors. There is evidence that a powerful corporate brand can command a premium with consumers, and can help to raise stock price with investors as well. Examples of strong corporate brands might include McDonalds and BMW.

- Brand equity. Brand equity is a narrower indicator than both reputation and corporate brand. It is defined as the premium that a consumer will pay to purchase a branded product as compared to a non-branded product with similar characteristics. So, for example, Coca-Cola is considered to have a high brand equity because consumers will pay more to purchase Coca-Cola than they will to purchase a store brand cola with similar characteristics.

What Measurements Are Used?

Measuring a firm's reputation is an area of active creativity and vigorous competition. A recent article in PR Week highlights five competing systems of measurement. One of the primary areas of difference lies in which stakeholder groups are included in the measurement. Some of the measurement systems, such as the Fortune Most Admired list, focus only on stakeholders in the business and investment worlds. Other systems, such as Walker Information's Corporate Reputation Report, includes groups such as customers, employees, and the community. The chart on the next page (Bovet, 1999) provides a quick overview of the five major systems.

Key Outcome Measurements

Corporate reputation research shows that corporate reputation typically is driven by the price, features, and quality of the goods and services that the corporation produces. But more and more, it is also driven by the corporation's commitment to CE. For example, a press analysis determined that 25% of all IBM news coverage in the US was related to its citizenship activities in the community, in education and in the public interest. Many of the articles and electronic media covered IBM's technology leadership as well as its citizenship activities, thereby supporting reputation in both the product and citizenship domains. (Litow, 2000)

For all of the apparent importance of reputation, and the obvious interest that it has garnered from PR firms and academicians, it is striking that there are relatively few publicly available studies that explore the quantitative connection between CE and reputation. We note in this section a number of the most important of these studies.

Environics Millennium Poll

The Environics Millennium Poll is one of the key quantitative measurements of consumer expectations of corporate social performance. With the collaboration of the Prince of Wales Business Leaders Forum, and The Conference Board, Environics coordinated a survey on the consumer

Measurement Systems Overview

Research System & Partners	Parameters	Pros	Cons
Fortune Most Admired Mike Barrett, Fortune Magazine Clark Martire & Bartolomeo	Eight characteristics used to compile indexes for 55 industries that can be used to make comparisons both within and between industry groups. Reputation criteria include: innovativeness, quality of management, employee talent, quality of products/services, long-term investment value, financial soundness, social responsibility, use of corporate assets	17 years in business; widely accepted standard; ranks 55 industries in eight categories to come up with numerical index. Database includes 10,000 corporate executives and securities analysts. Independent of PR	Too focused on financial aspects; doesn't take account of all stakeholders, such as employees, customers, media
Corporate Equity Performance System John Gilfeather, Yankelovich Partners Harlan Teller & Jim Sloan, Hill & Knowlton	Measures key constituencies on five major criteria and calculates a numerical index. Criteria include: awareness, familiarity, overall impression, perceptions, and likelihood to engage in supportive behavior, such as product/stock purchases, support in controversy, joint ventures	Proven effect on price/earnings ratios. Covers the waterfront of constituencies	May be a little hard to explain to management. Proprietary
GCI Corporate Brand Study Brandon Borrman, GCI Group Robert Berrier, Berrier Associates	Sensitivity analysis combines front-end interviews with companies and stakeholders and back-end interaction of weighted variables	Takes account of internal and external opinions about a company, avoids survey bias. Uses weighted variables that take account of differences in companies and their specific products and goals; open-ended, no given set of attributes is measured	New analysis model just introduced; only pilot-tested. Proprietary
CoreBrand Analysis™ Jim Gregory, Corporate Branding	Calculates Corporate Branding Index and Brand Power score based on collection of advertising, financial and reputation analysis	Proof that strong corporate brand impacts stock price. Uses database of nearly 800 Fortune 1,000 companies in 33 industries dating back to 1990	Comes at research from advertising research rather than PR perspective. Proprietary
Reputation Quotient Charles Fombrun, NYU Joy Sever, Harris Interactive Gary Thompson, Shandwick International	Produces a Reputation Quotient based on a 30-item instrument that measures general appeal, strategic positioning, economic and social performance on ten variables. Attributes include workplace, appeal, capability, value creative, credibility, distinctiveness, leadership, impact, citizenship and performance	Looks at variety of criteria; can do quickly; has academic standing. Non-proprietary	Would take certain proprietary measures away from other PR firms; the theory is that a uniform approach would lift all boats
Corporate Reputation Report Kimberly Graham Lee Walker Information	Engineered leveraging technology to get reputation measurement in eight weeks. Produces a snapshot and index of reputation plus a diagnostic tool broken down by stakeholder groups. Measures product/service quality, management quality, financial performance, work environment, corporate citizenship	Addressing a need in small and medium-size markets, relatively low cost	Still new and evolving tool, relatively untested, being introduced at academic conferences. Proprietary

expectations of corporate social responsibility, reaching at least 1,000 citizens in each of 23 countries on six continents - a total of 25,000 interviews in May 1999. The survey found that, across the globe, roughly 2 in 3 consumers want companies to go beyond their historic role of making a profit and obeying laws: they want companies to contribute to broader societal goals as well. Fully half the population in countries surveyed are paying attention to the social behaviour of companies. Over one in five consumers report either rewarding or punishing companies in the past year, based on their perceived social performance, and almost as many again have considered doing so. (Environics, 1999)

Conference Board 1999 Study of Consumer Expectations

As part of the Environics Millennium Poll, The Conference Board surveyed 1000 Americans in 1999, and found that almost 89% agree large companies should do more than focus only on achieving profitability within the law. 42% said that they held companies completely or partially responsible for helping to solve social problems like crime, poverty, and lack of education. Fully one third said that companies should focus on setting higher ethical standards, going beyond what is required by law, and actively helping build a better society for all.

The Conference Board found that consumers are willing to back up their expectations with action as well. 46% of respondents said that they had carried out a purchase decision in favor of a company, or decided to speak out in favor of a company because of a positive perception of its social responsibility. 49% of respondents said that they had decided not to purchase a product or service from a company, or had spoken critically of a company, because it did not meet their standard for being a socially responsible company. (The Conference Board, 1999)

Council on Foundations Report on Corporate Citizenship

One of the studies showing the clearest link between CE, consumer behaviour and reputation is the model developed by Walker Information as part of the Council on Foundations report on Corporate Citizenship. This model uses survey research data to develop correlation coefficients showing the linkages between reputation, brand loyalty, economic value and societal value. Walker's definition of "societal value" is essentially equivalent with the definition of CE, and includes the following items:

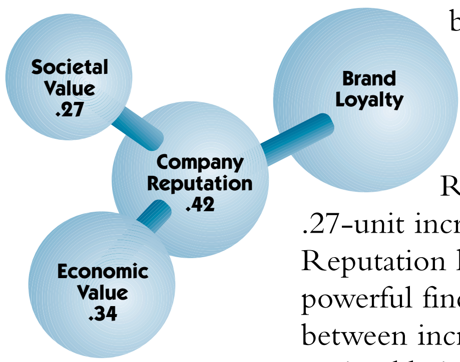
- Good corporate citizen
- Good employee treatment
- Cares about environment
- Strong ethics and good business practices
- Financial stability

Walker's definition of "economic value" also is quite familiar, and includes:

• Price
• Quality
• Service

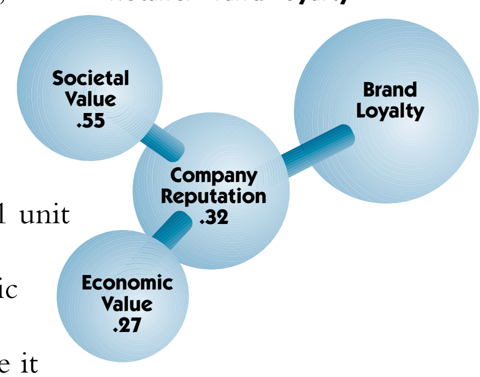
Walker Information published results for two companies, a manufacturer and a retailer. The results for the manufacturer showed that a 1-unit increase in Societal Value led to a .27-unit increase in Company Reputation, while a 1-unit increase in Economic Value led to a .34-unit increase in Company Reputation. A 1-unit increase in Company Reputation led to a .42 unit increase in Brand Loyalty. This is a powerful finding, and shows that there is a direct and strong connection between increases in societal value (driven by CE), and noticeable increases in Company Reputation and Brand Loyalty.

Manufacturer Brand Loyalty



The results for the retailer showed that a 1-unit increase in Societal Value led to a .55-unit increase in Company Reputation, while a 1-unit increase in Economic Value led to a .27-unit increase in Company Reputation. A 1-unit increase in Company Reputation led to a .32 unit increase in Brand Loyalty. Again, this is a powerful finding, and shows that there is a direct and strong connection between increases in societal value (driven by CE), and noticeable increases in Company Reputation and Brand Loyalty. It is also interesting to note that for the retailer, Societal Value is a stronger driver of Company Reputation than is Economic Value – while the reverse is true of the manufacturer. If it costs just as much to increase Economic Value by 1 unit as it does to increase Societal Value by 1 unit, the manufacturer's best strategy is to increase Economic Value, and the retailer's best strategy is to increase Societal Value. This is an important finding, because it suggests that the extent to which companies will benefit by investments in CE varies significantly from company to company and industry to industry. This also supports the notion advanced above that increases in CE are most helpful when they are tied in closely to a company's strategy and its key success factors. (Council on Foundations, 1996)

Retailer Brand Loyalty



What's Missing?

There are clearly a number of process measurements that show that CE can help to create changes in corporate reputation, and with that, consumer behaviour. There is also some limited publicly available data that allows us to form efficiency measurements. In particular, the Walker Information survey data provides us with one example of an efficiency measurement, and a methodology for gaining more. There are, however, no publicly available ROI measurements – no measurements that look at the costs versus the benefits.

Potential Approaches for Improving Measurements

The key goal to pursue now is the development of a standard definition of reputation, and a universally accepted method for measuring it. Until there is a widely accepted approach, it will not be possible to gather enough information that is comparable across enough companies to permit researchers and CEOs alike to draw definitive conclusions about when and how investments in CE can yield positive returns to the corporation.

This is an opportune moment to pursue this goal. There is considerable interest among business managers in the development of a universal method for measuring reputation, as reported in the May 31, 2000 issue of *PR Week*. The most intense pressures for developing a universal method are coming from the accounting community and from the Public Relations (PR) community. The accounting community is very interested in developing objective methodologies for valuing intangibles, because so much of the value of the most rapidly growing companies is in their intangible assets - knowledge, leadership, employee skills, and reputation. As long as these assets are not able to be valued and placed on the balance sheet, the financial statements of the companies that are driving change in the economy come to be less and less relevant in predicting the future financial health or value of those companies. As a result, there is considerable pressure building within the Financial Accounting Standards Board (FASB) to develop consistent and universally accepted methods for valuing intangibles, and to require that companies place the value of the intangibles on their balance sheets.

The PR field is also very interested in developing universally acceptable methods for valuing reputation. The Council of PR Firms, an important industry association, is spearheading the movement for a universal standard. The Council of PR Firms believes that industry members would benefit significantly from the adoption of a standard measure. If corporations were to adopt a standard measure and to start measuring their reputations over time, PR firms would benefit from the implementation projects that will spring up when corporations seek to improve or maintain their reputations. Secondly, the creation of a universal standard would enable PR companies to gather data showing the ROI of particular types of PR interventions. This would, of course, be of enormous use to both PR firms and their clients.

Given this strong interest from multiple sources within the business community, now is an advantageous time for advocates of increased CE to forge partnerships to define and measure reputation in ways that take into account community concerns. As was noted above, some of the measurement systems (for example, the Fortune America's Most Admired Companies list) do not include the community as an important stakeholder, while others do. If advocates can work together with business groups to ensure that the concerns and perceptions of communities are factored into the measurement of reputation, then it will be much easier to get top management to take community concerns seriously in the future. This will be particularly true if reputation gets measured and placed on every company's balance sheet, as some accountants are suggesting should occur.

Risk Management

What Are the Potential Benefits?

Advocates claim that increased CE can help companies manage and reduce their risks. They note that the management of risk has become more difficult due to the globalization of risk, heightened surveillance by NGOs and civil society, and increased demands for transparency. Advocates advance two primary arguments for how increased CE can help a company manage its risks. The first claim is that engaging in CE can help avoid harms associated with socially irresponsible or illegal behaviour perpetrated by employees, and to mitigate the harms to the corporation created by accidents or mistakes. Building a socially responsible culture helps to ensure that employees take their responsibilities to community and environment seriously, and helps to create a reservoir of goodwill between company, customers and community, which can be drawn down upon in moments of crisis and adversity. An increased commitment to CE can help to ensure that when a company's actions are monitored closely, that the picture that emerges is flattering rather than detrimental.

The second, more complex claim, is that engaging in increased CE will help companies to better understand and manage risks that come from new and unfamiliar sources. When a company makes itself more transparent, and enters into honest and open dialogues with advocacy groups across the globe, it develops a new network of contacts and knowledge that helps it to identify quickly new and potentially damaging risks. The network of contacts can help it to develop effective responses and better manage these risks. Interacting with the network can also allow the company to become proactive in its management of risks, and to change the risks it faces by changing the views of key advocates, legislators, and peers.

Which Managers Are Interested?

The management of risks to operations, quality, customer relations, financial stability and reputation ultimately rests with the top management team. Depending on the industry and the type of risk exposure, there may be managers with a particular focus on specific risks as well. For example, most financial corporations have one or more managers responsible for managing currency risk; manufacturing corporations have one or more managers responsible for managing environmental risks; multinational corporations have one or more managers responsible for managing political risks, and so on.

What Indicators Are Used?

There are many complex and specialized indicators used in risk management, which vary depending on industry and location. It may be helpful to think of indicators grouped into categories, as follows:

- Operational and systems risks – Are the corporation's core operations reliable and resilient?
- Financial risks – Can the corporation's profitability be disrupted by shifts in exchange rates, interest rates, and currency movements?
- Information and technology risks – What are the risks inherent in the corporation's use of data and technology?
- Compliance risks – Are all of the corporation's operations in compliance with applicable laws and regulations?
- Environmental risks – To what extent can the corporation's activities create environmental hazards? How are these hazards being controlled?
- Reputation risks – What are the potential sources of damage to the corporation's reputation? How are these being managed?
- Political risks – To what extent does political instability, including terrorism, pose a threat to the company's operations and personnel?

Clearly, it is not easy to develop quantitative measures for all these indicators. Companies can and do, however, track these indicators to help manage the risks involved.

Key Outcome Measurements

The first argument noted above is that increased CE will help reduce the incidence of illegal or socially irresponsible behaviours by managers or employees, and mitigate the harm to the company caused by such activities, and by accidents and mistakes as well. There is some publicly available evidence that increased CE reduces the incidence of illegal or socially irresponsible behaviour. The evidence is primarily in the form of case examples in which businesses are actively engaged in addressing these issues. For example, it is clear that the garment industry is very serious about ensuring that workplace conditions in the supply chain meet a minimum international standard. Failing to meet a minimum international standard, particularly for environmental conditions in the workplace, may not be illegal, but can often be considered by consumers to be quite socially irresponsible. Because consumer backlash against perceived social irresponsibility has been so dramatic, the use of third-party auditors to examine and verify that suppliers are meeting workplace standards has dramatically increased in the past several years. The development of workplace standards, and their enforcement through independent monitors, should reduce the incidence of illegal and socially irresponsible behaviours by managers in the supply chain.

There is also considerable evidence that a failure to develop internal systems to monitoring and correcting ethical and legal abuses can cost companies large sums of money. One example of the potential stakes involved in developing strong internal systems can be seen in the US "corporate sentencing guidelines", which went into effect in 1991, and which apply to businesses, partnerships, unions, and other entities. These sentencing guidelines impose stiff fines on corporations for a wide variety of wrong-doings. For example, in 1996, Daiwa Bank was fined $340 million for offenses arising out of its delay in reporting an enormous trading loss - the largest criminal fine in U.S. history. Archer Daniels Midland was fined $100 million in 1996 for an antitrust violation. These fines show the magnitude of the costs of failing to comply with regulations and laws. (Kaplan, 1998)

The link to corporate social performance can be seen in the fact that the guidelines offer significant incentives for corporations to adopt ethics and compliance programs, which is a key element of corporate social performance. The guidelines mandate that the fine for wrong-doing be greatly reduced if the company could demonstrate that it had implemented an effective compliance program prior to the point in time at which the wrong-doing occurred. Government prosecutors have also expressed a willingness to decline to prosecute a company for an employee's offense if it can show that it had an effective compliance program in place before the offense. Being able to avoid prosecution is an even greater incentive than being able to have the fine reduced or eliminated. (Kaplan, 1998)

Similar approaches are taken by many regulatory agencies. For example, the US Environmental Protection Agency announced a policy in December 1995 that provides for eliminating or substantially reducing the "gravity component" of a civil fine, and agreeing not to recommend the case for criminal prosecution, when certain compliance and disclosure conditions are met.

In addition to potentially large regulatory fines, there is also noteworthy evidence that suggests that behaving in ways that are egregiously socially irresponsible and illegal is detrimental to shareholder value. In 1997, Jeff Frooman of the University of Pittsburgh analyzed 27 event studies that measured the stock market's reaction to incidences of socially irresponsible and illegal behaviour. These event studies used product recalls, environmental lawsuits, anti-trust lawsuits, and regulatory fines as indicators of socially irresponsible or illegal behaviour. The analysis showed that companies that engaged in irresponsible or illegal behaviours in ways that were egregious enough to invoke regulatory and legal sanctions suffered very significant losses in shareholder wealth that were never recovered. (Frooman, 1997)

There is also case evidence that suggests that a long-term commitment to CE can help to build trust and faith in the company's good intentions. This can be critically important in moments of crisis. Consumers are more willing to give a company the benefit of the doubt when the company has a long history of exemplary behaviour. For example, many experts believe that the long history of commitment to consumer safety was part of the reason that Johnson and Johnson was able to weather the Tylenol crisis.

The second major argument noted above is that increasing CE, and in particular, becoming more transparent and entering into dialogue with advocacy groups, will help a company to identify and manage risks coming from new and unfamiliar sources. Currently, this argument is supported mainly by case evidence, especially case evidence of how a failure to become more transparent and enter into a dialogue with advocacy groups has caused corporations to fail to identify and manage risks from unfamiliar sources. Good examples of this type of failure includes Shell's difficulties with Brent Spar and Nigeria, Nike's difficulties with workplace conditions in its supplier chain, and Monsanto's difficulties with its sales of genetically modified seeds. Shell's management, in retrospect, is very clear that their unwillingness to be transparent and enter into a dialogue with advocacy groups reduced their ability to identify and manage risks, causing great problems for the company. They have since committed themselves to a much more transparent and inclusive approach.

Shell's positive experience with its more transparent and inclusive approach provides support for the argument that this approach enables companies to better identify and manage risk. They have been able to work with stakeholder groups to get a better understanding of the different points of view that stakeholders bring, and how the company's intended actions are likely to appear (either positively or negatively) from the point of view of its key stakeholders. They also have found that by being in dialogue, they can influence the views of some of the key stakeholders, and come to help them understand some of the dilemmas that Shell is facing. (Raynard, forthcoming)

What's Missing?

At this point in time, the most pressing need is for the development of process measurements, showing how and whether increased CE can help improve a corporation's risk management. The case studies suggest that this is so, but there is no publicly available quantitative data proving the mechanism and the scale of the improvements. This is particularly true for the second argument advanced by advocates - that increased transparency and dialogue enables companies to better identify and manage risks from new sources. A definitive study showing whether and how this occurs would give a major boost to CE in this area.

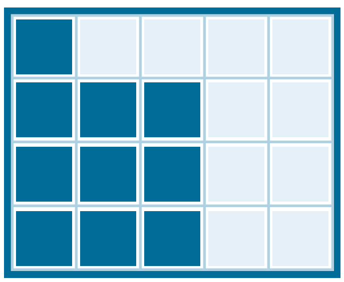
Potential Approaches for Improving Measurements

There are a number of accounting firms, including

PriceWaterhouseCoopers and Arthur Andersen, that have very active risk management practices. These firms are natural allies to collaborate with advocates to determine how increased CE affects a corporation's ability to analyze and manage risk. One way to get started would be to create a consortium of accounting firms, consulting firms, advocates, and researchers to develop a database of case examples of how CE has affected risk management. This database would then enable researchers to conduct an inductive analysis across the case examples to develop themes, identify issues, and extract hypotheses about the mechanisms through which increased CE can improve a company's ability to identify and manage risk. A second step would then be to develop a few focused pilot programs to assess more concretely a number of different mechanisms, and their relative ability to help companies improve their risk management.

Scorecard: Risk Management

SCORE 1 2 3 4 5 NOTES



	NOTES
INFO TYPE	Data are largely qualitative and/or anecdotal, although there are a few high-profile examples of the financial costs of 'getting it wrong.' Link to legal dimension is important, particularly in the USA.
RELEVANCE	Risk management is seen as highly relevant, but evidence only covers high profile cases for visible companies. Data not so relevant for companies engaging in low profile community actions.
SOURCE	Advocacy sources are only partly convincing, and arguably less so over time. Company sources of significance of risk dimension are very convincing, as are major consultancies specialising in area.
ATTITUDES	Increasing acceptance of risk element marks an overcoming of resistance often based on degree of corporate arrogance.

Government Regulations/Regulatory Oversight

What Are the Potential Benefits?

Advocates claim that CE can help companies smooth the way for regulatory approvals, and reduce the number and costs of regulatory challenges. In their view, increasing CE can be an important business tool for any industry in which close regulatory oversight is of strategic importance. This can include industries such as banking, insurance, utilities, natural resources and health care.

Advocates believe that the benefits that CE can bring are particularly evident in situations in which the company needs to secure and maintain the license to operate. The more sensitive the resource, the more difficult it is to get the license to operate, and the more imperative it is for a company to demonstrate that it will be both a good steward for the resource and a good corporate citizen. Resources here include not only natural resources, such as water, oil, timber, and mineral ores, but also public resources, such as a portion of the radio spectrum, the right to distribute power and telephone services, and even the right to run a national lottery. In the case of particularly sensitive resources, governments may not only determine which company receives the license, but also may enter into a partnership with the company directly to control the resource.

Which Managers Are Interested?

In industries in which winning regulatory approvals and avoiding regulatory challenges is an important strategic issue, the CEO and top management team are closely interested in government relations. In these industries, managers responsible for sales also can be interested in these issues. This is particularly true if the company's CE activities are seen as being helpful in persuading regulators to allow the company to bid on, or in improving the chances of winning, the license to operate. Finally, the managers of business units that are the targets of close regulatory oversight are also interested in these issues. Maintaining good relationships with regulatory agencies and important agencies is a key part of their management task.

In industries in which there is less of a profound governmental presence, these issues usually will be handled by the manager who has responsibility for external affairs. This could include the head of government affairs, public relations, or legal affairs.

What Indicators Are Used?

The indicators used to evaluate the corporation's performance in managing its regulatory affairs are primarily qualitative. Was the company able to win the regulatory approvals needed to execute its strategic plan? Did the company win and maintain the license to operate in key markets? Has the company been able to avoid the sorts of regulatory challenges that its rivals are confronting?

For example, Motorola evaluates its CE activities by looking at whether its host countries are willing and able to separate out Motorola from other American companies and interests when host countries and the US have political difficulties. Is Motorola tarred with the same brush as all other US companies, or have its CE activities helped to persuade the host country that it is a valued and valuable corporate citizen, no matter what problems the US and the host country are currently having? (Wiggenhorn, 1999)

Key Outcome Measurements

There are many interesting case examples and quotes from key managers on how CE helps to help achieve regulatory approvals and reduce regulatory challenges. For example, the staff at the former NationsBank indicated that its investment in communities helped NationsBank in its acquisition of Barnett Bank in 1997. Cathy Bessant, the former President, Community Investment, for NationsBank noted, "Both NationsBank and Barnett Bank have made significant investments in meeting community needs over the past decade. In addition to being good business with high community value, these investments played an important role in providing a positive regulatory review of the merger, allowing it to be completed in a timely way and with minimum cost. The senior management of the bank is convinced that the investment in meeting community needs has been invaluable in allowing it to attain its strategic goals for growth and market development." (Weiser, 1997)

We were not, however, able to find quantitative measurements of how increasing CE activities affected regulatory approvals or regulatory challenges. We believe that quantifying CE's effect on regulatory approvals and regulatory challenges is difficult, if not impossible to achieve for the following reasons:

1) The regulatory oversight process is complex, with many actors and influences. It will be quite difficult to draw a direct causal link between specific CE activities and specific regulatory decisions. CE activities are just one part of all of the activities of the company considered in the regulatory process. Accordingly, even under the best of circumstances, it is hard to imagine how one could create a measurement process in which it would be possible to separate out and measure the effect that just the CE activities had on the regulatory process.
2) It is difficult to get quantifiable data from regulators about how much a particular CE activity influenced their decision to award regulatory approval, or to reduce or quash a regulatory challenge. Regulators operate in the public eye, and so must be extremely careful about describing the details of their decision-making process. They have very little to gain, and much to lose, from participating in public research that exposes the inner-most workings of their decision process.
3) It is difficult to get top management to provide honest public disclosure of their government relations goals. A public disclosure of the government relations goals might reduce or eliminate the benefit that could be obtained from the CE activity. For example, consider the case in which a business' key public affairs goal is to persuade legislators that it does not need to be regulated. Its strategy would be to paint such a strong picture of civic virtue and compassion for the consumer that there would be no public support for regulation. Clearly, increasing CE can help a company to portray itself as having high levels of civic virtue and compassion for consumers. However, if a company were to admit publicly that the only reason it was increasing its CE was solely to avoid regulation, and that it would abandon its CE activities if the threat of regulation went away, it would suddenly shift from looking good to looking very bad. It would shift from being a paragon of civic virtue to being a cynical manipulator of public opinion.

Please note, though, that the fact that quantitative measurements are difficult or impossible to obtain does not mean that it is not possible to be persuasive about the benefit of CE. In this domain, presenting case studies showing how CE can improve the regulators' perception of the company is often sufficient to persuade even the most skeptical of managers. The following two case studies offer good examples.

Suez Lyonnaise des Eaux

Franco-Belgian company Suez Lyonnaise des Eaux is one of the world's largest water management companies. It is planning to continue growing its international water business rapidly - its current strategic plan calls for a 60% increase over five years. (Suez Lyonnaise des Eaux, 2000) But in order to grow at this pace, the company must persuade governments across the world, especially in developing countries, that privatizing their water concessions, and allowing the company to manage them, will reduce costs and increase quality without creating social unrest.

Access to water is a politically volatile issue, particularly if the management company charges for use of water. This can create significant problems in relations with very low income communities, especially those with no history of being charged for water, or with a history of being charged but not paying. The extreme difficulties that UK's International Water Ltd. faced in Cochabamba, Bolivia's third-largest city, gives a notable example. In April, 2000, protests over a 20% increase in water bills brought about by privatization in Cochabamba left six dead, and led to a state of emergency. The Bolivian government eventually backed away from the price increases, which in turn led International Water Ltd. to cancel its Cochabamba water-supply contract. (Arai, 2000)

One long-standing method of addressing the fact that cities have both affluent and poor water users has been to cross-subsidize water use, with the rich shouldering more of the burden than the poor. Suez Lyonnaise des Eaux is experimenting with additional methods of working with NGOs, governments, and local community members to reduce the costs of installing water and sewage-treatment systems as well. For example, in Bolivia, Argentina and the Philippines, the company has given local partners and community members tools to help dig and install the pipe network. They have also redesigned the piping layout, reducing the number of pipes required to serve a neighborhood. In El Alto, Bolivia, these alternative solutions have helped reduce the installation cost of water-supply systems to $41-47 per household from $133-$159. The cost of installing sewers was cut from $58-68 from $194-$290. Still, some cross-subsidy is still needed, given that the average monthly family income in El Alto is around $70. (Arai, 2000)

In a second example, the company has developed a partnership with the University of Sao Paulo and the local government to collect and treat waste water from a low-income community bordering a lagoon in Sao Paulo, which is a major source of drinking water for the city. The partnership approach is intended to help the company both provide a low-cost solution to managing water quality, and also to demonstrate its attractiveness as a partner to local governments. This will help position the company well for future competition for water-concession management. Several of the big state-owned water utilities in Brazil are expected to go up for auction this year, with more to come in the following years. (Arai, 2000)

Suez Lyonnaise des Eaux has also experimented with helping governments to solve other types of social problems as well. In France, Suez Lyonnaise des Eaux built a national network of relationships with local public authorities to help young people suffering long term unemployment get back into work. The company has developed a 'dual mentoring' approach that integrates the complementary competencies of public sector bodies to build people's social skills and the company's ability to build their professional skills. This approach has proven effective, and again has helped to demonstrate the attractiveness of Suez Lyonnaise des Eaux as a partner to local government authorities. (Zadek and Nelson, 2000)

Placer Dome

Placer Dome is a major mining company headquartered in Canada. Placer Dome's principal product and source of earnings is gold, although significant quantities of silver and copper also are produced. Its community engagement activities at the startup of the Las Cristinas mine in Venezuela is a good example of how and why community engagement can help ensure continued regulatory support in a complex environment. (The following description is adapted from Davidson, Mendez, and Bovarnick, 2000)

In 1991, Placer Dome de Venezuela (a subsidiary of Placer Dome) entered into a joint venture agreement with the Corporacion Venezolana de Guayana (CVG), a public organization with responsibility for regional mining development. The joint venture's goal was to secure the systematic exploration and, if feasible, the large-scale commercial development of the Las Cristinas gold deposits.

There are many layers of regulatory oversight at Las Cristinas. In addition to CVG's role, other governmental agencies having jurisdiction over the Las Cristinas site include three national government agencies, the national Supreme Court, a state government agency, the governor and the local Mayor. In the absence of a strong government presence in the zone, the local community members themselves are extremely active in seeking assistance from whomever they can elicit it, to increase social services and promote economic development.

The political and social situation around the potential mine is turbulent. The joint venture's own assessment of the situation is that "The situation is politically charged and potentially explosive, where most stakeholders, including the government agencies, are functionally weak." (quoted from Davidson, Mendez, and Bovarnik, 2000).

The potential explosive nature can be seen in the following example. When mining activities were suspended due to a drop in gold prices in 1999, a delegation of miners and community leaders showed up at the joint venture's camp gate, demanding that the joint venture open up the property to small scale miners who had been displaced when the joint venture started exploration. They threatened disruptive actions, negative press coverage, and application of community pressure in order to force the company to respond to community livelihood needs in the aftermath of the suspension of activities. The joint venture was able to expand its involvement in small-scale mining to include an additional four newly formed miners' associations, working within the concession, under the terms of a negotiated agreement, with company supervision in technical and environmental areas.

In order to address the expressed needs of the community, Placer Dome, acting through the joint venture, has focused on two partnership building exercises involving business, the community, NGOs, and governmental agencies. The first partnership is aimed at establishing a community based health care system for the Las Cristinas area. The second partnership is aimed at increasing the capacity of small scale miners to earn a living without degrading the environment, and without needing continuing access to the joint venture's land and financial support. These partnerships are both moving forward positively. (David, Mendez, and Bovarnick, 2000)

The Suez Lyonnaise des Eaux and the Placer Dome examples shows why corporate engagement with the local community and the national government to improve local social services and economic activities makes sense both for the business and for the community. The local business unit mitigates the risk of civil actions, shutdowns, and negative publicity. The local community wins the resources it needs to improve its citizens' quality of life. The parent company improves its reputation as an "operator of choice", which it can then use to help win the rights to operate in other settings.

What's Missing?

As noted above, we were not able to find any quantitative measurements of the impact of CE on government relations. We believe that these measurements are at best difficult, if not impossible to attain. Accordingly, even though quantitative measurements are missing, we believe that they are not worth pursuing. Rather, it would be valuable to pursue work leading to a deeper understanding of how and when CE helps improve government relations in ways that create business value for corporations.

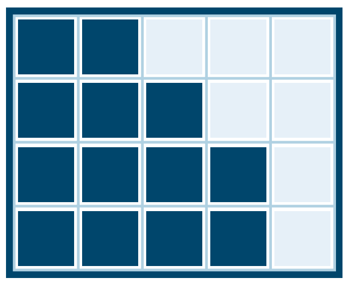
Potential Approaches for Improving Measurements

An exciting next step in developing a deeper understanding of how and when CE improves government relations would be to develop assemble case studies and best practices, organized by industry, and to conduct site visits and cross-cutting analyses to develop an understanding of over-arching themes. The World Bank's Business Partners for Development program provides a good example of how this can be done. The Business Partners for Development program has developed working groups focused around particular industries and issues, together with a cross-cutting group charged with distilling and communicating lessons learned across the working groups. This approach appears to be both successful and well worth replicating.

A second approach, also promising, would be to identify potential pitfalls in acquiring the license to operate, and to create an inventory of case studies that demonstrate how CE can help companies to avoid these pitfalls.

Scorecard: Government Relations/Regulatory Oversight

SCORE 1 2 3 4 5 NOTES



SCORE	NOTES
INFO TYPE	Almost exclusively qualitative and anecdotal.
RELEVANCE	Relevant to companies in highly regulated industries, engaged in major government contracts, expanding into international markets, and/or involved in major transactions such as mergers and acquisitions.
SOURCE	Emerging from the corporate community, so considered good quality.
ATTITUDES	Aspect would meet no attitudinal resistance.

B. Measurements of Effect on Business Functions

Human Resources

What Are the Potential Benefits?

Advocates claim that CE can create benefits in the human resources and workforce development area in a wide variety of ways, including the following.

- Increased employee satisfaction, performance, and retention: CE can improve employees' loyalty and job satisfaction, leading to better job performance and higher retention.
- Increased skills: CE can provide cost-effective ways to improve employees' skills and performance.
- Improved hiring and recruitment: CE can enable a company to tap and develop new pools of employees that can meet the company's immediate hiring needs. CE can also improve the company's image, enabling it to compete more successfully for new employees.
- Building the long-term pipeline of talent: CE can help companies ensure that they have a pipeline of talented workers ready to fill positions into the future.

Which Managers Are Interested?

The managers most interested in Human Resources and Workforce Development are those who are part of the HR function, as well as managers who have significant line responsibilities that include hiring and developing workers for their unit. At the senior management level, this could include the head of Human Resources, the head of Operations, and the managers of divisions or other large business units. Clearly, any manager with significant responsibilities for recruitment and training would have a significant interest. Particularly where training and development of talent are concerned, managers who have line responsibilities for production and operations often have an important role as well. For example, Motorola holds its plant managers responsible for hiring a workforce with the talents and skills needed to make the plants run well. Because of this, many Motorola plant managers have become deeply involved in CE activities such as school reform in the communities in which the plant is located, and from which the workforce is drawn. (Wiggenhorn, 1999)

What Indicators Are Used?

HR managers have developed a wide variety of indicators to track and manage the corporate workforce. Specific indicators include the following:

- Cost
  - Compensation costs, including benefits
  - Recruitment costs
  - Training and orientation cost per hire

- Outplacement/layoff costs
- Quality
  - Employee productivity
  - Absenteeism & lateness
  - Turnover rate
  - Promotion rate
  - Recruitment yield
  - New hires that meet or exceed hiring expectations
- Demand and Supply
  - Current and future positions that need to be filled
  - Cuts and reductions that need to be made
  - Pipeline for potential personnel
- Time
  - Recruitment cycle time
  - Time required for new hires to achieve full productivity
  - Time required to lay off/outplace
  - Time required to build pipeline

Key Outcome Measurements

In this section, we discuss the key outcome measurements separately for the different benefits claimed by advocates:

1. Increased employee satisfaction, job performance and retention
2. Increased employee skills
3. Improved hiring and recruitment
4. Building the long-term pipeline of talent

We first look in detail at each specific type of benefit, noting the arguments that are brought forward as to why CE has a positive effect, and then noting the supporting evidence and case studies.

1. Increased Employee Satisfaction, Job Performance and Retention

Proponents of CE advance the following arguments as to why and how increased CE increases employee satisfaction and job performance, and how this then leads to increased profitability for the firm:

a. Increased CE (of every variety) helps to improve the image of the company, which helps employees to feel better about the company, and about their work. This increases employee satisfaction and loyalty, which thereby increases employee job performance and retention. This, in turn, increases customer satisfaction, sales, and profitability.
b. Providing employees with superior and flexible benefits, which is a form of CE, increases employee satisfaction and job performance, and makes it easier to hire and retain employees. This investment reduces costs and increases profitability in the long run.

We will discuss the outcome measurements for each of these in turn below.

a. Increased CE (of Every Variety) Improves Company Image, Employee Satisfaction, and Customer Satisfaction

It is useful to break this argument into its component parts, and look at the outcome measurements that can be found for each part. The two component parts are:

(i) Increased CE (of every variety) helps to improve the image of the company, thereby improving how employees feel about the company, and improving their loyalty and job satisfaction

(ii) Increased employee loyalty and job satisfaction leads to increased customer satisfaction and retention, which leads to higher profitability.

We examine the evidence for each of these component parts in turn:

(i) Increased CE (of every variety) helps to improve the image of the company, thereby improving how employees feel about the company, and improving their loyalty and job satisfaction

Walker Information/Council on Foundations

In a research study sponsored by the Council on Foundations, Walker Information interviewed a representative sample of employees from a cross section of US employers. It found that a company's CE activities have a positive affect on the average employees' satisfaction and loyalty. In particular:

- Employees who perceive their companies as having good corporate social performance view them more positively and are therefore more committed to them. Corporate social performance is a key determinant of overall reputation, which also influences overall feelings about a job and employee commitment and morale. CE activities (including cause-related marketing, volunteer programs, and product and service innovations) are the primary determinant of corporate social performance.
- In addition, a company's support of employee volunteerism directly influences employees' feelings about their jobs. For example, employees involved in employer-sponsored community events were 30% more likely to want to continue working for that company and help it be a success. (The Council on Foundations, 1996)

Fleishman Hillard

Using survey data, Fleishman Hillard found that 87% of European employees feel greater loyalty to socially-engaged employers. (Fleishman Hillard, 1999)

Drumwright Study on Marketing Campaigns

Many companies have found that employees work harder when they know their efforts are benefiting a cause about which they care. *The Journal of Marketing* reported on Drumwright's study of 22 marketing campaigns — half associated with a social cause — which found that even when the cause-related marketing campaigns did not achieve their traditional economic benefits, such as increasing sales, they were highly effective in achieving company-oriented objectives, such as motivating the workforce. (Drumwright, 1996)

Cone/Roper Cause-Related Branding

Cone/Roper's study of cause-related marketing included questions on the impact of CE on employee attitudes for the first time in 1999. They found that there are strong correlations between employee loyalty and pride in their company, and the company's commitment to CE. In particular:

- Nine in ten workers whose companies have a cause-related marketing program feel proud of their companies' values versus 56% of those whose employers do not.
- 87% of employees feel a strong sense of loyalty to their companies with cause-related marketing programs, versus 67% of those employed in companies without one. (Cone Inc., 1999)

These studies provide reasonable evidence for what most managers take to be self-evident: employees feel better about working for a company that they perceive to be doing good things for the community. It should be noted that these studies are only process-level measurements: they show that increasing CE improves employee satisfaction and loyalty. None of the studies, however, is an efficiency measure. The studies do not show that increasing CE is a more efficient way of increasing employee satisfaction and loyalty than other methods (for example, providing subsidized lunches or better working conditions). Nor are the studies ROI measurements - none of the studies shows the benefit gained in increased loyalty and satisfaction is greater than the money spent on improving CE.

We now turn to evidence for the second component in the link between increased CE, employee job satisfaction, and profitability.

(ii) Increased employee job satisfaction and loyalty leads to increased customer satisfaction and retention, which leads to higher profitability.

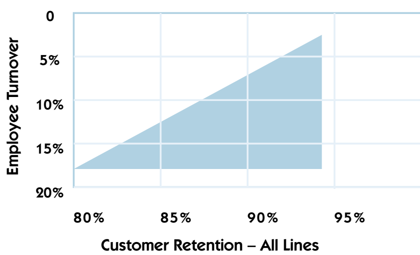
There is a wealth of evidence supporting this contention. Some of the most powerful findings are as follows:

Towers Perrin

Towers Perrin has analyzed the impact of employee turnover on financial performance, and has found powerful evidence that decreases in employee turnover can drive increases in financial performance in a variety of industries. The chart below shows correlations between employee turnover, customer retention, and financial performance in the property and casualty insurance industry.

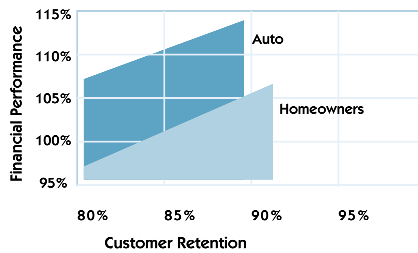
Links between Employee Turnover and Financial Performance
In Property-Casualty Insurance

Employee Turnover and Customer Retention



Towers Perrin, 2000

Customer Retention & Financial Performance



Towers Perrin, 2000

The Value Chain at Sears

A compelling piece of evidence showing that motivated employees help a company increase its profits comes from Sears. Sears has developed a rigorous quantitative model that analyzes and predicts the relationships between management quality, employee behaviour and financial performance at Sears. Its research reflects the following:

- Improving employee attitudes by 5 points drives a 1.3 point improvement in customer satisfaction, which in turn drives a 0.5% improvement in revenue.
- At Sears, 0.5% improvement in revenue means additional sales of $65 million per year. At its current after-tax margin and price-earnings ratio, those extra revenues increase its market capitalization by nearly $80 million.

This shows the potentially powerful bottom-line impact of improvements in employee attitude at Sears. These findings, combined with those noted above, present a compelling picture of how corporate social performance can create increases in employee satisfaction and loyalty, which can create increases in customer satisfaction, which can create increases in revenue, profits and market capitalization. While Sears is a singular example, we believe that the results should be equally true at other companies in which line employees are the key point of contact with customers. (Rucci, Kirn and Quinn, 1997)

We turn now to look at the data supporting the second major claim that advocates make linking increased CE with improved HR outcomes, and from there to improved profitability.

b. Providing employees with superior and flexible benefits, which is a form of CE, increases employee satisfaction and job performance, and makes it easier to hire and retain employees. This investment reduces costs and increases profitability in the long run.

In reviewing studies on CE, there is always a gray area between what is clearly CE, and what are "business basics". Much of the world of compensation, benefits, and employee relations falls into this gray zone. Is it truly CE to provide health and pension benefits to the top management team? No - it's a business basic. Is it truly CE to a provide health and pension benefits to low-wage employees when none of your competitors do? Some managers would argue yes, others would argue no. We will simply present the evidence without taking a stand on the issue of whether or not providing employees with superior and flexible benefits is a form of CE.

There is considerable evidence linking superior and flexible benefits with increased employee satisfaction, and with increased ability to hire and retain employees. While the studies do not demonstrate the exact causality, it seems likely that part of the reason that superior and flexible benefits have assumed greater importance has been the changes in social structure over the past several decades. For much of the US and UK workforce, it now takes two wage earners to approximate the quality of life that one wage earner could achieve a generation ago. Women have entered the workforce in significant numbers, and much of the workforce is working longer hours. This means that employees are less likely to have the time, or a spouse with the time, to address family and social concerns outside of their working hours. This makes flexible benefits, family supportive packages, and opportunities to address to social and community concerns through work of much greater interest than before.

An example of the links between superior and flexible benefits, and employee satisfaction and job performance, is the following:

Fortune 100 Best Companies to Work For in America

The companies included on the Fortune list of "100 Best Companies to Work for in America" generally are regarded as having some of the best benefits programs in the world. Linda Grant, writing in the January 1998 issue of Fortune, reported that the publicly traded companies on this list (61 of the 100 companies) posted 5 year average annual gains of 27.5% versus 17.3% for the Russell 3000, an index of large and small companies that mirrors Fortune's 100 Best. The ten year gains show the same result: the publicly traded companies posted average annual returns of 23.4% versus 14.8% for the Russell 3000. This shows a strong correlation between achieving superior corporate social performance in compensation, benefits, flexibility, and career paths, and achieving better financial performance. Of course, the fact that there is a correlation does not tell us whether superior benefits, compensation, etc. cause better financial performance, or vice versa. The link between the two, however, is indisputable. (Grant, 1998)

2. Increased Employee Skills

The second major area in which advocates claim that CE can help improve corporate performance is in helping to increase employees' skills. Advocates advance the following claims here:

a. CE, especially volunteerism and service learning, can be powerful tools for increasing employees' skills and creating management development opportunities.

b. Providing training to entry-level workers and low-wage incumbent workers, which is a form of CE, increases productivity, job satisfaction and retention enough to repay the cost of the investment in training.

As before, we will review the data for each of these claims in turn below.

a. CE offers tools for employee development and training.

There is a growing body of experience that suggests that volunteerism and service learning can be powerful tools for increasing employees' skills and creating management development opportunities.

Corporate Citizenship Company

A 1998 study by the Corporate Citizenship Company found:

- Staff who participated in volunteer programs measured their competency gains with "before and after" self-assessments. These staff assessed their performance as showing an overall improvement of 17 percent. The supervisors who assessed the same staff rated them as showing an overall improvement of 14 percent. Both findings compared favorably with the ratings of traditional training programs.
- The top three competencies showing the most development gain were communication skills, collaboration and team-working skills, and creative thinking skills. (Corporate Citizenship Company, 1998)

b. Providing training to entry-level workers and low-wage incumbent workers, which is a form of CE, increases productivity, job satisfaction and retention enough to repay the cost of the investment in training.

There has been considerable discussion and debate on this topic. In general, companies tend to spend far more money per person training highly skilled employees and managers than they do on providing training to entry-level workers. A number of advocates have raised arguments and conducted pilot studies to show the benefits to the firm of investing in training for entry-level workers. This is regarded as a form of CE because it increases the skills and earnings abilities of individuals who are often low-income and low-skilled.

Knowledge Supply Chain Design for Training

MIT has been working with a number of companies to develop new ways to train entry-level workers. They have been able to apply techniques derived from supply-chain process improvements to the knowledge supply chain. This has led to significant improvements in the total cost for recruiting, hiring, training, and retaining the entry-level workforces. For example, at EMC Corporation, applying these processes to the knowledge supply chain led to the following improvements:

- Reduced hiring cycle from 90 days to 40 days
- Doubled productive output of new hires
- Reduced mis-hires from 5% to less than 1%
- Eliminated 6 weeks of On-the-Job-Training (OJT)
- Net impact is $50K reduction in total of cost per trained entry-level

technician (versus costs of former recruitment, training, and retention policies and procedures) (Hanson, 2000)

3. Improved Hiring and Recruitment

The third major claim that advocates make is that increased CE will help companies to become better able to get the workforce that they need. There are two primary components to this claim:

a. Increased CE (of every variety) will improve corporate reputation, thereby making it easier to hire employees.

b. Hiring individuals who are unemployed, underemployed, or on welfare, which is a form of CE, is a good way for the company to get the workforce it needs, and will provide additional benefits by diversifying the company's reservoir of skills and experiences.

As above, we will review the evidence in turn for each of these claims.

a. Increased CE (of every variety) will improve corporate reputation, thereby making it easier to hire employees.

The claim here is that firms that have higher levels of CE will have better reputations, and that this will encourage potential employees to sign up with them, rather than their competitors. This claim doesn't seem too controversial. In fact, it is hard to imagine how having a better corporate reputation would make it harder to recruit employees. Nonetheless, we note some good examples of research and case studies supporting this point.

Turban and Greening

This study found that ratings of a firm's corporate social responsibility were related to ratings of the firm's reputation and attractiveness as an employer, suggesting that such performance may provide a competitive advantage by attracting potential applicants. In addition, attractiveness as an employer correlates significantly with ratings of a firm's community relations, employee relations, and product quality. (Turban and Greening, 1997)

Cone/Roper

This 1999 survey found that good corporate reputation is the second most important consideration for people when choosing an employer. (Cone Inc., 1999)

Important Characteristics in an Employer

Factor	Ranking
Career growth potential	1
Good corporate reputation	2
Starting salary	3
Fringe benefits	4
Record of high yield for shareholders	5
Good sports and social facilities	6

Our interviews suggest that results noted in this table may be more true for junior staff than for senior staff. For example, interviews with headhunters for top executive positions suggest that the most senior executives rarely if ever consider the CE reputation of a firm as a key element in their decision about whether or not to pursue a position with the firm. Reputation is considered, but mainly in terms of the reputation of the firm as a competitor among peers.

Our interviews also show some interesting qualitative dimensions to this finding. Senior managers at Shell reported that there was a tremendous loss of morale and a significant downturn in recruitment when Shell suffered its difficulties in Nigeria and with Brent Spar. However, once Shell had made its commitment to CE, through much greater transparency and engagement with external stakeholders, it found that it was suddenly swamped with potential employees interested in joining Shell. They believed that Shell's use of CE would help it to better predict future risks, and better succeed in a turbulent world.

b. Hiring individuals who are unemployed, underemployed, or on welfare, which is a form of CE, is a good way for the company to get the workforce it needs.

How do you persuade skeptical managers to expend more money and effort to hire and train entry-level workforces from social groups that have many individuals on welfare, or that have high levels of unemployment and underemployment? In the US currently, the answer is obvious - show the managers that it will help them fill job slots. Given the unprecedentedly low unemployment rates, companies are struggling to find employees, and being able to tap new pools of potential qualified employees is a clear benefit. The key issue has been to show that the new pools of employees can yield qualified candidates who can perform well in their new jobs. Experience with the Welfare-to-Work population, which has been carefully studied over the past several years, shows that this is indeed the case.

Welfare to Work Partnership: Employer Survey

The Welfare-to-Work Partnership conducted a survey of 600 employer-members to ask about their experience in hiring former welfare recipients. Findings include:

- 65% had hired former welfare recipients
- 62% found that former welfare recipients had better retention rates than other employees
- 77% of companies hiring former welfare recipients hire them for promotion-track jobs, and 91% offer former welfare recipients opportunities for training
- 90% of the former welfare recipients receive pay raises as fast as their non-welfare colleagues. (Welfare to Work Partnership, 2000)

4. Building the Long-Term Pipeline of Talent

The key arguments here are not about whether CE can help to build the long-term pipeline of talent. It is generally accepted by most managers that corporate participation in apprenticeship programs, school reform, and school-to-work efforts can help to build the long-term pipeline of talent. The more important questions are whether it is worth the cost, and how to do it in a way that avoids the "free rider" problem (the employer bears the cost of training people in the pipeline, but a company that hasn't shared in that cost gets the benefit by hiring them).

In the US, one of the key areas of corporate focus in education has been the development of school-to-work systems, similar in some ways to the apprenticeship systems in Europe. Corporations have been working with school systems in joint experiments and pilot projects aimed at determining how best to develop a system that works for youth as well as for business.

National Employer Leadership Council

The most careful and complete study of the costs and benefits of school-to-work programs was undertaken by The National Employer Leadership Council (NELC). NELC studied 8 companies' school-to-work programs recently, and found solid evidence of a positive ROI for the school-to-work programs in most of the companies studied. As NELC notes in its report, "No employer who participates in school-to-work programs does so for immediate business gain. What matters most to business is improving student achievement. Recent studies indicate that school-to-work programs do produce measurable improvements in academic performance - and other benefits for students as well... [This] study shows that employers, too, reap measurable business benefits from school-to-work, quantified in terms of:

- reduced recruitment costs;
- reduced training and supervision costs;
- reduced turnover;
- increased retention rates;
- higher productivity of students; and
- higher productivity and promotion rates of school-to-work program graduates who eventually are hired compared with those of other newly hired workers."

NELC worked with a voluntary group of companies to develop a way to define the aspects of return on investment and measure success. Each of the selected companies participated in school-to-work programs that focused on contextual learning designed to raise academic achievement. That learning came in the form of student internships; apprenticeships; or paid, part-time employment. Each company had:

- created and implemented a formal school-to-work program;
- collected data on costs and benefits; and
- gathered experiences and outcomes to share with the public.

The companies and NELC calculated the benefit cost ratios for each company's program. These ratios represent the dollar value of the program benefits divided by the dollar value of the program costs.* For example, a ratio of 1.15 means that for every dollar spent or contributed to a school-

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* This ratio takes into account that costs and benefits do not occur simultaneously; costs typically precede benefits. Therefore, an appropriate discount rate was applied to costs and benefits.

to-work program, a company earned its dollar back— plus an additional 15 cents in benefits ($1.15 divided by $1.00 = 1.15). Any ratio above 1, then, represents a positive return on investment. The ratios vary in most of these participating companies because multiple sites or departments participated.

The NELC report detailed the specific results as follows:

- Autodesk. Ranging from 1.15 to 2.99 across departments, with a median of 2.32.
- Charles Schwab. Ranging from 0.40 to 5.64, depending on whether the company's forecasts of long-term benefits from higher employee retention rates are realized.
- Crown Auto World. Ranging from 1.39 to 3.21, depending on employee retention rates and additional profits from technicians hired from the program.
- Eastman Kodak. Ranging from 0.87 to 1.05, depending on the productivity of student apprentices.
- McDonald's. Ranging from 0.97 in Lady Smith, Wis., to 0.88 to 1.02 in New Albany, Ind., depending on cost savings from higher retention rates among apprentices.
- Siemens. Ranging from 1.07 to 1.79 in Lake Mary, Fla., depending on training and supervision cost savings from apprentices later hired as full-time employees. Ranging from 0.54 to 0.59 in Wendell, N.C., depending on how many hours per year students work.
- Sutter Health. 1.39, if students perform work similar to that done by employees.
- BellSouth. BellSouth's job shadowing program did not lend itself to calculating precise benefit-cost ratios. The benefits of one-day job shadowing for students are substantial, but the financial returns to BellSouth for this short-term program are negligible. Programs with student involvement sustained over time are more apt to yield bottom-line returns than single-day programs.

The NELC report concluded, "The benefits of school-to-work programs exceed the costs in nearly three out of four companies studied. Moreover, these results include all costs incurred by employers - even if some of the costs were shouldered by private foundations or public agencies, which often is the case. Had the study taken into account outside funding assistance, some of the returns would have been even higher. Finally, these results reflect startup costs spread over a short period and a small number of students. As the programs continue and serve more students, the startup costs will be spread over more years and more students, which will lead to more favorable results." (National Employer Leadership Council, 1999)

What's Missing?

Our research has uncovered many process measurements, which prove that increased levels of CE can help improve key HR indicators such as employee satisfaction, job performance, recruitment and retention. However, our work has uncovered only a few efficiency measures, and only one ROI measure (the NELC study). Clearly, much more work is needed to document when and how CE activities can add value through the HR function.

Clearly, we are not the first set of researchers or managers to be interested in the ROI for such important business issues as flexible benefits, training for entry-level workers, and hiring from disadvantaged populations. And yet, there are essentially no publicly available studies. Why is this the case?

There are a number of significant barriers preventing companies and researchers from developing ROI measurements for these HR practices. The first, and most important, is that the accounting systems that most companies use to gather and manage information about costs are not set up to in ways that make it easy to associate costs with changes in HR indicators. This occurs because accounting systems are not designed to allow managers or researchers to easily measure the complete costs of days lost, times late, and work not done.

It is possible to get measurements of some of the simpler aspects of these issues. For example, many companies can calculate the direct costs of the time and resources expended in recruiting, hiring, and orienting new personnel. These include the direct costs of the personnel involved in hiring, recruiting and orienting, plus the direct costs of advertising, hosting, and seeking out potential hires.

However, there are a variety of additional costs that are important and much harder to calculate. In the case of hiring and retention, there is the cost of low productivity during the training period, and the "disruption cost" when someone leaves. There is also a loss of knowledge and a loss of the ability to learn when there is high turnover. For example, Jobs for the Future noted the experience of one manufacturing plant, in which there was very high turnover and a high use of temps. Researchers there showed that an important cost to turnover was the fact that knowledge never accumulated enough among machine operators to allow them to give feedback to the designers about what was working well and not working well in the designs. (Jobs for the Future, 2000)

Particularly in companies in which knowledge work is a key component of value added, there are complex costs that accrue to the firm when there are high levels of turnover, and low levels of employee loyalty and satisfaction. For example, the loss of a low skill worker bumps low skill tasks up to higher skilled workers, and therefore reduces productivity. There are also much subtler costs, such as the costs of the loss of learning and team spirit in an environment that has high turnover versus one that does not. (Hanson, 2000)

A second important barrier is the time frame. Some types of investments will not show benefits for years (for example, school reform or long-term training programs). It is difficult to show ROI for many new approaches because the investments haven't matured. This links up to the problem that training is shown as a cost, rather than capitalized as an investment. Managers who invest in training show costs now, but no benefits.

These two barriers can not only make it difficult to show ROI, but also can lead to under-training of staff. For example, Jobs for the Future noted the case of a major manufacturer, which has a policy in which each plant manager rotates from one plant to the next on a five year basis. The quality of the next assignment depends on how well the plant manager performs in his current assignment. Managers who invest heavily in training for staff during their five year tenure, and who can't show the benefit during their tenure, would hurt their career chances. As a result, the staff tended to be under-trained. (Jobs for the Future, 2000)

Another important barrier is that managers are afraid to measure the ROI because it might not give the answer that they want. As one manager noted during the course of the study, "We don't even want to talk about it because we are afraid it might come out negative." Because of the long time frame required for reaping benefits of training, managers are sometimes concerned that a short-term ROI study will show that training costs more than it benefits.

A fourth and final fourth barrier to gathering ROI measures is that many of the experts, researchers and funders who are gathering data about the costs and benefits of workforce development and training, are most interested in measuring benefits to participants, not to employers. Thus they are not gathering information that could be used to help companies better determine the ROI for the company (as opposed to the individual).

Potential Approaches for Improving Measurements

Although there are many barriers, there is also considerable interest in developing better measurements, particularly ROI measurements, that show how and when CE activities can create value in the HR function. The most fruitful approaches appear to be those in which a neutral and well-respected organization convenes key HR managers from a set of leadership companies as well as other experts, and jointly sets an action research agenda to develop these measurements over time, using data and experience from participating companies. The companies agree to share their data with this trusted third party, which takes the data and aggregates it, and then shares the aggregated data with the group. The convening organization also is generally permitted to release the aggregated data publicly.

Approaches of this sort are being pursued by many organizations, including Jobs for the Future, the National Association of Manufacturers, and the

US Chambers of Commerce in their WINS partnership; by the Boston College Center for Corporate Community Relations in its National Work Life Project; by MIT in its Leaders for Manufacturing Program; and by Walker Information and the Council of Foundations in the Measuring the Value of Corporate Citizenship project.

These approaches - with a neutral convener and broad industry participation — have several important benefits. First, they ensure that issues being addressed are timely and of considerable interest to participants. Secondly, it ensures that the managers participating in the study are ready and willing to act on the research results once they are made available. Since we know that action by leadership companies is the single best way to galvanize action by the majority of corporations in an industry, this will help ensure that positive results will be translated into results broadly. Thirdly, the presence of a respected third party helps to ease concerns about releasing potentially sensitive data to competitors and to critics. This helps to ensure that leadership companies are willing to participate, and are willing to share the data broadly once it is collected. All of these benefits help to ensure broad dissemination of the data, and industry willingness to act on the data once it becomes available.

It is worth noting that many of the experts involved in these activities are drawn from accounting firms, reputation consulting firms, and HR consulting firms. These are natural allies for this work, and can serve as important conduits for the dissemination of the findings. One of the potential outcomes of this work would be to provide an impetus for one or more of these firms to design a better accounting and costing methodology for the HR function, and to help to get the system accepted and used more broadly. This would have a significant benefit for the field.

Scorecard: Human Resources

SCORE	1	2	3	4	5	NOTES
INFO TYPE	■	■	■	■		Largely high quality data, including a rich blend of quantitative and business survey results, although the data on recruitment would be downgraded by most managers.
RELEVANCE	■	■	■	■		High level of relevance to many companies, particularly those faced with labour and skill shortages and high training costs of relatively mobile staff.
SOURCE	■	■	■	■		Direct survey data from high quality sources, with the more esoteric academic material perhaps being less credible to mid-level managers.
ATTITUDES	■	■				One of the areas where prejudice might reduce persuasiveness of data, particularly where diversity and class issues challenge HR approaches.

WORKFORCE DIVERSITY

What Are the Potential Benefits?

Promoting and managing diversity in the workforce is, first and foremost, a value in its own right. At a basic level, treating individuals equally and fairly, regardless of their race, gender, or creed, is a fundamental moral tenet. It also is clearly an element of CE.

In addition to the fact that it is a value in its own right, advocates claim that diversity in the workforce, when managed well, can create significant advantages for the firm. Well-managed diversity can help spur creativity and innovation and help firms compete more successfully for business. Equally importantly, it makes it easier for firms to hire and retain workers. This is particularly important now, as the entering workforce is considerably more diverse than the incumbent workforce, especially in the United States and in New Economy companies. Competing for new workers means competing to attract a diverse workforce. In the past five years, 33% of the new labour force entrants in the US were nonwhite. In the first decade of the coming century, scholars estimate that 80% of the new workers in the US will fall into the categories of women, people of color, and immigrants. (These categories are not mutually exclusive.) (Working Woman, 2000)

Which Managers Are Interested?

A wide range of managers are interested in understanding how to better promote and manage a diverse workforce. Clearly, managers who are part of the HR function are interested in this topic. Similarly, any manager with broad responsibility over the workforce will be interested, as the workforce is predicted to become steadily more diverse over time. At the senior management level, this could include the VP for Human Resources, the VP for Operations, Executive Vice Presidents and Division Managers. Many companies also have managers with specific responsibilities for increasing diversity, and for helping the corporation to better manage and promote diversity.

In addition, the senior management team is often interested in these issues. As will be shown below, failing to manage diversity well can have severe negative consequences for the organization, both internally and with customers and regulators. Managing diversity well can help to improve a company's image, and make it easier to achieve public relations and community relations goals.

What Indicators Are Used?

The indicators used fall into two broad classes. The first set measures how well the company is doing at promoting diversity within its workforce, management, and Board. These indicators include the following:

- Percentage of new hires from diverse backgrounds (this is sometimes compared to percentage of labour pool with diverse backgrounds)
- Percentage of overall workforce, management ranks, and senior executive ranks from diverse backgrounds
- Retention and promotion rates for employees from diverse backgrounds,

as compared to company averages for employees in similar positions
- Percentage of Board members with diverse backgrounds

The second set of indicators measures how well the workforce is performing. The measures here are essentially the same as the measures used by human resource managers in general. These were noted above on page 63, and will not be repeated here.

Key Outcome Measurements

There are two varieties of measurements showing the impact of promoting and managing diversity on the corporation. The first variety shows the significant costs that a company can incur when diversity is mismanaged or ignored. The following is a partial list of some of the multi-million dollar settlements paid out by major corporations for failing to manage diversity well:

- American General paid out $206 million in restitution to settle claims that it charged African Americans more for insurance than whites. (Africana.com, 2000)
- Texaco paid $176 million to settle a class-action suit brought on behalf of approximately 1,400 current and former African-American employees. (Alexander, 2000)
- Shoney's paid $132.8 million to settle a class-action discrimination suit brought by 20,000 employees and rejected applicants. (Alexander, 2000)
- Denny's paid $54.4 million to settle two class-action suits brought by minority customers who claimed some restaurants failed to seat or serve them. (Alexander, 2000)

Wright, Ferris, Hiller & Kroll

The investment community pays attention to these public signals about how a company is managing diversity. This study found that stock prices rose when companies announced they were the recipient of an award for managing and promoting diversity. They fell when companies announced discrimination suits. (Wright, Ferris, Hiller & Kroll, 1995)

Working Woman: Retention Issues

There are less obvious, but equally important costs, as well. When diversity in the workforce is poorly managed, companies have a harder time retaining women and people of color. A recent study showed that 65% of women of color leaving management positions said their companies failed to address gender bias, and 72% said that their companies didn't deal effectively with subtle racism. (Working Woman, 2000)

Cox and Beale: Costs of Mismanaging Diversity

Cox and Beale note that there are costs that companies incur due to mismanaging of diversity in their workforces. Some of the costs that they noted for companies that do not proactively manage diversity in their workforces are as follows:

- Employee absence and turnover: both of these cost factors tend to

increase when the composition of the work groups is changing toward more diversity.
- Reduced efficiency of communication: failure to manage cultural diversity well can result in slower or less effective communications.
- Reduced contribution to teamwork: research shows that groups that are more diverse, but do not have training in managing their diversity, perform less well than teams that are less diverse. Teams that are more diverse, and have training in managing their diversity, perform better than teams that are less diverse.

Overall, Cox and Beale conclude 'organizations that are more diverse than competitors but fail to effectively manage diversity could be at a cost disadvantage compared to those who either are less diverse or that manage it better'. (Cox, 1997)

While there are costs for mismanaging diversity, there are also benefits for managing it well. These benefits include increased competitiveness, increased innovation, and increased ability to hire and retain employees. B&Q's work with the disabled, noted in the section on Innovation and Learning below, provides a good case example of how this may occur. Other evidence includes the following:

McCartney: Competitiveness

Writing in *Consulting Magazine*, McCartney notes that major consulting firms are increasing their efforts to increase the diversity within their senior ranks. The clientele for the consulting firms is becoming more diverse, and firms are trying to reflect this diversity. While specific data on sales are not available, senior managers at consulting firms indicate that many of their clients demand a diverse team to work on their engagements. The firms find that unless they have a critical mass of minority and women partners, it is very difficult to send in the right team and win the contract. Managing diversity is recognized as being particularly important for firms seeking to have a global practice. (McCartney, 2000)

Cox and Beale: Innovation

Cox and Beale note that diversity in work groups, when managed well, can create benefits in innovation and problem-solving. A series of research studies showed that the level of critical analysis in work groups was higher in those that were subjected to minority views than those that were not. The presence of minority views improved the quality of the decision-making process whether or not the minority view ultimately prevailed.

Often, gaining the benefits of diverse views requires management and training. Cox and Beale noted the groundbreaking research of Harry Triandis, who compared the problem-solving scores of homogenous groups with those of two types of diverse groups: diverse with training and diverse without training. He found that diverse groups without training in managing their diversity produced lower scores than the homogenous groups, while those that were trained produced scores that averaged six times higher. This finding was confirmed by other researchers, including Nancy Adler of McGill University. (Cox and Beale, 1997)

Alexander: Hiring and Recruitment

Not surprisingly, experience shows that companies that make a significant commitment to managing and promoting diversity do well in hiring and promoting diverse workers. This is true even for companies with troubled records in the past. Consider Denny's and Texaco, noted above for the large fines paid for failing to manage diversity. Both committed themselves to major turnarounds, and are now seen as good places for a diverse workforce. For example, at Texaco, minorities accounted for nearly 4 in ten of new hires, and more than 20 percent of the promotions. At Texaco last year, women and minorities together accounted for 67% of the new hires and 66% of the promotions. In 1993, only one Denny's franchise was owned by an African-American. Today, African-Americans own 120 franchises - 14% of the company total. These and other changes led the Baltimore chapter of the NAACP to give Denny's the Corporation of the Year Award. (Alexander, 2000)

What's Missing?

There is very little research that looks at different methods and approaches for managing diversity, and how they help create business benefits. Leading practitioners in this field, such as Leroy Cox, Jr., Mary Gentile, David Thomas, and R. Roosevelt Thomas, Jr., are developing models and approaches that can help corporate managers to better understand and manage diversity in their corporations. But the field has not yet advanced to the point where researchers have been able to develop quantitative measurements on the benefits and costs to particular approaches in particular circumstances.

Potential Approaches for Improving Measurements

In our view, the key next step is to build on the work of the leading practitioners in this field, and develop a database of case studies of best practices in managing and promoting diversity. This database could then be used to extract principles and models for managing diversity, which could be applied by managers in a broad range of settings. Once the principles and models are better articulated, and more widely implemented, it will be possible to develop qualitative and quantitative measurements of the benefits of different approaches in different circumstances. But none of this can happen until current best practices are inventoried and analyzed.

Scorecard: Workplace Diversity

SCORE	1	2	3	4	5	NOTES
INFO TYPE	■	■	■			Data on financial penalties for mismanaging diversity is clearly of high quality. The academic studies also involve quantitative data.
RELEVANCE	■	■	■			Evidence on financial penalties persuasive – more so in US than elsewhere. Academic evidence less convincing – doesn't demonstrate causal links, i.e. ability to access diverse markets by having a diverse workforce.
SOURCE	■	■	■			Financial penalty data is real and case specific, whilst the studies are largely from academic and consultancy sources, which are treated with less confidence.
ATTITUDES	■					Difficult to produce a study suggesting diversity is a bad thing for business; underlying social limits to research make most data suspect. Strongest negative undeclared attitudes most likely to exist here.

Marketing and Sales

What Are the Potential Benefits?

The benefits of CE are perhaps clearest in the area of marketing and sales. In particular, cause-related marketing – defined as 'a commercial activity by which businesses and charities or causes form a partnership with each other to market an image, product or service for mutual benefit' – has shown dramatic benefits for both businesses and communities. Not surprisingly, it is now one of the most common types of CE. For example, a survey conducted by Business in the Community of 412 chief executives, marketing and community affairs directors in the UK in 1998 showed that 73% of the companies surveyed were engaged in some form of cause-related marketing. (Adkins, 1999)

There is a second marketing and sales benefit that is claimed for CE. This is in the area of diversity purchasing. The basic argument, advanced by advocates such as the Reverend Jesse Jackson, is that companies that purchase from low-income or minority communities will be better able to sell products to those communities. We will address this benefit in the section on diversity in purchasing below.

Which Managers Are Interested?

In general, managers in the marketing and sales functions are the most interested in understanding how CE can help to improve the company's image, market positioning, customer loyalty, and sales. Managers in community affairs, public relations, and human resources can also be interested, particularly in the effect of CE on the company's image and brand.

What Indicators Are Used?

The sales and marketing function has a very well-developed and complete set of indicators that managers use to gauge the effectiveness and efficiency of different ways of promoting sales and positioning the company and its brands. A representative list would include the following:

- Sales
- Awareness of product
- Interest in product
- Propensity to try or purchase product
- First-time purchases
- Repeat sales/customer loyalty
- Recommendations of product to friends, colleagues
- Switching away from product/customer defections
- Brand and image
- Product differentiation
- Brand awareness
- Brand equity
- Customer segmentation
- Customer demographics
- Customer psychographics
- Effectiveness of promotion and advertising media
- Number of impressions
- Ability to reach key consumer segments
- Increase in awareness and intention to purchase

Key Outcome Measurements

INCREASED SALES

Many companies report that cause-related marketing can significantly boost sales. For example:

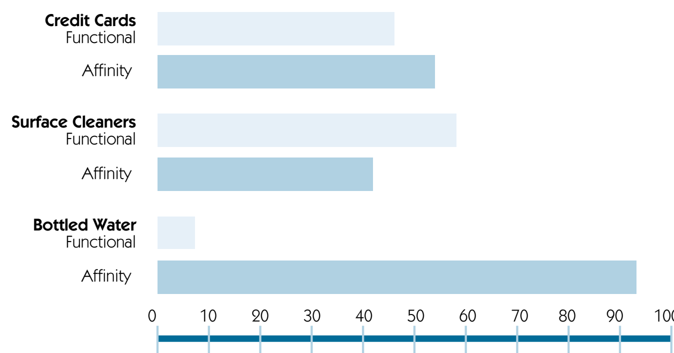
- American Express, which pioneered cause-related marketing in the early 1980's, linked the use of its cards to donations to restore the Statue of Liberty. During the first month of the promotional period, use of American Express cards rose by 28% compared to the previous year and new card applications increased by 45%. (Adkins, 1999)
- Sears created a partnership with Gilda's Club (a nonprofit organization that provides a network of local meeting places where people living with cancer can come together for emotional support, social events, and laughter) to promote special ties, scarves, and Levi's 550 jeans. Sears sold 100,000 ties and 30,000 scarves in several months, and sales of 550 jeans increased in-store by 56 percent in Gilda's Club cities, compared to 16 percent in non-Gilda's cities. (Adkins, 1999)
- Coca-Cola experienced a 490 percent increase in sales of its products at 450 Wal-Mart stores during a six-week campaign in 1997 with Mothers Against Drunk Driving, in which the company donated a portion of its sales to the organization. (BSR, 2000)
- London-based Diageo plc reported that between 1994 and 1998, 22 CRM projects helped it raise $600,000 for causes while increasing sales of tracked brands by 37 percent. (BSR, 2000)

CUSTOMER LOYALTY

Companies that have engaged in cause-related marketing report that their efforts help attract and build long-term relationships with customers. For example, affinity credit cards, in which a nonprofit organization benefits each time a consumer uses the card to make a purchase, help credit card companies develop long-term relationships with consumers.

There is growing evidence that affinity is a significant part of the value that consumers assign to specific products. Research International Ltd. (UK) conducted a global study looking at the importance of functional benefits versus affinity in three markets - surface cleaners, credit cards, and bottled water. They found that affinity outweighed functional performance marginally for credit cards, and significantly for bottled water as noted in the chart below. (Adkins, 1999)

Functional Performance vs. Consumer Affinity in Purchasing Decisions



CE can play an important role in building consumer affinity. Several studies over the past few years have shown that consumers are drawn to companies that are associated with a social cause or issue.

- In 1999, the U.S.-based Cone/Roper Cause-Related Trends Report found nearly two-thirds of Americans, approximately 130 million consumers, report they would be likely to switch brands (66% in 1993, 65% in 1998) or retailers (62% 1993, 61% 1998) to one associated with a good cause. (Cone Inc., 1999)
- Similar results were found internationally. Consumers responding to surveys indicated that they would be likely to switch brands because a company was associated with a good cause: UK (86%), Italy (75%), Australia (73%) and Belgium (65%). (Adkins, 2000)
- MORI surveyed 1935 British adults in 1998, and found that, within twelve months of the survey date, 30% had bought a product or service because of a link to a charitable organization, and 28% had boycotted a company's product on ethical grounds. (Adkins, 1999)

Corporate social performance cannot substitute for superior product quality, or for a more competitive price. But it can serve as a "tie-breaker" for products that are competing head-to-head, and that are closely matched in features and price. It can become a strategic advantage in a crowded and competitive marketplace. In some ways, it is not surprising that a number of the companies that are most closely identified with a commitment to corporate social responsibility - such as Levi Strauss, the Body Shop, or Ben & Jerry's - are in a consumer products business.

What's Missing?

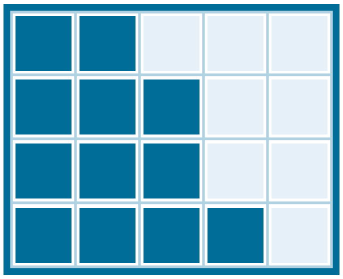
While there are many interesting findings noted above, in general, almost all the measurements are what we have been calling "process measurements". They show us that cause-related marketing can create positive changes in indicators that marketing and sales managers care about. But there are very few examples of efficiency measurements - measurements that show that cause-related marketing costs less to create a desired change in an indicator than other approaches, for example a series of television advertisements, or a mailing of free trial products. And there are no ROI measurements - measurements that would show that a company actually would make money if it invested funds in cause-related marketing. So, for example, we know that American Express spent $4 million on its cause-related marketing for the Statue of Liberty, and we know that that spending caused an increase in the credit card usage and card applications. But we don't know whether the increase in card usage and applications netted American Express more or less than $4 million.

It is quite difficult to get ROI measurements of the effects of marketing because many of them are long-term, and because there are many intervening variables between a consumer's exposure to a marketing stimulus, and the continued purchase of products over time. Most analysis of the value of differing marketing approaches tends instead to focus instead on efficiency measurements - the relative cost of different ways of achieving the same marketing result. So, for example, a marketing manager might compare two media outlets in terms of the cost per thousand impressions on potential customers, or might compare two marketing campaigns in terms of the increase in customer trials of products. Even this information is not easy to acquire, although it is much easier to acquire than information about the ROI of marketing activities.

Potential Approaches for Improving Measurements

As the evidence above indicates, there has been much good work already done in measuring the benefits of CE in marketing, especially in cause-related marketing. This work establishes a credible basis for asserting that CE creates benefits in marketing, especially for high-brand-value companies. The next step in improving measurements will be to develop efficiency measurements of the impact of CE. The key issue will be to develop a consensus from some of the leadership companies, nonprofit organizations, advertising agencies, and cause-related marketing specialists about what types of efficiency measurements they would find the most useful. From our perspective, an efficiency measurement that showed when and how cause-related marketing was a more efficient tool than media advertising would be extremely helpful. It is clear that cause-related marketing allows a different kind of approach to consumers, one that is more based on affinity and values than on slick images and well-known personalities. But it is not at all clear when and how this approach makes better business sense. Making progress on answering this question would help unlock new markets and new funding for cause-related marketing, and dramatically boost company commitment to CE.

Scorecard: Marketing and Sales



SCORE	NOTES
INFO TYPE	Actual sales figures linked to specific marketing campaigns are high quality, with attitudinal surveys about purchasing intentions being a far less convincing type of data.
RELEVANCE	Predictive power of attitudinal data would be suspect, and applicability of strong cause-related marketing data would be questioned beyond high profile brands.
SOURCE	Data coming from business results very credible, whilst the academic studies less so. Survey data from very credible sources.
ATTITUDES	No obvious reason for attitudinal blocks.

Innovation and Learning

What Are the Potential Benefits?

Proponents of CE claim that increased levels of CE can assist corporations to increase their levels of innovation and learning, particularly in unfamiliar markets. The speed of change, and the global reach of competition, has made innovation one of the keys to success in today's market.

Competition on a global scale has increased dramatically over the past 30 years. In 1970, world exports were $1.3 trillion, and had expanded (in constant dollars) to $4.3 trillion by 1995. Experts predict that the share of the world's market that is "globally contestable", i.e., open to global competitors in product, service, or asset ownership markets, will rise from about $4 trillion in 1995 (one seventh of the world's output) to approximately $21 trillion by the end of 2001 (one half of the world's output). (Atkinson and Court, 2000)

The pace of innovation and competition has increased as well. The need (and reward) for speed is clear for the dotcoms. But manufacturing companies feel the pressure, too. A recent study looking at best practices in new product development found that the average time to complete new products was 35.5 months in 1990, but had dropped 30% to 23 months by 1995. The time to develop a new car has dropped from six years in 1990 to two years today. 77% of Hewlett Packard's revenues are from products that are less than two years old. (Capelli, 1997).

But how can CE help? Does it really make sense to believe that engaging with communities will help corporations to increase their levels of innovation and learning?

To understand why advocates believe this to be true, it is necessary to look at the importance of networks and alliances in creating innovation and learning, particularly in the New Economy. Peter Drucker and other experts suggest that social capital (networks, shared norms and trust) may be as important as physical capital (plant, equipment, and technology) and human capital (intellect, character, education and training) in driving innovation and growth. (Atkinson and Court, 2000)

To succeed, businesses must increasingly move from the 'make and sell' to the 'sense and respond' approaches. Such a shift stresses the need for dynamic and resilient relationships with key stakeholders. One point of evidence supporting the importance that managers attach to networks is the dramatic growth in the number of networks of businesses in the recent past. In the US, the number of new technology alliances formed each year grew from approximately 80 per year in 1985 to approximately 225 per year in 1994. (Atkinson and Court, 2000).

Advocates of CE claim that increased levels of CE can help the company connect up to new and valuable networks. The networks created, if used well, can help the company to better identify potential risks and opportunities, and to understand how best to address them. Failing to develop these networks can leave the company blind to risks outside its normal "business space". The case of Monsanto, discussed below, is a cautionary tale about the potential damage such blindness can bring.

A number of leading businesses, particularly in the UK and Europe, have found that community engagement can be an investment in knowledge and a key learning method for both business and social good. Partnerships provide a "critical pathway" through which both businesses and the community can find new ways to work, develop skills, seize opportunities, and solve problems. For business, the potential lies in both building up its underlying enablers of long-term performance and in identifying and realizing specific business opportunities. (Sabapathy, 2000)

Advocates also claim that when a company uses increased CE to help it learn, it obtains a secondary benefit that is not directly related to the market or the product. The blocks that restrain a business from being able to successfully integrate CE into its practice are the same blocks that prevent the business from identifying new market opportunities rapidly as it is confronted with rapidly changing environments. Integration of CE practices requires the development of a learning culture, and this is at the heart of managing change. And managing change is an essential tool for success in future markets. CE can help companies to learn about new and unfamiliar territory - if they don't segment off the learning opportunity. (Sabapathy, 2000)

Which Managers Are Interested?

The managers most interested in spurring innovation and learning typically are the top managers, especially of corporations that are facing turbulent, complex and rapidly changing environments. This is especially true of global and New Economy businesses. Managers responsible for operations, for product development, and for marketing are often interested as well.

It is important to recognize that managers who are interested in innovation and learning may not use those words to describe their interests. Managers typically don't say "How are we going to learn?" Rather, they ask question like, "How are we going to deal with the complex, rapidly changing world that we are in? What are the main challenges we are likely to face in the coming months and years? What are the potential destabilizers of our position in the market? How do we develop our businesses competencies to identify these problems and respond to them?"

When answering these questions, the manager is likely to point to the need to develop an organization that is flexibly focused on a range of potential challenges and opportunities, and constantly alerted, and re-alerted, to what they are.

What Indicators Are Used?

The central proposition that advocates for CE are advancing is that increased levels of CE will help improve a company's ability to identify new challenges and new opportunities, and respond quickly and appropriately. Accordingly, the indicators must provide information on how well a company is able to identify new challenges and new opportunities, and respond quickly and appropriately.

There are a variety of indicators that can be used. Some are quantitative:

- Time to market
- Number of patents
- % of sales coming from new products and services
- % of profits coming from new products and services

Some indicators, however, are qualitative:

- Did the company identify crises and opportunities, assess their importance accurately and develop ways of dealing with them faster than its competitors?
- Did the company correctly assess which potential challenges were NOT important, and accordingly, not waste time dealing with them?

Key Outcome Measurements

There have been several analyses of the impact of CE activities on the company's ability to innovate and learn, and to identify new challenges and new opportunities and respond quickly and appropriately. Kanter, in "From Spare Change to Real Change: The Social Sector as a Beta Site for Business Innovation", notes that leading companies have discovered that working together with nonprofit and government organizations to solve social problems can give them new insights and approaches to creating business opportunities as well. Solving community needs creates opportunities "to develop ideas and demonstrate business technologies, to find and serve new markets, and to solve long-standing business problems". (Kanter, 1999)

Zadek and Scott-Parker, in "Unlocking Potential: The New Business Case for Employing Disabled People", note similar findings. Companies that redesign their work so that they can increase the number of people with disabilities who can be employed discover new and better ways to organize work, increase employee productivity, improve their image in the community, and discover new products and services to sell. (Zadek and Scott-Parker, 1999)

There are also quite a number of case studies that make the point in a compelling way. We present several of these case studies here.

B&Q: Learning from Diversity

B&Q is the largest Do-It-Yourself (DIY) retailer in the UK with 300 stores and 25,000 employees. Together with its subsidiaries it is the third largest DIY retailer in the world. (B&Q, 2000). B&Q is a good example of a company that has learned that engaging in CE can help improve its image and its sales, and has developed a culture that supports continued exploration of this area.

In the late 1980s, B&Q was rapidly expanding, opening stores all over the UK. Staff recruitment on such a large scale became problematic. As a result, the company turned its focus to less typical recruitment sectors, such as women returning to work after a career break, the long-term unemployed and individuals over 50. After a detailed review, B&Q decided to focus its recruitment drive on the older generation.

In 1989, as an experiment, B&Q opened a store in Macclesfield, UK, staffed entirely by individuals over 50. Some initial concerns were raised regarding the more physical aspects of the job and working with computerised systems, but these concerns did not turn out to be a problem. The experiment proved very successful and an independent survey published two years later showed that in practically every respect - customer service, short-term absenteeism, staff turnover and sales - the Macclesfield store's staff outperformed other stores. B&Q then adjusted its recruiting policies store-wide to be better able to attract and retain older workers. The benefits continue to be felt. (B&Q, 2000)

B&Q then went on to focus on developing better service for disabled people. B&Q did this both because it felt that it had an obligation to serve disabled people well, but also because the purchasing power of disabled people is large and growing. Currently, the spending power of disabled people is estimated at 45-50 billion pounds per year in the UK and 188 billion dollars per year in the US. (Zadek and Scott-Parker, 2000)

As with its experience with employees over 50, it started by focusing on a single store. B&Q completely redid the store to make it totally accessible. This included changes in the store layout, signage, and merchandising, training processes, and outreach processes. The results were also dramatic, including improved sales, reduced turnover and improved morale. (Sabapathy, 2000)

After analyzing the costs and potential benefits, B&Q decided to expand the program to the entire company. It worked with a national disability group to create a training program for the entire company, and had every store get involved. Each store develops relationships with local disability groups, and has a store champion who works on disability issues. The disability groups help the local stores to address the specific needs of local disabled residents by establishing customized relationships between local staff and local disabled groups. (Sabapathy, 2000)

B&Q's practice in the workplace around age and disability has reduced significantly turnover and improved morale. B&Q's programs have increased its free advertising at the local and corporate level, and have helped improve sales.

B&Q also found some important and unexpected benefits that arose because of its engagement with the disabled community. It entered the engagement to improve service to disabled people. But by reworking its systems and approaches to serve disabled people better, it learned how to improve customer service for all of its customers. Working with disabled people was a laboratory that helped it to understand better what all customers wanted, not just what the disabled wanted. As its Managing Director, Martin Toogood noted, "If we can get it right for disabled people, then we can get it right for most people." (Zadek and Scott-Parker, 2000)

Monsanto: Missing the Signal

Monsanto's recent difficulties with public rejection of its genetically modified (GM) foods were due, in part, to a failure to correctly pick up and interpret signals in an unfamiliar market and in different cultures. Monsanto did not have a mode of effectively engaging and learning about risks, and understanding how to manage them, in the consumer market in Europe.

Prior to public concern about GM foods, Monsanto's primary spheres of engagement were with food producers and regulatory bodies. These groups, Monsanto's core stakeholders, were giving Monsanto consistent and positive signals about the safety and value of its products. The US Food and Drug Administration, after a lengthy process, had ruled in 1992 that GM foods generally pose no more risk to health than ordinary foods, and hence do not need to be labeled. In 1999, President Clinton pinned the National Medal of Technology on four Monsanto researchers for pioneering bioengineered crops. And most importantly, sales of GM seeds had skyrocketed. Last year, more than a third of the corn grown in the US, and almost half the soybeans were grown from GM seeds. (Stipp, 2000)

Given this background, it is in some ways understandable that Monsanto might dismiss consumer fears over the potential negative impact of GM foods. Nonetheless, the fears were deeply held, and Monsanto failed to address them in any adequate way. During 1999, major European supermarket chains stopped selling GM foods. A number of major food companies, including Gerber and Kirin, stopped buying them as ingredients. By the end of 1999, US food processors were paying a premium for non-GM crops, and Archer Daniels Midland advised its farmer-suppliers to segregate GM from non-GM crops. (Stipp, 2000)

The financial impact on Monsanto was intense and negative. By February, 2000, the value that the financial markets placed on Monsanto's $5 billion per year agricultural business unit was less than zero. Clearly, the failure to understand and manage consumer concerns caused tremendous damage to Monsanto's shareholder value. Not all of this can be attributed to a failure to engage in more positive ways with its many communities. But other seed companies who manufacture GM seeds have been able to work more productively to avoid some of the problems that have beset Monsanto, in part because they have developed better and deeper relationships with their communities, and with key NGO representatives in those communities. (Stipp, 2000)

KPMG: Transferring the Learning

One of the key issues in gaining the benefits from CE is being able to capture the learning created through CE, and transfer it to other parts of the corporation. KPMG's work with the Network Drugs Advice Project (NDAP), an NGO dedicated to reducing drug abuse in the UK, provides an interesting case in point. KPMG structured its relationship with NDAP to create benefits for both NDAP and KPMG. Initially, KPMG and NDAP agreed to have NDAP serve as a "live case study" for professionals in the tax practice. KPMG created a conference at which NDAP presented its mission, activities, and an initial business plan for its operations to the tax professionals. The tax professionals then worked to develop advice on improving the business plan and business structure. Both sides felt the conference was a tremendous success - NDAP left with excellent advice on its situation, and the tax professionals felt that the case study was memorable and enhanced their learning because it presented business issues in a new and fascinating format. The initial conference was so successful at achieving KPMG's professional development goals that the NDAP case was used at a series of KPMG training events across the UK.

The relationship between KPMG and NDAP worked so well that when the UK professional development staff was asked to provide training in a new method of project management, they turned to NDAP again. KPMG and NDAP developed a new "live case study". In this case, NDAP presented a marketing plan for a new project, and the KPMG staff were asked to apply the new project management tools to the marketing plan. Once again, NDAP left the case study experience with excellent advice, and the

KPMG staff were able to integrate the new project management tools into their professional "toolkit". KPMG staff felt that having the case study focused on an NGO was helpful because it took them outside their normal range of clients and activities, and yet had the same basic business issues that they face with all their clients. In addition, the fact that they were providing advice on a worthy cause made their efforts more memorable, enhancing the learning benefit. By carefully structuring its work with NGOs, KPMG was both able to create community benefit, and also cascade learning throughout its organization. (Sabapathy, 2000; Kabel, 2000)

In addition to these cases noted here, there are a number of the other cases that we have discussed elsewhere which have implications for learning and innovation. Suez Lyonnaise des Eaux, for example, profiled on page 59, provides a good example of how companies can use CE to help develop innovative ways of reducing costs and serving new markets. The companies profiled in the section on Innovations That Expand the Market, starting on page 97, provide good examples as well.

What's Missing?

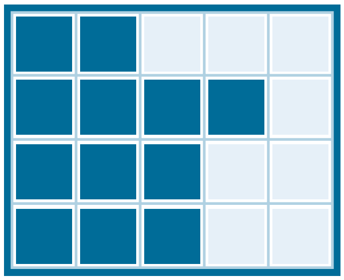
There are only a few pieces of comparative evidence that look across a variety of industries at how and when CE can be used as a tool for improving a company's ability to learn and innovate. This sort of cross-industry comparison would be very helpful in developing a deeper understanding of when and how CE can be most effectively used to help spur learning and innovation. Are there particular types of businesses, or particular industries in which CE helps create value? Does the type of CE that creates value vary depending on the customers and stakeholders of the business? Gaining the ability to answer these sorts of questions would help provide practical guidance to managers as they try to determine the best way to spend limited resources.

Potential Approaches for Improving Measurements

One potential approach would be to help create learning networks of managers and other key stakeholders, who could share best practices and help to deepen the understanding of how and when engagement builds the ability to learn and innovate. The learning networks could help to assemble and integrate cross-cutting themes and lessons that emerge when practice is compared across businesses and across industries. In putting together such learning networks, it would be useful to work with organizations who are already committed to this agenda. In the United States, this would include organizations such as the Boston College Center for Corporate Community Relations, Business for Social Responsibility, The Committee For Economic Development, and The Conference Board. In Europe and the UK, this would include organizations such as the European Business Network For Social Cohesion, the Institute for Social and Ethical AccountAbility and the Prince of Wales Business Leaders

Forum. These organizations could both help to create the learning networks, and could also be a conduit for distributing the findings of the networks more broadly.

Scorecard: Innovation and Learning



SCORE	1 2 3 4 5	NOTES
INFO TYPE		Focus on anecdotal, largely qualitative evidence is limiting.
RELEVANCE		Rapidly increasing interest in innovation and knowledge management makes this area feel highly material and applicable, particularly in HR and senior management.
SOURCE		Case material from business executives generally convincing, whilst speculative generalisations are less convincing because they come from advocates of the innovation argument.
ATTITUDES		Potential attitudinal blocks regarding diversity issues.

Diversity in Purchasing

What Are the Potential Benefits?

Advocates claim that purchasing from a diverse supplier base can assist companies to increase their competitiveness in a number of ways. First, it can help increase their ability to innovate and develop better products, particularly for ethnic or culturally diverse markets. Advocates claim that suppliers who are members of a particular ethnic or cultural group are better able to understand the specific needs and interests of members of that group than suppliers who are not part of that group. Therefore, they are better able to help their customers identify and seize new opportunities for products and services that will be attractive to that group.

A second claim advanced by advocates, which was discussed briefly above, is that purchasing from a diverse supplier base will help to improve a company's ability to sell products and services to particular ethnic or cultural groups. There are two parts to this claim. The first is that members of a particular ethnic or cultural group will be favorably impressed by a company that purchases from suppliers that are part of their community. Price and quality being equal, they would rather purchase from a company that supports their community than one that does not. The second is that purchases from suppliers that are part of particular ethnic or cultural communities help to increase the purchasing power in those community. This then creates the capacity for the members of the community to increase their purchases of goods and services, thereby raising company sales.

The final benefit that advocates claim is that companies will be better able to sell to customers who have policies or regulations requiring their vendors to purchase from a diverse supplier base. This is becoming relatively less important in the US over time, particularly because a number of key judicial rulings have made it much more difficult for public sector agencies to promulgate and enforce such policies in their purchasing.

Which Managers Are Interested?

Clearly, the managers most interested in increasing the diversity in the purchasing and supplier development functions are those with responsibility for purchasing. It is quite unusual, however, for a purchasing manager to pursue this strategy without direct support (or orders) from a higher-level manager. Purchasing departments, particularly in the largest corporations, are under intense pressure to reduce costs, improve quality, and decrease lead time. An important strategy being pursued to accomplish these goals is to reduce the supplier base, and to move toward purchasing and invoicing via the Internet. Both of these strategies have the effect of favoring the largest suppliers. Unfortunately, since most suppliers from diverse ethnic and cultural communities are relatively small, this also means that it makes it more difficult for them to compete successfully. Thus, purchasing managers need support and direction from their superiors if they are to pursue increases in diversity purchasing successfully and vigorously.

The managers that are typically most interested increasing diversity purchasing are in marketing (especially marketing to diverse ethnic and cultural groups), corporate relations, and the senior management team. These managers are better positioned to see the benefits that diversity purchasing creates, and to push the company to change its purchasing strategy in ways that permit the inclusion (and sometimes development) of a more diverse supplier base.

What Indicators Are Used?

Purchasing managers use a broad set of indicators to measure the attractiveness of particular suppliers. The following are some of the most important:

Product and service indicators

- Price
- Features
- Quality
- Reliability
- Delivery time

Company indicators

- Management capacity
- Experience and track record
- Financial strength
- Production capacity
- Labour relations
- Certifications (quality, environmental, social)

Company/supplier interaction indicators

- Assists company to develop innovative, successful products and services

- Able to integrate into company's "just-in-time" delivery system
- Increases "value-added" to customer experience
- Gives company access to important information, expertise or assets

Potential Approaches for Improving Measurements

Diversity purchasing is a significant and growing part of corporate practice, particularly with larger corporations. There has been a remarkable increase in growth of sales from diverse suppliers to major corporations over the past twenty years, growing from $1.0 billion in 1977 to $41.0 billion in 1997. Many Fortune 500 corporations make very significant levels of purchases from diverse suppliers. For example, most of the major auto companies have set and achieved aggressive targets for diversity purchasing. This year, Ford is anticipated to purchase $2.7 billion of goods and services from minority suppliers (approximately 5% of its total purchases), GM to purchase approximately $1.5 billion, and Chrysler to purchase approximately $1.0 billion (DiversityInc.com, 2000; National Minority Supplier Development Council, 2000)

Thus, judging by the behaviour of managers at successful companies, there is a significant benefit to increased diversity purchasing. Similar to workforce diversity, however, there is very little quantitative data that is publicly available to demonstrate the bottom-line benefit of these activities. We note below the few studies that are available. But we also provide some quotations from senior executives at companies that have made significant commitments to diversity purchasing, explaining why they chose to do so.

Initiative for a Competitive Inner City: Partnerships with Minority Companies

This research focused on a number of specific partnerships between major corporations and minority suppliers, particularly those at the Ford Motor Company and at State Street Bank. The research showed that partnerships between minority-owned businesses and the corporations helped the corporations develop better products designed for the minority communities and improve customer loyalty in this market segment. (Initiative for a Competitive Inner City, 2000)

Lucent: Customer Preferences

Lucent conducted a study in 1997 of the factors that influenced minority and ethnic consumer choice of long-distance telephone service provider. Lucent found that the third most important factor, after price and quality, was whether the long-distance service provider was viewed as being a positive presence in the particular minority or ethnic community. One of the most important determinants of whether the company was a positive presence was whether it had created jobs and income for members of the ethnic or minority community. To the extent that diversity purchasing was seen as creating jobs and income for members of the community, it would influence the choice of long-distance service provider. (Eurick, 1997)

Senior Management Perspective

We present the following quotes from leading executives to give some additional evidence as to when and how diversity purchasing can help create business benefits.

Arthur Martinez, Chairman and CEO, Sears Merchandising Group

> Minority business enterprises identify the special needs of the growing minority population. . . supplying goods and services specific to that sector. An alliance with a minority supplier can help to eliminate costly mistakes as corporations expand into minority markets.
>
> By maintaining a large pool of potential vendors, a company widens its scope of innovative ideas, methods and markets. Minority vendors enhance those capabilities by providing valuable, culturally specific opportunities to help create new markets. In many cases, minority entrepreneurs identify lucrative markets long before mainstream companies make the same discoveries. (Barnett, 1995)

Les McCraw, Chairman and CEO, Fluor Corporation

By providing opportunities to enterprises owned by women and minorities, we accomplish several goals:

> - we help increase the economic growth and development in the communities that we serve
>
> - we provide jobs by expanding the capacity of small business, we enhance community relations
>
> - we meet the objectives of our clients
>
> This provides us with a competitive advantage. As a global services company, we know that diversity is smart business. Within our constantly changing business environment, it's become an important key to survival and growth. (Barnett, 1995)

Chris Galvin, Vice Chairman and CEO, Motorola, Inc.

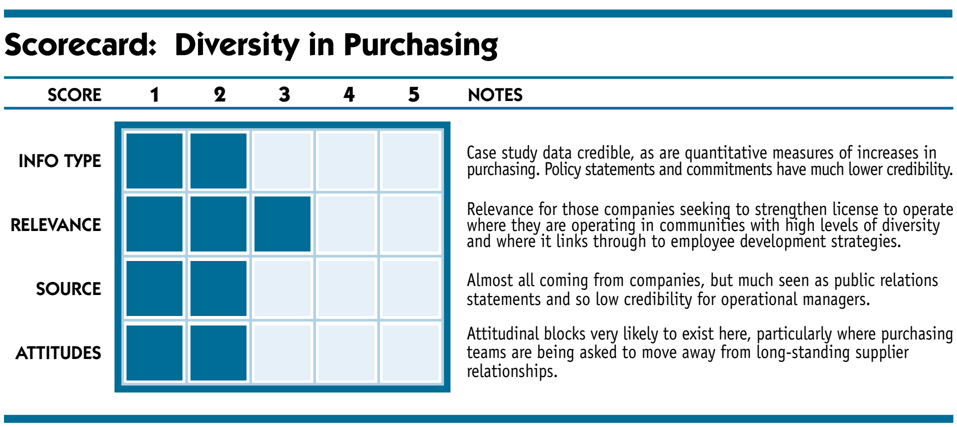
> At Motorola, the business case of diversity is clear. We are committed to diversity because it ensures us a competitive edge. Valuing diversity is also part of the Motorola culture, where creativity, flexibility and innovation by all our associates are key to continued success. Motorola values strong relationships with minority- and women-owned businesses and suppliers for the same reasons. In order to meet business challenges, we must utilize a broad spectrum of talents reflecting our employee, supplier, and customer bases. It just makes good sense. (BSR, 2000)

What's Missing?

Clearly, there is a paucity of quantitative data showing the link between increased diversity purchasing and bottom-line benefits. It would be especially helpful to have better data showing the link between diversity purchasing and increased sales in diverse ethnic and cultural communities.

Potential Approaches for Improving Measurements

In our view, the key step is to develop quantitative data showing whether and when diversity purchasing is an important factor in the buying decisions of members of diverse ethnic and cultural groups. For example, it would be quite valuable to complete an international survey which showed what percent of the members of diverse ethnic and cultural communities would choose products which were made by companies that had a diverse supplier base over similarly priced products from companies that did not. It would be important to work closely with the leadership organizations already active in this field in fielding such a survey. In the US, leadership organizations would include the National Minority Supplier Development Council, the National Black Chamber of Commerce, and the U.S. Hispanic Chamber of Commerce, among others.



C. Innovations That Expand the Market

Overview

In the previous two sections, we examined a range of quantitative measurements of CE's impact, both for the whole corporation, and also for specific functions. In this section, we focus on innovations that expand the scope of a corporation's profitable CE activities. The key question: how and when does expanding CE activities actually increase the profitable market for a corporation's goods and services?

The answer rests in the company's ability to innovate. For a company to expand its CE business profitably, it almost always must develop new products and services that expand the market, and enable profitable business where none was possible before. These innovations are often complex and difficult to implement, which is why corporations have not already implemented them. Unfortunately, companies usually cannot simply expand the CE aspects of their businesses and make more money. Rather, there usually is a complex web of drivers, including some that foster expansion of CE activities, and others that oppose it. True creativity and discipline is required to unlock the potential for new business that both benefits communities and is profitable for business.

For example, when Bank of America created its Neighborhood Advantage home mortgage product, which served lower-income first-time homeowners, it not only had to significantly change its underwriting techniques, but it also had to experiment with new ways of compensating its loan origination staff. Before Neighborhood Advantage, the compensation for loan originators was tied, in part, to the total dollar volume of loans that they originated. But the Neighborhood Advantage program was targeted to serve homeowners whose average size loan would be much smaller than the rest of the market that Bank of America served. If the compensation for the loan originators wasn't changed, the program would not get the attention from the loan originators that it would need to succeed. Bank of America did change the compensation to include the number of loans as well as the total dollar volume of loans, which helped to garner loan originator attention and make the program a success.

In order to understand this dynamic better, this section will focus on specific innovations within particular industries. By narrowing our focus down to a particular industry segment, we will be able to get a clearer view of the nature of the innovation, and the process by which it was developed and tested. In order to show a variety of examples, and different types of innovations, we look at three industries - financial services, retailing, and insurance. For each industry, we describe:

- The focus of the innovation
- Which managers are interested
- The indicators that are used
- The drivers affecting innovation
- Examples of innovation that expand the market

Measurements of these innovations are sometimes quantitative, and sometimes qualitative. The key role for measurements here is to validate the value of the innovation. Is this truly profitable? Is this innovation worth scaling-up? In this context, for each industry we also look at what measurements are needed to prove more clearly the value of particular innovations, and at promising approaches for obtaining these measurements.

Financial Services Industry

What is the Focus of the Innovation?

In this section, we will focus on one aspect of CE in the financial services: expanding financial services provided by banks in low-income communities. The reason that increasing this is considered to be CE is that advocates for these communities believe that they are significantly underserved by banks, and that this lack of service is imposing a harm on the community and its residents.

Which Managers Are Interested?

There is a wide range of managers that are interested in how to expand services in low-income neighborhoods. The reasons for their interests tend to differ fairly dramatically depending on where in the bank's organization they sit. For example, managers at the local level typically see expansion into low-income markets within the context of increasing sales of existing products and services. In contrast, managers at the division level typically see expansion into low-income markets within the context of entering or leaving particular lines of business and particular geographies. Finally, executives at the top levels in the bank typically view the decision to expand services in low-income communities primarily in the context of its impact on the public relations for the bank as a whole. This is because the size of the low-income market is usually quite small relative to the entire market for the bank's services. For example, Neighborhood Housing Services of America, which is a national network of NGOs originating home mortgages in low-income neighborhoods, lends $500 million per year in home mortgages across the US. While this is a respectable number, it is only is 0.5% of the total $1 trillion mortgage market. Accordingly, increasing overall bank profitability by increasing product sales to low income communities is usually not key focus of senior management.

What Indicators Are Used?

Managers at the local level and division level tend to use the following indicators:

- Total dollar amount and number of loans that can be originated and sold (now and in the future)
- Performing loan volume, as measured by delinquencies and total losses
- Total dollar amount and number of deposit products
- Pricing for deposit products
- Fees earned from credit products, deposit products and banking services
- Transaction costs for credit and deposit products

Managers at the senior level tend to use less quantitative measures. They tend to be more interested in understanding how expanding banking services can help to improve the bank's image. The one quantitative measure that is frequently used is the impact of the investment on the bank's Community Reinvestment Act (CRA) rating. This rating is reviewed carefully by regulators, and comes under particularly intense scrutiny when a bank is seeking to acquire or be acquired by another bank.

What Drivers Affect Expansion of Services?

DRIVERS SUPPORTING EXPANSION

There are many drivers that are moving banks toward expanding the products and services that they provide in low-income neighborhoods. The clearest driver is the ever-increasing competition for sales to customers. The traditional middle and upper income markets are saturated with banking and non-banking institutions, all seeking to provide an ever-widening array of financial products to the same set of customers. Shopping for mortgages on-line makes price and feature comparisons easy, and has increased the competitive pressure that banks feel.

In times of falling interest rates, some of the need to increase sales can be met by refinancing mortgages. However, in times of rising interest rates, this source of additional volume tends to be cut off, and the competition for the remaining customers becomes fiercer.

In addition to competition for sales, there is also increased competition for deposits. Disintermediation - the flight of funds from banks to other investment opportunities - has drained deposits and forced banks to turn to more expensive sources of capital. Any market which can provide banks with loyal customers who will maintain checking and savings deposits is valuable.

There is also regulatory pressure for banks to expand the services they provide in low-income neighborhoods. In America, for example, the Community Reinvestment Act requires banks to track and report their lending activities by geography. Banks receive ratings, depending on their performance in providing loans to the areas from which they draw deposits.

DRIVERS OPPOSING EXPANSION

Even though there are many drivers pushing banks toward providing more services in low-income neighborhoods, there are also many drivers opposing the expansion of services in these neighborhoods. One important driver opposing the expansion of services is the lower average dollar volume per transaction. This is a particularly important consideration for products such as home mortgages. The cost of originating a home mortgage does not decrease proportionately with the decrease in the total dollar amount of the mortgage, while the fees that a bank receives often do. Clearly, if smaller mortgages are priced in exactly the same way as larger mortgages, they will be less attractive to originate, because (on a dollar for dollar basis) they will have higher costs and lower fees.

The same is true for checking accounts. The lower the average dollar balance in the account, the lower the value of the account to the bank. All other issues being equal, it is more attractive to pursue higher-income individuals, who will keep higher average balances, than it is to pursue lower-income individuals, who will keep lower average balances.

A second important driver pushing banks away from expanding services in low income neighborhoods is the fact that most banks now sell the loans that they originate on the secondary markets, rather than holding them in their portfolios. The secondary market has precise standards for the types of loans it will accept, and the average bank customer from a low income neighborhood is less likely to meet these standards than is the average bank customer from a high income neighborhood.

Finally, there is also the issue of cultural barriers. Cultural barriers can keep bank officers from understanding how to sell their products and services in low-income neighborhoods, and may prevent them from being properly able to assess risk in these neighborhoods. This holds them back from being able to successfully do business in low-income neighborhoods.

Examples of Innovation That Expand the Market

PMI Mortgage Insurance Company/Chickasaw Nation

PMI Mortgage Insurance Company is the third largest provider of mortgage insurance in the United States. It has assisted over 1.7 million people in buying their homes, and has over $8 billion in affordable housing commitments.

Home ownership on Native American reservations in the US is stunningly low. While home ownership in the US is approximately 66%, home ownership rate on the reservations is approximately 1%. The low rate of home ownership is due to in part to low income, in part to complex laws regarding property and land ownership, and in part to cultural differences. And yet, despite these historically challenging problems, PMI saw the potential for a $650 million market in serving the home ownership needs of these communities.

PMI's decision to pursue this market, and to develop the innovations needed to make entering the market profitable, were triggered by several factors coming together. The first was the personal commitment of Roger Haughton, its chairman, who saw first-hand the need and the opportunity when he participated in a Habitat for Humanity home-building event on a Native American reservation in North Dakota. The second was the Native American Housing Assistance and Self-Determination Act, passed in 1996, which provided the framework for conventional home mortgage lending on a widespread scale. The third was a partnership with the National Association of Indian Housing Councils, which helped to build relationships with key actors in the community and government.

Working collaboratively with the Chickasaw Nation, First Americans Mortgage, the National Association of Indian Housing Councils, and Freddie Mac, PMI designed a new mortgage insurance product and risk-sharing program. PMI agreed to insure home mortgages originated under this program, assembled a consortium of lenders to make the loans, and enlisted Freddie Mac to purchase the mortgage-backed securities. The product design, which only requires 1% down from the borrower, is innovative in that it involves a shared risk between PMI and the Chickasaw Nation. This risk-sharing arrangement allows PMI to provide this product profitably at a reasonable price. The product has been so successful that PMI was able to open discussions with several other Native American nations within six months of its launch on the Chickasaw reservation. (Social Compact, 1999)

What's Missing?

Although there are many interesting examples of banks that are expanding their services into low-income communities, there is still very little publicly available information about transaction costs for products in these markets. Many banks still are not convinced that this new business will be profitable once transaction costs are factored in.

It is quite difficult to get good information about transaction costs for several reasons. The simplest is that many of the banks that are succeeding in these markets are unwilling to share information about their transaction costs. They regard this information as being highly sensitive and a strategic weapon. They know how to operate in ways that make money. Why tell their competitors?

Secondly, many banks don't have sophisticated cost allocation systems, so that their transaction cost data doesn't reflect true "variable cost" of the transaction. The accounting systems are not oriented toward creating a product by product analysis of profit and loss. Advocates also have not pressed hard for study of transaction costs, because they are worried that transaction costs for services in low income communities may truly be higher, on a dollar for dollar basis, than costs for the same services in high income communities. If this were true, and were made widely known, it might make it harder to persuade banks to increase lending to low income communities.

Potential Approaches for Creating Additional Innovation

The approach taken by PMI and its collaborators provides a good guide to how additional innovations might be created. The first step for any organization interested in creating additional innovations is to assemble a working group of banks, regulators, and community experts who are very interested in expanding the lending that banks do in a particular area of the low-income market. The goal for the working group should be to develop a product innovation that will better enable banks to meet the communities' needs while increasing their own profitability. In addition, the working group should develop ways of measuring costs and revenues, and collect data, that provide evidence of the true costs and benefits of participating in this market and the best ways to conduct a profitable lending business in this market.

Retail Site Selection

What is the Focus of the Innovation?

We will focus on the siting of retail stores in low-income neighborhoods in inner cities. This is considered to be CE because these areas have significantly fewer retail stores per capita than other locations. Advocates claim that the lack of stores creates costs for the inner city resident, including higher prices, lower quality, and less choice. It also depresses land values, decreases the tax base, and reduces the number of jobs available to residents.

Which Managers Are Interested?

In general, the key issue is how a retail chain that has developed a successful strategy and operating format in middle and upper-income neighborhoods can expand that strategy into stores in the inner city. The manager that is responsible for making this decision is the head of the real estate division for the chain. This division has the responsibility for choosing the locations of new stores, and overseeing the construction process.

There are other managers who are interested in data on how profitable stores are in the inner city, and they come from a wide range of job titles, ranging from CEO to VP of Operations to VP of Marketing to Regional VP. These managers, who often champion the cause of inner city locations, typically understand the attractiveness of the density of urban markets, and are interested in expanding into untapped locations. They often are aware that their competitors appear to be successfully operating stores in these locations, and want to be able to do so as well. However, the real estate division is typically the final decision-maker when it comes to choosing a site.

What Indicators Are Used?

The real estate division uses a wide array of indicators, which can be grouped into two sets: indicators that predict how well stores will do before they are opened, and indicators that show how well a store is doing once it is operational.

Pre-Opening Indicators

Before making the decision to open a store, retail chains employ a sophisticated array of indicators and models to create predictions of how well stores will do in particular locations. The models draw data from a wide variety of sources, including information on:

- Population location, density, demographics and purchasing habits
- Foot traffic and vehicular traffic patterns
- Competitor store locations
- Site characteristics (size, configuration, grading, drainage)
- Municipal services and zoning
- Environmental issues

The models differ significantly across the different types of retail stores. For example, models for mass market retail differ from the models for supermarkets, which differ from those for specialty retail. Within each type of retail store, there are different models for high end, mid-range, and discount segments.

Operating Indicators

Once stores are opened, the most important indicators of store performance are sales volume and profit margin. Sales volume typically is measured by sales per square foot, and is a number that companies are often willing to share. Sales volume is not as important as the profit margin by store (or by square foot), because high sales revenue becomes meaningless if the profits are eaten up by higher-than-average operating costs.

Profit margin is usually measured by profit as a percent of sales. Unlike sales volume, which is often shared, profit margin by store is a very tightly guarded secret. This makes it very difficult for organizations that are not already operating in the inner city to predict how profitable their stores might be, even when they have good information about the sales volumes their stores would be likely to achieve.

What Drivers Affect Increased Store Siting?

Drivers Supporting Increased Store Siting

The overwhelming driver propelling companies to site stores in low-income neighborhoods is the need to create revenue growth. Retail store chains perceive that they must either grow or die. High-income and moderate-income communities are already "over-stored". The competition is brutal, and inroads being made by e-tailers are only increasing the pressure. The inner city is an area which both shows significant potential for growth, and a low level of chain competition.

For many chains, a closely related driver is their competitive positioning vis-à-vis other major chains. Even when a cost/benefit analyses suggests that their stores (as currently organized and managed) will not do well in inner-city communities, a significant move by a competitor into a new market can often cause senior executives to feel compelled to develop strategies for maintaining their competitive position by entering the new markets as well.

Anne Habiby of the Initiative for a Competitive Inner City (ICIC) noted a recent example. A major health and beauty aid retailer came to ICIC because it noted that several of its major competitors had high sales volume in low income neighborhoods, and were expanding rapidly in these areas. The retailer did not have many stores in inner city locations, and the stores that it had there were not particularly good performers. The retailer's executives surmised that their competitors must be profitable, or their competitors wouldn't be expanding so rapidly. But their own models indicate that their stores wouldn't be profitable in these locations. They wanted to figure out what type of innovations might be needed in order to duplicate their competitors' success. In this case, direct observations of its competitors showed that they had been able to broaden their product mix and sell mass market items because supermarkets and mass market retailers hadn't penetrated the inner city locations. This suggested ways of adjusting the merchandising of the stores to achieve higher sales and profitability. (Habiby, 1999)

Drivers Opposing Increased Store Siting

Even though chain store managers are extremely interested in growth, there are two powerful barriers that push them away from siting additional stores in inner city low-income neighborhoods. The first is that their calculations predict that inner city locations will not yield enough demand to make the stores profitable. The second is that they are concerned that the culture, values and operations of a suburban chain will not work in an inner-city location.

1. Concerns about store profitability

The economic reality that real estate managers face is that cost of making a mistake in choosing a site far exceeds the benefits of choosing correctly. If a site is chosen in error, the chain bears the entire cost of creating the store. If the site is chosen correctly, the chain gets the profits each year. The costs of creating a store far outweigh the annual profits. Given this economic reality, if the chain does not already have successful sites in the inner city, real estate managers tends to be quite cautious in evaluating new sites in the inner city.

For many retail store chains, the models used to predict store sales show that new stores in inner city locations will not have high enough sales to be profitable. This makes the real estate managers extremely reluctant to recommend opening stores in those locations.

There is data available showing that competitors' stores have high sales per square foot in inner city locations. However, managers worry that these high sales per square foot may not necessarily translate into high profits for their stores. They are concerned that differences in operating costs will lower margins and make stores in the inner city unprofitable.

2. Concerns about transplanting culture, values and operations

Managers whose chains do not have many stores in inner city locations are often concerned that they don't know how to operate in this market. They don't have experience in this market, and they don't have people on their staff who are familiar with (or from) this market. They are afraid of making an egregious mistake in merchandising, advertising, operations, etc., that will not only hurt an individual store, but the brand as well. They are worried about being "terribly wrong".

Retailers are concerned about how to adjust their operations in all categories: inventory, merchandising, management, marketing, and security. They are concerned that they might have to do unusual things in their inner city operations, which may cost them enough additional money to wipe out their profit margin. (Habiby, 1999)

Examples of Innovations That Expand the Market

Target is a favored retailer among inner-city Hispanics. According to a study conducted by ICIC and PriceWaterhouseCoopers, 52% of inner-city Hispanics report making a purchase from Target over a twelve month period, compared to 49% of overall US consumers and 30% of inner-city African Americans. (Habiby, 1999)

Much of the inner-city success that Target has experienced may be due to tailoring an operations and merchandise mix strategy that better meets the needs of inner-city Hispanic consumers. Target's store in the Boyle Heights area of East Los Angeles, a largely Hispanic area since the 1940s, is an excellent example of this. With the help and input of the Boyle Heights community, this store was transformed into a Hispanic-oriented prototype store.

Most of the Boyle Heights store's customization revolved around larger-than-average Hispanic family size and higher levels of spending on children-related products. Target moved the children's department from the back wall corner to front and center. It expanded children's clothing from 30 racks to about 72 racks. It also made the toys section into a full-size department year round, rather than shrinking it after Christmas, and bolstered the supply of the youth-oriented clothing brands which have proved popular with Hispanics. Other non-children related changes included adding more petite sizes, installing bi-lingual shoe charts, stocking more small size shoes and increasing the selection of products used in Hispanic-oriented cuisine. These changes have made Target's Boyle Heights store a great success with the inner-city Hispanic shopper. (Coleman, 1999)

By adopting these subtle deviations from the standard Target format, Target has gained powerful insight into micro-marketing to the inner-city Hispanic customer and competing effectively in inner-city retailing.

A second, and very different example, of how retailers are innovating to enter low-income urban neighborhoods comes from the efforts of Ahold to enter low-income markets in Europe. Ahold is The Netherlands' largest retailer. It is principally focused on food, and employs 230,000 people world-wide.

Ahold saw that operating effectively in deprived urban areas would require working with the government and other companies to create a sound "investment climate". Ahold worked with local government and 9 other non-competitive retailers (including Rabobank and MacDonald's) to develop a comprehensive urban development plan for the Dutch town of Enschede. The plan included investment commitments from each company. The plan is enabling all 10 companies involved to invest and operate successfully in the town, where individual action alone would not have sufficed. Partnership between business and government enabled the creation of conditions for market success, which could not have been created by either side acting alone. (Nelson and Zadek, 2000).

What's Missing?

There is considerable interest among major retail chains in expanding their operations in the inner city. Retailers from a wide variety of segments, including Home Depot, WalMart, K-Mart, Pathmark, Timberland and Old Navy are testing out sites in inner city locations. But many more have not yet committed to expanding into inner city neighborhoods. There are two primary causes for this reluctance. The first is that when the retailers use the conventionally available data in their models, the models predict that their stores will not be profitable. Second, and just as important, many retailers do not see enough examples of success that they think are relevant to their particular niche. The fact that WalMart is doing well in low-income neighborhoods is not a fact that will persuade Nordstrom's to open up a store there. Nordstrom managers will need to see an example of another high-end department store doing well before they will be persuaded.

Potential Approaches for Improving Measurements

There are a number of promising approaches to addressing these concerns. They can be grouped under three headings:

1. Improve the data available to retailers.
2. Help retailers revise and improve their models.
3. Find examples of stores that are thriving in inner city locations and publicize their "best practices".

Improve the data

The data sources that are used by national retail chains to predict profitability in new store locations are often are drawn from national samples, which do not always prove accurate when applied to inner city locations. A number of leading NGOs, including ICIC, Social Compact and Shorebank are pursuing a strategy for developing alternative and better data sources to address this problem. Their research has uncovered a host of new data sources, and ways to revise traditional data sources, that enable retailers to get a much clearer look at the purchasing power, growth rates, and purchasing preferences of inner city communities. The new data often shows attractive potentials masked by traditional data sources.

Improve the models

The models that the retail chains have developed are based on years of work in determining which variables are most useful in predicting sales performance. However, even though the models are sophisticated and well-tested, they have been developed (for the most part) in suburban and high-income settings. Thus, it is likely that revisions to the model—changes in the types of data examined, and the relationships postulated between data and sales performance—can improve the model as it is used in a low-income urban setting. Again, leading NGOs, including Shorebank, are working to develop refined models that are more appropriate for the inner-city setting.

Publicize successes and 'best practices'

Research by a wide variety of organizations has helped to point out clearly that there is a vibrant market for retail sales in inner city neighborhoods. There are literally hundreds of examples of successful retail operations in these neighborhoods. Yet until recently little was known about them, in part because the retailers were often independent stores with no reason to spend time publicizing their success to other retailers. A wide variety of trade associations, NGOs and business schools have taken on the task of documenting these success stories, and developing an understanding of what constitutes "best practices" in these settings. Examples include work performed by the Food Marketing Institute, the International Council of Shopping Centers, the International Franchise Association, ICIC, and the Kenan-Flagler Business School.

Each of the three varieties of approaches has considerable potential to be expanded, thereby speeding the development of retail stores in low-income urban locations, and improving the services and job opportunities available to residents of these neighborhoods.

Homeowners Insurance

What is the Focus of the Innovation?

We will focus on increasing the sales of homeowners insurance to low-income homeowners in inner cities. This is considered to be CE because low-income homeowners in urban settings often do not have insurance coverage that fully protects the market value of their homes from loss. This jeopardizes their ability to rebuild their home or purchase a new one in event of catastrophic loss. Since a home is often a family's single largest financial asset, this places both their living quarters and their financial assets at increased risk.

There are two aspects to this problem. The first aspect is that homeowners in low-income urban neighborhoods often find that they cannot buy enough insurance to preserve or enhance the market value of their assets and their communities. This can occur either because the type of insurance coverage that would let them fully insure the market value of their assets is not easily accessible, or because the insurance is accessible, but it is too expensive for them to afford. If there is a loss, they may be unable to afford the needed repairs, and may end up abandoning their home. They lose their home, which is typically their largest financial asset, and the neighborhood diminishes in value as well.

The second aspect of the problem is that some insurance companies perceive that they cannot profitably sell insurance in low-income urban neighborhoods. A portion of this may be based on perception - insurers find properly and fairly underwriting risks in the neighborhood to be especially challenging, or are biased against the residents of the neighborhood, and so are unwilling to write insurance policies, even though the policies would be profitable. It is especially troubling that several major insurance carriers in the US have settled multi-million dollar suits alleging that they have been selling insurance in ways that are racially biased.

Even though this problem may be based partially on perception, it is also based in economic reality as well. A number of studies of the costs of losses in homeownership insurance show that low-income neighborhoods typically have higher losses per $1000 of insured value. For example, the Insurance Research Council studied costs of loss in eight cities across the US, analyzing the costs for urban neighborhoods versus the suburbs immediately surrounding the city. Its study demonstrated that homeownership insurance losses were significantly higher per $1000 of insured value in low-income urban neighborhoods than for suburban neighborhoods immediately adjacent to the city. Since losses account for approximately 65% of the cost of sales for most insurers, this provides compelling evidence that selling insurance in low-income neighborhoods is, in fact, less profitable than selling similar policies in the immediately adjacent suburbs. (Insurance Research Council, 1997)

Which Managers Are Interested?

As with the banking industry, there are a number of managers at different levels of the organization that are concerned with this issue for differing reasons. At the local or regional level, the key individual is the business manager responsible for the business territory in which the low-income neighborhood is located. This manager has broad responsibilities for increasing sales and reducing or avoiding risks in the business territory. He or she is typically quite interested in understanding whether and how increased sales in low-income neighborhoods will affect both revenues and costs. Because the suburbs have been saturated with insurance sales, the inner city often is one of the few areas with an obvious potential for increased sales. However, this potential attraction is mitigated by a concern that the losses may exceed the company's average losses on similar policies, and so make the business unprofitable.

In addition to the regional sales manager, there is often a manager at the corporate level responsible for driving new sales in inner city or ethnic markets. This manager typically is deeply interested with developing new ways of reaching new customers, identifying risks, and writing profitable new business. He or she is often an advocate for these communities within the company, and works with a range of partners to help achieve the goal of increased profitable sales.

In many insurance companies, the managers responsible for public relations also are closely involved with the company's CE activities. In recent years, many companies have explored the urban market through public relations managers, and then evolved to staff this activity with managers whose primary responsibility is defined as increasing sales in urban markets.

At the most senior levels of the organization, the CEO, CFO, and General Counsel are often interested in the company's activities in inner-city markets. As with banking, this is usually not because the inner city has the capacity to add significantly to the company's overall revenues or profitability. The inner city, although important, is typically too small a portion of the overall revenues of large companies to have much effect on the bottom line. Rather, the senior management is concerned that the company should be seen as a good corporate citizen and a good source of insurance for all, regardless of race, gender, or creed. Unlike the banking industry, the insurance industry has not come under federal regulation for its investment and sales in low-income communities. In order to continue to avoid federal regulation, the insurance companies must maintain a positive public profile. (It should be noted that senior executives in insurance companies never admit to this as being a motivating factor for their investments in low-income neighborhoods in public statements. However, many expert observers of the industry believe that this is an important motivator for industry actions.)

What Indicators Are Used?

The managers responsible for the business territory, as well as those with responsibility for increasing profitable sales in ethnic or urban markets tend to use the following indicators:

- Total dollar amount and number of policies that can be written (current and future)
- Losses for a typical homeowner being underwritten, including frequency and severity of losses by hazard, and insured losses per 1000 dollars of coverage by hazard
- Current transaction prices for the variety of policies now being offered in the market
- Sales, underwriting, and administrative costs for the types of insurance being written
- Marketing and pricing strategies being pursued by competitors

Managers at the senior level tend to use less quantitative measures. They tend to be more interested in understanding how expanding insurance sales in low-income neighborhoods can help to improve the company's image. They also tend to watch strategic moves by competitors, as well as actions and signals from state regulators and from state and federal legislators.

What Drivers Affect Increased Sales?

DRIVERS SUPPORTING INCREASED INSURANCE SALES

The most important driver is the need for new markets and revenue growth. This is a pressing need for insurance companies of every size and strategy, but is particularly pressing for insurance companies that are publicly traded. Insurance company managers are keenly aware of the fact that the traditional markets that they have been pursuing - middle and upper income individuals - are extremely competitive. They are also aware, at least in the US, that the areas of the market that will have the most growth in the next decade are urban and ethnic neighborhoods. Accordingly, companies are spending considerable time, effort, and money trying to determine the best way to expand their presence in these markets profitably.

Companies also face pressures from regulators, advocates, regulators, and legislators. It is clear that insurers sell less insurance in low-income neighborhoods, and that this has had a disproportionate impact on people of color. This has been a very contentious issue, with boycotts, lawsuits, and threatened regulation coming into play over the past thirty years in the United States.

DRIVERS OPPOSING INCREASED SALES

As noted above, one of the most important drivers holding companies back from increased sales is data showing that low-income areas have higher losses per $1000 of insured value. Prices for insurance policies are regulated on a state-by-state basis, and most states require that policies with similar underwriting characteristics have the same prices over a fairly broad geographic territory. Since location in a low-income neighborhood cannot be used as an underwriting characteristic, this means that policies in low-income neighborhoods must be priced in the same way as similar policies written in higher-income neighborhoods. Accordingly, they are likely to be less profitable.

A second, and equally important, driver holding insurance companies back from increasing sales in low-income neighborhoods is the long time frame required before it is clear whether or not a particular set of policies is actually profitable. In the homeownership insurance business, the homeowner typically pays in premiums of hundreds of dollars each year. Once every two or three decades, the typical homeowner suffers an insured loss, and the insurer has to pay out tens of thousands of dollars. The fact that the losses are very large relative to the premiums, and relatively infrequent, makes it quite hard to know whether the particular policy is profitable or not in the short term. There is a third driver that increases the potency of the second driver. In many states, insurance policies cannot be canceled unless the owner fails to pay, or for other serious cause. Simply the fact that the policy is unprofitable is not sufficient grounds to cancel the policy. These two drivers together - the relatively long time frame required to know whether a particular set of policies is profitable, and the fact that insurers may be compelled to maintain policies even if they are unprofitable - combine to make insurers quite cautious about entering new markets.

Examples of Innovations That Expand the Market

State Farm Fire & Casualty, Nationwide Insurance Enterprise, and Travelers Property Casualty Loss Prevention Partnerships Program

The Insurance Research Council, noted above, showed that the costs per $1000 of insured value were higher in low-income neighborhoods than in nearby suburban neighborhoods. However, Insurance Research Council noted that careful analysis of its data showed that the causes of loss differed dramatically from city to city, implying that these causes of loss might be able to be mitigated through concerted action. For example, the major hazard driving increased loss in Chicago was fire loss, whereas in Philadelphia, the major hazard driving increased loss was water loss. This suggested that understanding and mitigating the factors creating increased fire hazard in Chicago might be able to reduce the loss costs in Chicago's low income neighborhoods down to the same level as the suburbs. If this could be done, it would dramatically increase the profitable market for insurance sales in Chicago. Similarly, attacking water loss in Philadelphia's low income neighborhoods, and reducing it, might increase the profitable market insurance sales there.

Based on this analysis, a number of major insurers, led by State Farm, Nationwide, and Travelers, came together with Neighborhood

Reinvestment Corporation (a nonprofit that supports a national network of nonprofits helping to create homeownership in low income neighborhoods) to create the Loss Prevention Partnerships Program. This program's goal is to assist low-income homeowners to identify and mitigate specific hazards to their homes, thus making the homes safer, and reducing insurance losses as well.

The Loss Prevention Partnership Program will operate in six cities across the United States for the next five years. In each city, there is a local partnership, led by a nonprofit organization specializing in helping low-income individuals buy and maintain homes. The partnership includes local insurers, banks, government agencies, police and fire departments, and insurance regulators. Partnership activities in each city include public education about potential hazards, free home safety inspections, and a low-interest loan fund to assist homeowners to finance mitigation activities, such as the replacement of faulty boilers, overloaded wiring systems, and leaky roofs.

In attempting to mitigate insurance losses, the local partnerships face additional challenges relating to the housing market and the economic realities of the cities and neighborhoods in which NeighborWorks® organizations work. In many of these neighborhoods, real estate values have been appreciating at a lower rate than the prevailing norm. Lower income homeowners typically own their home because it provides shelter, stability, and community — a place to live. Their economic decisions relating to their home (e.g. maintenance, rehab) are usually not driven by the implications for their house as an appreciating financial asset. Likewise, homeowners in these neighborhoods are more likely to face the financial pressures of limited incomes. In this context, it is more difficult to persuade homeowners to invest in loss-mitigation activities such as upgrading wiring or replacing a roof. For example, in very low-income neighborhoods in North Central Philadelphia, the average house sells for $35,000. A new roof can cost as much as $10,000. Accordingly, replacing the roof may not seem like a wise investment. But not replacing the deteriorating roof increases the likelihood of water damage, which is covered under most high-quality homeownership insurance policies.

In order to persuade homeowners that mitigation activities are a good investment, the local partnership has to work with other community development organizations to build a critical mass of interest and activity in the neighborhood, which can help to slowly put upward pressure on home prices. It is this upward movement of home prices that provides incentive for homeowners to view their homes as financial assets, and to start making further investments in their homes. Investments in mitigation activities can help then reduce the frequency and severity of loss, and also increase the value of the homes in the neighborhood.

What's Missing?

While there are a number of very promising approaches to expanding profitable sales of insurance in low-income neighborhoods, there is still a paucity of data proving precisely how and whether increased sales actually make money. As noted above, this is due in part to the long time line required to develop data proving profitability. There is still a pressing need for additional data that explores the cost-effectiveness and profitability of particular approaches to increasing sales of insurance in low-income neighborhoods.

Potential Approaches for Improving Measurements

The partnership noted above provides a good example of a promising approach for gathering improved measurements of the cost-effectiveness and profitability of methods for increasing sales of insurance in low-income neighborhoods. The key issue in any of these projects is to gain approval at the outset for gathering and sharing data that will allow companies to determine cost-effectiveness and profitability. For example, all the participants in the Loss Prevention Partnerships Program have agreed to gather and share data on such key variables as the severity and frequency of loss, the demographics of the neighborhood and the homeowners in which the activities are taking place, and the changes in the insurance market over time. The data will be collated by an independent and respected entity (Roosevelt University), which will issue reports on a regular basis. This will help to ensure that a broad range of companies will be able to benefit from the research, and use it to develop and assess their own approaches to increasing sales in low-income neighborhoods.

Conclusion

This paper has presented many of the most important publicly available quantitative measurements that show the benefit to corporations of increasing their Corporate Engagement (CE). As this paper has demonstrated, there are much credible data showing a variety of benefits to increasing CE. However, it is also clear that many corporations still have not increased CE in most of their functions.

We showed that this paradox has arisen from a number of sources, most importantly because many managers disbelieve in the validity of the studies, and don't see them as being relevant to the particular issues and circumstances that they face. To respond to this issue, we developed a framework for understanding the goals and concerns of managers, and for presenting case examples and research studies to disbelieving managers in a way that is persuasive and compelling.

Our review highlighted the following key results:

1) Disbelievers can be right. Many of the studies that purport to show benefits do not, in fact, prove their point. Some are poorly designed; others use unreliable indicators; some show that there is a financial benefit, but don't show the cost required to attain that benefit, or the relevance of the benefit to the underlying business strategy.
2) Disbelievers are often wrong. There are many well-crafted, reliable studies from reputable sources that do show business benefits to increasing CE. The most compelling evidence shows that CE can create significant business benefit when it is clearly linked to a core business goal or strategy. Dismissing this evidence is often rooted in misunderstanding, fear and ignorance rather than calculated assessment.
3) Disbelievers are increasingly mistaken to dismiss the potential benefits from CE. This is because of the potential impact of CE on the ability of companies to build and manage their knowledge base in a way that enables financially attractive innovation in products and processes.

This paper reflects some of what we have learnt from the disbelievers, and offers some concrete advice for those who will similarly engage in such conversations in the future. Clearly, although there is much that is known about when and how CE creates business value, there is much yet to be learned. We welcome feedback, criticism, and information about additional evidence both supporting and challenging our views.

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Appendix A: Contacts for the Study

US Contacts

Lisa Acree	Business for Social Responsibility
Richard Anderson	RIA Group
Ruth Bass-Green	Mount Holyoke
Bill Boler	Business for Social Responsibility
Torrance Childs	Fleet Boston
David Collins	Johnson and Johnson (ret'd)
Barbara Dyer	Hitachi Foundation
Phyllis Eisen	National Association of Manufacturers
Mark Feldman	Cone Communications
Mindy Fried	National Work Life Institute
Paul Fronstein	Employee Benefit Research Institute
Ellen Galinsky	Family and Work Institute
Mary Gentile	Aspen ISIB
Ruth Green	Markle Foundation
Ann Habiby	Initiative for a Competitive Inner City
Kirk Hanson	Stanford Graduate School of Business
Bill Hanson	Massachusetts Institute of Technology
Lisa Hicks	Jobs for the Future
Fitzroy Hillaire	Avon
Robin Hodess	Carnegie Council
Helen Hopkins	Timberland
Michele Kahane	Ford Foundation
Jill Kassner-Lotto	Work in America Institute
George Knight	Neighborhood Reinvestment Corporation
B. J. Kyzr-Sheeley	Walker Information
Jessica Laufer	Laufer/Green/Isaac
Stan Litow	IBM
Dona Long	NMSDC
Jack Mills	Jobs for the Future
Edgar Murphy	Nortel Networks
Melanie Oliviero	MacArthur Foundation
Amy Perler	Cisco Systems
Todd Pittman	Neighborhood Reinvestment Corporation
Pete Plastrik	On Purpose Associates
Rafael Reyes	ICIC
Joel Rogers	Center on Wisconsin Strategies
Jeffery Schmidt	Towers Perrin
Joy Sever	Harris Interactive
Nancy Sharp	Lucent Technologies
Neil Smith	SmithOBrien
Ursula Surgalski	Applied Materials
Gail Snowden	Fleet Boston
Judy Taylor	Jobs for the Future
Julie Vickers	Compaq Computer
David Vidal	The Conference Board
Sandra Waddock	Carroll School of Management
Jim Walsh	University of Michigan
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UK/European Contacts

Most of the individuals on this list were contacted by Peter Raynard, as part of work he performed for this project.

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Jenny Edwards	DARAJA
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Bill Eyres	Co-op Bank
Thomas Fisher	NEF
Albert Fisher	Social Venture Network Europe
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Beth Ginsberg	Probus
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Craig Mackenzie	Friends Provident
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Peter Rogan	CWS
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Ros Tennyson	PWBLF
Virginia Terry	Sustainability
Fran Van Dyke	Sustainability
Alexis Vaughn	Sustain
Perry Walker	NEF
Liz Walton	Social Exclusion Unit
Helen Wesly	Centre for Tomorrow's Company
Jennifer Woodard	PriceWaterhouse Coopers

Appendix B: Resource Websites

Websites for US Organizations

Aspen ISIB, www.aspeninst.org/isib

The Aspen Initiative for Social Innovation through Business (Aspen ISIB), a policy program of the Aspen Institute, encourages business to engage and invest in solutions to problems that undermine social and business environments.

Business for Social Responsibility, www.bsr.org

BSR's mission is to be the leading global resource providing members with innovative products and services that help companies be commercially successful in ways that demonstrate respect for ethical values, people, communities and the environment.

Center for Work and Family, www.bc.edu/bc_org/avp/csom/executive/cwf/frames.html

The Boston College Center for Work and Family, located within the Wallace E. Carroll School of Management, is a research organization dedicated to increasing the quality of life of working families by promoting the responsiveness of workplaces and communities to their needs. The Center uses three core strategies to pursue its mission: research, workplace partnerships, and communication & information services.

Cone Communications, www.conenet.com

A strategic marketing communications firm with a passionate commitment to the new and innovative.

Employee Benefit Research Institute, www.ebri.org

EBRI seeks to contribute to, to encourage, and to enhance the development of sound employee benefit programs and sound public policy through objective research and education.

Families and Work Institute, www.familiesandworkinst.org

The Families and Work Institute addresses the changing nature of work and family life.

Initiative for a Competitive Inner City, www.icic.org

The Mission of the Initiative for a Competitive Inner City is to build healthy economies in America's inner cities that create jobs, income and wealth for local residents.

Jobs for the Future, www.jff.org

Jobs for the Future's goal is to devise and disseminate strategies that engage young people and adults in their own learning and equip them to shape their futures.

Markle Foundation, www.markle.org

The Markle Foundation advocates communications media and information technology to change the world.

Neighborhood Reinvestment Corporation, www.nw.org

The Neighborhood Reinvestment Corporation, a national nonprofit, was created in 1978 by an act of Congress to revitalize America's older, distressed communities by establishing and supporting a national network of local nonprofit organizations.

National Minority Supplier Development Corporation (NMSDC), www.nmsdc.org

Providing a direct link between corporate America and minority-owned businesses is the primary objective of the National Minority Supplier Development Council, one of the country's leading business membership organizations. It was chartered in 1972 to provide increased procurement and business opportunities for minority businesses of all sizes.

Work in America Institute, ww.workinamerica.org

Work In America Institute's mission is to advance productivity and the quality of working life through the principles of sound human resource practices which are applicable in all industries.

Websites for UK/European Companies

Business in the Community, www.bitc.org.uk

Members of Business in the Community are committed to developing business and community excellence by continually improving, measuring and reporting the impact their business has on their environment, workplace, marketplace and community.

Centre for Tomorrow's Company, www.tomorrowscompany.com

The Centre for Tomorrow's Company provides a network of people at the forefront of a growing, influential movement which aims to make a real and meaningful difference to British business culture and success. Its mission is to inspire and enable tomorrow's companies to compete with the world's best.

The Institute for Social and Ethical Accountability (ISEA), www.accountability.co.uk

ISEA was founded in 1996 as an international membership organisation, based in the United Kingdom. It is a professional body committed to strengthening the social responsibility and ethical behaviour of the business community and non-profit organisations.

The Prince of Wales Business Leaders Forum , www.pwblf.org

The Prince of Wales Business Leaders Forum is an international educational charity set up in 1990 to promote responsible business practices internationally that benefit business and society, and which help to achieve social, economic and environmentally sustainable development, particularly in new and emerging market economies.

Sustainability, www.sustainability.co.uk/sustainability.htm

Our mission is to help create a more sustainable world by encouraging the evolution and widespread adoption of thinking and practices which are socially responsible, environmentally sound, and economically viable - satisfying the 'triple-bottom line of sustainable development'.

John Weiser is a partner in the firm of Brody • Weiser • Burns. John specializes in working with organizations to shape business strategies that achieve social goals. He provides assistance with strategic planning, business analysis, and the development of business/community partnerships. John co-founded Brody • Weiser • Burns in 1984 to pursue his vision of business as a force for social change, after two years with the Boston Consulting Group. He is the author of several papers on the business case for corporate involvement.

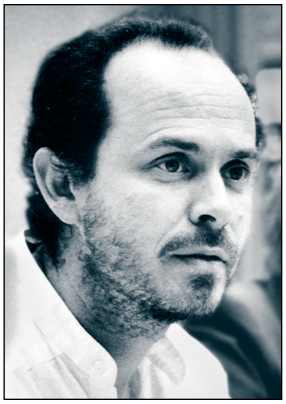
John graduated magna cum laude in mathematics from Harvard University. He holds a Masters Degree in Public and Private Management from the Yale School of Organization and Management.

Recent client engagements include the following:

- National Home Safety Partnership. John worked with staff from the Ford Foundation and the Neighborhood Reinvestment Corporation (a nonprofit organization focusing on housing and community development issues) to create the National Home Safety Partnership. This is a coalition of homeowners insurers, city agencies, foundations, and community-based organizations that is working to make homes safer and to reduce insurance losses in six cities across the US. Activities include safety education, free home inspections, and long-term, low-interest loans for home repairs. Major funding for this partnership has been received from insurance companies, including State Farm, Nationwide, and Travelers, and from the Ford Foundation.
- Ford Foundation Corporate Involvement Initiative. John served as one of the managing consultants for this Initiative from 1994 to the present. The Corporate Involvement Initiative has developed a number of promising new models for corporate engagement, created a database of best practices, and produced a wide range of seminars, conferences and marketing materials aimed at broadening awareness and interest in these new approaches.

John can be reached at johnw@brodyweiser.com. For more information on client engagements and publications, see the firm's web site: www.brodyweiser.com.

Simon Zadek is Chair of the Institute of Social and Ethical AccountAbility, having been Development Director of the New Economics Foundation and Chair of the Ethical Trading Initiative until the end of 1998. He is currently Visiting Professor at the Copenhagen Business School.



Simon works internationally as advisor, external reviewer and trainer, currently for example with the Land Bank (South Africa), Novo Nordisk (Denmark), and The Body Shop; at the governance level of multi-stakeholder alliances - for example he is on the Steering Committee of the Global Reporting Initiative, the Operating Council of the Global Alliance for Workers and Communities, and the International Advisory Committee of the Copenhagen Centre; and through his research and writing.

His publications in the field include *Building Corporate Accountability* (with Peter Pruzan and Richard Evans), *Making Values Count* (with Claudia Gonella and Alison Pilling) and more recently *Partnership Alchemy* (with Jane Nelson), *Ethical Trade Futures*, and *Unlocking Potential: the New Business Case for Employing Disabled People* (with Susan Scott-Parker). He has written on diverse topics such as environment and trade, innovation and social responsibility, indicators for sustainable development, Buddhist economics, social entrepreneurs, utopia and economics, and sustainable consumption. He is currently completing a book entitled *The Civil Corporation*.

Simon can be contacted at zadek@csi.com and further information on his activities and publications can be found at www.zadek.net.