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Value Creation through Voluntary Sustainability Initiatives

Case Study Research on Strategies for Sustainable
Competitive Advantage

Summary:

Through mapping how firms create value with CSR in general and inter-organizational voluntary sustainability initiatives in particular, the author creates a strategy matrix that links CSR-strategy to firm strategy and gives clear recommendations to managers on which out of four generic CSR-strategies to pursue.

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I would like to send a few words of gratitude to my former boss and colleague at the University of St. Gallen, Nils Peters. I thank him for putting so much effort into this project, for believing in my theories, and especially for questioning them.

Peter Beckman, Göteborg

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1. INTRODUCTION

1.1 BACKGROUND

The process leading up to this document started in the spring of 2007. It was in the office of Dr. Joerg S. Hofstetter at the University of St. Gallen in Switzerland. A little earlier that spring he and Nils Peters, a researcher and Ph. D. student, had invited me to join their research project¹ on voluntary sustainability initiatives (VSIs). VSIs are inter-organizational, collaborative, processes in which firms cooperate with non-governmental organizations (NGOs) and other stakeholders to jointly address some social and/or environmental issue. Working as a research assistant, in parallel to my business studies, my first task was gathering data on a large number of VSIs, in order to find suitable cases that we could study more thoroughly. Some weeks after I joined the project we were just about to start conducting case studies and I was getting more and more involved in the project. We were approaching the interview phase and Joerg was explaining the stakeholder perspective to me. With a major in corporate finance I was not ready to accept that the stakeholder perspective was something other than just putting fancy words on the fundamental idea of shareholder value maximization. We had a long and interesting discussion on the subject. After the discussion I still did not fully agree with the concept so when I left Joerg's office my mind was set on understanding how firms use VSIs to fulfill that overriding target, value creation. I had to understand the strategic choices of whether and how to invest in voluntary sustainability initiatives, in order to show that it is not just pure kindness on behalf of a firm's owners that causes firms to start or join a VSI.

¹ The research project is called Inter-organizational design of voluntary sustainability initiatives. More information can be found under:
<http://www.logistik.unisg.ch/org/logm/web.nsf/wwwPubInhalteGer/Interorganizational+design+of+voluntary+sustainability+initiatives?opendocument>

1.2 PROBLEM DISCUSSION

Currently, most large firms have special corporate social responsibility (CSR) reports besides their normal financial reports. Most also have special CSR pages on their websites. Instead of arguing with NGOs, many firms now *cooperate* with NGOs to jointly address social or environmental issues. Observers of this development naturally ask themselves why. While studying a large amount of corporate communication on the issue, I observed that improved social and environmental performance was rarely communicated as a major profit driver. Therefore I asked myself if firms around the world were struck by lightning and like the creature of Dr. Frankenstein came alive with a newly grown conscience. Instead of making profits, were they now thinking that they should be doing “good”? Interestingly, many researchers have found that there is not necessarily a mutually exclusive choice between the two targets and many have even found that more often than not, doing good is connected to doing well (Dowell, Hart, & Yeung, 2000). There does not, however, seem to be a direct, mechanical, relation between CSR and financial performance. In general, one can say that most executives, one way or another, addresses CSR as an issue when formulating corporate or firm strategy. Simultaneously, there is little logical structure or theories to assist those executives in formulating a CSR-strategy that adds value. The issue is therefore interesting to study, especially from a practical perspective and in relation to overall firm strategy.

In parallel to the developments in CSR, another global trend has been evolving. Power has been shifting from national governments to multi-national enterprises and the scope of regulation has been changing from national to global (Egels-Zandén & Hyllman, 2007). Therefore, non-governmental organizations (NGOs) are getting an increasingly important role in the regulative process (ibid) and firms are often cooperating directly with NGOs in their corporate social responsibility (CSR) work. Firms’ social conduct is being regulated on a market basis rather than by governments and this is one reason why voluntary sustainability initiatives, as one form of CSR, are so interesting to study.

Many firms source an increasing share of their products from suppliers in developing countries, where legal requirements often are more relaxed than in Europe or North America. To deal with the many social and environmental challenges connected to this sourcing, an increasing number of firms, especially in Europe and North America, establish VSIs in collaboration with different stakeholders (Schaltegger & Petersen, 2000). An example of this is Unilever, which cooperated with the World Wide Fund (WWF) to establish the Marine Stewardship Council, an initiative aimed at ensuring a sustainable supply of fish (Hamprecht J. , 2006b). A second example is the large number of firms, for example IKEA, Adidas, and Gap Inc., that are, participating in the Better Cotton Initiative, an initiative intended to create a new commodity-cotton, produced according to higher social and environmental standards (bettercotton.org) (Bexell, 2008). Suppliers, competitors, advocacy nongovernmental associations, and governmental agencies increasingly consider participating in this type of initiatives.

If it is the case that CSR efforts are intended to create value, such investments occur in a wide range of industries, and it is uncertain whether it creates value or not, the issue does not differ from other issues of corporate strategy. It also means that treating the issue as a matter of whether CSR creates value or not, as many researchers have previously done, is simplistic and offers little advice to managers who think about whether or not to invest in improving the CSR of their firms. A strategy that is good for one firm is not necessarily good for another. To be able to draw conclusions that are valuable to managers it is therefore necessary to start developing an improved understanding of the diverse issue of corporate social responsibility and its relation to corporate strategy.

The purpose of corporate strategy is value creation (Collis & Montgomery, 2005). The core problem for this thesis is therefore to understand how value is created through corporate social responsibility. On one hand, improving social or environmental performance is costly. On the other hand, if customers prefer responsible firms, customer value is created when corporate social

responsibility is improved. To create shareholder value, the customer value must be transformed into a positive effect on profits, or a risk reduction. When faced with a decision about whether or not to invest in a VSI, as one type of CSR activity, the problem for managers is to, ex ante, decide on if the revenue side is larger than the cost side, at least in the simple case.

Many researchers have studied the tradeoff between CSR and profit (Burke & Logsdon, 1996) and in many cases they have been able to identify mechanisms of how CSR can lead to economic benefits for firms (e.g. *ibid*). These findings are valuable for understanding the issue. For developing competitive strategy, however, they offer little advice, since they do not deal with the issue of relative competitive advantage. If competitors can imitate an initially profitable strategy, the strategy is of little value, unless it makes the entire industry more profitable. Otherwise, the excess profits will be competed away.

Taking a more theoretical view, profitability is the product of on one hand the efficiency with which a firm produces customer value, and on the other hand the share of this customer value that the firm can capture. The efficiency of customer value creation is probably best explained by the resource based view (RBV) (Barney, 1991). The level of customer value capturing is a matter of competition and is probably best explained with Porter's five competitive forces (Porter, 2008).

An interesting dimension of CSR–strategy that makes it different from other areas of competitive strategy is the indirect relation between CSR and firm-value. One may argue that customers prefer sustainable products to other products and that producing sustainability in an efficient manner therefore is the way to go for increasing profits through CSR. This is not different from any other type of differentiation and is probably a good explanation to a lot of the current CSR activities. Still, the amount of firms engaging in CSR vastly exceeds the amount of firms using CSR for differentiation so some additional explanation seems necessary. The fact that so many firms engage in CSR activities suggests that firms feel forced to engage in these activities and therefore institutional theory might offer some explanatory power.

There are many formats for working with CSR. I have found voluntary sustainability initiatives (VSI) particularly interesting since they add another dimension to CSR; collaboration between NGOs and business. The objectives of firms and NGOs appear to be different, or sometimes even contrary, to each other. Firms are generally trying to maximize shareholder value while NGOs are trying to minimize the problems related to some social or environmental issue. If improving social and environmental performance does not enhance firm-value there is no incentive for firms to voluntarily work together with NGOs in VSIs. Simultaneously, if VSIs do not help NGOs with their target of improving social and environmental standards it is not meaningful for NGOs to cooperate with companies in such initiatives. The fact that firms and NGOs *do* cooperate suggests that the two targets are not contrary, but rather that both firms and NGOs can pursue their targets more efficiently if they cooperate. VSIs must, therefore, be expected to create value *and* create social or environmental benefits. This relation is the final reason why I have chosen to study VSIs. It could, of course, be the case that managers take their businesses into such initiatives for personal reasons and thus create agency cost. The sheer amount of VSIs and general CSR activities does, however, suggest otherwise.

1.3 PURPOSE

Up to this point, research on CSR strategy has often focused on *if* social and environmental investments add value to firms. With this thesis I have tried to start developing an understanding on the question of *for which* firms social and environmental investment makes sense.

MANAGERS ARE FREQUENTLY PUZZLED WITH THE QUESTION OF WHETHER AND HOW THEY SHOULD ESTABLISH A VOLUNTARY SUSTAINABILITY INITIATIVE. MY RESEARCH AIMS TO SUPPORT THEIR DECISION-MAKING.

2. METHODOLOGY

This chapter will describe the choice of methodology and how the research project has been carried out.

For several reasons I have chosen to focus on voluntary sustainability initiatives. Firstly, such initiatives deal with one issue at a time and therefore offer a comprehensible unit of analysis. Secondly, the fact that NGOs participate in the initiatives means that it is reasonable to expect that the initiatives actually do improve corporate social and environmental performance. Thirdly, the multi-stakeholder aspect of VSIs makes sure that I, as a researcher, can get different views on the issue.

2.1 CHOOSING METHODOLOGY

As voluntary initiatives constitute a relatively new research field, I argue that the concepts will need to be developed in exploratory research. To date, the number of firms that have established talks on voluntary sustainability initiatives is not large enough yet to allow for a large-scale quantitative research approach. Much can be learned from studying previous research on corporate social responsibility but additionally some cases must be studied more carefully. The reason foremost to be able to understand the value-creating process more thoroughly and partly because VSIs have not been the normal research object in previous studies on how CSR add shareholder value. The qualitative nature of the problem at hand, understanding how firms use VSI to create value, also motivates the chosen research approach. Yin (2003) claims that when *"a 'how' or 'why' question is being asked about a contemporary set of events, over which the investigator has little or no control, case study research has a distinctive advantage over other methodology strategies."* Clearly, this is the case here.

My data analysis method has been that of constant comparison (Glaser & Strauss, 1967). The constant comparison method can be described as a process

where data is collected, hypotheses are made, more literature is studied, additional data is collected, new hypotheses and themes are identified and so on. This method was chosen because it is well suited for developing rather than testing theories (Glaser & Strauss, 1967, p.103 - 105), as is the objective of this thesis. The main tools I used for the analysis were process sheets, describing the initiatives as they developed over time; tables of interesting quotes; and also a large amount of notes on different observations and reflections. All these were developed over time as I found new information and suggested new concepts and theories.

It is important to clearly state that I have been trying to develop, rather than test, theories. It is important because the choice between testing and creating theory greatly affects the decision on what type of methodology to use. Glaser & Strauss (1967), the fathers of the grounded theory methodology, states that: *“conflict is created when sociologists do not clearly and consciously choose which will receive relative emphasis [testing or creating theory] in given researches because of too great an adherence to verification as the chief mandate for excellent research.”*

The grounded theory methodology calls for an open mindset and therefore I started the process without conducting a preparatory literature review. Instead I started by gathering data on a large number of VSIs. These were found by browsing the websites of firms and NGOs, and by searching in databases for both scientific and news articles. After this initial scan of the VSI-universe I started to conduct case studies. As the case studies developed over time and as I saw a need of new angles of observation, more literature was added. The most important parts of this theory are described in the theoretical framework section. Most of the theory was added very late in the process. The two most important separate concepts for this thesis are the resource based view and the concept of institutional theory. The largest part of the theoretical framework section is, however, devoted to a literature review over suggested mechanisms for how CSR adds value. Most of the presented theory is used for giving support to logically explained relationships.

2.1 CASE SELECTION

Considerate case selection is vital for ensuring the construct validity as well as the internal validity of the case studies. In quantitative research, construct validity examines the degree to which a scale measures what it claims to measure (Churchill, 1979). In case study research construct validity is determined throughout two research phases: the case selection and the data analysis. Throughout the case selection, I determine construct validity by selecting cases that are suited for verifying the studied phenomena. The main problem to overcome in order to fulfill the purpose of this thesis is to understand the value creating logic of CSR. That means that for the construct validity it is important that I study initiatives that are truly intended to create value *and* are also expected to create social and/or environmental benefits. The participation of both firms and NGOs in the studied, voluntary, initiatives is the primary argument for sound construct validity. As was mentioned earlier, those are the overriding objectives of firms and NGOs respectively and their joint and voluntary participation implies an intention to fulfill both objectives.

There are a large variety of different types of voluntary sustainability initiatives. Because of this, in combination with the limited time available for the study, the scope of the different types of initiatives to study must be limited. For two reasons I chose to examine voluntary sustainability initiatives that are including *multiple* stakeholders: First, these roundtables enjoy a greater societal support (Peters et al. 2007). Second, the study of roundtables involving several stakeholders allowed me to gain access to multiple sources of evidence. Through being able to gain data from multiple and diverse parties, I could even more firmly ensure the construct validity of the case studies (Yin, 2003). For reasons of credibility I also focused on initiatives that are externally monitored. I also focused on initiatives that mainly affect firms' supply chains. By studying supply-chain affecting initiatives the study was limited to initiatives that demand firms to change its business activities. Therefore it was possible avoid so called "green-washing" initiatives. "Green-washing" refers to firms trying to

improve their social and/or environmental performance through philanthropic activities such as for example donations, i.e. activities that eases a firm's bad conscience but does nothing to change the business itself.

To identify a broad range of initiatives, partly to get an overview of the universe of VSIs and partly to identify potential case studies, I searched the Internet and consulted researchers with more experience in the area. I then gathered more information on 78 initiatives in an excel sheet with brief but structured descriptions, a long-list. I then applied the previously mentioned criteria to the long-list in order to narrow down the amount of potential case study initiatives. I then had a short-list of initiatives that I studied closer individually to decide on the most suitable initiatives.

The purpose of this study is, as was stated in the introduction, to draw conclusions that are valuable to corporate strategy decisions. To do that, my approach has been that understanding how competitive advantage is created for a firm within a voluntary sustainability initiative is of outmost importance. A firm could of course pursue the same targets without cooperating with further stakeholders and therefore it has been my emphasis throughout the process to try to understand how firms use other parties of the initiative for value creation. The first case I studied, DressCode, was devoted especially to this end.

DressCode, also known as the Swedish Clean Clothes Campaign, was an ambitious attempt to create a system for external monitoring of the supply chains of the Swedish apparel industry. The initiative did, however, fail before it was implemented in the the participating firms. The focus of the DressCode case analysis was at understanding the roles of the different participants and the bargaining of resources during the initiative creation. The fact that the DressCode initiative failed made it especially interesting to include in the study since it offers a clear contrast to more successful cases. The fact that it failed also implies that there was some inherent friction in the initiative. Because of this friction I expected to be able to more clearly be able to observe the bargaining between the different participants.

The second case I studied was the Roundtable on Sustainable Palm Oil (RSPO). It is an initiative that was started by the major Swiss retailer Migros in collaboration with the World Wide Fund (WWF) and it is addressing the social and environmental issues regarding palm oil production. The reason for choosing this initiative was firstly that it fulfills the criteria that I set up earlier, namely: NGO involvement, external monitoring and supply chain impact. Further, it has been a highly successful initiative with clear proof of institutional change. Since VSIs normally aim at setting a new social or environmental standard I was looking for a successful case that had received the support of a large number of competitors. This case was probably one of the most successful cases of all the 78 in the long list. The initiative had been scientifically studied before which was advantageous for two reasons. First, the screening of initiatives can only be brief and there is a risk of choosing initiatives that later turns out to be less suitable than they initially appear. Choosing a previously studied initiative made me certain of getting at least one that met my criteria also after a thorough investigation. This of course does not make the initiative more interesting per se but due to the large amount of time it takes to conduct a case study it was important to make sure that at least one had been successful. Naturally, choosing an already studied initiative also reduces the amount of time that is necessary for conducting the case study

I have further on studied the Better Cotton Initiative (BCI), an initiative by the International Finance Corporation (IFC) and WWF. The IFC is the corporate branch of the World Bank. Even though it has not yet defined a standard for what better cotton is, the initiative has gained the support of many important cotton purchasers around the world such as IKEA, Adidas and Wal-Mart. At the time of writing this thesis the BCI is collaborating with different stakeholders, such as cotton farmers, in cotton producing areas around the world. The BCI aims at setting the global standard for a new class of cotton that is meant to substitute the current commodity-cotton with a more sustainable one.

The RSPO-case is used extensively in chapter 4, to explain the value creating logic of VSIs. DressCode and the Better Cotton Initiative are briefly summarized in the appendix.

2.2 DATA GATHERING

I structured the data collection process for each case study in four steps. First, to get a general understanding of the case I studied easily accessible sources such as the web pages of the different participants and newspaper articles. This step was done for each of the 78 initiatives in the previously mentioned long-list and it was then done more thoroughly for the initiatives in the short-list.

The second step was to construct process sheets for the three case study initiatives in order to get a better overview, to identify sequential gaps that needed to be addressed in the interviews and to help me in the interviews. Researchers had previously studied two of the chosen cases; DressCode and the Roundtable on Sustainable Palm Oil, so studying their reports started the second step. For the Better Cotton Initiative I used the web pages of the different participating organizations to get a simple process sheet that was then developed during the interviews that followed.

Step three was to conduct interviews with the involved firms. For the DressCode case, interviews were done with Ann-Marie Heinonen, Information Manager of KappAhl and Ingrid Schullström, CSR Manager of H&M. Both KappAhl and H&M are Swedish clothing retailers that were founding members of the DressCode initiative. For the Roundtable on Sustainable Palm Oil I interviewed Johann Züblin, Head of Standards and Social Compliance at Migros Switzerland and Dr. Marcus Rehm, Director for Sustainability Management at the board office of the German bank West LB. The Swiss retailer Migros was the initiator of the RSPO and West LB is a member of the RSPO. For the Better Cotton Initiative, interviews were conducted with Lise Melvin, the initiative manager of the BCI; Henrik Lampa from H&M; Anna Bexell from IKEA; Dr. Jason Clay from the WWF US; and Mark Eckstein of the IFC. All interviews except the one with Johann

Züblin were conducted as telephone interviews. Johann Züblin I met in the MIGROS headquarters in Zürich, Switzerland. That interview and one of the two interviews with Anna Bexell were conducted together with Nils Peters, a researcher at the University of St. Gallen; I conducted all other interviews. Anna Bexell was the only interviewee who took part in two interviews. The reason for not interviewing NGO representatives in the DressCode and RSPO initiatives were that I was not able to get any replies on my interview invitations to NGO and trade union representatives in the DressCode and in the RSPO I was not able to fit NGO interviews into my time schedule. Both the DressCode and the RSPO have, as was previously mentioned, been studied before, why I deem the amount of data on the views on NGOs to be satisfactory.

After each interview the interviewee was given the opportunity to read a transcript of the interview and correct any misunderstandings. The length of the interviews varied between a half and two and a half hours, with the vast majority lasting two hours. In order not to steer the respondents, the interviews were not structured in any specific way other than that they tried to cover all phases of the initiatives.

The last step was to compare the data that was gathered in the first three steps. Critically comparing the different data sources helped me to come up with a reliable description of the different events of the cases as well as their relationships (Pentland, 1999).

3. THEORETICAL FRAMEWORK

3.1 ALTRUISM VS. CAPITALISM

Many authors, corporate executives, journalists, and others claim that firms have responsibilities that go *beyond* their basic responsibilities to society and their responsibility to their owners. The basic responsibilities to society include, beyond the legal requirements, to also adhere to the basic ethical norms in society. Such ethical norms are similar to what one might refer to as common decency. There are some things that you just do not do, no matter what the law says. Further-going social and environmental responsibilities would mean that firms should do more than is necessary, according to the basic societal norms, and therefore sacrifice part of the owners' economic profit to this end. On this matter, this thesis took its starting point in the view of Friedman (1970) who states that the social responsibility of business is to increase its profits. If corporate executives would be pursuing these further-going targets they would in fact be taking someone else's (the owners') money and spend it on issues of their own choice. This can hardly be justified and even less, be seen as a responsibility. Firms can of course have other objectives than maximizing profits but this is the choice of the owners, not their employees in form of executives. Even more important, the shareholder wealth maximizing view does not exclude investment in social and environmental performance, it only excludes such investment that shows an *ex ante* negative net present value. Therefore my analysis will be based upon the assumption that the initiative participants are trying to add value with their efforts.

This thesis mainly draws on the literature of the resource-based view. The resource-based view argues that a firm's competitive advantage can be derived from strategic resources that the firm controls. Secondly, the thesis draws on the literature on institutional entrepreneurship. Institutional entrepreneurship examines how different actors, such as firms, behave in order to set new societal norms.

3.2 THE RESOURCE BASED VIEW

The resource-based view (RBV) is a theoretical concept that tries to explain a firm's competitive advantage through the resources it controls. In a frequently cited article, Barney (1991) defines resources as *"all assets, capabilities, organizational processes, firm attributes, information, knowledge etc. controlled by the firm that enable the firm to conceive of and implement strategies that improve its efficiency and effectiveness"*. He identifies value, rareness, limitability and substitutability as important characteristics of resources for sustainable competitive advantage.

Important to notice is that the RBV is intended for a specific firm and not for a representative sample of firms (Hamprecht J. , 2006b), meaning that resources are not valuable per se, rather they are valuable to specific strategies. Wernerfelt (1984) explained that resources and products are two sides of the same coin and that observing the resource profile of a firm it would be possible to say what product-market the firm should be in and vice versa.

One specific group of resources that is of a special interest to this thesis is network resources. They are not specifically controlled by the firm but can be used by the firm to create and implement its strategies (Gulati, 1999). Since voluntary sustainability initiatives are alliances it is relevant to incorporate network theory in the analysis of them. A number of researchers have shown that the resources of alliance partners of a firm (network resources) can be transferred through inter-firm interactions and can add value to the focal firm (Lavie, 2006). The larger amount of such resources a firm has, the larger is the opportunity set of that firm (Gulati, 1999).

Lavie (2006) extends the resource-based view to incorporate the network resources of interconnected firms. Lavie looks at how the firm creates value in an alliance by looking at alliances as either pooling alliances (scale) or a complimentary alliance (scope). He sees the alliance formation as a trading of resources where the *"internal rent from the focal firm's own resources will*

depend on positive and negative complementarities with the shared and non-shared resources of its alliance partners”.

3.3 INSTITUTIONAL THEORY

Institutional theory tries to explain firm behavior through the societal context in which it operates. A firm must comply with institutional norms to keep its legitimacy (Bansal P. , 2005). A firm can also influence its societal context, a behavior called institutional entrepreneurship (Powell, 1988). This can be done through, for example, spreading or withholding information from its environmental policy (Bansal & Clelland, 2004). Because it is a target of NGOs, changing societal norms is an inherent target of voluntary sustainability initiatives. Therefore I believe institutional entrepreneurship to be a part of the value creating process that is being studied in this thesis. For example, if firms communicate that they are successful in one field of their environmental policy, they can draw media and NGO attention to this issue and therefore put pressure on their competitors to follow their lead.

3.4 HOW SOCIAL/ENVIRONMENTAL PERFORMANCE LEADS TO COMPETITIVE ADVANTAGE

The idea of profit maximizing firms does not mean that firms should never do better than the basic societal norms. In fact, a large stream of research has shown that investing in social and environmental performance can indeed add value to firms, for example directly through reduced risk (Feldman, Soyka, & Ameer, 1996; Godfrey, 2005) and through positive reputation, brand, effects (Gardberg & Fombrun, 2006).

The basic societal demands are changing over time and it has been shown that a proactive environmental strategy can pay off. For example Nehrt (1996) shows first-mover advantages for pollution prevention in the pulp and paper industry. I will here provide a summary of five different ways in which corporate social

responsibility activities add value to a firm. Later on, these findings, in combination with findings from the case studies, will be used in the next chapter for creating a framework model of how firms use VSIs to create value.

GAINS FROM RISK MANAGEMENT

Godfrey (2005) explains that firms engaging in philanthropic activities will gain insurance-like benefits in two ways: *"(1) the degradation of relationship-based intangible assets will be tempered by positive moral capital (less trust is violated, reputation is not tarnished as much, loyalty suffers but remains, etc.) and (2) punishments and sanctions by stakeholders will be mitigated (stakeholders may forego sanctions altogether or they will impose less severe sanctions than in the absence of positive moral capital)."* Feldman et al. (1996) analyze a sample of 300 large public firms in the United States to see if investments in environmental management lead to risk reduction, and if financial markets value such risk reduction. Their findings suggest that investments in environmental management lead to substantial reduction in the perceived risk of a firm, with an accompanying increase in a public firm's stock price, of perhaps five percent (Dowell, Hart, & Yeung, 2000).

Argenti (2004) argues that firms that are highly visible in the market place and firms that are socially responsible are more likely to be attacked by NGOs. This observation is also supported by Bansall & Bogner (2002). Following this argumentation, highly visible firms should have larger potential gains from risk reduction through CSR. Werther & Chandler (2005) state what they call the *"branding law of corporate social responsibility"*. They define the law as: *"the importance of CSR to any organization is directly related, and rises in proportion, to the value of the firm's global brand."*

GAINS FROM INTANGIBLE STRATEGIC ASSET BUILDING

Fombrun, Gardeberg, & Barnett (2001) argue that *"a citizenship portfolio helps a company build reputational capital and so enhances its ability to negotiate more attractive contracts with suppliers and governments, to charge premium prices for its products, and to reduce its cost of capital."* In the same article they

introduce the concept of *reputational risk*, which they define as “*the range of possible gains and losses in reputational capital for a given firm.*” This is a merging of the insurance concept and the concept of reputational gains which gives a risk/return relationship that is analogue to the risk/return relationship of corporate finance, where the higher the expected return is, the higher is the risk.

Building up a firm’s legitimacy is also building up a resource for competitive advantage since, among other things; it helps the firm with acquiring other valuable resources such as top managers, quality employees, financial resources, technology, and government support (Zimmermann & Zeitz, 2002).

FIRST MOVER ADVANTAGES

For example Barney (1991) explains that the first firm in an industry to implement a new strategy can obtain a sustained competitive advantage through gaining “*access to distribution channels, developing goodwill with customers, or developing a positive reputation.*” This cannot be the case, however, if the resources are homogenous across the industry. To be able to realize first mover advantages a firm must have information about the opportunity that its competitors do not have, otherwise other firms in the industry would implement the same strategy in parallel (Barney, 1991).

Dowell, Hart & Yeung (2000) suggest that “*Interest groups and nongovernmental organizations expose unsound corporate environmental practices, raise consumer awareness, and put pressure on governments to discipline polluters even if the pollution is in overseas locations. Through these means poor environmental performance is translated into bad public image, lower consumer goodwill, and ultimately, lower firm value. Aware of this disciplinary effect, far-sighted managers conscious of firm value opt to maintain a high level of environmental practice, even where regulations do not require it.*”

Lieberman & Montgomery (1988) explains that even though firms can gain first mover advantages through for example technological leadership or preemption

of scarce assets, the advantages can be mitigated by for example free-riding by competitors.

GAINS FROM INSTITUTIONAL CHANGE

What can a firm do if it does not have a relative information advantage and cannot see opportunities before its competitors? The answer is of course to create opportunities, or as Powell (1988) calls it, institutional entrepreneurship. If the idea of first mover advantages is combined with the idea of firms as institutional entrepreneurs that are affecting societal demands (institutional diffusion) we can see that firms can create relative competitive advantage through being first movers. It has for example been shown that firms acting early upon trends in sustainability can realize first mover advantages through affecting the direction of the trends (Falck & Heblich, 2007). If a firm can identify an issue, improve its social and/or environmental performance concerning that issue, and then work together with for example NGOs to raise public awareness on that issue, firms will force their competitors to follow their example through affecting the basic societal demands that all firms must comply with (see e.g. Friedman, 1970). Since the public accepts NGO statements as the truth (Argenti, 2004), collaborating with NGOs will boost the legitimacy of an initiative and therefore also boost first mover advantages. From a resource perspective the value of the resources of the different firms are changing due to changes in the industry structure (Barney, 1991). By being an institutional entrepreneur a firm can try to change the societal demands and the industry structure in a favorable way.

GAINS FROM RELATIONAL RESOURCES

Since there is more knowledge about sustainability in a firm's stakeholder network than only within the firm, a firm's relational resources are valuable for identifying the possibilities for action (Sharma, 2005). To use a financial expression it expands a firm's investment opportunity set.

Lavie (2006) defines a firm's ability to "*identify, evaluate, assimilate and exploit external knowledge*" as absorptive capacity. This resource is valuable to firms

since it allows them to learn from the other parties of the initiative. If a firm engages in a Voluntary Sustainability initiative and have strong relational resources it may be able to build up new valuable resources or reinforce existing ones.

The new or strengthened resources can be used in the initiative itself, they can be leveraged across the firm to be valuable in other business activities and they may be valuable in future business activities. In the future business activities they can be valuable both because they can help the firm in doing these activities better and because they may allow firms to be able to undertake activities that would have been impossible or non-profitable without the new resources.

Another interesting benefit of good relational resources is that when firms build relations to stakeholders and comply with their demands, the stakeholders, such as NGOs, give support to, or at least avoid criticizing, them (Bansal & Bogner, 2002).

TO SUM UP, A FIRM CAN USE VOLUNTARY SUSTAINABILITY INITIATIVES TO HEDGE SOCIAL & ENVIRONMENTAL RISKS, TO IMPROVE THE FIRM'S REPUTATION (BRANDING), TO AFFECT THE SOCIETAL DEMANDS ON BUSINESSES IN A FAVORABLE WAY, AND TO ACQUIRE NEW AND VALUABLE RESOURCES.

4. A VALUE CREATION FRAMEWORK FOR VSIS

The following model is meant to be a framework that schematically summarizes the value creating process of voluntary sustainability initiatives. It was created during the process of this thesis, from literature studies, from reading about a large number of initiatives and while conducting the case studies. In the next section of this chapter, the Migros – palm oil – case will be used to demonstrate the framework.

What makes this framework different from the previously described value creating mechanisms is that it is (1) created with voluntary sustainability initiatives in mind, (2) intended to describe the whole value creating picture, and (3) entirely based on the logic of competitive advantage.

4.1 THE MODEL

Figure 1 is meant to show how firms use VSIs to achieve a sustained competitive advantage. Each arrow shows a close to mechanical relation where one box leads to another. For example, the *identification of issue* step is not only a prerequisite for the *initiative creation* to take place but it also leads to it since if a value adding strategy is identified, it will be pursued. The underlying idea is that managers, in pursuit of value maximization, are rational and therefore only implement strategies that are expected to add value.

Further, *initiative creation* leads to implementation since NGOs otherwise would not have any incentive to participate.

The implementation of a strategy is what directly leads to competitive advantage, which in turn leads to one of two things. Either the competitors are unable to duplicate the strategy, which means that a sustained competitive advantage has been achieved, or competitors can, and therefore will, duplicate the strategy, which per definition leads to institutional diffusion. This

institutional diffusion will, because it is anticipated in a valuable strategy, lead to a sustained competitive advantage, through for example first mover advantages. The exception to this is cases where resource acquisition is the anticipated source of sustained competitive advantage.

The participation in a VSI can lead to the acquisition of intangible strategic assets, such as knowledge and reputational assets. Because such assets are valuable and because they are acquired throughout the process, they lead directly to competitive advantage and are therefore placed beside the central process in Figure 1. In this arrow I also include the acquisition of relational resources, since they are also built up as the firm collaborates with the NGO.

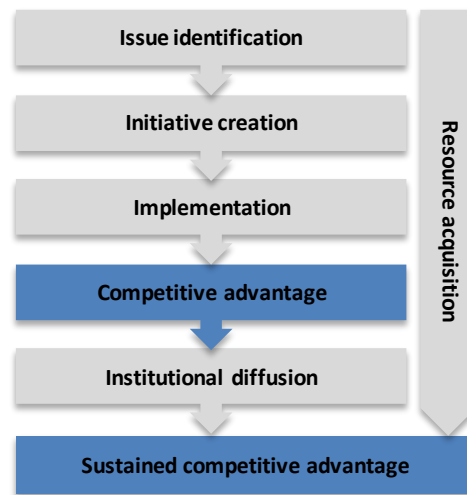


FIGURE 1: ILLUSTRATING THE LOGICAL MECHANISMS OF VSIs LEADING TO COMPETITIVE ADVANTAGE

ISSUE IDENTIFICATION

The process starts with the identification of the issue, for example the negative social and environmental effects of palm oil production in developing countries. The reasons for choosing a specific issue are:

1. Threat (Feldman, Soyka, & Ameer, 1996; Godfrey, 2005)
2. Opportunity (Gardberg & Fombrun, 2006)

According to Sharma (2005) *"the company needs gatekeepers to monitor the objectives and influences of stakeholders and translate this information for the*

internal constituents of the firm." Having good gatekeepers is an absorptive capacity resource that expands the investment opportunity set of the firm. As previously mentioned a good stakeholder network is also a resource that expands the investment opportunity set and also, through helping a firm to identify an issue earlier than its competitors, it helps a firm with realizing first mover advantages. If a firm is able to, before its competitors, identify an issue with potential for a successful VSI and if successful VSIs create value, it would be a source of competitive advantage, following the logic of Barney (1991). Therefore, the successful identification of an issue leads to the creation of an initiative.

INITIATIVE CREATION

The initiative creation phase is when the firm engages external parties to join the initiative, negotiates with the external parties and then jointly develops the initiative, i.e. decides on how, when, and what to do.

Lavie (2006) proposes that: *"the internal rent derived from the focal firm's resources will depend on positive and negative complementarities with the shared and non-shared resources of its alliance partners."* Finding the right partners is therefore of importance.

Lavie also proposes that: *"at the time of alliance formation, the more favorable the contractual agreement, the smaller the relative scale and scope of resources, the more attenuated the relative opportunistic behavior, and the stronger the bargaining power of the focal firm relative to its alliance partners, the greater the firm's ex ante appropriated relational rent will be."* This means that the initiative creation phase to a large extent is a bargaining of resources. If a firm wishes to gain the support of external stakeholders it must intend to implement the measures decided upon in the initiative creation phase and therefore this phase leads to implementation.

IMPLEMENTATION

This stage is where the firm/firms will implement the measures that came out of the initiative creation phase. Here the firm/firms/partners need different

resources, for example supply chain management capabilities, to efficiently and effectively implement the chosen measures.

In the implementation phase the firm executes the intended measures and therefore improves its social and/or environmental performance. If the customers within the industry (or other stakeholders such as financiers or suppliers) appreciate this improvement, it creates competitive advantage and therefore forces the competitors of the firm to also implement similar measures.

COMPETITIVE ADVANTAGE

If the firm has been able to successfully identify an opportunity or threat, develop a strategy, and implement it, the firm should realize above normal returns due to reduced risk or higher expected profits. This should put pressure on competitors to follow a similar strategy in order to, for example, hedge the same risks. This is a first step of institutional diffusion. If the competitors can copy the strategy and realize the same returns the focal firm has only found short-term competitive advantage (Collis & Montgomery, 2005).

NGO support is valuable for a number of different reasons. Especially important is that NGOs are trusted so their statements are accepted as true (Argenti, 2004). If the initiative is successful in implementing its strategy and NGOs support it, this should have a boosting effect on competitive advantage. For example banks and other investors can believe in the risk reducing effects of the initiative and thus reduce the cost of capital; customers will probably appreciate the sustainability improvements more if they trust them and strong stakeholder support should also put more pressure on competitors to change as well. If NGOs have valuable knowledge their participation can allow firms to learn and to create better strategies through an extended investment opportunity set (Sharma, 2005; Lavie, 2006). Finally, NGOs can help firms communicate their efforts (Hamprecht J. , 2006b).

INSTITUTIONAL DIFFUSION

When the partners accept the initiative and when the amount and size of participating organizations reach a critical mass, the initiative becomes the industry norm. The norm, according to institutional theory, will make other, non-participating, organizations comply with the norm. The norm will be the new minimum level requirement for societal acceptance, that is, a level that all firms within an industry must comply with.

An important aspect of VSIs' institutional diffusion is that competitors are allowed to join the initiative. If this was not the case, NGOs would not see the initiative as credible. This means that being part of the initiative and adopting to its requirements will not create a sustained competitive advantage. This further implies that institutional diffusion and asset building are the ways to sustainable competitive advantage.

SUSTAINED COMPETITIVE ADVANTAGE

At this stage, after setting the new standard, all competitors should have an equally good performance regarding the issue of the initiative and therefore the short-term advantages of the participating firms should have disappeared. However, through institutional entrepreneurship, the initiating and the participating firms have jointly been able to affect societal demands in a way that suits their particular resources, creating a sustainable competitive advantage.

RESOURCE ACQUISITION

The resource acquisition effects of participating in the initiative are taken out of the central process since these effects happen throughout the process and lead directly to sustainable competitive advantage. Resource acquisition includes things such as organizational learning and brand building. Depending on its absorptive capacity, a firm will be able to learn throughout the initiative process. The knowledge, relationships etc. that have been accumulated throughout the process will allow the firm to more efficiently and effectively

carry out other initiatives. In other words, learning is building resources for sustainable competitive advantage. If a firm's pioneering efforts are observed and appreciated by the society, these efforts will lead to a reputational gain, which also is a resource for competitive advantage.

4.2 THE MIGROS – PALM OIL – CASE

As we moved into the new millennium in the winter of 1999/2000 Migros, a major Swiss food retailer, identified palm oil as an upcoming issue on the ever-changing sustainability agenda. Palm oil is the world's second most important oil crop after soy oil. Oil palms are grown in tropical areas of Asia, Africa and South America. Due to its high productivity and a globally increasing demand for edible oils as well as for bio fuels, palm oil production has increased rapidly over the last decades, often at the cost of sensitive biotopes such as tropical rain forests. Migros, just as most other food retailers, uses palm oil in many of its products, ranging from margarine to cosmetics. To address the issue, Migros teamed up with the WWF in an initiative to promote sustainable palm oil. Starting with changing its own supply chain and its in-house production, Migros was able to initiate the Round Table on Sustainable Palm Oil (RSPO), the globally largest initiative of the WWF with some 209 ordinary members in January 2008 (RSPO.org, 2008). The RSPO is constantly growing and sustainable palm oil has become an international de facto standard.

The case will now be more thoroughly presented, following the same steps as the value-creating framework.

IDENTIFICATION

For Migros, it was Dr. Robert Keller, the head of R&D at Migros' fats and detergents manufacturing subsidiary MIFA AG who identified the issue (Hamprecht J. , 2006b). On the 10 November 1999, Dr. Keller read an article about the deforestation of Borneo in the Swiss Newspaper Tages Anzeiger. The article was written by Andreas Bänziger and was called: *Instead of tropical wood, Borneo delivers margarine*. Robert Keller realized that this issue didn't

only affect Mifa, but the entire Migros since palm oil is used in so many different products. Keller's first reaction was to write a letter to the editor of the newspaper where he described the relatively small role of European vegetable oil consumption. At the same time he admitted that there was a problem and that new production methods for palm oil had to be established. Dr. Keller now contacted Mr. Johann Züblin at Migros to jointly address the issue. This was a good move since Mr. Züblin had both experience and a personal network concerning rainforest issues.

Mr. Züblin at Migros explains that there are numerous ways for the firm to identify relevant issues. They are getting ideas from inside (like MIFA) and outside (suppliers, "weak-ties" to stakeholders) via email, meetings, etc. It is clear that specific individuals are playing an important role *"depending on specific people and their personal network inside and outside MIGROS"*.

INITIATIVE CREATION

Internally, Migros created a cross-functional working group to deal with the issue. At Mifa, the R&D department tried to reduce Migros' dependence on palm oil through substituting it with sunflower oil. Additionally, Bruno Manser, the founder of the NGO Bruno Manser Fonds, was contacted to get external input on how to solve the problems surrounding palm oil. Bruno Manser had profound knowledge on working with similar issues in the affected regions; he had even been living with the Penan people of Borneo. *"After the first discussions with Mr. Keller we jointly discussed the issue with Bruno Manser. We knew that he lived in Indonesia and therefore had long experience in working with the political and environmental issues in the regions that were affected. In these discussions we tried to use his profound knowledge of this region for jointly developing first attempts of a solution for the problem."*

The contact with Bruno Manser did not lead to long-term collaboration so shortly thereafter Migros contacted WWF Switzerland. Migros had previous experience in working together with WWF. Since 1997 the two organizations

had been cooperating around sustainable wood purchasing and Migros knew WWF as a pragmatic and solution oriented partner. In May 2000 a first meeting was held between Migros and WWF. The first meeting was successful and throughout the rest of the year the two organizations collaboratively developed a list of criteria for sustainable palm oil purchasing.

When discussing what is necessary to get NGOs on board an initiative it becomes clear that the participating firm must have both credibility and also something to offer the participating NGOs: *“Since we [Migros] are the largest grocery retailer in Switzerland we have the sufficient capital and human resources to finance and manage such an initiative”*. Besides the human and financial resources, trust and a good track record in sustainability issues are important: *“Since ethical, social and environmental responsibilities are central corporate values at MIGROS we already had a very similar general attitude to the palm oil issue as the WWF”*. *“We think WWF believed in our good will and our ability to reliably engage in the project since most of our products are produced in our own facilities, which also commit themselves to the MIGROS values to be an environmentally friendly and responsible business.”* For getting NGOs on board, additionally, influence over the supply chain seems valuable: *“We believe that our ability to produce products fulfilling the new criteria was supporting WWF’s trust and commitment to the project.”*

IMPLEMENTATION

In June 2001 Migros decided to adapt to the new criteria (Robert Keller, 2006). The plan was to do it in three steps. First, Migros would switch its margarine production to sustainable palm oil. Second, Migros would switch the entire purchasing of its factories to sustainable palm oil. Third, Migros would demand of external suppliers to only process sustainable palm oil in their products.

Throughout the year Migros started to look for palm oil suppliers who were willing to fulfill the new criteria. Purchasing sustainable palm oil would naturally be more expensive than normal palm oil but through negotiating with several suppliers simultaneously it was possible to keep the expected cost-increase at

moderate levels. Substituting some of the palm oil with sunflower oil also helped Migros with mitigating a potential cost-jump. Migros managed to reduce its palm oil purchasing volume by a third (Hamprecht J. , 2006b).

WWF wanted a third party to join the initiative. They felt that to get sufficient credibility it was necessary to include an organization with experience from similar issues that could help in fine-tuning the criteria and auditing the compliance of them at the plantations. WWF found the Oxford-based firm ProForest. Now Migros had established criteria for and a supply of sustainable palm oil as well as external monitoring and could start implementing their three-step plan.

Johann Züblin thinks that their integrated supply chain was valuable for Migros to effectively put the initiative into action: *“As we have the control over the production of nearly 60% of the products that are sold in our supermarkets we have direct access to the supply-network of palm oil. This allowed us to really implement the new criteria in our products.”*

COMPETITIVE ADVANTAGE

If the initiative has been successful in the first four phases, the firm should be able to realize competitive advantage and therefore add value. This is simply what was already mentioned in the theoretical framework section where reference was made to Dowell, Hart and Yeung (2000) who showed that firms adopting a single stringent global environmental standard have much higher market values. I argue that this effect is boosted by the acceptance of the initiative by normative stakeholders. The mechanism behind this, I argue, works through the lower perceived risk that Feldman et al. (1996) claims to be the reason for the added value of the firm. If, for example, an NGO accepts the initiative, the capital market should see this as a guarantor for the success of the initiative and therefore it should lower the perceived risk and hence add value. An example of how this works practically is the German bank West LB, which sometimes even put RSPO participation in the covenants of lending agreements (Rehm, 2007).

For the same reason, external monitoring should boost the value-adding effect of the initiative. Migros understood this effect and they addressed the issue at an early stage: *“already in the design phase we wanted to see which of our new criteria really could be measured afterwards.”* My reason for categorizing the risk hedging effect as short-termed is that the competitors of the initiating firm could take similar measures and also hedge the risk. There are surely also sustainable competitive advantages to be realized from a voluntary sustainability initiative even without institutional diffusion, most notably the reputational gain from leading the way in the sustainability area.

INSTITUTIONAL DIFFUSION

The final step of the initiative was to expand it to include further partners and to try to make it become a global standard. This has allowed Migros to enjoy a much more passive role and has forced competitors to also buy the more expensive sustainable palm oil.

Institutional diffusion is a result of both efforts directed hereto by the firm as well as a more or less mechanical effect from the success of the initiative. When the initiating firm realizes gains, such as reduced risk, that the competitors also can realize, the competitors will have strong incentive to pursue these gains through duplicating the strategy. Therefore, success of an initiative leads to institutional diffusion. In the theoretical framework I argue why it makes sense for firms to actively pursue institutional change. Take for example investors such as banks. If banks observe risk reduction for firms taking part in the initiative, they can offer the participating firms relatively cheaper capital.

For Migros, communicating with the banks was one channel of putting pressure on other stakeholders to join the RSPO. They did this by explaining to the banks the risks of ignoring the societal demand for sustainable palm oil and by explaining the importance of palm oil in the food industry (Hamprecht J. , 2006b). This raised the awareness of some banks such as West LB, which has now joined the RSPO. In an interview Dr Markus Rehm of West LB explains that they have understood that this is an issue of increasing importance. *“First of all,*

we are an important player in financing many parties in the palm oil supply chain and therefore we want to join the initiative to learn more about this issue and how it affects us." He also explains that the RSPO works as a tool for them when they are trying to convince their clients in working with these issues. Therefore it is important that the RSPO can offer a ready solution that can be presented to clients. Another very important aspect is that the RSPO can offer information and insight into the sustainability performance of current and potential clients. Dr Rehm says that through their participation West LB wants to strengthen the RSPO through lobbying for very clear criteria so that they can be sure whether a client is living up to the expectations or not. Now West LB can even put RSPO participation in the covenants when acquiring new clients.

Migros used several different channels for communicating the RSPO to stakeholders. They used their member magazine, a marketing campaign, and their annual report (Hamprecht J. , 2006b). Another example of how stakeholders contribute to institutional diffusion was when the British NGO Friends of the Earth persuaded Tesco and other supermarkets to work with RSPO. Their basic message to consumers was that a retailer kills orangutans (Smith D. , 2007)². WWF also contributed separately through using the initiative as a showcase in a campaign against rainforest deforestation that they did together with Greenpeace. In August 2002, Migros received a price from the United Nations for their efforts.

The RSPO has been highly successful in achieving institutional diffusion, which is supported by the following statements by Mr. Züblin at Migros: *"As we now have 40 % of the world's demand for palm oil bundled in the RSPO we now have the broad acceptance and purchasing power to simply demand the new criteria for new suppliers of palm oil where we formerly had to convince those suppliers of the benefits of the new approach"*

"It feels as if we have reached a critical mass where new entrants join the initiative by themselves. We can now take a much more passive role. For

² <http://www.guardian.co.uk/environment/2007/mar/25/conservation.theobserver>

example, one retailer that had experienced a lot of pressure from the media called us and asked how to join. We just said that there is the homepage, just read through the information and fill in the form."

CLOSING THE CIRCLE

At this stage of the VSI process a firm can enjoy a rather passive role. The initiative has been institutionalized and competitive advantage achieved. Further, existing resources for institutional entrepreneurship have been strengthened and new have been built. These resources can now be used for creating new

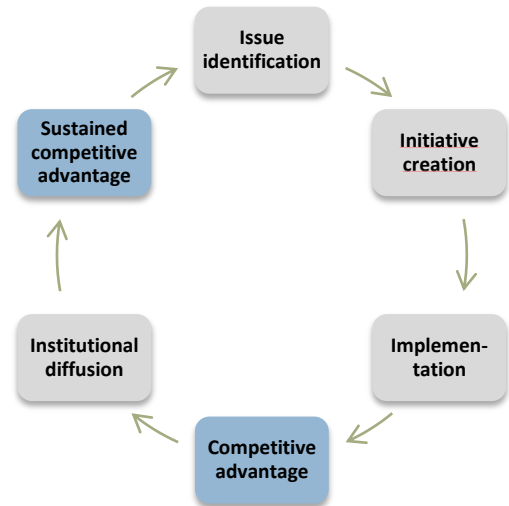


FIGURE 2: THE VALUE CREATING PROCESS BECOMES CONTINUOUS

initiatives. Mr Züblin: "We

learned very much from this process. A lot of the things we can just copy-paste into new projects. For example: When we want to do this for coffee, the people in the purchasing department just say: Ok, we have done this before, it's no problem to do it for coffee as well." The learning is also actively managed in order to draw as many advantages as possible from the initiative: "The problem is that what we've learned is dependent on only a few persons. We are now trying to institutionalize the knowledge. For example, we have created a new position called issue management."

5. DISCUSSION - A CSR-POSITIONING MATRIX

So far, the value-creating logic and process of voluntary sustainability initiatives has been investigated, described and supported. Those findings are interesting per se but far from revolutionizing. In a practically oriented thesis the important thing is discussing the implications of the findings and therefore the last chapter of the thesis is devoted to developing a strategy matrix that is based on the findings in the earlier chapters. The matrix will have two axes, one representing an internal view and one representing an external view on competitive strategy.

THE EXTERNAL VIEW

The literature review showed that sustainability improvements, in the short run, can add value through improving the reputation of a firm and through hedging the risks concerning social and environmental issues. Remembering that the value of a firm is the present value of all its expected future cash flows, (with the larger the cash flows and lower the risk-the higher the value of the firm), this implies that a firm which cash flows are dependent on its reputation, such as a branded consumer goods firm, is more sensitive to its sustainability performance than is a firm which cash flows depend to a greater extent on the traditional price and quality aspects of their products or services, such as utilities or original equipment manufacturers (Werther & Chandler, 2005).

To break down the risk hedging function I suggest that the sustainability risk is the product of the probability of being criticized and the cost of being criticized. Also, the more visible a firm is in the market place the higher is the probability of being controlled by media and NGOs (Argenti, 2004). Summing up the external view, a firm's brand should be a good proxy for the leverage of the risk/return relationship of voluntary sustainability initiatives since firms which cash flows are highly depending on their brand can realize more gains from a proactive strategy than for example utilities or OEMs due to (1) larger potential loss in brand value, (2) higher probability of being reviewed by media or NGOs because of a higher profile and (3) larger potential gains from brand diversification.

From an external point of view, the incentives for differentiating, branded firms to actively engage in CSR are much stronger. Compared to other firms, these firms appear to have much more to win from good sustainability performance and more to lose from poor. The relationship offers valuable insight but does not explain the frequent CSR programs among energy firms or other non-differentiated businesses in cost focused industries. Analyzing the issue from a firm-internal perspective offers some further understanding.

THE INTERNAL VIEW

In the case studies I found that the specific resources of a firm are important for the success of an initiative, for bargaining with the other participants, for implementing the strategy and for affecting societal demands. Hence resources related to those issues are important for creating competitive advantage through voluntary sustainability initiatives.

In the studied cases I observed that NGOs join voluntary sustainability initiatives together with firms in order to efficiently and effectively execute their objectives of improving social and environmental conditions in firms and their supply chains. NGOs can have a similar impact by investigating firms and raising public awareness on different issues to force firms to change their conduct. Doing this, however, means that they must spend resources. If the NGOs instead cooperate with firms, the firms can finance the process so that the NGOs can improve corporate social and environmental performance without raising cost and thereby getting much impact from little effort (cost). To maximize their impact, NGOs want as many and as large firms as possible to join and to have as high improvement requirements as possible on the participating firms. This means that what they want is access to firm resources such as firm size, purchasing power, number of employees, etc. in combination with the necessary firm resources to successfully implement strict standards.

From a firm's perspective their resources are assets that they can use in bargaining with NGOs for their acceptance and support. A firm with large resources should therefore be able to get more exclusivity i.e. a leading role in

the initiatives in which they participate, which consequently should lead to improved relative competitive advantage towards their competitors. Other authors have found the specific knowledge of NGOs to be a particularly important factor (Economist, 2008). The case studies also show that NGO participation can boost the value creation of the initiative in several steps of the value creating model and therefore it can be valuable even for firms with very large market power resources to have NGOs join.

5.1 COMBINING THE INTERNAL AND EXTERNAL VIEWS

Following the previous two sections there seems to be two distinct firm characteristics affecting a firm's choice of a suitable CSR-strategy, the relative importance of a firm's brand, and its resources for institutional entrepreneurship within corporate social and environmental performance. The latter can be boiled down to market power (accumulated good NGO relations are obviously also of great importance but in the long run also these can be boiled down to market power).

Because the two views, the internal and the external, appear to be independent of each other (there are certainly highly influential firms in non-branded industries and vice versa) the two can be put together into a matrix outlining four general CSR-strategies. The four different strategies apply to different firms depending on their resources and their brand values.

For managers the decision on which strategy to follow boils down to two questions: (1) do we have the resources to successfully lead an initiative? (2) Would attention and public praise following our efforts add value to our products or services?

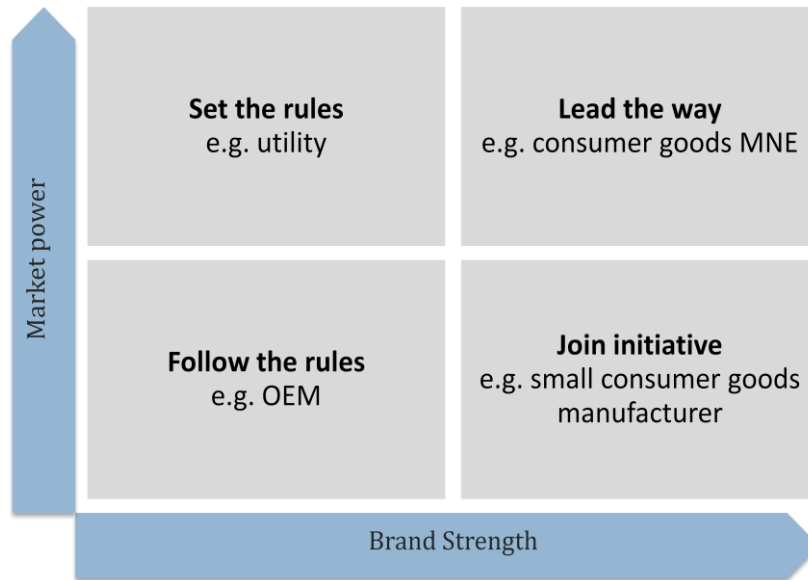


FIGURE 3: A CSR-STRATEGY MATRIX SHOWING FOUR GENERAL CSR-STRATEGIES

FOLLOW THE RULES

The first strategy is the most passive one. Firms that don't have the ability to affect the societal demands or the ability to charge premium prices for superior social or environmental reputation will simply not find it worthwhile to go beyond minimum requirements. An example would be an original equipment manufacturer (OEM), for which customers specify a required quality level and then buy from the manufacturer with the lowest price. For such a firm the most efficient strategy appears to be to follow the basic societal demands and the demands of their customers. Going beyond minimum requirements would not be a differentiating factor since customers specify what they are willing to pay for. A differentiating factor would instead be the ability to produce in a sustainable manner. This would, however, be customer segmentation, not CSR.

SET THE RULES

A firm with much market power is in a completely different situation. A firm that have the resources to affect the basic societal demands but cannot charge premium prices because of superior social or environmental performance could benefit from using its power to change the minimum requirements for itself *and*

for its competitors. Take for example a large energy producer. It might be interested in tight CO₂ regulation if it can use a superior R&D resource to more efficiently than its competitors change its production system to lower emission levels. Such regulation could also be beneficial if the firm already possesses over hydropower plants with low CO₂ emissions. The point of this strategy is not that customers will be willing to pay more because of higher moral standards. The point is that the costs associated with an improved conduct will have a more severe impact on the profitability of competitors. Since minimum standards affect all competitors, prices will go up, causing increased profits to the firms with low relative cost increases.

JOIN INITIATIVE

This strategy is well exemplified by many of the firms that have joined the RSPO after MIGROS or the three smaller firms in the DressCode initiative (see appendix). They did not have the resources to drive an initiative on their own but had, in many cases, strong brands that exposed them to the risk of external critique. Joining an initiative will help hedging the risks but will give them less positive attention and less influence over the initiative than if they would have been driving the initiative themselves.

Staying out of initiatives will expose a firm to risk of being criticized when it does not live up to the new standard. Therefore a firm that stays out of the initiative will be at a disadvantage when it must live up to a standard that it has not been able to affect or even anticipate as efficiently as its competitors in the initiative.

Creating a separate initiative will probably not be a successful strategy either, since such an initiative will be outcompeted by the initiative with relatively larger market power and credibility.

LEAD THE WAY

Firms that in addition to strong resources for institutional entrepreneurship also sell branded products or services, for example large consumer goods multi-nationals, will be able to leverage these characteristics through shaping the competitive environment and simultaneously add reputational value. This

strategy is well exemplified by Migros, which initiated and led the RSPO initiative. Migros had the necessary resources and it was also able to charge premium prices for its products. Even though other firms joined the RSPO later on, Migros is still associated with driving the issue. Through leading the way beyond the rules, Migros was able to both gain reputational advantages and affect the rules in a favorable way.

The difference between branded firms with and branded firms without market power can be made clear when thinking about the way to use so called eco-branding. In Sweden, the major eco-brand in the dairy sector is called KRAV. Smaller competitors in the industry, such as Milko, Skånemejerier, and Falköpings mejeri (falkopingsmejeri.se; milko.se; skanemejerier.se), all use the KRAV label for their eco-products. The Danish dairy giant, Arla, which dominates the Swedish dairy-market, does not, however, brand its eco-products with the KRAV label, even though it sources its ecological milk from KRAV-certified farms. For the smaller players, buying KRAV-milk and adding the label to some products, is an easy way to exploit a market segment, but it will not give rise to competitive advantage, since the strategy is easily duplicated. Arla, on the other hand, can build its own eco-brand, that it controls, and thus gains relative power over the KRAV organization.

THE LOGIC OF THE EXCEPTIONS

It must certainly be possible to find exceptions to the four strategies. There is however some logic that argues that such exceptions would tend to destroy rather than create value. A firm that invests more into its social/environmental performance than its customers are willing to pay for is wasting money since the firm is not paid for its efforts. A firm that is moving to the right in the matrix is building its brand and should take advantage of it in order to sustain or improve profitability. This shift is, however, not necessarily easy. Porter (1998), for example, argued that a firm's positioning involves "*a firm's total approach to competing*". Simultaneously, a firm that wishes to move up in the matrix must acquire the necessary resources to be successful and will otherwise be outperformed by competitors with stronger resources. Take for example first-

mover advantages: Leading the way can create many advantages (e.g. Barney, 1991 and Dowell, Hart, & Yeung, 2000) but being a follower also has its upsides, for example through free-riding (Lieberman & Montgomery, 1988).

Note finally that one strategy is not generally better than the other. It's all about choosing the appropriate strategy for each firm in order to maximize shareholder wealth.

A FIRM THAT HAS STRONG MARKET POWER AND IS NOT USING IT IS NOT MAXIMIZING ITS VALUE. A FIRM THAT HAS A LARGE BRAND VALUE BUT IS NOT SECURING ITS SOCIAL/ENVIRONMENTAL PERFORMANCE IS TAKING UNNECESSARY RISK.

6. REFLECTIONS/FUTURE RESEARCH

This thesis took an ambitious leap from the current state of research to developing a strategy matrix while studying only three cases. Therefore the possibility to generalize the findings is limited. At the current state of research, there is strong logic supporting the model. In order to be able to generalize it into other parts of CSR it is, however, necessary to study it in relation to a broader range of CSR activities. Even though the value-creating model is built on scientific findings from well renowned literature, more cases should be studied in order to find out alternative processes, and for identifying more resources for institutional entrepreneurship. I suggest that task to be the starting point for further on developing the area of CSR strategy.

The contribution of this thesis to strategy science and practice is that it shows that CSR-strategy is an integrated part of business strategy generally and should not be treated as a separate issue. The most appropriate CSR-strategy is determined by positioning and resources.

The creation of this thesis was triggered by a discussion on the logic of the stakeholder perspective and at this point it might be a good idea to refer back to that discussion. I found that CSR is not contrary to shareholder value maximization, a finding that should come as no surprise. Already in 1776 the famous economist Adam Smith (1776) stated:

“It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest.”

Remembering that people, i.e. customers, generally prefer good social and environmental performance over bad, of course companies fulfilling the wishes of their customers create more value. The same thing goes for other stakeholders, such as investors or regulators. The framework that is outlined in this thesis will hopefully help managers structure their thinking on how that value can be captured.

7. BIBLIOGRAPHY

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7.1 INTERVIEWS

DRESSCODE:

- Ann-Marie Heinonen - Information Manager, KappAhl
- Ingrid Schullström - CSR Manager, H&M

THE ROUNDTABLE ON SUSTAINABLE PALM OIL:

- Johann A. Züblin – Head of Standards and Social Compliance, Migros Switzerland
- Dr. Marcus Rehm - Director for Sustainability Management at the board office, West LB

THE BETTER COTTON INITIATIVE:

- Lise Melvin - Initiative manager of the BCI
- Henrik Lampa – Environmental Coordinator, H&M
- Anna Bexell – Global Cotton Coordinator, IKEA
- Dr. Jason Clay - Senior Vice President Market Transformation, WWF US
- Mark Eckstein – Senior Environmental Specialist & Social Development Department, International Finance Corporation (IFC)

8. APPENDIX – CASE STUDY SUMMARIES

8.1 CASE STUDY SUMMARY: THE BETTER COTTON INITIATIVE

The Better Cotton Initiative (BCI) is a VSI aimed at improving the social and environmental impact of producing cotton. Rather than creating a new brand of organic cotton it is focusing on improving the bulk of cotton production, commodity cotton. The initiative was jointly started by the International Finance Corporation (IFC) and the World Wide Fund (WWF).

Mark Eckstein of the IFC and Jason Clay of WWF were both working with agribusiness and commodities in their respective organizations. The two developed a memorandum of understanding between the IFC and WWF, which basically said that they would work jointly on the development of better management practices in selected commodities. The two organizations commissioned research on ten commodities and then decided to move further with four; sugar, palm oil, soy, and cotton. They then initiated a two-day stakeholder meeting around cotton in November 2004 (the four commodities had separate initiatives). In the meeting there were representatives from research, NGOs and private companies. The companies were H&M, Adidas, the Gap, Nike and IKEA and from the financial sector ABN-Amro and Rabobank were represented. The companies all had a relation to IFC and/or WWF prior to the meeting.

When I conducted interviews with the BCI participants in the summer and fall of 2007, the BCI had held a number of stakeholder meetings. The first meet was mainly a two day brainstorming session around what the problems and potential solutions were. The second meeting, in June 2005, focused more on defining the scope of the initiative and also identified organizational needs of the initiative, such as hiring a manager and having a budget. In the third meeting, several new NGOs and companies joined in. In the fourth meeting, in March 2006, the discussions were much more about governance than issues.

This was a turning point in the process since the BCI became institutionalized, in the sense that the ownership of the process shifted away from the initiators to becoming a multi-stakeholder owned initiative.

After appointing an initiative manager, Lise Melvin, in September 2006 and sorting out some of the governance issues, the process picked up speed. It was not until after the fall of 2006 that the governance system of the BCI and the vision and mission was decided. Since then, the number of participants has been growing and approaching its initial target at an accelerating pace.

KEY FINDINGS IN THE BCI CASE:

The BCI gave several interesting findings. It showed the value of NGO relations for firms. All of the firms who have had the most influence over the initiative had relations to the initiating organizations prior to the initiative. The case was also important for understanding the bargaining of influence over the initiative.

An interesting observation over how the initiative has developed is that there seems to be a lot of path dependency in setting up the initiative. The firms who had previously been working with tracking, tracing and auditing their supply chains with regard to codes of conduct were very reluctant to use other forms of systems, which the NGOs would have preferred. This has been a significant obstacle for the process and also shows the importance of learning.

Speaking to Mark Eckstein and Jason Clay was additionally very valuable because of their vast experience from VSIs. Their input made it clear that risk reduction is the main driver behind corporate involvement in VSIs.

8.2 CASE STUDY SUMMARY: THE DRESSCODE

DressCode was a voluntary sustainability initiative in the Swedish apparel industry. Its purpose was to improve the working conditions in the supply chain of the participating Swedish clothing retailers, especially in developing countries. It was a cooperation between four of the largest clothing retailers in the country, H&M, KappAhl, Lindex and Indiska, together with several NGOs,

most notably the young Fair Trade Centre which was a main driving force and finally several trade union representatives. To improve the social standards in the supply chains of the firms the project aimed at formulating a harmonized code of conduct and to put in place a monitoring system for the code.

The project led to proposal of a code of conduct for the suppliers with specified demands for the retailers. The proposal was named DressCode. (The name was never ratified by all parties of the project but is publicly recognized and used in the two articles about the project). The code was based on UN human rights and central ILO conventions but went even further in its demands. Among other things it contained demands of "reasonable salary", "reasonable working hours", "a safe and healthy working environment" and "a demand for the suppliers to primarily offer permanent employment".

The four firms together with the NGOs initiated a number of discussions on how one common code of conduct should look and how to implement independent monitoring of the compliance to it. These discussions constituted the basis for the project that I, and several other authors, call the DressCode initiative.

To evaluate different independent monitoring methods, pilot studies were initiated within DressCode at the suppliers of the four firms in India, Bangladesh and China. Four audits were made by the NGOs and trade unions in cooperation with local organizations (H&M b).

In spite of three years of intense work with significant investments of both time and money from all parties the initiative was never put into action. A long way into the project, all parties were agreeing on the general principles but in 2002 when it was time to put the plan into action the unions suddenly rejected the proposed code of conduct and the monitoring system. The trade unions' withdrawal from the DressCode led to a failure of the entire initiative. The four firms, however, still believed in codes of conduct but they all went their separate ways to perform the audits themselves. In 2005 H&M joined the Fair Wear foundation (H&M b), an initiative that is similar to the DressCode project. H&M also has an own organization of around 50 factory auditors (H&M a).

KappAhl started working with a Norwegian ethical trading initiative (Initiativ for Etisk Handel) and did SA8000 audits through external parties. Later they joined the Business Social Compliance Initiative (BSCI) which has gained strong support with over 80 participating firms, mainly European retailers. KappAhl has been active in developing the BSCI (bsci-eu.org). Also Lindex joined the BSCI and was one of the main driving forces to develop that initiative (bsci-eu.org). Indiska is still conducting its own audits without external monitoring.

KEY FINDINGS IN THE DREDDCODE CASE:

The DressCode case added much value to my understanding of the very important role of credibility in VSIs. It is probably the most important driver for firms to join with NGOs. At the same time, when credibility is at risk for any of the involved parties, it can jeopardize the entire initiative.

The interviews and studied texts showed the de facto bargaining of resources that take place in setting up an initiative. In the larger picture there is also competition between different initiatives, adding an important dimension to the subject.

Ingrid Schullström of H&M mentioned that the initiative enabled firms to work together, which she thinks would have felt unnatural without external parties. This points both in the direction that VSIs create a “neutral ground” and that this allows for collaboration, which in turn is an efficient way for competitors to handle a common threat.