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Review on CSR Issues Based on Value Chain Model and its Implications

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ABSTRACT

Value chain model is usually used to analyze a firm's business value creation activities so as to propose and implement a more scientific business competition strategy to win in the market. This study however, intends to apply this model to explore the CSR issues faced by each line and staff functional department in a business organization and understand the issues in a systematic way. It concludes that value chain is a more systematic model for analyzing CSR issues of a business organization, any ethical problem along the value chain of a firm is unique itself for a specific function involved but its impact is holistic and may be fatal to the firm as a whole. It implies that the understanding of a firm's CSR issues based on value chain model is an important foundation for scientifically managing or preventing the related problem. Only when all the CSR issues in each line and staff function have been managed can a firm handle the real challenge of sustainable development.

Key words: Business ethics, CSR, value chain, analysis, implications

INTRODUCTION

CSR (Corporate Social Responsibility) refers to the balancing practice of interests between different stakeholders of a firm in managerial decisions or business operations. The CSR is also considered to be an umbrella term under which the ethical rights and duties existing between companies and society are debated. The concept of ethics or business ethics can be traced back to the traditional Aristotelian and Confucian cultural values in thousands of years in the human history but CSR is a more modern concept dating back to no more than a hundred year's history when Sheldon (1923) first put forward the idea of corporate social responsibility, arguing that a firm's production should be integrated with the community of nearby human beings, obeying by the law, ethical codes and obligations. In the 1950s, Friedman (1953) put forward the theory of shareholders' interests as the only social responsibility of a firm, arguing that other than the making of profits to investors, any activity taken by a firm was not ethical itself as it violated the interests of shareholders. In the 1980s, however, Freeman (1984) put forward his theory of stakeholders, considering that the interests of a firm should be more than those of the shareholders and they should include

the protection of those of its different stakeholders like customers, suppliers, government, community, employees, managers, etc. In the 1990s, Carroll (1991) put forward his theory of four levels of CSR, including economic CSR, legal CSR, ethical CSR and altruistic CSR. Elkington (1998) put forward his idea of triple bottom lines which covered financial, social and environmental bottom lines rather than the past single profit-making or financial bottom line, to satisfy the three-pronged forks of profitability, environmental quality and social justice.

Value chain refers to all the functional inputs that a firm provides along the process of transforming raw materials to delivered products or services. Value chain analysis model can be traced back to the 1980s, when Porter (1985) published his book of *The Competitive Advantage*, putting forward the world-famous value chain analysis model and at the same time, Kogut (1985) proposed his theory of value chain which also plays an important role for the formation of global value chain theory today. In addition, Gereffi (1994, 1999) and Gereffi and Korzeniewicz (1994) researched on the relationship between commodity chains and global capitalism and the analysis framework of global value chain which has further enriched the related theory of global value chain. In addition, there are other related theories like production

network contributing to the development of value chain theory which focuses on the network relationship between firms and the subsequent formation of larger economic community.

In the existing theories of value chain, however, the focuses of analysis or research have been mainly put on the process of value creation and every functional inputs and outputs involved along the chain in order to reduce operating costs of every function and increase the competitiveness of firms. There are few direct research findings on the relationship between CSR and value chain in the existing academia filed of the world. This study will to make a review on CSR issues of firms based on value chain model and point out some implications for the management of modern business ethics and CSR which may be a new contribution or enrichment to the related theory and practice.

This study will answer the following three research questions: Is value chain a systematic model for analyzing the CSR issues of a firm? What are the ethical problems of a firm’s each specific function along the value chain? What are the implications of understanding a firm’s CSR issues based on value chain model?

LITERATURE REVIEW

Among all the researchers and their theories on value chain as mentioned above, Porter (1985) and his theory of value chain, Kogut (1985) and his theory of value-added chain, Gereffi and Korzeniewicz (1994) and their theory of global value chain, etc., are the most famous and influential.

Theory of value chain: Porter (1985), professor of Harvard Business School, points out in his book of Competitive Advantage that each firm is actually a collection of activities undertaken during the whole process of product design, production, sales, delivery and after-sales service. These activities together can be indicated by the term of value chain. According to Porter (1985), a firm’s value creation is completed by a series of primary activities and support activities (Fig. 1).

Primary activities relate directly to the physical creation, sale, maintenance and support of a product or service. They include inbound logistics, operations, outbound logistics, marketing and sales and service. Support activities provide support, advice, or assistance to the above-mentioned primary functions, including procurement (purchasing), human

resource management, technological development and infrastructure (such as accounting, legal, administrative and general management).

Along the value chain of a firm, all the primary and support activities are different but mutually linked with each other directly or indirectly to form the process of value creation. The value created by a company is the profit margin: Value created and captured-cost of creating that value = margin. The more value an organization creates, the more profitable it is likely to be. When a firm provides more value to its customers, it will build its competitive advantage. Therefore, Porter’s value chain model is a systematic research tool on a firm’s competitiveness.

Theory of value-added chain: Kogut (1985) puts forward his own concept of value-added chain in the study of designing global strategies: Comparative and competitive value-added chains, arguing that value chain is basically a process of various inputs integrating technology, raw materials and labor, then transforming them into finished products and finally completing value circulation through market exchanges and consumer purchases. In the chain of value creation, a single firm may only participate in a certain section, or the firm may take the whole value-added process into its management system of different levels, because the firm’s business activities and technology will have something to do with other firms along the global value chain. The comparative advantage that a nation has determined which section or sections along the global value chain a firm can focus on producing and selling so as to be more competitive.

Compared with Porter’s emphasis on the value chain of a single firm’s competitiveness, Kogut’s idea of value-added chain can reflect the relationship between the vertical separation of value chain and the reallocation of global space which thus paves an important foundation for the theoretical formation of global value chain.

Theory of global commodity chain: Gereffi and Korzeniewicz (1994) put forward the theory of Global Commodity Chain (GCC) in the book of ‘Commodity Chains and Global Capitalism’ based on the analysis of American retailing value chains and the combination of value chain model and industrial organization. Subsequently, Gereffi (1999) illustrates a commodity chain’s framework for analyzing global industries. In the background of economic

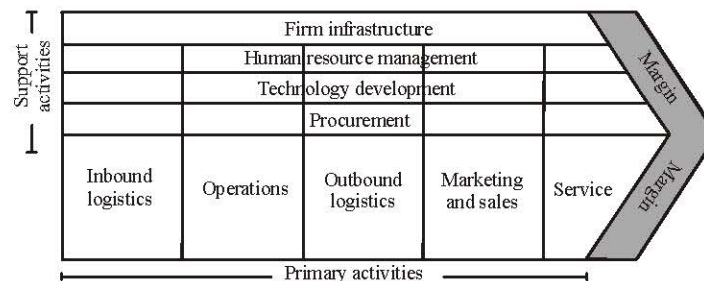


Fig. 1: Porter’s generic value chain, website source: Mind Tools (2014)

globalization, they argue that the process of commodity production is formed by a cross-border production system covering the integrated production network of various different-scale enterprises and establishments along the global commodity chain. In the international production network, any section of the commodity chain will include the input of raw materials or semi-finished products, the supply of labor, transportation, marketing and final consumption, etc.

Later on, Humphrey and Schmitz (2000, 2002), Gereffi *et al.* (2003), as well as Kaplinsky and Morris (2003), respectively make researches on the issue of governance and upgrading in global value chains and their findings have further enriched the field and scope of the related studies. For example, there are four parts of global commodity chains emphasized by Gereffi *et al.* (2003) which should be paid great attention to in the practice, such as input-output, territoriality, governance and institutional framework, among which governance and institutional framework, for example, laws and regulations, norms and principles are in fact the issues which influence the management of global value chains and also the CSR or business ethical issues concerning the competitiveness and sustainability of firms' going global.

In China, there are also some researchers who have done studies on global value chains from different perspectives, for instance, Zhang (2006) makes a study on the transformation and upgrading of local clusters under global value chains; Xie and Li (2007) make an analysis of the industrial upgrading of clusters within the global value chain; previous researchers make a research on the industrial upgrading and industrial garden development under the global value chain; Tan and Ma (2009) make an analysis of myths and realities of China's apparel industry from a global value chain perspective, arguing that China's apparel industry is at the lowest level of the global value chain and most local enterprises have not entered the mainstream global value chain and are still internationally uncompetitive. Lin (2014) makes a speech on the impact of global value chains on China and proposes policy implications. In a word, worldwide scholars and researchers have made a systematic analysis or investigation of value chains, global commodity chains, or global value chains from multi perspectives of definition, governance, evolution, industry and upgrading and on this basis, they have primarily built the concept of evolved value chain and its theoretical

framework of analysis which will be beneficial and important for modern firms and policy makers as references.

Researches on value chain and CSR: Research directions concerning the CSR issue or organizational ethical problem from the perspective of value chain or global value chain are topics of recent academic studies in the academia. De Chiara and Spina (2011) makes a research on the topic of MNCs' CSR and value chain and frames MNCs' behavior within CSR, stressing the importance of a different approach to the management of local resources and stakeholders and arguing for a shift of perspective concerning workers, suppliers and community, from resources to be exploited to partners and co-creators of MNC values. In the previous literature author discusses the issues of organizational ethics from the perspective of value chain in his book of *Business Ethics: NOW*, arguing that along the value chain of a business, CSR issues or business ethical scandals may occur in both line functions and staff functions.

Zhang (2006) in China makes a speech on the relationship between social responsibility and value chain based on the case of Sanlu Tainted Milk Scandal, suggesting that firms' undertaking of corporate social responsibility should have a method to avoid no returns and should integrate CSR and value chain management together to achieve a win-win situation of contributing to society and increasing corporate value. In literature there are some researches on the win-win model for CSR and value chain management and some made an analysis of wine firms' CSR issues occurring from raw material supply to consumer consumption which is much closer to the present research topic but lacks a kind of global vision and systematic consideration of these CSR issues. Zhu (2013) makes a keynote presentation of the analysis of organizational ethics based on value chain, arguing that value chain is a systematic analysis model for organizational ethical issues and there are unique ethical issues in a specific function along the value chain of a firm but the occurring of a function's ethical issue is holistic or fatal to the whole organization.

On the basis of the above review of literature and with reference to the related model proposed by previous researches the author presents the following theoretical analysis framework for the analysis of CSR issues based on value chain model (Fig. 2).

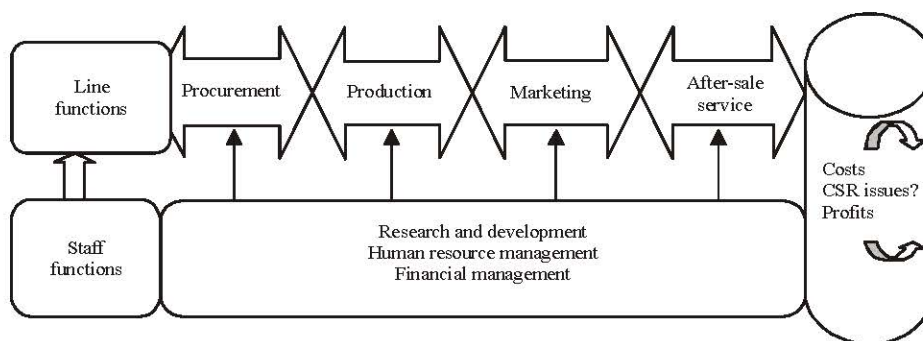


Fig. 2: Theoretical analysis framework for the present research

For a company, any line and staff functional input will be involved with the factor of costs along the value chain. To minimize costs will mean the compromise or reduction of quality, function, or reliability, etc., so, that CSR issues may occur. All the line and staff functional activities are connected with each other to create value to the company as a whole and their relations are not only just between an organization's internal departments but also between them and their external stakeholders such as suppliers, customers, communities and creditors.

The above framework will be used as the basic model for the following analysis of this present research but when it is used for analyzing CSR issues of a multinational corporation or an international firm, these issues will become more complex as a result of the extension of the value chain to a global value chain.

ANALYSIS OF CSR ISSUES BASED ON VALUE CHAIN MODEL

Line functions and CSR issues

Procurement-related CSR issues: Procurement function itself has a value chain involved where ethical problems such as business bribery and kickbacks or commissions may take place to reduce the quality of the purchased raw materials or increase the operation cost of the firm, thus benefit the supplier or the procurement manager but damaging the interest of the investor. The CSR issue of procurement may be the other way around when the procurement manager delays or refuses to make the payment for the supply or delivery of the supplier which may harm the interest of the supplier. Of course, when the procurement is completed with a foreign source or by importing from other countries, the CSR issue may be the evading of import tax for the imported raw materials or work-in-progress.

The Chinese food business scandal of Sanlu Tainted milk in 2008 was actually a case of procurement-related CSR issue, in which the raw material of milk supplied from suppliers or farmers contained the chemical element of melamine. Such a dangerous but cheaper raw milk purchased purposely by the procurement manager reduced the cost and increased the profit but as a result of such an irresponsible behavior causing the death or illness of more and more babies, the firm was punished and put out of business overnight. An American Food MNC in China, Shanghai Hushi Food Co., is now reported by the media about its supply of overtime meet to fast food giants like McDonalds, KFC, Pizza Hut and so on in 21st, July 2014. Shanghai Hushi Food Co., has been charged and sealed out and the case is now under investigation. It is said that in recent years in China, over 14 fast food firms have been involved with business scandals. Most of them are related with the procurement or supply-related CSR issue in value chains which has aroused the attention of both the authority and the public. More and more people have thus changed their idea about the consumption of these brands of fast food, for example, according to the most recent web survey, over 68.9% people surveyed reply that they will not buy these brands of food any more (Xinhua Netnews, 2014).

Production-related CSR issues: This area of CSR issues deals with the duties of a company to ensure that products and production or operation processes do not cause harm. Some of the more acute ethical dilemmas in this area arise out of the fact that there is usually a degree of danger in any product or production process and it is difficult to define a degree of permissibility, or the degree of permissibility may depend on the changing state of preventative technologies or changing social perceptions of acceptable risk.

Any commercial firm will pursue the production of "Cheaper, quicker and faster" to maximize profits and this production behavior will lead to the compromise of product quality or the reduction of production safety in short-cut ways, thus production-related CSR issues arise unavoidably. As seen from the above figure, inherently dangerous products or services such as tobacco, alcohol, weapons, etc., may make the consumer become addictive or even kill the consumer's life while inferior or problematic raw materials used in production such as low-quality food and tires, or unsafe new technologies used in production such as genetically-produced grains and mobile phone radiation may also damage the interest of consumers or even endanger the life of consumers.

In addition, a firm uses hazardous or environmental-unfriendly production methods in its production process may cause environmental problems such as waste materials and water, carbon emissions, or other environmental pollution issues which damages the interest of local communities or even the whole human society. In China, the behavior of "Taking bile from live bears" to make Chinese herbal medicine has aroused a lot of concerns about the humanistic production method of pharmaceutical companies. This is also a good example of production-related CSR issues.

Marketing and sales-related CSR issues: In the function of marketing and sales, a firm may conduct a series of unethical behaviors causing damages to customers' interests. In the whole process of advertising, pricing and selling, a lot of CSR issues occur as result of firms' marketing strategies or practices of exaggeration, cheating, price-fixing and anti-dumping and so on. In terms of CSR issues of advertising, marketing strategies like false marketing, bait and switch marketing, green-wash marketing, viral marketing, ambush marketing, electronic spam, attack advertising, sex marketing, etc., are examples of CSR issues. In terms of CSR issues of pricing, price fixing, price discrimination, price skimming and pricing control are examples of damaging interests of customers and competitors. In terms of CSR issues of selling, examples are purposely delayed or refused delivery after getting pay from buyers or customers, anti-competitive practices such as the manipulation of loyalty and supply chains and antidumping behaviors and so forth.

After-sales service-related CSR issues: In the function of after-sales service, socially responsible business conducts may add value to a firm and increase its reputation and fame but irresponsible business behaviors may reduce the loyalty of customers and even spoil the future of the whole company. After-sales service-related CSR issues are normally seen as a

firm's buck-passing acts at the request of repairing or changing a product, the cheating of customers by means of repairing a small matter at the cost of big one, the use of inferior components to replace high-quality components or to repair, the lack of pricing transparency in repairing or maintenance and so forth.

Staff functions and CSR issues

R and D-related CSR issues: In the function of research and development, in order to reduce the cost of research and development, such CSR issues may happen, for example, in product testing, the conducting of unethical animal testing, the use of economically disadvantaged groups such as students, children or babies as test objects, the insufficient testing before launching into markets and so on which may damage animal rights, children rights and consumer rights. In intellectual property protection, such CSR issues may be frequently seen, for instance, patent infringement or misuse, copyright infringement or misuse, trademark infringement or misuse, industrial espionage, the practice of attracting key employees away from a competitor to take unfair advantage of the knowledge or skills they may possess, etc., which directly damages the interest of competitors.

Human resource management-related CSR issues: Human resource management-related CSR issues can be observed from the core responsibilities or main functions of human resource managers in the company. Human resource management usually has five core responsibilities which include staffing, recruitment and selection, training and education, performance evaluation and compensation and separation, each of which may be involved with CSR issues in the practice (Fig. 3).

From the Fig. 3, it is seen that there are specific unique CSR issues which may take place in any one of these human resource management functions of a firm. For instance, before recruitment, in the step of staff planning, the manager of human resource department may make a tailor-made job description for some targeted job vacancy applicants so, that

only these candidates are fit for application. In recruitment and selection, CSR issues of various discrimination may happen, for example, age discrimination, gender discrimination, racial or religious discrimination, disability discrimination, appearance discrimination, university discrimination (only graduates from 985 and 211 Chinese universities are able to apply) and other CSR issues in recruitment and selection, such as the enforced working condition of workplace surveillance, drug or health testing or scanning before signing labor contracts, child labor, the appointment of someone by favoritism, etc. In employee training and education, the lack of training or improper training for newly-recruited employees before starting their work, the unfair opportunities of on-the-job training or off-the-job training given to some employees and so forth. In employee evaluation and compensation, the firm's less pay than the minimum wage required by law, pay discrimination based on gender, no pay for over-timing, delayed or deducted pay for workers, no pay for employee social security, the problem of occupational safety and health care, the excessive payment made to corporate CEO's and top management, etc. In separation, the CSR issue of at-will employment contract to fire employees, the firing of employees in the excuse of their whistle-blowing, the downsizing or firing of employees based on race, age, gender, religion, or any other discriminatory acts.

It should be further pointed out that in international human resource outsourcing activities of a firm, unique and more complicated CSR issues of human resource management may arise, when the outsourcing activities mean the loss of jobs for employees in the outsourcing company in one nation and the increase of job opportunities for those in the outsourced firm in another nation.

Financial management-related CSR issues: In the staff function of financial management, there are three main duties or distinct areas which involve CSR issues. They are financial transactions, accounting and auditing. In the management of financial transactions, the CSR issues of business bribery, kickbacks and facilitation payments may be in the (short-term)

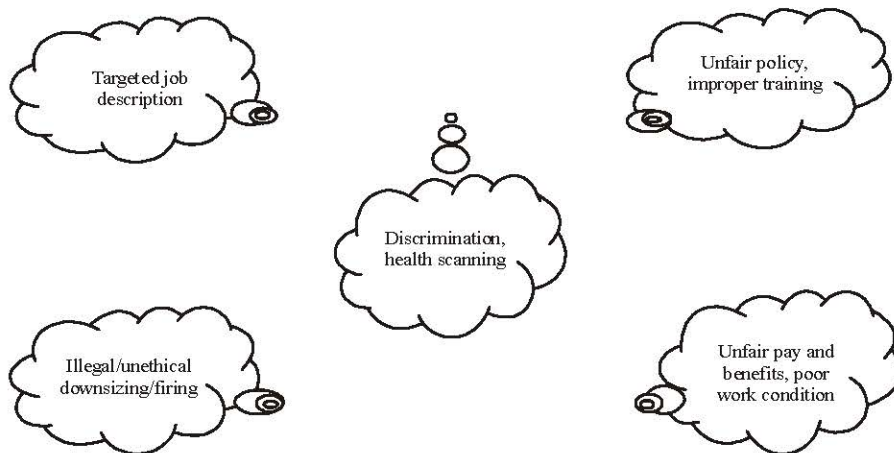


Fig. 3: Core human resource management responsibilities and CSR issues

or distinct areas which involve CSR issues. They are financial transactions, accounting and auditing. In the management of financial transactions, the CSR issues of business bribery, kickbacks and facilitation payments may be in the (short-term) interests of the company and its shareholders but these practices may be anti-competitive or offend against the values of society; insider trading and securities fraud may benefit some investors but concern a kind of criminal manipulation of the financial market, damaging the interest of other investors. In the function of accounting, common CSR problems are creative accounting, earnings management, misleading financial analysis, etc. In the function of auditing, certified financial statements provided by a third party accounting firm adds value and trust to the reputation of the firm and increases the confidence of the public and investors but CSR issues may arise because the firm and the auditing party may have established a kind of cooperative under-the-table relationship, so that the auditing party may lose its integrity and independence in providing the auditing certification to the financial statement, thus damaging the investment interest of investors or the tax-income interest of the government or local community. Enron accounting scandal caused by creative accounting which was revealed in October 2001 and eventually led to the bankruptcy of the firm, is a very good example of the CSR issue of financial management.

CONCLUSION

On the basis of reviewing the existing literature, the study constructs a theoretical analysis framework for systematically analyzing CSR issues based on value chain model and argues that when value chain model is used for analyzing CSR issues of a multinational corporation or an international firm, the CSR issues will be become more complex as a result of the extension of the value chain to a global value chain.

The whole research concludes that value chain is a more systematic model than the existing ones for analyzing CSR issues of a business organization; any CSR problem of a function along the value chain of a firm is unique itself for the specific function involved but its impact is holistic and may be fatal to the firm as a whole.

The research finding implies that the understanding of a firm's CSR issues based on value chain model is an important foundation for scientifically managing or preventing the related problem. Only when all the CSR issues in each line or staff functional department have been effectively managed can a firm handle the real challenge of sustainable development. Therefore, the enhancement of value chain management is key to the management of a firm's CSR issues.

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