

Corporate Responsibility

## The connected world in 2006

**Government policy, NGO engagement, innovation, transparency, and increased accountability are the big themes for the next year**

### The European Union

Environmental policies look set to play second fiddle to jobs in 2006 even though Commissioners are split on whether environmental rules are a cost burden or a spur to innovation. **Economic factors** will be key in how several issues play out during 2006

These will include the **EU Emissions Trading Scheme**. Member states must submit their second lot of national action plans to cut industrial emissions of CO<sub>2</sub> by 30 June. Such plans will apply for 2008 until 2012, the period the EU has committed to cut greenhouse gases by 8% compared to 1990 levels under the Kyoto Protocol.

The EU now agrees that environmental policy development should be tied to the principles of **'better regulation'**. These require strict economic impact assessments to be made before every legislative proposal.

Other environmental policy issues due to be discussed in the European Council include **clean air**, the **marine environment**, **waste** and **recycling** and **natural resource use**. With regard to **REACH**, the draft chemical regulations, they are expected to get their second reading in Parliament and Council. A **final agreement** will be struck under the **Finnish Presidency** by the end of 2006.

The Council will also debate its review of the EU's **sustainable development** strategy. Watch for the eventual balance between content and rhetoric.

The much delayed **EU Communication on CSR**, due out in late January, will be in line with the themes of the reinvigorated Lisbon Agenda and 'better regulation' approach and is expected to firmly promote the voluntary approach to CSR across the region. One consequence of this will be to make existing **CSR instruments** even more important.

Despite the cancellation of the mandatory **Operating and Financial Review** requirement in the UK, companies will continue to produce them, as activist investors, NGOs and trade unions will maintain their pressure for greater corporate accountability. The UK's CSR minister will maintain his historical silence.

### Central Europe and Eurasia

The region will continue its economic growth, based on either EU integration, outsourcing or energy prices. **Civil society institutions** will face a tough challenge during 2006, since worried governments will be keen to discredit democracy-connected NGOs. Western driven initiatives such as the **Extractive Industries Transparency Initiative** will continue to gain ground in countries seeking stock market cash, like **Kazakhstan**, but may be undermined by **China's** dash for oil and gas and **Russia's** energy strategy. The vast **Baku-Tbilisi-Ceyhan** oil



pipeline will begin pumping Azeri crude; expect more complaints from NGOs as it does so.

### Africa

Africa will continue to struggle in its quagmire of **corruption**, **poor governance** and **low value commodity exports**. However, some governance bright spots are emerging with the forthcoming trial of former deputy president **Jacob Zuma** in **South Africa** on corruption charges. **Nigeria** too appears intent on making some progress on anti-corruption. Initiatives and companies seeking to raise Africa's production of **finished goods** will gain more ground, and debt forgiveness, loans and development aid will begin to be channelled more effectively into **micro-business**, **credit** and **infrastructure**, although much will still be lost to corruption and poor management. **Capacity building** in government officials, business people and communities will emerge as a major theme for companies to partner with NGOs on in the region. **Transparency** will be seen as important, with expanded oil and gas production in West Africa in particular, increasing the spotlight on places like **Nigeria**, **Angola**, **Equatorial Guinea**, **Sao Tome**, **Chad**, **Sudan**, **Algeria** and **Western Sahara**. **China's** influence in Africa will worry many, who will point to its bankrolling of the **Sudan** government for oil exports as evidence of a race to the bottom. The **Kimberley process** of diamond certification will up the ante for laggard governments.

### The United States and Canada

Reticence on the part of the Bush administration on **climate change** is well known and will be maintained. The US Government will point to its promotion of low carbon technologies, clean development mechanisms, **nuclear** and **clean coal** encouragement as evidence it takes the issue semi-seriously. By contrast, the **Canadians**, the **Eastern states** and **California** will continue to raise the bar nationally with their discussions on greenhouse gas limits. The **General Audit Office** recommendations of late 2005 on co-ordination and consistency of myriad corporate responsibility issues encouraged by differing state agencies across the US will be ignored. However, America's largest companies, more exposed to the corporate responsibility debate, may begin to increase the pressure on their government and announce more **voluntary measures** and collaborative **partnerships** with NGOs and sector peers to improve their social and environmental performance globally. Executive **management contracts** will receive closer attention from investors, although CEO salaries will escape the degree of attention they deserve.

**Canada** will maintain and increase its considerable lead of the US

regarding **greenhouse gas** issues, push companies harder on **climate change mitigation**, whilst further seeking to develop its **natural resources**, such as shale oil and tar sands.

### Latin America

In Latin America, the challenge of **poverty in weak economies** will continue to challenge both government and business. Governments will continue to struggle with the trade-offs of the **Americas free trade agreement** - how to protect their most economically vulnerable citizens, like small farmers - and at the same time get better access to markets. These events will lead even more companies to look at "**bottom of the pyramid**" issues of product development for poorer citizens.

The CSR movement will continue to develop, especially on the coat-tails of an improving economic situation. This trend will be reinforced by a continued development of the market for CSR drivers. These will include more focused efforts by civil society and management and better awareness by the media and big buyers. The laggards will continue to be **consumers, governments** and the **financial markets**. Do not expect too much, but the trend is positive.

Regionally, **Brazil, Chile** and **Costa Rica** will continue to lead on CSR issues, while **Mexico** will drag its feet. Government actions on social issues will be closely watched in **Bolivia, Venezuela**, and **Argentina**.

### Asia (minus China)

**Privatisation** will increasingly become the Asia-Pacific region's major corporate responsibility theme. **Energy security** in particular will loom large as both a privatisation/corporate responsibility and a wider political issue.

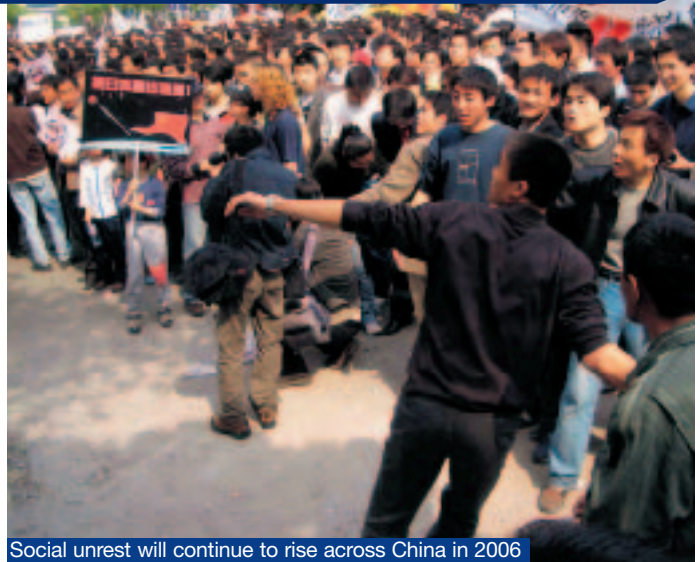
**Corporate governance** will be confirmed as a regional obsession. But many in the region will hit back, arguing increased regulations are just kowtowing to the West, are "**non-tariff trade barriers**", and are not applicable in Asia.

The **supply chain** will be talking back. As Western buyers attempt to generate greater transparency and accountability among their Asian suppliers, whilst not accepting the "**transfer costs**", manufacturers will argue their standards will drive up prices and put others out of business.

The systematic stripping of Indonesia's and Burma's remaining **forest** cover will continue unabated, due to low government interest in prevention and high demand in China, the US and Europe.

### China

More indications will emerge that China is failing to hold together **diverging** and **differentiating communities** and its **rich/poor divide**. Tensions will continue to fester and the Communist party will



Social unrest will continue to rise across China in 2006

slouch closer to its own eventual demise. The **political turf war** between local governments and Beijing will get hotter.

China's CSR issues will continue to be many and varied: **factory working conditions, political freedoms, the environment, and internet censorship**.

Brand-name firms like **Microsoft, Wal-Mart, Shell** and **Disney** will increasingly be seen as part of the solutions. NGOs, the press and investors will seek to hold them accountable. The spotlight will only get brighter as the **2008 Olympics** in Beijing approaches.


The **Chinese government** and people see the Olympics as their global platform to showcase the country's remarkable **economic modernisation**. NGO and trade union campaigners will see the Olympics as their **greatest platform** for publicity on global labour, human rights and environmental issues, and begin to plan accordingly.

### Non-Governmental Organisations

On the international front, the growing political **backlash** against NGOs is set to continue, as governments seek to control them in less democratic regions, such as **Russia**. Business will continue to be suspicious of the varied NGO sector, but will increasingly engage with credible NGOs. The separation between NGOs, which believe in collaboration and those that do not, will become more apparent.

Big NGOs such as **WWF** and **Oxfam** will re-assert their desire to censure companies and sectors, where needed, with some major reports. **Agriculture** and its supply chain impacts on workers and the environment will be a major issue for many campaigning NGOs, as will human rights when **John Ruggie**, United Nations Special Representative for Business and Human Rights, submits his first report to the UN.

It will become easier for more progressive companies to form



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Partnerships: the way forward in 2006

**partnerships** with NGOs and for them to make use of NGO expertise. But credibility will become increasingly dependent not on the symbolism of partnerships but on the outcomes, their actual **goals and performance**.

There will be further efforts on the part of hitherto far-flung but similarly interested groups to **better co-ordinate** NGO activities and campaigns. **NGO accountability** concerns will continue to be of concern to many, and one or more of the larger NGOs will respond with their own accountability agenda.

Across developing nations, local NGOs, bolstered by partnerships with international NGOs, will find greater traction in communities at a time when faith in governments and the business sector is faltering. The challenge for business will be to foster **effective collaborations** with these NGOs.

### Public policy

There will be renewed and broader calls for progressive governments, mostly in the EU, to shape the market for responsible business through public policy, beginning with **public procurement**. 2006 may see the emergence of a re-focus on how **markets can be shaped** to benefit the 'good' company, product or service at the expense of the 'bad'. Academics, thinkers and government policy makers will begin to seriously consider how the playing field can be levelled through public policy whilst maintaining business flexibility and freedom to innovate and create jobs. The **energy sector** will attract most attention, as governments recognise that while some issues are emerging rapidly, such as climate change, competition for **dwindling oil and gas** reserves, and geo-strategic risks, this is not being matched by **technological and infrastructure** developments.

### Business strategy

2006 will be about corporate responsibility delivering **real differentials** amongst competitors, as companies learn to focus their investment to deliver real business gains.

More companies will be seeking to develop products and services that can support societal needs and generate revenues. **General Electric's** Ecomagination initiative will begin to be felt beyond its supply base and other companies will rush to cash in on **alternative energy and environmental technologies**.

By using corporate responsibility as a proper **business management tool** and as an integral part of the business planning process, in 2006 smarter companies will define better where to invest – and where not to – in particular areas and issues relating to corporate responsibility that can support their business strategy. CSR will evolve further as a tool to measure and build '**social capital**'.

### Disclosure and transparency

The growing frustration with corporate responsibility reporting – both in respect of reporting being done, and reporting not yet being done – will continue to mount. Companies will begin to look beyond CSR reports and into mainstream communication, advertising and direct customer engagement. This may be in the form of '**corporate social campaigning**' on CSR issues which run across billboards, TV advertising and investor engagement road-shows. This move away from reports and into **direct communication** will be significant during 2006.

CSR reports will increasingly become commodified and polarised (have one: good; do not have one: bad) and part of the CSR communications focus will shift internally. This **focus on employees** will aim to hedge on recruitment/retention and also to drive CSR into the corporate 'DNA' of companies.

**Investors** too will be targeted, as more companies begin to explain the link between their CSR programmes and business models. The new **Global Reporting Initiative** guidelines will be released and will answer many of the complaints raised in the past concerning their use, but not all. GRI usage among companies will rise, as will 'communications on progress' by **Global Compact** participants. At the level of public debate, expect more attention to issues such as why more developing country businesses, public authorities and NGOs are not reporting, as well as on what **difference** reporting is making on the ground.

The **UK Information Commissioner** will push for more transparency in cases involving government dealings with corporations. Campaigners will continue to highlight the activities of **business lobbyists** in rent-seeking and undermining sustainable development in London, Washington and Brussels.

### Litigation

The courts witnessed a flurry of litigation filed during the course of the last few months of 2005. 2006 will see **increased aggressiveness** on the part of campaigners to bring their issues to the US courts as well as jurisdictions outside of the US.

2006 will also see more **foreign direct liability** cases against companies, beginning in the UK courts. More **US Alien Tort Claims Act (ATCA)** cases will reach settlement, as corporate defendants run out of options for having claims dismissed at the preliminary stages.

Internationally, companies will of course have to face up to some new treaty regimes relating to CSR, such as the **Framework Convention on Tobacco Control** and the Rotterdam Convention on **hazardous chemicals**.

### Investors and markets

The notion of "materiality" is forcing environmental, social and governance issues into the **mainstream** of the investment industry. Revised **Principles for Responsible Investment** will be formally launched by the **UN** sometime around March 2006.

Investors are set to become more active on critical reporting issues, such as **human capital** and **carbon** usage as corporate disclosure continues to lag behind expectations. The UK's shock abandonment of the mandatory requirement for an **Operating and Financial Review** by listed companies sets the stage for a more aggressive civil society focus on transparency which will be reflected across the activist investor community.

In 2006 the mainstream financial markets will be pushed by campaigners to focus more on environmental, social and governance

issues with respect to long-range investment horizons. 2006 will see an increase in the growing body of evidence highlighting the fact that specific CSR related issues can be material to **corporate profitability** and relevant to long-term investment returns. Don't expect an overnight revolution but mainstream analysts will increasingly link issues such as **climate change**, **labour conditions**, and **HIV/AIDS** to business value drivers.

There will be more research into emerging-market companies, and the **Enhanced Analytics Initiative** will continue to encourage investment research that considers the impact of extra-financial issues on long-term company performance. Pressure will grow on **institutional investors** to publish their **voting records** at companies.

### Corporate power, tax, lobbying

Mounting concern over the impacts of **corporate concentration** will continue into 2006. Such concentration will further expose a major area where voluntary CSR programmes have limited, if any role. In 2006 this may aid in refocusing attention on how **competition policies** can be modernised to cope with global liberalisation. Corporate **lobbying**, general transparency and issues such as corporate **tax payments** and internal **transfer pricing** as an immoral method of **tax avoidance** will rise further up the public and media agenda. In the coming year there will also be more attention to the role of government and the civil service over the transparency of their business connections. In 2006 we may even see a move towards a **code of practice for government** to begin to control their complicity with the **lobbying efforts** of companies and in particular, **business associations**.

### Collaboration

2006 will be the year in which some governments begin to grasp that their role is one of practical progress **catalyst** as well as wielder of the stick of censure or the carrot of economic incentive. More forward thinking governments, particularly across the European Union, will encourage companies and NGOs to **engage** and **partner** to tackle important policy issues. Such partnerships will increasingly drive collaborative, networked sustainable development learning. In turn this will lead to product and service innovation for smarter companies.

Advances in **global communication**, **technology**, its **distribution** and enabling of **collaboration** will mean that in 2006 research and development of new business methods, models and management practices can be ever more quickly distributed around the globe. Over the next twelve months the gradual, global realisation that costs cannot be forever **externalised** in the connected world will increase the momentum for world-wide understanding that problems must be tackled collaboratively. ■

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